REPORT TO COUNCIL
City of Sacramento

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STAFF REPORT
October 25, 2005

Honorable Mayor and
Members of the Council

Subject: City Positions on November 2005 Ballot Measures

Location/Council District:
Citywide.

Recommendation:

This report forwards the city positions approved by the Law & Legislation Committee for propositions on the November 2005 state ballot for consideration and action by the Mayor and City Council. This report also forwards resolutions opposing Proposition 74, 75 and 76 for consideration and action by the Mayor and City Council.

Contact: Patti Bisharat, Government Affairs Manager, 808-8197

Presenters: Patti Bisharat, Government Affairs Manager, 808-8197

Department: City Manager's Office

Organization No: 0310

Summary:

There are currently eight (8) propositions on the November 8, 2005 state ballot. This report provides information on each measure, positions taken by the League of California Cities, the recommendation of staff on a City position for each proposition and the positions approved by the Law & Legislation Committee on October 18, 2005.

Committee/Commission Action:
The Law and Legislation Committee took action on city positions on the 2005 November propositions as follows:

Oppose: Proposition 73, 74, 75, 76, 77
No Position: Proposition 78, 79, 80

The Committee also directed staff to bring forward to Council resolutions opposing Propositions 74, 75 and 76. The resolutions are Attachment I to this report.

Background Information:

Staff reviewed the eight state ballot measures on the November 2005 ballot. In developing recommendations on whether to support, oppose, neutral or take no position on the various ballot measures, staff considered whether the measures would directly affect the City or its operations. If the measure would have no direct effect on the City, staff recommends taking no position.

The eight state ballot measures, the positions by the League of Cities, staff and the Law & Legislation Committee are:

Measure	Title	League of Cities Position	Staff Recommended City Position	Law & Leg Approved Position
Proposition 73	Waiting Period and Parental Notification Before Termination of Minor's Pregnancy	No position	No position	Oppose
Proposition 74	Public School Teachers. Waiting Period for Permanent Status.	No position	No position	Oppose
Proposition 75	Public Employee Union Dues. Restrictions on Political Contributions. Employee Consent Requirement.	No position	Neutral	Oppose
Proposition 76	State Spending and School Funding Limits.	Support	Support	Oppose
Proposition 77	Redistricting.	No position	Neutral	Oppose
Proposition 78	Discounts on Prescription Drugs.	No position	No position	No position
Proposition 79	Prescription Drug Discounts. State-Negotiated Rebates.	No position	No position	No position
Proposition 80	Electric Service Providers. Regulation.	No position	No position	No position

A copy of the information provided by the Attorney General and analysis of each proposition by the Legislative Analyst is included as "Attachment II" of this report.

The following is a brief summary of each of the propositions:

PROPOSITION 73
WAITING PERIOD AND PARENTAL NOTIFICATION BEFORE TERMINATION OF MINOR'S PREGNANCY. INITIATIVE CONSTITUTIONAL AMENDMENT.

Amends California Constitution, defining and prohibiting abortion for unemancipated minor until 48 hours after physician notifies minor's parent/guardian, except in medical emergency or with parental waiver. Mandates reporting requirements. Authorizes monetary damages against physicians for violation. Fiscal Impact: Potential unknown net state costs of several million dollars annually for health and social services programs, the courts, and state administration combined.

PROPOSITION 74
PUBLIC SCHOOL TEACHERS. WAITING PERIOD FOR PERMANENT STATUS. DISMISSAL. INITIATIVE STATUTE.

Increases probationary period for public school teachers from two to five years. Modifies the process by which school boards can dismiss a teaching employee who receives two consecutive unsatisfactory performance evaluations. Fiscal Impact: Unknown net effect on school districts' costs for teacher compensation, performance evaluations, and other activities. Impact would vary significantly by district and depend largely on future district personnel actions.

PROPOSITION 75
PUBLIC EMPLOYEE UNION DUES. RESTRICTIONS ON POLITICAL CONTRIBUTIONS. EMPLOYEE CONSENT REQUIREMENT. INITIATIVE STATUTE.

Prohibits using public employee union dues for political contributions without individual employees' prior consent. Excludes contributions benefiting charities or employees. Requires unions to maintain and, upon request, report member political contributions to Fair Political Practices Commission. Fiscal Impact: Probably minor state and local government implementation costs, potentially offset in part by revenues from fines and/or fees.

PROPOSITION 76
STATE SPENDING AND SCHOOL FUNDING LIMITS. INITIATIVE CONSTITUTIONAL AMENDMENT.

Limits state spending to prior year's level plus three previous years' average revenue growth. Changes minimum school funding requirements (Proposition 98). Permits Governor, under specified circumstances, to reduce budget appropriations of Governor's choosing. Fiscal Impact: State spending likely reduced relative to current law, due to additional spending limit and new powers granted to Governor. Reductions could apply to schools and shift costs to other local governments.

PROPOSITION 77
REDISTRICTING. INITIATIVE CONSTITUTIONAL AMENDMENT.

Amends state Constitution's process for redistricting California's Senate, Assembly, Congressional and Board of Equalization districts. Requires three-member panel of retired judges selected by legislative leaders. Fiscal Impact: One-time state redistricting costs totaling no more than $1.5 million and county costs in the range of $1 million. Potential reduction in future costs, but net impact would depend on decisions by voters.

PROPOSITION 78
DISCOUNTS ON PRESCRIPTION DRUGS. INITIATIVE STATUTE.

Establishes discount prescription drug program for certain low- and moderate-income Californians. Authorizes Department of Health Services to contract with participating pharmacies for discounts and with participating drug manufacturers for rebates. Fiscal Impact: State costs for administration and outreach in the millions to low tens of millions of dollars annually. State costs for advance funding for rebates. Unknown potentially significant savings for state and county health programs.

PROPOSITION 79
PRESCRIPTION DRUG DISCOUNTS. STATE-NEGOTIATED REBATES. INITIATIVE STATUTE.

Provides drug discounts to Californians with qualifying incomes. Funded by state-negotiated drug manufacturer rebates. Prohibits Medi-Cal contracts with manufacturers not providing Medicaid best price. Fiscal Impact: State costs for administration and outreach in low tens of millions of dollars annually. State costs for advance funding for rebates. Unknown potentially significant: (1) net costs or savings for Medi-Cal and (2) savings for state and county health programs.

PROPOSITION 80
ELECTRIC SERVICE PROVIDERS. REGULATION. INITIATIVE STATUTE.

Subjects electric service providers to regulation by California Public Utilities Commission. Restricts electricity customers' ability to switch from private utilities to other providers. Requires all retail electric sellers to increase renewable energy resource procurement by 2010. Fiscal Impact: Potential annual administrative costs ranging from negligible to $4 million, paid by fees. Unknown net impact on state and local costs and revenues from uncertain impact on electricity rates.

Financial Considerations:

None.

Environmental Considerations:

None.

Policy Considerations:

The recommended positions are consistent with the Council adopted legislative principles related to retaining local control over issues impacting the City.

Emerging Small Business Development (ESBD):

None.

Respectfully Submitted by:

Patti Bisharat, Government Affairs

Recommendation Approved:

ROBERT P. THOMAS
City Manager

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RESOLUTION NO.

Adopted by the Sacramento City Council

October 25, 2005

OPPOSING PROPOSITION 74 AND 75 ON THE 2005 NOVEMBER STATE BALLOT

Whereas, Proposition 74 reduces protections to teachers against unfair dismissal without commensurate improvements in due process, and

Whereas, Proposition 74 will likely make it even more difficult to recruit qualified teachers in a city suffering from a dire shortage of such teachers, and

Whereas, Public Employee unions in California may lawfully use union dues for political purposes, and

Whereas, Corporation spending for political purposes far exceeds that of unions, and

Whereas, Proposition 75 expressly requires union members to state a year in advance if their dues may be used for political purposes, and

Whereas, Proposition 75 makes no such commensurate requirement for corporations, and

Whereas, Proposition 75 would unfairly create obstacles to union support of political activity, and

Now, therefore be it resolved that, the City Council of the City of Sacramento opposes Proposition 74 and 75 on the November 8, 2005, special election ballot.

RESOLUTION NO.

Adopted by the Sacramento City Council

October 25, 2005

OPPOSING PROPOSITION 76 ON THE 2005 NOVEMBER STATE BALLOT

Whereas, Proposition 76 will reduce funding for vital local programs including police and fire protection, education and health care, resulting in fewer police on the streets and fewer firefighters able to respond to emergencies; and,

Whereas, Proposition 76 will allow the Governor to unilaterally reduce or eliminate subventions to cities and counties for local public safety through the Citizen's Options for Public Safety (COPS) program which will provide $100 million in FY2005-06, and for transportation projects provided by Proposition 42; and,

Whereas, Proposition 76 will cap spending supported by voter approved taxes, such as Proposition 111's gas tax that supports local and state transportation programs, Proposition 10's tobacco tax for early childhood programs, and Proposition 99's tobacco tax for anti-smoking programs and indigent medical care; and,

Whereas, Proposition 76 casts uncertainty on the exposure of Proposition 172 voter-approved revenues for local public safety functions to future reductions by action of the spending cap provisions; and,

Whereas, Proposition 76 authorizes the Governor to ignore all other provisions of the California Constitution when making reductions to appropriations in the state budget, which would allow the elimination of state reimbursement to local government for revenues lost as a result of the homeowner's property tax exemption which, for cities alone, totals $100 million annually; and,

Whereas, Proposition 76 does damage to our schools by drastically undermining the voter-approved Proposition 98, which will lead to more overcrowded schools, teacher layoffs, and fewer textbooks and classroom materials; and,

Whereas, Proposition 76 will cap spending for support of the health, mental health and human service programs that were shifted from the state to counties as a part of the 1991 realignment, including In-Home Supportive Services, Foster Care, Child Protective Services and basic mental health programs, placing greater fiscal pressure on local negotiations related to redevelopment and annexation; and,

Whereas, Proposition 76 will cap tax assistance programs available for senior citizens in California including the Senior Citizens' Property Tax Assistance program for seniors, blind and disabled residents, the Senior Citizens' Property Tax Deferral Program for low-income and disabled homeowners, and the Senior Citizens' Renters' Tax Assistance Program for seniors, blind and disabled.

Now, therefore, be it resolved that the City Council of the City of Sacramento opposes Proposition 76 on the November 8, 2005 special election ballot.

PROPOSITION 73

WAITING PERIOD AND PARENTAL NOTIFICATION BEFORE TERMINATION OF MINOR'S PREGNANCY. INITIATIVE CONSTITUTIONAL AMENDMENT.

Official Title and Summary

Prepared by the Attorney General

WAITING PERIOD AND PARENTAL NOTIFICATION BEFORE TERMINATION OF MINOR'S PREGNANCY. INITIATIVE CONSTITUTIONAL AMENDMENT.

- Amends California Constitution, prohibiting abortion for unemancipated minor until 48 hours after physician notifies minor's parent/legal guardian, except in medical emergency or with parental waiver.
- Defines abortion as causing "death of the unborn child, a child conceived but not yet born."
- Permits minor to obtain court order waiving notice based on clear, convincing evidence of minor's maturity or best interests.
- Mandates various reporting requirements.
- Authorizes monetary damages against physicians for violation.
- Requires minor's consent to abortion, with certain exceptions.
- Permits judicial relief if minor's consent coerced.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- Potential unknown net state costs of several million dollars annually for health and social services programs, the courts, and state administration combined.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

PRIOR STATE LEGISLATION

In 1953, a state law was enacted that allowed minors to receive, without parental consent or notification, the same types of medical care for a pregnancy that are available to an adult. Based on this law and later legal developments related to abortion, minors were able to obtain abortions without parental consent or notification.

In 1987, the Legislature amended this law to require minors to either obtain the consent of a parent or a court before obtaining an abortion. However, due to legal challenges, the law was never implemented, and the California Supreme Court ultimately struck it down in 1997. Consequently, minors in the state currently receive abortion services to the same extent as adults. This includes minors in various state health care programs, such as the Medi-Cal health care program for low-income individuals.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

PROPOSAL

NOTIFICATION REQUIREMENT

This proposition amends the California Constitution to require, with certain exceptions, a physician (or his or her representative) to *notify* the parent or legal guardian of a pregnant minor at least 48 hours before performing an abortion involving that minor. (This measure does not require a physician or a minor to obtain the consent of a parent or guardian.) This measure applies only to cases involving an "unemancipated" minor. The proposition identifies an unemancipated minor as being a female under the age of 18 who has not entered into a valid marriage, is not on active duty in the armed services of the United States, and has not been declared free from her parents' or guardians' custody and control under state law.

A physician would provide the required notification in either of the following two ways:

- *Personal Written Notification.* Written notice could be provided to the parent or guardian personally—for example, when a parent accompanied the minor to an office examination or to obtain the abortion itself.
- *Mail Notification.* A parent or guardian could be sent a written notice by certified mail so long as a return receipt was requested by the physician and delivery of the notice was restricted to the parent or guardian who must be notified. An additional copy of the written notice would have to be sent at the same time to the parent or guardian by first-class mail. Under this method, notification would be presumed to have occurred as of noon on the second day after the written notice was mailed.

EXCEPTIONS TO NOTIFICATION REQUIREMENTS

The measure provides the following exceptions to the notification requirements:

Medical Emergencies. The notification requirements would not apply if the physician certifies in the minor's medical record that the abortion is necessary to prevent the mother's death or that a delay would "create serious risk of substantial and irreversible impairment of a major bodily function."

Waivers Approved by Parent or Guardian. A minor's parent or guardian could waive the notification requirements, including the waiting period, by submitting a signed, written waiver form to the physician.

Waivers Approved by Courts. The pregnant minor could ask a juvenile court to waive the notification requirements. A court could do so if it finds that the minor is sufficiently mature and well-informed to decide whether to have an abortion or that notification would not be in the minor's best interest. If the waiver request is denied, the minor could appeal that decision to an appellate court.

A minor seeking a waiver would not have to pay court fees, would be appointed a temporary guardian and provided other assistance in the case by the court, and would be entitled to an attorney appointed by the court. The identity of the minor would be kept confidential. The court would generally have to hear and issue a ruling within three business days of receiving the waiver request. The appellate court would generally have to hear and decide any appeal within four business days.

For text of Proposition 73 see page 56

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

The proposition also requires that, in any case in which the court finds evidence of physical, sexual, or emotional abuse by the parent or guardian, the court must refer the evidence to the county child protection agency.

State Reporting Requirement

Physicians are required by this proposition to file a form reporting certain information to the state Department of Health Services (DHS) within one month after performing an abortion on a minor. The DHS form would include the identity of the physician, the date and place where the abortion was performed, the minor's month and year of birth, and certain other information about the circumstances under which the abortion was performed. The forms that physicians would file would not identify the minor or any parent or guardian by name. Based on these forms, DHS would compile certain statistical information relating to abortions performed on minors in an annual report that would be available to the public.

Penalties

Any person who performs an abortion on a minor and who fails to comply with the provisions of the measure would be liable for damages in a civil action brought by the minor, her legal representative, or by a parent or guardian wrongfully denied notification. Any person, other than the minor or her physician, who knowingly provides false information that notice of an abortion has been provided to a parent or guardian would be guilty of a misdemeanor punishable by a fine.

Relief From Coercion

The measure allows a minor to seek help from the juvenile court if anyone were to attempt to coerce her to have an abortion. A court would be required to consider such cases quickly and could take whatever action it finds necessary to prevent coercion.

FISCAL EFFECTS

The fiscal effects of this measure on state government would depend mainly upon how these new requirements affected the behavior of minors regarding abortion and childbearing. Studies of similar laws in other states suggest that the effect of this measure on the birthrate for California minors would be limited, if any. If it were to increase the birthrate for California minors, the net cost to the state would probably not exceed several million dollars annually for health and social services programs, the courts, and state administration combined. We discuss the potential major fiscal effects of the measure below.

State Health Care Programs Savings and Costs

Studies of other states with laws similar to the one proposed in this measure suggest that it could result in a reduction in the number of abortions obtained by minors within California. This reduction in abortions performed in California might be offset to an unknown extent by an increase in the number of out-of-state abortions obtained by California minors. Some minors might also avoid pregnancy as a result of this measure, further reducing the number of abortions for this group. If, for either reason,

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

this proposition reduces the overall number of minors obtaining abortions in California, it is also likely that fewer abortions would be performed under the Medi-Cal Program and other state health care programs that provide medical services for minors. This would result in unknown state savings for these programs.

This measure could also result in some unknown additional costs for state health care programs. If this measure results in a decrease in minors' abortions and an increase in the birthrate of children in low-income families eligible for publicly funded health care, the state would incur additional costs. These could include costs for medical services provided during pregnancy, deliveries, and infant care.

The net fiscal effect of these cost and savings factors, if any, on the state would probably not exceed costs of a few million dollars annually. These costs would not be significant compared to total state spending for programs that provide health care services. The Medi-Cal Program alone is estimated to cost the state $13.0 billion in 2005–06.

State Administrative Costs

The DHS would incur first-year state costs of up to $350,000 to develop the new forms needed to implement this measure, establish the physician reporting system, and prepare the initial annual report containing statistical information on abortions obtained by minors. The ongoing state costs for DHS to implement this measure could be as much as $150,000 annually.

Juvenile and Appellate Court Costs

The measure would result in increased state costs for the courts, primarily as a result of the provisions allowing minors to request a court waiver of the notification requirements. The magnitude of these costs is unknown but could reach several million dollars annually, depending primarily on the number of minors that sought waivers. These costs would not be significant compared to total state expenditures for the courts, which are estimated to be $1.7 billion in 2005–06.

Social Services Costs

If this measure discourages some minors from obtaining abortions and increases the birthrate among low-income minors, expenditures for cash assistance and services to needy families would increase under the California Work Opportunity and Responsibility to Kids (CalWORKs) program. The magnitude of these costs, if any, would probably not exceed a few million dollars annually. The CalWORKs program is supported with both state and federal funds, but because all CalWORKs federal funds are currently committed, these additional costs would probably be borne by the state. These costs would not be significant compared to total state spending for CalWORKs, which is estimated to cost about $5.1 billion in state and federal funds in 2005–06. Under these circumstances, there could also be a minor increase in child welfare and foster care costs for the state and counties.

For text of Proposition 73 see page 56

PROPOSITION 74

PUBLIC SCHOOL TEACHERS. WAITING PERIOD FOR PERMANENT STATUS. DISMISSAL. INITIATIVE STATUTE.

Official Title and Summary

Prepared by the Attorney General

PUBLIC SCHOOL TEACHERS. WAITING PERIOD FOR PERMANENT STATUS. DISMISSAL. INITIATIVE STATUTE.

- Increases length of time required before a teacher may become a permanent employee from two complete consecutive school years to five complete consecutive school years.
- Measure applies to teachers whose probationary period commenced during or after the 2003–2004 fiscal year.
- Modifies the process by which school boards can dismiss a permanent teaching employee who receives two consecutive unsatisfactory performance evaluations.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- Unknown net effect on school districts' costs for teacher compensation, performance evaluations, and other activities. The impact would vary significantly by district and depend largely on future personnel actions by individual school districts.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Most of the employees of K–12 school districts are referred to as "certificated" employees. These consist mainly of teachers but also include instructional specialists, counselors, and librarians. All of these employees must have some type of license (or certificate) prior to being employed by a district to show basic qualifications in their job area.

Job Status of Certificated Employees. Under current state law, certificated employees serve a *probationary* period during their first two years of service

LENGTH OF STATES' PROBATIONARY PERIOD FOR K–12 TEACHERS

One Year	Two Years	Three Years			Four Years	Five Years
Connecticut	**California**	Alaska	Kansas	Oregon	Kentucky	Indiana
North Dakota	Illinois	Alabama	Louisiana	Pennsylvania	Michigan	Missouri
South Carolina	Maine	Arizona	Massachusetts	Rhode Island	North Carolina	
	Maryland	Arkansas	Minnesota	South Dakota		
	Mississippi	Colorado	Montana	Tennessee		
	Nevada	Delaware	Nebraska	Texas		
	New Hampshire	Florida	New Jersey	Utah		
	Vermont	Georgia	New Mexico	Virginia		
	Washington	Hawaii	New York	West Virginia		
		Idaho	Ohio	Wisconsin		
		Iowa	Oklahoma	Wyoming		

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

with a school district. During the probationary period, state law currently requires certificated employees to be evaluated at least once a year. At the end of the employees' first or second year, school districts may choose not to rehire them without offering specific reasons. If not rehired, probationary employees do not have the right to challenge the decision. At the start of their third year, certificated employees are considered *permanent* (or tenured). (See the nearby boxes for some additional information related to California's probationary policies for certificated employees, primarily teachers.)

Dismissal Process for Permanent Employees. Under current state law, permanent certificated employees may be dismissed for unsatisfactory performance as well as a variety of other reasons (such as dishonesty and unprofessional conduct). Most permanent employees must be evaluated at least once every two years. If, however, they receive an unsatisfactory evaluation, they must be assessed annually until they achieve a satisfactory evaluation or are dismissed. Regardless of the reason for a dismissal, the dismissal process (also set forth in state law) consists of about a dozen stages. The process begins with a school district specifying reasons for dismissal and providing a 30-day notice of its intent to dismiss. If requested by the employee, the process includes a formal administrative hearing and the right to appeal to a Superior Court and then a Court of Appeal. Before being dismissed for unsatisfactory performance, the school district must first provide employees a 90-day period to allow them an opportunity to improve their performance.

PROPOSAL

Proposition 74 would change existing state law in the following ways.

Extends Probationary Period to Five Years. The proposition extends from two to five years the probationary period for new certificated employees.

Modifies Dismissal Process for Permanent Employees. The proposition states that two consecutive unsatisfactory performance evaluations constitute unsatisfactory performance for the purposes of dismissing permanent employees. In these cases, the school board would have the discretion to dismiss the employee and the board would *not* have to:

- Provide the 90-day period currently given to permanent employees to allow them to improve their performance.
- Provide as much initial documentation identifying specific instances of unsatisfactory performance (beyond that included in the evaluations themselves).

The effect of these changes would be to reduce requirements in the initial stages of the dismissal process and potentially place greater focus on the evaluation process. Although these changes would apply to all certificated employees, their primary effect would be on teachers.

For text of Proposition 74 see page 58.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Brief History of California's Probationary Policies

From 1927 to 1982, California had a three-year probationary period. Over this time, probationary employees typically had at least limited legal rights to challenge dismissal decisions.

The most recent major change to the state's probationary policies occurred in 1983 when the probationary period was shortened from three to two years. In addition, certain legal protections then afforded to probationary employees were removed. These policies remain in effect today.

Fiscal Effects

The proposition would affect costs relating to teacher compensation, performance evaluations, and other activities.

Effect on Teacher Compensation Costs

The proposition would affect school district teacher costs in a variety of ways. The net impact would depend on future district actions, and these effects would vary significantly by district. For example, districts would experience *reduced* teacher costs in the following cases:

- Given the longer probationary period, districts could dismiss more teachers during their first five years. This could result in salary savings by replacing higher salaried teachers toward the end of their probationary period with lower salaried teachers just beginning their probationary period.
- Similarly, due to the proposition's modifications to the dismissal process, school districts might experience greater turnover among permanent teachers. This too would result in teacher-related savings from replacing higher salaried veteran teachers with lower salaried, less experienced teachers.

In contrast, districts would experience *increased* teacher costs in the following instances:

- The supply of teachers could be reduced because the longer probationary period and modified dismissal process might be perceived as increasing job insecurity. This would have the effect of putting upward pressure on teacher compensation costs.
- The longer probationary period could lead districts to retain some struggling new teachers beyond the current two-year period to give them additional chances to succeed. By retaining these teachers—instead of replacing them with lower-cost entry level teachers—this would have the effect of increasing teacher salary costs above what they otherwise would have been.

As noted above, the net impact on a school district could vary significantly, depending on such factors as the local labor market, the perceived desirability of working in the district, and district actions in response to the measure.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Effect on Evaluation Costs

The proposition would increase teacher performance evaluation costs. Under current law, employees must receive at least three evaluations over their first five years. Under the proposition, they would need to receive five evaluations over this same period. That is, districts would need to conduct up to two additional evaluations for probationary employees. In addition, given the higher stakes involved with unsatisfactory evaluations, school districts might spend more time documenting these assessments.

These costs would also vary significantly from district to district. The costs could range from minor (for districts meeting these additional tasks with existing administrative staff) to more significant (for those adding additional staff to meet these responsibilities). Depending on how districts respond, the statewide costs could range from relatively minor to the low tens of millions of dollars annually.

Other Fiscal Impacts

The measure would have other potential impacts on the state and school districts.

Administrative and Legal Costs. The proposition's effect on school district administrative and legal costs is unknown. On the one hand, the proposition simplifies the dismissal process by requiring slightly less documentation and eliminating the special 90-day notice required for dismissals due to unsatisfactory performance. This would likely result in some administrative savings. On the other hand, given the somewhat simplified dismissal process, teacher dismissals might become more frequent. As a result, the number of teacher requests for administrative hearings and appeals, and their associated costs, could increase.

Bargaining Costs. Collective bargaining costs could increase as a result of the proposition. Evaluation procedures are subject to collective bargaining and are commonly found in teacher contracts. To the extent the evaluation process became higher stakes, related negotiations might take longer and be more costly. These costs would be associated with revising the evaluation process, refining evaluation standards, and/or defining unsatisfactory performance. The state would pay any additional costs, as it currently reimburses local school districts for their collective bargaining expenses.

Recruitment and Training. To the extent that districts have more or less teacher turnover as a result of this measure, their recruitment and training costs would be affected accordingly.

For text of Proposition 74 see page 58

PROPOSITION 75

PUBLIC EMPLOYEE UNION DUES. RESTRICTIONS ON POLITICAL CONTRIBUTIONS. EMPLOYEE CONSENT REQUIREMENT. INITIATIVE STATUTE.

Official Title and Summary

Prepared by the Attorney General

PUBLIC EMPLOYEE UNION DUES. RESTRICTIONS ON POLITICAL CONTRIBUTIONS. EMPLOYEE CONSENT REQUIREMENT. INITIATIVE STATUTE.

- Prohibits the use by public employee labor organizations of public employee dues or fees for political contributions except with the prior consent of individual public employees each year on a specified written form.
- Restriction does not apply to dues or fees collected for charitable organizations, health care insurance, or other purposes directly benefitting the public employee.
- Requires public employee labor organizations to maintain and submit records to Fair Political Practices Commission concerning individual public employees' and organizations' political contributions.
- These records are not subject to public disclosure.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- Probably minor state and local government implementation costs, potentially offset in part by revenues from fines and/or fees.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Unions for Government Employees. Groups of government employees—like employees in the private sector—can choose to have a union represent them in negotiations with their employers over salaries, benefits, and other conditions of employment. Individual government employees may choose whether or not to join the union that represents their group of employees. A union's negotiations affect all employees in the group—both members and nonmembers of the union. As a result, members of the group—whether they join a union or not—typically pay a certain level of dues and/or fees to a union for these bargaining and representation services.

Use of Union Dues or Fees for Political Purposes. A union of government employees may engage in other types of activities unrelated to bargaining and representation. For instance, public employee unions may decide to charge additional dues for various political purposes, including supporting and opposing political candidates and issues. Any fees collected from a nonmember of a union cannot be used for these types of political purposes if the nonmember objects. Each year, unions must publicly report what share of their expenditures was for political purposes.

PROPOSAL

This measure amends state statutes to require public employee unions to get annual, written consent from a government employee in order to charge and use that employee's dues or fees for political purposes. This requirement would apply to both members and nonmembers of a union. The measure would also require unions to keep certain records, including copies of any consent forms.

FISCAL EFFECTS

The state and local governments could experience some increased costs to implement and enforce the consent requirements of the measure. The amount of these costs is probably minor. Some of these costs could be partially offset by increased fines for not complying with the measure's provisions and/or fees charged by government agencies to cover the costs of processing payroll deductions for union dues and fees.

For text of Proposition 75 see page 59

PROPOSITION 76

STATE SPENDING AND SCHOOL FUNDING LIMITS. INITIATIVE CONSTITUTIONAL AMENDMENT.

Official Title and Summary

Prepared by the Attorney General

STATE SPENDING AND SCHOOL FUNDING LIMITS. INITIATIVE CONSTITUTIONAL AMENDMENT.

- Limits state spending to prior year's level plus three previous years' average revenue growth.
- Changes state minimum school funding requirements (Proposition 98); eliminates repayment requirement when minimum funding suspended.
- Excludes appropriations above the minimum from schools' funding base.
- Directs excess General Fund revenues, currently directed to schools/tax relief, to budget reserve, specified construction, debt repayment.
- Permits Governor, under specified circumstances, to reduce appropriations of Governor's choosing, including employee compensation/state contracts.
- Continues prior year appropriations if state budget delayed.
- Prohibits state special funds borrowing.
- Requires payment of local government mandates.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- The provisions creating an additional state spending limit and granting the Governor new power to reduce spending in most program areas would likely reduce expenditures relative to current law. These reductions also could apply to schools and shift costs to other local governments.
- The new spending limit could result in a smoother pattern of state expenditures over time, especially to the extent that reserves are set aside in good times and available in bad times.
- The provisions changing school funding formulas would make school and community college funding more subject to annual decisions of state policymakers and less affected by a constitutional funding guarantee.
- Relative to current law, the measure could result in a change in the mix of state spending—that is, some programs could receive a larger share and others a smaller share of the total budget.

ANALYSIS BY THE LEGISLATIVE ANALYST

SUMMARY

This measure makes major changes to California's Constitution relating to the state budget. As shown in Figure 1, the measure creates an additional state spending limit, grants the Governor substantial new power to unilaterally reduce state spending, and revises key provisions in the California Constitution relating to school and community college funding.

The combined effects of these provisions on state spending are shown in Figure 2. The main impact is a likely reduction in spending over time relative to current law. In addition, the measure could result in a smoother pattern of state spending and a different mix of state expenditures.

Each of the measure's key provisions is discussed in more detail below.

BACKGROUND

CALIFORNIA'S STATE BUDGET

California will spend about $113 billion to provide public services through its state budget this year.

FIGURE 1

PROPOSITION 76: MAIN PROVISIONS

✓ **An Additional State Spending Limit**
- Places a second limit on state expenditures, which would be based on an average of revenue growth in the three prior years.

✓ **Expanded Powers for Governor**
- Grants the Governor substantial new authority to unilaterally reduce state spending during certain fiscal situations.

✓ **School Funding Changes**
- Changes several key provisions in the State Constitution relating to the minimum funding guarantee for K–12 schools and community colleges.

✓ **Other Changes**
- Makes a number of other changes relating to transportation funding; loans between state funds; and payments to schools, local governments, and special funds.

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ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

FIGURE 2

PROPOSITION 76: KEY FISCAL EFFECTS

✓ **Effects on Spending**

- The additional spending limit and new powers granted to the Governor would likely reduce state spending over time relative to current law. These reductions also could shift costs to local governments (primarily counties).
- The new limit could also "smooth out" state spending over time, especially to the extent reserves set aside in good times are available in bad times.
- The new spending-reduction authority given to the Governor and other provisions of the measure could result in a different mix of state spending. That is, some programs' share of total spending would rise and others would fall relative to current law.

✓ **Effects on Schools**

- The provisions changing school funding formulas would make school funding more subject to annual decisions of state policymakers and less affected by a constitutional funding guarantee.
- Budget reductions resulting from the spending limit or Governor's new authority could apply to schools.

About four-fifths of this total—around $90 billion—will come from the state's General Fund for such major programs as elementary and secondary (K–12) education, higher education, health and social services, and criminal justice. The money to support General Fund spending is raised largely from the state's three major taxes—personal income tax, sales and use tax, and corporation tax.

The remaining one-fifth of total state spending is from hundreds of special funds—that is, funds in which specific revenues (such as excise taxes on gasoline or cigarettes) are dedicated to specific purposes (such as transportation or health care).

State and local government finances are closely related to one another in California. For example, most state spending for K–12 education, health, and social services is allocated to programs that are administered by local agencies. In some cases, program costs are shared between the state and local governments.

STATE'S FISCAL SITUATION

California has faced large annual shortfalls in its General Fund state budget since 2001–02. These shortfalls developed following the stock market plunge and the economic downturn that took place in 2001, which caused state revenues to fall sharply below the level needed to fund all of the state's spending commitments. Although revenues are growing again and the state has made progress toward resolving its budget problems, policymakers will need to take additional actions to address a likely state budget shortfall in 2006–07.

AN ADDITIONAL STATE SPENDING LIMIT

CURRENT LAW

Since 1979, California has imposed annual spending limits on the state and its thousands of individual local governments. The annual limit for each jurisdiction is based on its spending in 1978–79 (the base year), adjusted each year for growth in population and the economy. State government spending is currently about $11 billion below its spending limit, meaning that the present limit is not currently constraining spending. The large gap between the limit and actual expenditures opened up in 2001–02 following the steep revenue downturn in that year.

PROPOSAL

This measure adds a *second* limit on the annual growth in *state* expenditures. Beginning in 2006–07, combined expenditures from the state's General Fund and special funds would be limited to the prior-year level of expenditures, adjusted by the *average* of the growth rates in combined General Fund and special fund revenues over the prior three years.

In years in which actual spending falls below the limit, the spending limit for the subsequent year would be based on the reduced level of actual expenditures. Spending could temporarily exceed the limit in the event of a natural disaster (for example, fire, floods, or earthquakes) or an attack by an enemy of the United States.

What Happens If Revenues Exceed the Limit? If revenues exceed the limit, the excess amount would be divided proportionally among the General Fund and each of the state's special funds. The exact way in

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ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

which this allocation would occur is not specified in the measure. The portion of the excess revenues that is allocated to special funds would be held in reserve for expenditure in a subsequent year. In the case of the General Fund, its share of the excess revenues would be allocated as follows:

- *25 percent*—the state's reserve fund.
- *50 percent*—allocated through annual budget acts to repay any of the following: (1) the Proposition 98 maintenance factor outstanding (see below) at a rate of no more than one-fifteenth of the amount per year; (2) state-issued deficit-financing bonds; and (3) loans made from the Transportation Investment Fund in 2003–04 through 2006–07, with annual amounts not to exceed one-fifteenth of the amount outstanding as of June 30, 2007.
- *25 percent*—for road, highway, and school construction projects.

Funds allocated for the above purposes would not be counted as expenditures for purposes of calculating the following year's spending limit.

Fiscal Effect

Based on budget actions taken in 2005 and the recent strong revenue growth trend, the new spending limit is unlikely to constrain state expenditures in 2006–07—its first year of implementation. This is because the limit would likely exceed projected revenues and expenditures under current law.

Over the longer term, however, we believe that the spending limit could have significant impacts on annual state spending. This is because of the way in which the new spending limit would interact with changes in the economy and state revenues over time. California's revenues are highly sensitive to economic changes. That is, they tend to grow fast during the upside of business cycles when the economy is expanding, and slow—or fall—when the economy is on the downside of business cycles. As a result, the new spending limit—which is based on a rolling average of past revenue growth—would grow more *slowly* than actual revenues when the economy is accelerating, and grow *faster* than actual revenues when the economy is in recession. This is illustrated in Figure 3, which shows the relationship between annual revenues and the proposed spending limit during periods of strong and weak revenues.

The *net* impact of this measure on expenditures over time would depend on whether the state were able to "set aside" enough reserve funds during revenue expansions to maintain spending during periods of revenue softness.

- If it *were* able to set aside sufficient funds, the main impact of the spending limit would be to *smooth out* spending over time—restraining spending during economic expansions and permitting additional spending (supported from its reserves) during revenue downturns. In terms of Figure 3, this means that enough reserves would need to be set aside during the "excess revenues" period to maintain spending at the limit during the "low revenues" period.
- However, if the state *were not* able to accumulate large reserves, the limit would likely result in *less* spending over time. This is because the state would not have enough reserves available to cushion the decline in revenues during bad times. When this occurred, the reduced level of actual spending during periods of low revenues would then become the new, lower, "starting point" from which the next year's spending limit is calculated. This could cause the spending limit to ratchet down over time.

Effects on Ability to Raise Taxes. The impact of the limit on the state's ability to raise taxes to fund spending would depend on the specific situation:

- The state *would* be able to raise taxes or fees and immediately use the proceeds during periods of revenue weakness, when total receipts would likely be below the spending limit.
- The state *would not*, however, be able to raise revenues and *immediately* use the proceeds if spending was already at the limit. It would, however, *eventually* be able to use new tax proceeds as the impact of the tax increase worked its way into the new spending limit's adjustment factors over several years.

The latter situation would be relevant if the state were considering tax or fee increases either (1) to support new or expanded services or (2) when the state was attempting to eliminate an *ongoing* budget shortfall.

Over time, we believe the operation of this limit would likely reduce state expenditures relative to current law.

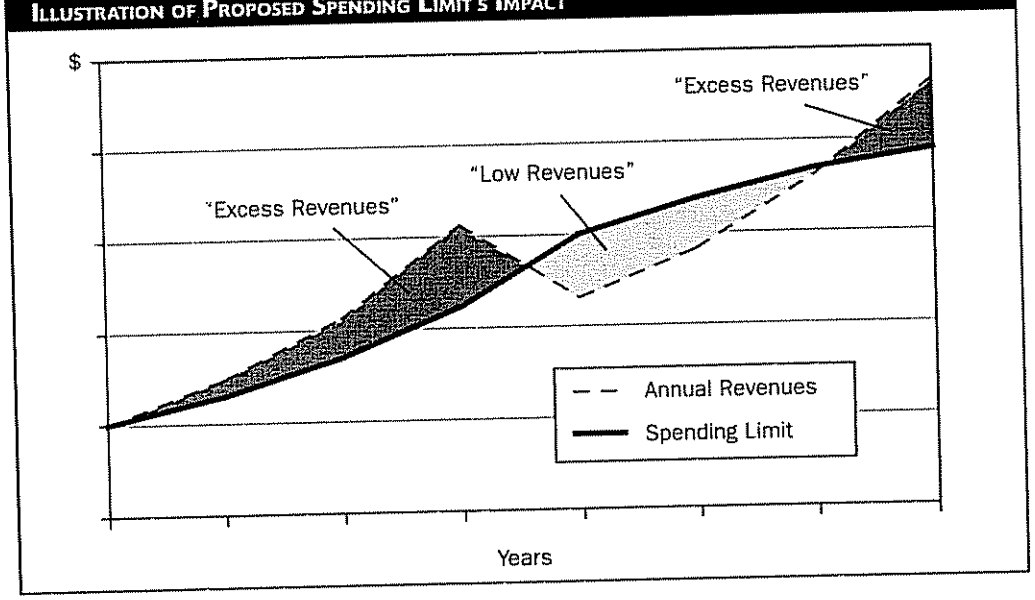
Expanded Powers for Governor

Current Law

Basic Provisions. The State Constitution requires that the Governor propose a budget by January 10 for the next fiscal year (which begins each July 1), and that the

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

FIGURE 3
ILLUSTRATION OF PROPOSED SPENDING LIMIT'S IMPACT



Legislature pass a budget by June 15. The Governor may then either sign or veto the resulting budget bill. The Governor may also reduce spending in most areas of the budget before signing the measure. However, this line item veto authority cannot be applied to programs where expenditures are governed by separate laws. The vetoes can also be overridden by a two-thirds vote of each house of the Legislature. Once the budget is signed, the Governor may not unilaterally reduce program funding.

Balanced Budget Requirements. Proposition 58 (approved by the voters in March 2004) requires that budgets passed by the Legislature and ultimately signed into law be balanced. This means that expenditures cannot exceed available revenues.

Late Budgets. When a fiscal year begins without a state budget, most expenses do not have authorization to continue. However, a number of court decisions and legal interpretations of the Constitution have identified certain types of payments that may continue to be made when a state budget has not been enacted. Thus, when there is not a state budget, payments continue for: a portion of state employees' pay; principal and interest payments on bonds; and various other expenditures (such as general purpose funds for K–12 schools) specifically authorized by state law or federal requirements.

Midyear Adjustments. Under Proposition 58, after a budget is signed into law but falls out of balance, the Governor may declare a fiscal emergency and call the Legislature into special session to consider proposals to deal with the fiscal imbalance. If the Legislature fails to pass and send to the Governor legislation to address the budget problem within 45 days after being called into special session, it is prohibited from acting on other bills or adjourning in joint recess.

PROPOSAL

This measure makes changes relating to late budgets and grants expanded powers to the Governor.

Late Budgets. If a budget is not enacted prior to the beginning of a new fiscal year, this measure requires that the spending levels authorized in the prior-year's budget act remain in effect until a new budget is enacted. Thus, funding would continue for all state programs that had received budget act appropriations in the prior year.

Fiscal Emergency. The measure grants the Governor new powers to (1) declare a fiscal emergency based on his or her administration's fiscal estimates, and (2) unilaterally reduce spending when an agreement cannot be reached on how to address the emergency.

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ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Specifically, the measure permits the Governor to issue a proclamation of a fiscal emergency when his or her administration finds either of the following two conditions:

- General Fund revenues have fallen by at least 1.5 percent below the administration's estimates.
- The balance of the state's reserve fund will decline by more than one-half between the beginning and the end of the fiscal year.

Once the emergency is declared by the Governor, the Legislature would be called into special session and then have 45 days (30 days in the case of a late budget) to enact legislation which addresses the shortfall. If such legislation is not enacted, the measure grants the Governor new powers to reduce state spending (with the exception of the items discussed below)—at his or her discretion—to eliminate the shortfall. The Legislature could not override these reductions.

Application of Reductions. The reductions may apply to *all* General Fund spending except for (1) expenditures necessary to comply with federal laws and regulations, (2) appropriations where the reduction would violate contracts to which the state is already a party, and (3) payment of principal and interest that is due on outstanding debt. Any General Fund spending related to contracts, collective bargaining agreements, or entitlements for which payment obligations arise after the effective date of this measure would be subject to these reductions.

Impact on Entitlement Spending. A significant portion of state General Fund spending is for entitlements. These are programs where individuals who meet specific eligibility criteria—involving, for example, age, income levels, or certain disabilities—have a right to receive the service. Major entitlements include, for example, various health and social services programs for low-income individuals. Most of these programs are administered by local agencies.

This measure gives the Governor the authority to reduce the amount of money available to fund an entitlement program. However, it does not give the Governor authority to modify specific laws that govern, for example, who is eligible to receive the service, the amount of a grant, or the scope of services provided under the program. Absent changes to these underlying laws by the Legislature, it would appear that the entitlement programs would continue to be administered in accordance with the laws that were in effect at the time of the Governor's reductions. When the funding remaining after the reductions was exhausted, the state would no longer have the obligation to fund the entitlement for the remainder of the fiscal year.

Fiscal Effect

This measure would grant new authority to the Governor to make reductions in almost all state spending. The fiscal effect of this change in individual years would depend on budget-related priorities of Governors and Legislatures. Over time, however, this grant of authority to the Governor to reduce spending would likely result in less state spending relative to current law. It could also result in a different mix of expenditures. That is, some programs' share of total spending would rise and others would fall relative to current law.

Effect on Local Governments. California counties administer most state health and social services entitlement programs. Also, counties fund other health and social services programs for low-income people who do not qualify for such state services. If the Governor reduced state funding for entitlement programs, some costs to pay for certain programs could shift to counties and there could be increased demand for locally funded health care and social services programs. The Governor also could reduce other state funding provided to local governments.

SCHOOL FUNDING CHANGES

Current Law

Proposition 98 is a measure passed by the voters in 1988 which established in the State Constitution a "minimum funding guarantee" for K–12 schools and community colleges (K–14 education). The intent of Proposition 98 is for K–14 funding to grow with student attendance and the state economy. California currently devotes about $50 billion in Proposition 98 funds to K–14 education annually. Of this total, about $37 billion is from the state's General Fund, and the other $13 billion is from local property tax revenues. Each year, the minimum guarantee is calculated based on a set of funding formulas. Under the main funding formula (referred to as "Test 2"), the guarantee increases each year roughly in line with school attendance and the state's economy. Figure 4 summarizes how Proposition 98 works and how this measure would change it.

Proposition 98 also has an alternative—and less generous—funding formula (called "Test 3") that generally takes effect when the state is experiencing slow growth or declines in its revenues. Funding

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

FIGURE 4

HOW THE MEASURE WOULD CHANGE SCHOOL SPENDING GUARANTEE FOR K–12 AND COMMUNITY COLLEGES

How Current Guarantee Works

- ✓ ***Proposition 98 Minimum Guarantee.*** Is based on the operation of three formulas ("tests"). The operative test depends on how the economy and General Fund revenues grow from year to year.
  - ***Test 1—Share of General Fund.*** Provides 39 percent of General Fund revenues. This test has not been operative since 1988–89.
  - ***Test 2—Growth in Per Capita Personal Income.*** Increases prior-year funding by growth in attendance and per capita personal income. This test is generally operative in years with normal-to-strong General Fund revenue growth.
  - ***Test 3—Growth in General Fund Revenues.*** Increases prior-year funding by growth in attendance and per capita General Fund revenues. Generally, this test is operative when General Fund revenues fall or grow slowly.
- ✓ ***Suspension of Proposition 98.*** This can occur through the enactment of legislation passed with a two-thirds vote of each house of the Legislature, and funding can be set at any level.
- ✓ ***Long-Term Target Funding Level.*** This would be the K–14 education funding level if it were always funded according to the provisions of Test 2. Whenever Proposition 98 funding falls below that year's Test 2 level, either because of suspension of the guarantee or the operation of Test 3, the Test 2 level is "tracked" and serves as a target level to which K–14 education funding will be restored when revenues improve.
- ✓ ***Maintenance Factor.*** This is created whenever actual funding falls below the Test 2 level. The maintenance factor is equal to the difference between actual funding and the long-term target amount. Currently, the K–14 funding level is $3.8 billion less than the long-term target funding level—that is, the current outstanding maintenance factor is $3.8 billion.
- ✓ ***Restoration of Maintenance Factor.*** This occurs when school funding rises back up toward the long-term target funding level. Restoration can occur either through a formula that requires higher K–14 education funding in years with strong General Fund revenue growth, or through legislative appropriations above the minimum guarantee.

What This Measure Does

- ✓ ***Eliminates Future Operation of Test 3.*** In low-revenue years, the Proposition 98 minimum guarantee would no longer automatically fall below the Test 2 level.
- ✓ ***Eliminates Future Creation of Maintenance Factor.*** If in any given year K–14 education was funded at a level less than that required by Test 2 (through suspension or Governor's reductions), there would no longer be a future obligation to restore that funding shortfall to the long-term target. These reductions would permanently "ratchet down" the Proposition 98 minimum guarantee.
- ✓ ***Converts Outstanding Maintenance Factor to One-Time Obligation.*** The measure converts the outstanding maintenance factor (estimated to be $3.8 billion) to a *one-time* obligation. Payments to fulfill this obligation would be made over the next 15 years. These payments would *not* raise the future Proposition 98 minimum guarantee (in contrast to existing law).
- ✓ ***Counts Future Appropriations Above the Minimum Guarantee as One-Time Payments.*** Spending above the minimum guarantee would not raise the base from which future guarantees are calculated.

for schools also can be reduced directly through a two-thirds vote of the Legislature. This is referred to as "suspension" of the guarantee. When Test 3 or suspension occurs, the state generally provides *less* in K–14 funding. The state is required to keep track of this funding gap, which is referred to as the "maintenance factor." Under current law, the state would end the 2005–06 fiscal year with a $3.8 billion maintenance factor created in prior years.

As state revenues improve, Proposition 98 requires the state to spend more on schools to catch up with its long-term target funding level by making

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ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

maintenance factor payments. When this occurs, the maintenance factor is said to be "restored." These restorations become part of the base for the next year's Proposition 98 calculation.

The formulas allowing for less generous K–14 funding during weak revenue periods (Test 3) and more generous funding during subsequent strong revenue periods (maintenance factor restoration) were added by Proposition 111, which was approved by the voters in 1990. These modifications to the original version of Proposition 98 were made to allow the guarantee to automatically slow down during "bad" economic times and rise again during "good" economic times.

Proposal

Test 3 and Maintenance Factor Eliminated. This measure eliminates Test 3 and maintenance factor, undoing the changes made by Proposition 111. Thus, the Constitution would no longer allow for automatic reductions in the minimum funding guarantee in difficult times nor would it automatically restore funding in good times. The Legislature would retain the authority to suspend Proposition 98; however, the nature of suspension would change. Since the maintenance factor would no longer exist, a suspension would result in a permanent downward adjustment to the minimum guarantee. Similarly, if the Governor unilaterally reduced Proposition 98 funding during a fiscal emergency, these reductions would also permanently lower the minimum guarantee.

Outstanding Maintenance Factor Converted to One-Time Obligation. The measure also converts the outstanding maintenance factor (estimated to be $3.8 billion) to a *one-time* obligation. Payments to fulfill this obligation would be made over the next 15 years. These payments would not raise the future Proposition 98 minimum guarantee (in contrast to existing law).

Future Spending Above the Minimum Guarantee Would Not Permanently Raise the Guarantee. Under current law, if the Governor and Legislature spend more money on K–14 education than is required by the minimum guarantee in a given year, the higher spending level generally becomes the "base" from which the next year's minimum funding guarantee is calculated. In this regard, a higher-than-required appropriation in one year typically raises the K–14 education minimum funding levels in subsequent years. Under this measure, future spending above the guarantee would be counted as *one-time* funding and would no longer raise future Proposition 98 minimum guarantee amounts.

Outstanding Settle-Up Obligations Would Be Paid Within 15 Years. The estimate of the minimum Proposition 98 funding guarantee for a particular fiscal year will usually change after the budget's enactment. If these changes result in a higher guarantee calculation, the difference between the guarantee and the actual level of appropriations becomes an additional K–14 education expense. This is referred to as "settle up." Existing settle-up obligations for past fiscal years currently total over $1 billion. Under current statutes, these will be paid at roughly $150 million per year beginning in 2006–07. This measure would require that these settle-up obligations be fully paid within 15 years.

Fiscal Effect

Given the uncertainty about future economic growth and budgetary circumstances, it is not possible to predict how the measure's changes would affect actual state spending for K–14 education and other programs. In general, the elimination of Test 3 and future maintenance factors means that year-to-year changes in the minimum guarantee would be less volatile than in the past—absent a suspension or a reduction by the Governor.

Decreases Minimum Guarantee Over Long Term. Over time, however, the net impact of the Proposition 98 changes and related changes in the measure would be to *lower* the minimum guarantee for K–14 education, as discussed below:

- Since K–14 education accounts for almost 45 percent of the state's General Fund budget, it is likely that policymakers would need to consider reductions in this area whenever the budget fell significantly out of balance. Whenever such spending was reduced—either through suspension or through Governor's reductions—the state would no longer be required to restore that reduction in the minimum funding guarantee in subsequent years.
- The provision making future appropriations over the minimum guarantee one-time in nature would also hold down the minimum guarantee relative to current law. For example, if this provision applied to 2005–06, it would convert an estimated $740 million in appropriations above the guarantee in the 2005–06 budget to one-time spending. This would lower the minimum guarantee for 2006–07 by a similar amount compared to current law.
- By converting the $3.8 billion outstanding maintenance factor to a one-time obligation, the measure eliminates the requirement for $3.8 billion to be restored into the annual base funding over time.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Combined, these changes would result in a lower minimum guarantee over time compared to current law.

Unknown Impact on K–14 Spending. A lower guarantee, however, *does not* mean that *actual* spending for schools would necessarily be lower. Policymakers would still be free to spend more than required by the minimum guarantee in any given year. Since spending above the guarantee for K–14 education would no longer permanently ratchet up the guarantee, future Legislatures and Governors might be more likely to spend above the minimum guarantee in a given year. Overall, the measure's Proposition 98-related changes would result in the annual budgets for K–14 education being more subject to annual funding decisions by state policymakers and less affected by the minimum guarantee.

Interactions with Other Provisions of the Measure. While the Proposition 98-related changes, by themselves, would not necessarily reduce K–14 education spending, other provisions of the measure might have that effect. To the extent, for example, that the measure constrains overall spending, budget reductions resulting from the spending limit or Governor's new authority could apply to schools.

OTHER CHANGES

PROPOSITION 42 TRANSFERS

Current Law. In 2002, the voters approved Proposition 42. This measure requires that sales taxes on motor vehicle fuel be transferred from the General Fund to a special fund for transportation. This special fund, called the Transportation Investment Fund (TIF), supports capital improvements and repairs of highways, roads, and public transit.

Proposition 42 includes a provision allowing for its suspension when the Governor finds (and the Legislature concurs) that the transfer will have a significant negative fiscal effect on General Fund programs. To help address the state's major budget shortfalls, the Governor and Legislature partially suspended the Proposition 42 transfer in 2003–04 ($868 million) and fully suspended the transfer in 2004–05 ($1.2 billion). Legislation passed with the 2003–04 and 2004–05 budgets designated the suspensions as "loans" from the TIF, to be repaid by the General Fund in 2007–08 and 2008–09.

Proposal. This measure prohibits the suspension of Proposition 42 transfers after 2006–07. The total amount of transfers that were suspended through June 30, 2007, would be paid within 15 years, at an annual rate of no less than one-fifteenth of the cumulative amount owed. The measure also permits the Legislature to authorize the issuance of bonds by the state or local agencies that are secured by the anticipated repayments of suspended Proposition 42 transfers.

Fiscal Effect. The inability to suspend Proposition 42 would result in a more stable funding stream for transportation.

LOANS FROM SPECIAL FUNDS

Current Law. In addition to the Proposition 42 loans discussed above, the Governor and Legislature have borrowed available balances from other special funds in the past to cover General Fund shortfalls. The amount of these loans outstanding at the conclusion of 2005–06 is expected to be roughly $1 billion. Some of the loans have specified repayment dates. In other cases, budget language requires that the loans be repaid when the funds are needed to carry out the operations of the particular special fund.

Proposal. Under this measure, such loans would be prohibited beginning in 2006–07 (except for short-term cash-flow borrowing purposes). Outstanding loans from special funds as of July 1, 2006, would be repaid within 15 years.

Fiscal Effect. Taken together, these provisions would result in more stable funding for some special fund programs.

PAYMENT OF MANDATE CLAIMS

The State Constitution requires the state to pay local governments for new or expanded programs which it imposes on local governments. In past years, the Governor and Legislature have deferred payments for mandate claims filed by school and community college districts and noneducation local governments (counties, cities, and special districts). Current law requires the state to pay within fifteen years any unpaid noneducation mandate claims incurred before 2004–05. There is no specific time frame for payment of unpaid education claims. This measure (1) shortens to five years the period in which the state must pay overdue noneducation mandate claims and (2) sets a 15-year deadline on payment of overdue education mandate claims. The measure also states that Proposition 98 funds allocated to schools "shall first be expended . . . to pay the costs for state mandates incurred during that year." This would change the state's current practice of providing specific funding to reimburse each school and community college district for its state-mandated activities.

Fiscal Effect. These provisions would have the effect of increasing state costs over the next five years with a comparable reduction over the subsequent ten years.

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PROPOSITION 77

REDISTRICTING. INITIATIVE CONSTITUTIONAL AMENDMENT.

Official Title and Summary

Prepared by the Attorney General

REDISTRICTING. INITIATIVE CONSTITUTIONAL AMENDMENT.

- Amends process for redistricting California's Senate, Assembly, Congressional and Board of Equalization districts.
- Requires panel of three retired judges, selected by legislative leaders, to adopt new redistricting plan if measure passes and after each national census.
- Panel must consider legislative, public comments/hold public hearings.
- Redistricting plan effective when adopted by panel and filed with Secretary of State; governs next statewide primary/general elections even if voters reject plan.
- If voters reject redistricting plan, process repeats, but officials elected under rejected plan serve full terms.
- Allows 45 days to seek judicial review of adopted redistricting plan.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- One-time costs for a redistricting plan. State costs totaling no more than $1.5 million and county costs in the range of $1 million.
- Potential reduction in costs for each redistricting effort after 2010, but net impact would depend on decisions by voters.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Every ten years, the federal census counts the number of people living in California. The California Constitution requires the Legislature after each census to adjust the boundaries of the districts used to elect public officials. This process is called "redistricting" (or sometimes "reapportionment"). The primary purpose of redistricting is to establish districts which are "reasonably equal" in population. Redistricting affects districts for the state Legislature (Assembly and Senate), Board of Equalization (BOE), and the U.S. House of Representatives.

Typically, redistricting plans are included in legislation and become law after passage of the bill by the Legislature and signature by the Governor. In the past, when the Legislature and Governor have been unable to agree on redistricting plans, the California Supreme Court oversaw the redistricting.

PROPOSAL

This measure amends the California Constitution to change the redistricting process for the state Legislature, BOE, and California members of the U.S. House of Representatives.

Panel of Retired Judges. This measure requires that a three-member panel of retired federal and/or state judges ("special masters") develop redistricting plans. The measure requires that the judges meet a number of criteria, including that they have never held partisan political office. (The nearby box provides more detail on the selection process for the special masters.)

Requirements of District Boundaries. The measure adds new requirements regarding the drawing of district boundaries. Among these requirements are:

- For the Legislature and BOE, population differences among districts cannot exceed 1 percent.
- Senate districts must be comprised of two adjacent Assembly districts, and BOE districts must be comprised of ten adjacent Senate districts.
- The plan must minimize the splitting of counties and cities into multiple districts.

In addition, when drawing boundaries, the panel could not consider information related to political party affiliations and other specified matters.

Schedule. A panel would be required to develop a redistricting plan for use at the next primary and general elections following the measure's approval and then following each future federal census.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Approval Process. In developing a plan, the panel would have to hold public hearings and could receive suggested plans from the public and the Legislature. Once the panel unanimously approves a redistricting plan, the plan would be used for the next primary and general elections. The Secretary of State would place the plan on the general election ballot for the voters to consider. If the voters approve the plan, it would be used until the next redistricting is required. If the voters reject the plan, another panel would be appointed to prepare a new plan for the next primary and general elections.

Funding. The measure specifies that the Legislature must make funding available from the Legislature's budget (which is limited under the State Constitution) to support the work of the panel. This could include employment of legal and other experts in the field of redistricting and computer technology. Funding for the panel would be limited to a maximum of one-half of the amount spent by the Legislature on redistricting in 2001 (adjusted for inflation beginning after the 2010 federal census). For the first redistricting plan under the measure (to be developed for use at the next primary and general elections following the measure's approval), the funding would be provided from the state General Fund.

MAJOR STEPS TO SELECT REDISTRICTING PANEL UNDER PROPOSITION 77

1. Judicial Council (an administrative body of the court system) collects list of retired judges willing to serve on a panel. The judges must not have:
   - Held partisan political office.
   - Changed their party affiliation since their judicial appointment.
   - Received income over the past year from specified political sources.
2. Judicial Council randomly selects a pool of 24 judges from the list of volunteers. The two largest political parties must have equal representation.
3. The four legislative leaders (two each from the majority and minority parties) nominate a total of 12 judges from the pool. The leaders each nominate three judges with party affiliations different than their own. Each leader is then able to eliminate one of the nominated judges.
4. From the nominated judges remaining on the list, three judges are selected at random to serve as the panel. Each of the two largest political parties must have at least one representative.
5. The selected judges pledge, in writing, to not run for offices affected by the districts they draw or accept public jobs (other than judicial or teaching) for the next five years.

FISCAL EFFECTS

Panel Allowable Costs. The Legislature spent about $3 million in 2001 on redistricting. This measure would limit panel costs for future redistricting efforts to half of this amount, adjusted for inflation. Therefore, the maximum amount allowable under the measure for each future panel would be about $1.5 million.

One-Time Redistricting Costs. Under existing law, the next redistricting plan would not be developed until after the 2010 federal census. The measure, however, requires that a redistricting plan be developed for use at the next primary election following the measure's approval. This additional redistricting plan would result in one-time state costs, which would total no more than $1.5 million for the panel's work. In addition, counties would experience some added one-time costs to implement the new district boundaries. These costs could be in the range of $1 million.

Impact on Future Redistricting Costs. The preparation of future redistricting plans (after 2010) under the measure would be on the same schedule as existing law. Due to the measure's limit on a panel's redistricting costs, there could be a reduction in the total amount the state spent for each redistricting effort. Any such savings would be available for other legislative expenses under the existing cap. If, however, voters rejected any redistricting plan, there would be some additional state and county costs for a new plan to be developed and implemented. Thus, the net impact on future redistricting costs in any decade would depend on decisions by voters.

Election Costs. Because the measure requires the redistricting plans to be approved by voters, it would result in costs to the state and counties each time a plan was placed on the ballot. These costs primarily would be related to preparing and mailing election-related materials. Since the approval of the plans could be consolidated with existing elections, the increased costs of the measure would probably be minor.

For text of Proposition 77 see page 64.

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PROPOSITION 78

DISCOUNTS ON PRESCRIPTION DRUGS. INITIATIVE STATUTE.

Official Title and Summary

Prepared by the Attorney General

DISCOUNTS ON PRESCRIPTION DRUGS. INITIATIVE STATUTE.

- Establishes discount prescription drug program, overseen by California Department of Health Services
- Enables certain low- and moderate-income California residents to purchase prescription drugs at reduced prices.
- Authorizes Department: to contract with participating pharmacies to sell prescription drugs at agreed-upon discounts negotiated in advance; to negotiate rebate agreements with participating drug manufacturers.
- Imposes $15 annual application fee.
- Creates state fund for deposit of drug manufacturers' rebate payments.
- Requires Department's prompt determination of residents' eligibility, based on listed qualifications.
- Permits outreach programs to increase public awareness.
- Allows program to be terminated under specified conditions

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- One-time and ongoing state costs, potentially in the millions to low tens of millions of dollars annually, for administration and outreach activities for a new drug discount program. A significant share of these costs would probably be borne by the state General Fund.
- State costs, potentially in the low tens of millions of dollars, to cover the funding gap between when drug rebates are collected by the state and when the state pays funds to pharmacies for drug discounts provided to consumers. Any such costs not covered through advance rebate payments from drug makers would be borne by the state General Fund.
- Unknown potentially significant savings for state and county health programs due to the availability of drug discounts.
- Potential unknown effects on state revenues and expenditures from changes in prices and quantities of drugs sold in California.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Prescription Drug Coverage. Currently, several state and federal programs provide prescription drug coverage to eligible individuals. The state's Medi-Cal Program, which is administered by the Department of Health Services (DHS), provides prescription drugs for low-income children and adults. The state's Managed Risk Medical Insurance Board administers the Healthy Families Program, which provides prescription drugs for children in low-income and moderate-income families who do not qualify for Medi-Cal.

Beginning January 2006, the federal government will provide prescription drug coverage to persons enrolled in Medicare, a federal health program for elderly and disabled persons. (This would include some persons enrolled in Medi-Cal who are also enrolled in Medicare.) Various other programs funded with state or federal funds also provide assistance to help pay part or all of the cost of drugs for specified individuals.

In addition, many Californians receive coverage for prescription drugs through private insurance that is purchased by individuals or provided by their employer or the employer of a member of their family.

Drug Discount Programs. California, a number of other states, and private associations and drug makers have established drug discount programs. These programs help certain consumers, including individuals who are not eligible for state and federal programs that provide drug coverage, purchase prescription drugs at reduced prices. Current California law, for example, requires retail pharmacies to sell prescription drugs at a discount to elderly and disabled persons enrolled in Medicare as a condition of a pharmacy's participation in the Medi-Cal Program.

PROPOSAL

This proposition creates a new state drug discount program to reduce the costs that certain residents of the state would pay for prescription drugs purchased at pharmacies. The major components of the measure are outlined below.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Discount Card Program. Under the new drug discount program, eligible persons could obtain a card that would qualify them for discounts on their drug purchases at pharmacies. The program would be open to California residents in families with an income at or below 300 percent of the federal poverty level—up to almost $29,000 a year for an individual or about $58,000 for a family of four. Persons enrolled in Medicare could obtain discount cards for drugs not covered by Medicare. Persons could not participate in the new drug discount program if they receive their drug coverage from private health insurance, from the Medi-Cal or Healthy Families Programs, or from other public programs supported with state or federal funding. Persons generally could not obtain a drug discount card for at least three months after leaving these private or public sources of drug coverage.

The new drug discount program would be administered by DHS, which could contract with a private vendor for assistance. Participants would enroll in the program by paying a $15 fee, and would pay an annual renewal fee of the same amount. Eligible persons could enroll or reenroll in the program at any pharmacy, doctor's office, or clinic, which chose to participate in the drug discount program. Applications and renewals could also be handled through an Internet Web site or through a telephone call center. The DHS would review applications and mail the drug discount cards to eligible persons, usually within four days.

The state would seek two types of discounts in order to obtain lower prices for persons with the new drug discount cards. First, pharmacies that voluntarily chose to participate in the program would agree to sell prescription drugs to cardholders at an agreed-upon discount negotiated in advance with the state. In addition, pharmacies would further discount the price to reflect any rebates the state negotiated with drug makers. (The pharmacies would subsequently be reimbursed for this second type of discount with rebates collected by the state from drug makers.)

The DHS could end the drug discount program if it found there were insufficient discounts to make the program work, if too few persons enrolled in the program, or if DHS could not find a vendor to help run the program.

Private Drug Discount Programs. The measure directs DHS to implement agreements with drug discount programs operated by drug makers and other private groups so that the discount cards would automatically provide consumers with access to the best discount available to them for a particular drug purchase.

Outreach Efforts. The measure directs DHS to conduct an outreach program to inform state residents about the new drug discount program.

Related Provisions in Proposition 79. Proposition 79 on this ballot also establishes a new state drug discount program. The key differences between Proposition 78 and Proposition 79 are shown in Figure 1.

The State Constitution provides that if a particular provision of a proposition that has been approved by the voters is in conflict with a particular provision of another proposition approved by the voters, only the provision in the measure with the higher number of yes votes would take effect. Proposition 78 specifies that its provisions would go into effect in their entirety, and that none of the provisions of a competing measure such as Proposition 79 would take effect, if Proposition 78 received the higher number of yes votes.

FISCAL EFFECTS

This measure could have a number of fiscal effects on state and local government. We discuss several major factors below that could result in costs or savings.

State Costs for Administration and Outreach Activities. The DHS would incur significant startup costs, as well as ongoing costs, for administrative and outreach activities to implement the new drug discount program created by this proposition.

This would include administrative costs to:

- Establish the new program, including any new information technology systems that would be needed for its operation.
- Operate the Internet Web site and the call center to receive applications for drug discount cards.
- Process applications and renewals of drug discount cards.
- Negotiate and collect rebates from drug manufacturers and make advance rebate payments to pharmacies.
- Coordinate the state's drug discount program with other private drug discount programs.

The state could also incur additional costs for the proposed outreach activities, potentially including costs for radio or television advertising, written materials, and other promotional efforts to make consumers aware of the drug discount program.

In the aggregate, these administrative and outreach costs would probably range from the millions to low tens of millions of dollars annually. The exact fiscal effect would depend primarily on the extent of outreach efforts and the number of consumers who chose to participate in the drug discount program.

For text of Proposition 78 see page 66

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ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

FIGURE 1
KEY DIFFERENCES BETWEEN PROPOSITIONS 78 AND 79

	Proposition 78	Proposition 79
General eligibility requirements	• California residents in families with an income at or below 300 percent of the federal poverty level. (About $29,000 annually for an individual and $58,000 for a family of four.) • No such provision.	• California residents in families with an income at or below 400 percent of the federal poverty level. (About $38,000 annually for an individual and $77,000 for a family of four.) • Also, persons in families with medical expenses at or above 5 percent of their family's income.
Persons excluded from coverage	• Persons with outpatient prescription drug coverage through Medi-Cal, Healthy Families, a third-party payer, or a health plan or drug discount program supported with state or federal funds (except Medicare beneficiaries). • Certain persons with drug coverage, during the three-month period prior to the month the person applied for a drug discount card.	• Persons with outpatient prescription drug coverage through Medi-Cal or Healthy Families (except Medicare beneficiaries). • No such provision.
Application and renewal fee	• $15 per year.	• $10 per year.
Method of obtaining rebates from drug makers	• Negotiated with drug makers. • No such provision.	• Negotiated with drug makers. • Subject to federal approval, links new drug discount program to Medi-Cal for the purpose of obtaining rebates on drugs.
Assistance to business and labor organizations	• No such provision.	• Establishes drug discount program to assist certain business and labor entities.
Prescription Drug Advisory Board	• No such provision.	• Creates new nine-member panel to review the access to and pricing of drugs.
Lawsuits over drug profiteering law	• No such provision.	• Changes state law to make it a civil violation for a drug maker to engage in profiteering from the sale of drugs.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

These costs could be partly offset by (1) any funds available for this purpose from a new special fund created by this measure, (2) any private donations received for this purpose, and (3) a portion of the enrollment fees collected for the program. The amount of donations that the state would receive on an ongoing basis for outreach activities is unknown. The amount of available special funds or the fee revenues that would be collected by the state is also unknown. In view of the above, it appears likely that a significant share of the cost of this program would be borne by the General Fund.

Costs for "Float." This measure requires the state to reimburse pharmacies for part of the amount that they discounted their drugs. This reimbursement reflects discounts for which the state receives rebates from drug makers.

The reimbursement to pharmacies must be made within two weeks after their claims are filed with the state. However, drug makers are required by the measure to pay rebates to the state on at least a quarterly basis. This means that the state could, in many cases, pay out rebates to pharmacies before it actually collects the rebate funds from drug makers. Moreover, any disputes that arise over the actual amounts owed for rebates could further slow payments of rebate funds by drug makers to the state.

This recurring gap in funding between when rebate money is collected by the state and when the state has to pay pharmacies is commonly referred to as float. The cost of the float is unknown, but could amount to the low tens of millions of dollars, depending on the level of participation in the program. Float costs would occur mainly in the early years of implementing this new program. After the program has been fully implemented, rebate funds collected from drug makers should be largely sufficient to reimburse pharmacies.

This measure permits the state to enter into agreements with drug makers to collect some rebate funds in advance. The amount of funding that the state would receive through such advance payments is unknown. Any float costs that exceeded these advance rebate payments would be borne by the state General Fund.

Potential Savings for State and County Health Programs. The drug discount program established under this proposition could reduce costs to the state and counties for health programs.

Absent the discounts available under such a drug discount program, some lower-income individuals who lack drug coverage might forego the purchase of their prescribed drugs. Such individuals might eventually require hospitalization as a result of their untreated medical conditions, thereby adding to Medi-Cal Program costs. Other individuals might "spend down" their financial assets on expensive drug purchases absent such discounts and become eligible for Medi-Cal. The exact amount of savings to the Medi-Cal Program from a drug discount program is unknown, but could be significant if the program enrolled a large number of consumers.

Similarly, the availability of a drug discount program could reduce costs for other state health programs. It could also do so for county indigent care by decreasing out-of-pocket drug expenses for low-income persons who require medications, thereby making them less likely to rely on county hospitals or clinics for assistance. The extent of these potential savings is unknown.

Other Fiscal Effects. This measure would affect both the prices and quantities of prescription drugs sold in California. In turn, this could affect taxable profits of drug makers and businesses that provide health care for their employees, as well as consumers' disposable income. These changes could affect state revenues. Changes in the prices and quantities of drugs sold could affect state expenditures as well. The net impact of these factors on state revenues and expenditures is unknown.

For text of Proposition 78 see page 66

PROPOSITION 79

PRESCRIPTION DRUG DISCOUNTS. STATE-NEGOTIATED REBATES. INITIATIVE STATUTE.

Official Title and Summary

Prepared by the Attorney General

PRESCRIPTION DRUG DISCOUNTS. STATE-NEGOTIATED REBATES. INITIATIVE STATUTE.

- Provides for prescription drug discounts to Californians who qualify based on income-related standards, to be funded through rebates from participating drug manufacturers negotiated by California Department of Health Services.
- Prohibits new Medi-Cal contracts with manufacturers not providing the Medicaid best price to this program, except for drugs without therapeutic equivalent.
- Rebates must be deposited in State Treasury fund, used only to reimburse pharmacies for discounts and to offset costs of administration.
- At least 95% of rebates must go to fund discounts.
- Establishes oversight board.
- Makes prescription drug profiteering, as described, unlawful.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- One-time and ongoing state costs, potentially in the low tens of millions of dollars annually, for administration and outreach activities for a new drug discount program. A significant share of these costs would probably be borne by the state General Fund.
- State costs, potentially in the low tens of millions of dollars, to cover the funding gap between when drug rebates are collected by the state and when the state pays funds to pharmacies for drug discounts provided to consumers. Any such costs not covered through advance rebate payments from drug makers would be borne by the state General Fund.
- Unknown potentially significant net costs or savings as a result of provisions linking state Medi-Cal rebate contracts and the new drug discount program.
- Unknown potentially significant savings for state and county health programs due to the availability of drug discounts.
- Unknown costs and revenues from the provisions regarding lawsuits over profiteering on drug sales.
- Potential unknown effects on state revenues and expenditures from changes in prices and quantities of drugs sold in California.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Prescription Drug Coverage. Currently, several state and federal programs provide prescription drug coverage to eligible individuals. The state's Medi-Cal Program, which is administered by the Department of Health Services (DHS), provides prescription drugs for low-income children and adults. The state's Managed Risk Medical Insurance Board administers the Healthy Families Program, which provides prescription drugs for children in low-income and moderate-income families who do not qualify for Medi-Cal.

Beginning January 2006, the federal government will provide prescription drug coverage to persons also enrolled in Medicare, a federal health program for elderly and disabled persons. (This would include

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

some persons enrolled in Medi-Cal who are also enrolled in Medicare.) Various other programs funded with state or federal funds also provide assistance to help pay part or all of the cost of drugs for specified individuals.

In addition, many Californians receive coverage for prescription drugs through private insurance that is purchased by individuals or provided by their employer or the employer of a member of their family.

Drug Discounts for Individuals. California, a number of other states, and private associations and drug makers have established drug discount programs. These programs help certain consumers, including individuals who are not eligible for state and federal programs that provide drug coverage, purchase prescription drugs at reduced prices. Current California law, for example, requires retail pharmacies to sell prescription drugs at a discount to elderly and disabled persons enrolled in Medicare as a condition of a pharmacy's participation in the Medi-Cal Program.

Drug Rebates for Medi-Cal. Federal law requires that drug makers provide rebates on their drugs to state Medicaid programs, such as Medi-Cal, so that the net price paid would be lower than that paid by most private purchasers. Also, the state negotiates for additional rebates from drug makers in exchange for giving the drugs made by those companies preferred status in the Medi-Cal Program. Preferred status means that doctors may prescribe a particular drug without receiving advance approval from the state. The rebates received by the state help reduce its costs for drugs for persons enrolled in Medi-Cal.

Linking Medicaid to Other State Programs. Some states have sought to obtain greater discounts from drug makers on prescription drugs for other health programs, including drug discount programs, by linking them to their Medicaid Programs. This approach involves allowing drug makers' products to have preferred status in their Medicaid Program only if the drug maker provides discounts or rebates on drugs for their non-Medicaid Programs. A 2003 U.S. Supreme Court decision has been interpreted to mean that states may do this as long as their actions would further the goals of Medicaid, such as providing assistance to individuals who might otherwise end up on the Medicaid rolls, and as long as they seek and obtain prior federal approval for their actions.

PROPOSAL

This proposition creates a new state drug discount program to reduce the costs that certain residents of the state would pay for prescription drugs purchased at pharmacies. The major components of the measure are outlined below.

Discount Card Program. Under the new drug discount program, eligible persons could obtain a card that would qualify them for discounts on their drug purchases at pharmacies. The program would be open to California residents in families with an income at or below 400 percent of the federal poverty level—up to about $38,000 a year for an individual or about $77,000 for a family of four. Discount cards would also be available to some persons in families with higher incomes with medical expenses at or above 5 percent of their family's income. Persons enrolled in Medicare could obtain discount cards for drugs not covered by Medicare. Persons could not participate in the new drug discount program if they receive their drug coverage from the Medi-Cal or Healthy Families Programs.

The new drug discount program would be administered by DHS, which could contract with a private vendor for assistance. Participants would enroll in the program by paying a $10 fee, and would pay an annual renewal fee of the same amount. Eligible persons could enroll or reenroll in the program at any pharmacy, doctor's office, or clinic which chose to participate in the drug discount program. Applications and renewals could also be handled through an Internet Web site or through a telephone call center. The DHS would review applications and mail the drug discount cards to eligible persons, usually within four days.

The state would seek two types of discounts in order to obtain lower prices for persons with the new drug discount cards. First, pharmacies that voluntarily chose to participate in the program

For text of Proposition 79 see page 69.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

would agree to sell prescription drugs to cardholders at an agreed-upon discount negotiated in advance with the state. In addition, pharmacies would further discount the price to reflect any rebates the state negotiated with drug makers. (The pharmacies would subsequently be reimbursed for this second type of discount with rebates collected by the state from the drug makers.)

Linkage to Medi-Cal Program. The measure links this new drug discount program to the Medi-Cal Program for the purpose of obtaining reduced prices on drugs purchased with drug discount cards. Specifically, the measure states that DHS may not contract with a drug maker for the Medi-Cal Program if that drug maker does not sell its drugs at a reduced price to the new drug discount program. This includes contracts by which the state obtains rebates on drugs in exchange for giving those drugs preferred status in Medi-Cal. If a drug maker does not agree to such a contract for its drugs, its drugs may be subject to an existing requirement that a doctor receive prior approval from the state before such drugs are prescribed for a Medi-Cal patient. In addition, this measure provides that the names of drug makers and whether they entered into such contracts shall be released to the public.

The measure specifies that these requirements would be implemented consistent with federal law. It further specifies that these provisions would not apply to a drug if there were not another equivalent drug available. Also, the measure provides that a Medi-Cal beneficiary who has already been prescribed a drug would be allowed to continue to receive it without prior approval.

Private Drug Discount Programs. The measure directs DHS to implement agreements with drug discount programs operated by drug makers and other private groups so that the discount cards would automatically provide consumers with access to the best discount available to them for a particular drug purchase.

New State Advisory Board. The measure creates a new nine-member Prescription Drug Advisory Board to review the access that state residents have to prescription drugs as well as the pricing of those drugs, and to provide advice and regular reports on drug pricing issues to state officials.

Outreach Efforts. The measure directs DHS to conduct an outreach program to inform state residents about the new drug discount program. The outreach activities are to be coordinated with the Department of Aging, other state agencies, local agencies, and nonprofit organizations that serve residents who might be eligible for the program.

Assistance to Businesses and Labor Organizations. The measure authorizes DHS to establish a drug discount program to assist certain businesses and labor organizations that purchase health coverage for employees and their dependents. The DHS could help these organizations to reduce their drug costs by arranging for discounts on drug prices with pharmacies and seeking to negotiate rebates on drugs on behalf of employees and their dependents.

Profiteering From Drug Sales. Existing state law does not limit the prices or profits that can be earned on the sale of prescription drugs in California. This measure changes state law to make it a civil violation for drug makers and certain other specified parties to engage in profiteering from the sale of prescription drugs. The definition of profiteering includes demanding "an unconscionable price" for a drug or demanding "prices or terms that lead to any unjust and unreasonable profit." Profiteering on drugs would be subject to prosecution by the Attorney General or through a lawsuit filed by any person acting in the interests of itself, its members, or the general public. Violators could be penalized in the amount of $100,000 or triple the amount of damages, whichever was greater, plus legal costs.

Related Provisions in Proposition 78. Proposition 78 on this ballot also establishes a new state drug discount program. The key differences between Proposition 78 and Proposition 79 are shown in Figure 1.

The State Constitution provides that if a particular provision of a proposition that has been approved by the voters is in conflict with a particular provision of another proposition approved by the voters, only the provision in the measure with the higher number of yes votes would take effect. Proposition 78, another measure on the ballot, specifies that its provisions would go into effect in their entirety, and that none of the provisions of a competing measure such as

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

FIGURE 1

KEY DIFFERENCES BETWEEN PROPOSITIONS 78 AND 79

	Proposition 78	Proposition 79
General eligibility requirements	• California residents in families with an income at or below 300 percent of the federal poverty level. (About $29,000 annually for an individual and $58,000 for a family of four.) • No such provision.	• California residents in families with an income at or below 400 percent of the federal poverty level. (About $38,000 annually for an individual and $77,000 for a family of four.) • Also, persons in families with medical expenses at or above 5 percent of their family's income.
Persons excluded from coverage	• Persons with outpatient prescription drug coverage through Medi-Cal, Healthy Families, a third-party payer, or a health plan or drug discount program supported with state or federal funds (except Medicare beneficiaries). • Certain persons with drug coverage, during the three-month period prior to the month the person applied for a drug discount card.	• Persons with outpatient prescription drug coverage through Medi-Cal or Healthy Families (except Medicare beneficiaries). • No such provision.
Application and renewal fee	• $15 per year.	• $10 per year.
Method of obtaining rebates from drug makers	• Negotiated with drug makers. • No such provision.	• Negotiated with drug makers. • Subject to federal approval, links new drug discount program to Medi-Cal for the purpose of obtaining rebates on drugs.
Assistance to business and labor organizations	• No such provision.	• Establishes drug discount program to assist certain business and labor entities.
Prescription Drug Advisory Board	• No such provision.	• Creates new nine-member panel to review the access to and pricing of drugs.
Lawsuits over drug profiteering law	• No such provision.	• Changes state law to make it a civil violation for a drug maker to engage in profiteering from the sale of drugs.

For text of Proposition 79 see page 69

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Proposition 79 would take effect, if Proposition 78 received the higher number of yes votes.

FISCAL EFFECTS

This measure could have a number of fiscal effects on state and local government. We discuss several major factors below that could result in costs or savings.

State Costs for Administration and Outreach Activities. The DHS, the Department of Aging, and the newly created Prescription Drug Advisory Board would, in combination, incur significant startup costs, as well as ongoing costs, for administrative and outreach activities to implement the new drug discount program created by this proposition.

This could include administrative costs to:

- Establish the new program, including any new information technology systems that would be needed for its operation.
- Operate the Internet Web site and the call center to receive applications for drug discount cards.
- Process applications and renewals of drug discount cards.
- Negotiate and collect rebates from drug manufacturers and make advance rebate payments to pharmacies.
- Assist business and labor organizations in obtaining drug discounts.
- Coordinate the state's drug discount program with other private drug discount programs.

As noted earlier, this measure links its new drug discount program to Medi-Cal contracts that permit some drugs to be prescribed to Medi-Cal patients without prior approval by the state. To the extent that additional prior approvals of drugs are required for Medi-Cal patients as a result of these provisions, DHS would incur additional administrative costs to process these requests.

The state would also incur additional costs for the proposed outreach activities, potentially including costs for radio or television advertising, written materials, and other promotional efforts to make consumers aware of the drug discount program.

In the aggregate, these administrative and outreach costs—including costs for business and labor assistance as well as processing additional Medi-Cal requests for prior approval of drug prescriptions—would probably range in the low tens of millions of dollars annually. The exact fiscal effect would depend primarily on the extent of outreach efforts and the number of consumers who chose to participate in the drug discount program.

These state costs could be partly offset by (1) up to a 5 percent share of the rebates collected from drug makers, (2) any private donations received for the support of outreach efforts, and (3) a portion of the enrollment fees collected for the program. Our analysis indicates that the 5 percent share of rebate funding alone is unlikely to offset these state costs. The amount of donations that the state would receive on an ongoing basis for outreach activities is unknown. The amount of fee revenue that would be collected by the state is also unknown. In view of the above, it appears likely that a significant share of the cost of this program would be borne by the state General Fund.

Costs for "Float." This measure requires the state to reimburse pharmacies for part of the amount that they discounted their drugs. This reimbursement reflects discounts for which the state receives rebates from drug makers.

The reimbursement to pharmacies must be made within two weeks after their claims are filed with the state. However, drug makers are required by the measure to pay rebates to the state on at least a quarterly basis. This means that the state could, in many cases, pay out rebates to pharmacies before it actually collects the rebate funds from drug makers. Moreover, any disputes that arise over the actual amounts owed for rebates could further slow payments of rebate funds by drug makers to the state.

This recurring gap in funding between when rebate money is collected by the state and when the state has to pay pharmacies is commonly referred to as float. The cost of the float is unknown, but could amount to the low tens of millions of dollars, depending on the level of participation in the new drug discount program. Float costs would occur mainly in the early years of implementing this new program. After the program has been fully implemented, rebate funds collected from drug

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

makers should be largely sufficient to reimburse pharmacies.

This measure permits the state to enter into agreements with drug makers to collect rebate funds in advance. The amount of funding that the state would receive through such advance payments is unknown. Any float costs that exceeded these advance rebate payments would be borne by the state General Fund.

State Costs or Savings From Linking Drug Discount Programs to Medi-Cal. As noted earlier, this proposition states that DHS may not enter into a Medi-Cal contract with a drug maker that did not agree to provide discounts on the price of their drugs for the new drug discount program. This provision could result in additional costs and savings to the Medi-Cal Program depending upon future actions by the federal government, drug makers, or doctors. For example, this provision could result in the state receiving fewer drug rebates from drug makers for the Medi-Cal Program, thus resulting in costs. On the other hand, this provision could result in savings in cases in which the removal of a drug from preferred status resulted in fewer prescriptions of the drug and its replacement by a less costly medication. The net fiscal effect of this provision on the Medi-Cal Program is unknown but could be significant.

Potential Savings for State and County Health Programs. The drug discount program established under this proposition could reduce costs to the state and counties for health programs.

Absent the discounts available under such a drug discount program, some lower income individuals who lack drug coverage might forego the purchase of their prescribed drugs. Such individuals might eventually require hospitalization as a result of their untreated medical conditions, thereby adding to Medi-Cal Program costs. Other individuals might "spend down" their financial assets on expensive drug purchases absent such discounts and become eligible for Medi-Cal. The exact amount of savings to the Medi-Cal Program from a drug discount program is unknown, but could be significant if the program enrolled a large number of consumers.

Similarly, the availability of a drug discount program could reduce costs for other state health programs. It could also do so for county indigent care by decreasing out-of-pocket drug expenses for low-income persons who require medications, thereby making them less likely to rely on county hospitals or clinics for assistance. The extent of these potential savings is unknown.

State Costs and Revenues From Provision on Profiteering From Drug Sales. This measure would have an unknown fiscal impact on state support for local trial courts, depending primarily on whether the measure increases the overall level of court workload. The number of civil cases that might result from this measure is unknown. Also, the measure could result in some additional costs for the Attorney General to prosecute profiteering cases. These costs are estimated by the Department of Justice to be less than $1 million annually. However, these costs could be offset to the extent that the state collected revenues from civil penalties in cases where civil prosecutions were successful.

Other Fiscal Effects. This measure would affect both the prices and quantities of prescription drugs sold in California. In turn, this could affect the taxable profits of drug makers and businesses that provide health care for their employees, as well as consumers' disposable income. These changes could affect state revenues. Changes in the prices and quantities of drugs sold could affect state expenditures as well. The net impact of these factors on state revenues and expenditures is unknown.

For text of Proposition 79 see page 69.

PROPOSITION 80

ELECTRIC SERVICE PROVIDERS. REGULATION. INITIATIVE STATUTE.

Official Title and Summary

Prepared by the Attorney General

ELECTRIC SERVICE PROVIDERS. REGULATION. INITIATIVE STATUTE.

- Subjects electric service providers, as defined, to control and regulation by California Public Utilities Commission.
- Imposes restrictions on electricity customers' ability to switch from private utilities to other electric providers.
- Provides that registration by electric service providers with Commission constitutes providers' consent to regulation.
- Requires all retail electric sellers, instead of just private utilities, to increase renewable energy resource procurement by at least 1% each year, with 20% of retail sales procured from renewable energy by 2010, instead of current requirement of 2017.
- Imposes duties on Commission, Legislature and electrical providers.

SUMMARY OF LEGISLATIVE ANALYST'S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- Potential annual state administrative costs ranging from negligible up to around $4 million for regulatory activities of the California Public Utilities Commission, paid for by fee revenues.
- Unknown net impact on state and local government costs and revenues due to the measure's uncertain impact on retail electricity rates.

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

Provision of Electricity Service. Californians generally receive their electricity service from one of three types of providers: investor owned utilities (IOUs), local publicly owned electric utilities, and electric service providers (ESPs). Investor owned utilities have a defined geographic service area and are required by law to serve customers in that area. The three largest electricity IOUs in the state are Pacific Gas & Electric Company, Southern California Edison Company, and San Diego Gas & Electric Company. The California Public Utilities Commission (PUC) regulates the IOUs' rates and how electricity service is provided to their customers (commonly referred to as "terms of service"). (See the nearby text box for definitions of commonly used terms throughout this analysis.)

Publicly owned electric utilities are public entities that provide electric service to residents and businesses in their local area. Unlike IOUs, they are not regulated by the PUC. Major publicly owned electric utilities include the Los Angeles Department of Water and Power, the Sacramento Municipal Utility District, and the Imperial Irrigation District.

The ESPs provide retail electricity service to customers who have chosen not to receive electricity service from the utility that serves their area. Instead, these customers have entered into "direct access" contracts with ESPs for their electricity. This electricity is delivered to these ESP customers through the transmission and distribution system of their local utility. There are currently eighteen registered ESPs operating in the state, generally serving large industrial and commercial businesses. The ESPs also provide electricity to certain state and local government entities, such as the California State University system, several University of California campuses, some community college districts, and some local school districts.

Under current law, ESPs are only required to register with the PUC for licensing purposes; their rates and terms of service are not regulated by the PUC. However, the PUC has applied certain additional requirements to ESPs (discussed below).

Currently, the IOUs provide about 71 percent of the electricity in the state; publicly owned electric utilities provide 14 percent; ESPs provide 11 percent; and the state's Department of Water Resources provides 4 percent (chiefly for the operation of the State Water Project).

Deregulation and Direct Access. California began the process of restructuring electricity service in the early 1990s by introducing competition into the generation of electricity, with the ultimate goal being lower prices for IOU customers. The plan ultimately adopted in 1996 included a "transition"

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Commonly Used Terms—Proposition 80

- ✓ ***Community Choice Aggregation***—The authority of a city or county to aggregate all the electrical demand of the residents, businesses, and municipal users under its jurisdiction and to meet this demand from an electricity provider other than the electric utility currently serving that local area.
- ✓ ***Direct Access***—Retail electricity service is provided to a customer directly from an electric service provider, rather than from the utility (local publicly owned or investor owned) that serves the customer's area.
- ✓ ***ESP (Electric Service Provider)***—Companies that provide retail electricity service directly to customers who have chosen not to receive service from the utility that serves their area. Customers of ESPs are referred to as "direct access" customers.
- ✓ ***IOU (Investor Owned Utility)***—Privately owned electric utilities that have a defined geographic service area and are required by law to serve customers in that area. The Public Utilities Commission regulates the IOUs' rates and terms of service.
- ✓ ***Procurement Process***—The process, overseen by the Public Utilities Commission, through which the IOUs secure long-term electricity supplies through competitive bidding.
- ✓ ***PUC (Public Utilities Commission)***—The state agency that regulates various types of utilities, including investor owned electric utilities.
- ✓ ***Renewables Portfolio Standard***—Requirement that electricity providers increase their share of electricity generated from renewable sources (such as wind or solar power) according to a specified timeline.
- ✓ ***Resource Adequacy Requirement***—Requirement of the PUC that IOUs and ESPs show that they will have adequate electricity supplies to meet projected demand and maintain system reliability.
- ✓ ***Time-Differentiated Electricity Rates***—An electricity rate structure under which customers would be charged different prices for electricity based on the time of day in which it is used, given that the availability and cost of providing electricity varies depending on the time of day.

period during which the IOUs were to sell off their fossil fuel power plants to independent generators, while retaining their hydroelectric and nuclear power plants. During this transition period, the PUC continued to regulate the IOUs' rates. Eventually, however, electricity purchases and customer rates were to be determined in a competitive market. In such a market, customers could choose to have the IOUs purchase the electricity on their behalf, or they could purchase electric power *directly* from ESPs through "direct access."

The deregulation process was put on hold in response to the energy crisis that arose in 2000 and early 2001. At that time, the combination of sharply rising electricity demand, lagging investment in new power plants, and other factors led to electricity shortages and sharply rising prices. At that point, two of the IOUs were still under the transition period and therefore remained under PUC rate regulation. These IOUs were not permitted to pass along the sharply rising wholesale costs to their customers and were pushed into near financial insolvency.

In response to the energy crisis, the state began purchasing electricity on behalf of the IOUs and halted several aspects of deregulation. Among these, the state prevented the IOUs from continuing to sell their power plants and suspended new direct access for IOU customers. Under existing law, this suspension will continue until long-term electricity contracts signed on behalf of the IOUs by the Department of Water Resources expire. The last of the contracts expires in 2015.

While individual customers are currently barred from entering into direct access service, current law does allow a city or county to aggregate all the electrical demand of the residents, businesses, and municipal users under its jurisdiction and to meet this demand from an electricity provider other than the local IOU, such as an ESP. This variation on direct access is referred to as "community choice aggregation."

Long-Term Procurement Process and Resource Adequacy Requirements. As required by current law, the PUC is currently overseeing a process through which the IOUs secure long-term electricity supplies through a competitive bidding process. Under this competitive "procurement process," the IOUs select a mix of electricity supplied by their own power plants and electricity provided under contract from other generators to meet their long-term electricity needs. The PUC approved the IOUs' first long-term procurement plans in April 2004.

For text of Proposition 80 see page 72.

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In addition, the PUC has adopted rules requiring both the IOUs and the ESPs to show that they will have enough electricity to meet projected demand, known as a resource adequacy requirement.

Renewables Portfolio Standard. Current law requires that electricity providers, including the IOUs, community choice aggregators, and ESPs, increase their share of electricity generated from renewable sources (such as solar or wind power) by 1 percent per year, up to 20 percent of their total electricity supply by 2017. This requirement is known as the renewables portfolio standard.

The PUC has adopted a policy of accelerating the 20 percent requirement to 2010, but this is not required by law. Current law does not require electricity providers to continue to increase the proportion of their electricity from renewable sources once they have reached the 20 percent requirement.

Time-Differentiated Electricity Rates. Generally, all but the largest electricity consumers pay electricity rates that do not change based on the time of day or season. The IOUs have submitted proposals to the PUC to implement a system of time-differentiated rates that would apply to more consumers. Under such a system, customers would be charged different prices for electricity based on the time of day in which it is used, given that the cost to the IOUs of providing electricity varies depending on the time of day. For example, during peak demand times, customers would pay higher rates, while they would pay lower rates during the lower demand times of the day. In theory, time-differentiated pricing would encourage consumers to reduce electricity consumption during periods of peak demand, typically hot summer afternoons when electricity supply is the tightest and therefore its cost is high. The PUC is currently considering IOU proposals to implement time-differentiated rates in a regulatory proceeding, and has not yet determined how such a system of rates would be applied to more consumers.

PROPOSAL

Overview of Measure. The measure addresses a number of aspects of the state's electricity market: the regulation of the ESPs and direct access, the procurement process, resource adequacy requirements, the renewables portfolio standard, and the use of time-differentiated electricity rates. Each of these aspects is discussed below.

Regulation of ESPs. The measure places the ESPs under the "jurisdiction, control and regulation" of the PUC. The measure specifies that the scope of this regulation includes the enforcement of requirements related to energy procurement, contracting standards, resource adequacy, energy efficiency, demand response, and the renewables portfolio standard. While the measure broadens the authority of the PUC to regulate the ESPs, it does not, however, specify the extent to which it would regulate ESP rates and terms of service.

Direct Access. In general, the measure bars any customer currently receiving electricity service from an IOU from switching to an ESP. Customers currently being served by direct access contracts with ESPs could continue to receive electricity service from ESPs, effectively "grandfathering" in their direct access service. Direct access customers could also return to IOU electricity service under specified conditions. The measure does not restrict current or future community choice aggregation.

Procurement Process. The measure requires that the PUC implement a long-term procurement process, and directs the PUC to consider a series of factors in evaluating the IOUs' long-term procurement plans. While the PUC generally now considers the factors listed in the measure, current law does not specify that all of these factors be considered.

The measure also requires that the first priority for IOUs in procuring new electricity is to be from "cost-effective" energy efficiency and conservation programs, followed by "cost-effective" renewable resources, and then from traditional sources such as fossil fuel burning power plants. This "loading order," as it is known, has been adopted by the PUC, but is not currently required by law.

Resource Adequacy Requirement. The measure requires both the IOUs and ESPs to show that they are able to meet peak demand with adequate reserves to ensure system reliability. This puts into law current PUC practice.

Renewables Portfolio Standard. The measure accelerates to December 31, 2010, the deadline for the IOUs and ESPs to meet the 20 percent renewable resources requirement, consistent with a recent PUC decision. The measure also deletes a provision in existing law that explicitly provides that electricity providers are not required to increase their share of electricity from renewable sources once the 20 percent requirement has been reached.

ANALYSIS BY THE LEGISLATIVE ANALYST (CONTINUED)

Time-Differentiated Electricity Rates. Under the measure, residential and small commercial customers with electricity use under a specified amount and in a building built before January 2006 could not be required to pay time-differentiated electricity rates without their consent.

Amending the Measure. The measure states that the Legislature may amend the measure only to achieve its "purposes and intent" and would require a two-thirds vote of both legislative houses and signature of the Governor to do so. To the extent that the measure puts into law existing processes and policies of the PUC that are not currently required by law, the measure would make it more difficult for the state to modify these practices and policies when, for example, conditions in the electricity market change.

FISCAL EFFECTS

State Administrative Costs to Implement Measure. The measure could increase the PUC's administrative costs, largely depending on the extent to which the commission exercises the broadened authority given to it under the measure to regulate the ESPs. The fiscal impact on the PUC could range from a negligible cost up to around $4 million annually. The upper end of the range would occur if the PUC regulates the rates and terms of service of the ESPs. The measure, however, would not increase the PUC's costs in areas where the measure puts into law existing PUC practices related to procurement, resource adequacy, and the renewables portfolio standard. Under current law, the potential additional costs would be funded by fees paid by electricity customers.

Uncertain Impact on State and Local Costs and Revenues. The primary fiscal effect of this measure on state and local governments would depend on the impact it would have on electricity rates.

Changes in electricity rates would affect government *costs* since state and local governments are large consumers of electricity. To the extent that the measure limits state and local governments from entering into new direct access contracts, the measure takes away an opportunity for these government entities to potentially reduce their electricity costs.

State and local *revenues* would be affected by the measure's impact on electricity rates, since tax revenues received by governments are affected by business profits, personal income, and sales—all of which in turn are affected by what persons and businesses pay for electricity.

It is not possible to determine the net effect of this measure on electricity rates (and hence state and local government costs and revenues), as the net impact would be influenced by several potentially offsetting factors. For example:

- To the extent that the measure increases certainty about the structure of the electricity market, this may encourage additional investment in the market. Such investment, including the construction of new generation, could increase the supply of electricity and potentially lower electricity rates.
- On the other hand, the measure's ban on customers entering into new direct access contracts with ESPs could result in higher electricity rates over the long term by limiting competition in the retail electricity market.

The measure's impact on retail electricity rates would be influenced by a number of factors, including the specific structure of the regulations adopted by the PUC to implement the proposition.

For text of Proposition 80 see page 72.