CITY OF
SAN JOSE
CAPITAL OF SILICON VALLEY

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Memorandum

TO: HONORABLE MAYOR AND CITY COUNCIL

FROM: Betsy Shotwell
Roxanne Miller

SUBJECT: SEE BELOW

DATE: August 4, 2009

Approved

Date 8/4/09

INFORMATION

SUBJECT: FY 2009-10 STATE BUDGET REVISIONS: IMPACTS TO THE CITY OF SAN JOSE AND THE SAN JOSE REDEVELOPMENT AGENCY

Governor Schwarzenegger on July 28 signed a package of 26 bills as amendments to close the $23.24 billion budget shortfall in the FY 2009-10 State Budget Bill. The revisions provide $24.159 billion in budget solutions without tax increases including: $16.125 billion in spending cuts; $3.492 billion in revenues accelerations; $2.18 billion in borrowing including $1.93 billion from local property tax revenues and $1.005 billion from funding shifts and $1.355 billion in other one-time savings including deferral of payments until July 1, 2010.

The revised 2009-10 budget provides $89.5 billion in revenues and transfers to the General Fund and authorizes General Fund spending at $84.6 billion. The Governor vetoed $489 million in General Fund appropriations to health and human service programs and other state departments to achieve a reserve of $500 million after the Legislature had sent him a budget plan with a negative reserve of $156 million. Democratic leadership is challenging the vetoes as illegal while the Department of Finance (DOF) and Legislative Analyst (LAO) are projecting a budget deficit of $7 to $8 billion in FY2010-11 and larger shortfalls in out years. The DOF, State Treasurer and Controller are evaluating the state's cash situation including issuance of IOUs and are expected to complete their cash projections in a few weeks.

In February, the state had enacted $36 billion in solutions to an estimated $42 billion General Fund budget gap and an additional $6 billion in solutions that voters failed to approve on the May 19 special election ballot. The $24 billion in new solutions brings to $60 billion the budget measures adopted this year to "restore balance to a state budget that has been decimated by the worst budget crisis in the state's history."

For San Jose, cities and redevelopment agencies impacts in the adopted Budget Revision package include:

Suspension of Proposition 1A – Diversion of $1.935 billion of local government property tax revenues in 2009-10. Estimated impact to San Jose: $19,571,597. Budget amendments (AB4x 14 and AB 4x 15) authorize $1.935 billion in property tax monies to be borrowed from cities, counties and special districts pursuant to Proposition 1A (2004). Under Proposition 1A, the Governor issued an emergency proclamation to suspend Proposition 1A on July 24. The suspension will divert 8 percent of the total property tax revenues received by cities, counties and special districts in 2008-09 (excluding debt levies). The county auditors are instructed to shift the 8 percent of each local government's share of property taxes to the county-level Supplemental Revenue Augmentation Fund to fund K-12 schools and other state programs that would otherwise be funded from the State General Fund. The maximum diversion from any one jurisdiction will be 8 percent of an entity's property tax collections and the state must repay the amount shifted, with interest, no later than June 30, 2013. The bill also includes a "hardship exemption" that requires local agencies to apply for by October 15. If an exemption is granted, the maximum diversion from any one jurisdiction amount borrowed will increase from other jurisdictions within that county.

Securitization -- The bill contains language to allow local government to bond against the state's promise to repay the funds and caps the amount of interest that can be paid on the bonds issued at 8 percent. If a city bonds against the Proposition 1A loan, the State will pay their interest up to 8 percent of issuance, as specified. If a city decides not to bond against the Proposition 1A loan, the state will pay the city at an interest rate to be determined by the state controller not to exceed 6 percent. The state financed loan repayment securitization program is intended to offset the local fiscal effect of the borrowing.

We are working with the League of CA Cities, CSAC and DOF to provide clean-up amendments to the Proposition 1A securitization authority that would allow bonds to be issued by the California Communities JPA and payments made to local agencies in the next few months. This timing is needed for cities to receive their funds from the bond issue prior to the normal December 10 property tax distribution date. This legislation will authorize a local government created joint powers authority to issue bonds against the state's repayment obligation to provide continuous funding to local agencies during the "borrowing" period.

Redevelopment - "Takes" $2.05 billion in redevelopment funds to close the state budget deficit. (AB4x 26) taking $1.7 billion in FY 2009-10 and another $350 million in FY 2010-11. San Jose Redevelopment Agency's take is estimated at $62 million in 2009-10 and an additional $12.8 million in 2010-11. The funds will be deposited in the county Supplemental Educational Revenue Augmentation Funds (SERAF) to meet the State's obligations to schools. The redevelopment agencies can extend their time limits for plan effectiveness and receipt of payment for one year after payment of their 2009-10 obligations. If an agency does not make its payment by the May 10 deadline it will suffer the "death penalty." An agency in 2009-10 can "suspend" use their low and moderate income housing funds to make the SERAF payment but its housing fund must be paid back by June 30, 2015. If the agency uses its housing funds to meet the SERAF payment and does not fully repay its low and moderate income housing fund by that time, its set-aside requirement for low and moderate income housing increases from 20 percent to 25 percent.

A similar "taking" of $350 million in redevelopment funds in 2008-2009 was found to be unconstitutional. In response to this year's unconstitutional taking of redevelopment funds the CA Redevelopment Association is preparing to file another lawsuit to challenge the State's budget action this year.

Highway Users Tax (HUTA) - The proposal to "seize" $1.7 billion in local gas tax revenues used for local transportation programs passed the Senate along with budget revisions but died in the Assembly. The two year proposal would have taken $986 million in 2009-10 and another $750 million in 2010-11 from local agencies. San Jose's share of the "take" would have been $15.7 million in 2009-10 and $11.6 million in 2010-11. However, as part of the cash deferrals, the monthly HUTA payments are being deferred from July through December 2009 with deferred payment to be paid after January 1, 2010 under AB 4X 16. San Jose's 2009-10 share of HUTA funds are estimated at $16.4 million with payments received monthly. Approximately $70,000 in interest lost.

Proposition 42 – The budget defers the first two quarterly payments of Proposition 42 for October 2009 and January 2010 to cities and counties until May 2010. These deferrals total $288 million statewide with $144 million for cities and counties. San Jose's share is $7.5 million annually in quarterly payments. Approximately $60,000 interest lost. Cities and counties are also scheduled to receive their third and fourth quarterly payments by May 31, 2010. These are deferrals and not loans so state is not required to pay back funds with interest.

With the adoption of the Budget Revisions to the 2009-10 Budget, the Governor and legislative leaders have once again agreed on a state budget that is "balanced." Yet, the Legislative Analyst and Department of Finance are quick to acknowledge the budget is already $8 billion out of balance with the newly adopted budget heavily dependent on borrowing and unconstitutional takings from local governments and redevelopment agencies.

A sustainable state budget "solution" will not be achievable until the state's economy moves into recovery and there is reform of the state's system of public financing. The Governor has announced he is calling the Legislature back into Special Session in September and given the Commission on the 21st Century Economy an extension to present their recommendations to change the state's income, sales and property tax systems to align them with the 21st economy and reduce the volatility in the state's revenues. We will continue to maximize the opportunities for the City to initiate and influence decision making with an emphasis on protection of local revenues and economic development and job creation to grow the economy. Additional information will be provided as it becomes available

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