

**CALIFORNIA INSTITUTE
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EXECUTIVE SUMMARY

The Federal Report is prepared by the California Institute staff for its semi-annual Board meetings. It details the legislative issues the Institute has worked on in 1996 and the products and services that the Institute provides to its Advisory Board and the congressional delegation.

LEGISLATIVE ACTIVITY

Since January 1996, the Institute has engaged in activities regarding a number of significant issues, including:

- **Immigration** -- The Institute continues to work to assess approaches for reimbursing states for certain costs of illegal immigration, and to monitor efforts to restrict various benefits to legal immigrants and reform laws regarding legal and illegal immigration.
- **Medicaid Formula** -- The Institute has analyzed the impact of proposed Medicaid formula changes on California, and provided the delegation with this fair share data.
- **Disaster Insurance** -- The Institute continues to focus on proposals for a national disaster insurance plan to cover damages caused by earthquakes and other natural disasters.
- **ISTEA Reauthorization** -- The Institute has provided continuous analysis of the reauthorization deliberations and will continue to focus on the issue in the 105th Congress.
- **Education** -- The Institute has worked with the delegation and a California K-12 alliance regarding California's interests in federal education funding allocations.
- **FDA Reform** -- The Institute will continue to provide the delegation with information on the importance of this issue to California's biomedical technology industry.
- **Tax Policy and Technology Industries**-- The Institute continues to advise the delegation regarding tax issues important to the state's technology community, including a targeted capital gains tax cut; a permanent research and development tax credit with an appropriate base year; and accelerated depreciation of semiconductor production equipment.
- **Budget, Appropriations, and Other Key Projects** -- The Institute will continue to track policy and funding for a range of important California concerns in transportation, defense, space, science, energy, trade, and other areas.

PRODUCTS AND SERVICES

To promote the exchange of policy views among the Congressional delegation, the Institute's Advisory Board members and others, and to provide timely information on legislative issues of importance to California, the Institute provides the following products and services:

- **Member Breakfasts** -- Advisory Board members are invited to attend a monthly breakfast hosted by the Institute featuring one or two members of the delegation.
- **Briefings** -- The Institute has sponsored briefings on several issues, including immigration, the 2000 census, the California economy, and defense downsizing.
- **Policy Papers** -- The Institute has recently produced papers on the Export Administration Act, federal formula grant allocations, the balance of payments between California and the federal government, and the use of poverty data in federal formulas.
- **Capitol Hill Bulletins** -- The Institute continues to monitor and report on federal issues of significance to California in its weekly *California Capitol Hill Bulletin*.
- **Electronic Products** -- The Institute continues to expand availability of its written products and other services via e-mail, a home page, and other electronic means.

I. CALIFORNIA INSTITUTE FEDERAL REPORT

The mission of the California Institute is to identify issues critical to the economic health of California, coordinate the development of research data pertaining to those issues, and communicate this information to the California congressional delegation in a manner that encourages the delegation to address the issues in a bipartisan fashion consistent with the best interests of California. In keeping with that mission, the California Institute has worked on the following issues over the last several months.

A. IMMIGRATION

The Institute has worked closely with the congressional delegation, the Governor's office, and other interested parties on numerous immigration issues this year. The pending FY1997 appropriations again contain \$500 million in funding to reimburse the states for the cost of incarcerating illegal immigrant felons. This same amount was also included in the final FY1996 budget agreement passed earlier this year. California, which currently spends almost \$400 million annually to incarcerate over 19,000 illegal immigrant criminals, could receive as much as 60 percent of this money.

This year also marked the passage of illegal immigration reform bills in the House and Senate. Although both bills initially contained provisions also overhauling legal immigration, the majority of those provisions were stricken and Congress will deal with separate legislation on them at a later time. The House passed its illegal immigration bill in late March. The Senate passed its version on May 2. Both bodies are currently negotiating a compromise between the two bills, and it is hoped that Congress will take final action on the compromise before Congress adjourns.

In general both bills crack down on illegal immigration by beefing up the number of border patrol agents and other INS personnel responsible for apprehending undocumented immigrants, and by instituting tougher enforcement provisions. For instance, the bills authorize the hiring and training of 1,000 new border patrol agents per year over the next five years. This will roughly double the border force to 10,000. Similarly, both bills call for a pilot program to test an employment verification system. Under the program, employers would call a nationwide hotline to determine whether new employees are eligible to work in the United States. The House program would be voluntary for employers during the test phase, while the Senate bill mandates that employers use the hotline.

A major difference between the two bills, however, is in the area of public education. The House passed a Proposition 187-type amendment, sponsored by Rep. Elton Gallegly (Simi Valley), that would give states the right to deny K-12 education to undocumented immigrant children. The Senate bill does not have a counterpart provision. Proponents of the Gallegly amendment have argued that the provision is a necessary part of breaking the magnet that draws illegal immigrants to the United States and easing the financial burden of illegal immigrants on the states. Opponents say its retention in the final legislation will result in increased crime among youths denied an education and will likely draw a Presidential veto. Reaching consensus on a compromise of the Gallegly amendment has held up negotiations between the two sides. Recent proposals have been structured around allowing the states to charge illegal immigrant children tuition. However, a final agreement has not yet been reached, and the issue has taken on political dimensions as the presidential election approaches.

As part of its efforts to provide the congressional delegation with useful and reliable information on various aspects of the debate, the Institute co-sponsored two immigration briefings with the Population Resource Center and the Sunbelt Institute. The first briefing was on March 1, 1996. The second briefing was held on September 10, 1996. Over 55 staff members from the California congressional delegation and other interested parties attended the second briefing. Three respected experts on immigration policy served on the panel. A detailed account of both briefings can be found in Section II.B.

A legal immigration issue that the Institute is working on with California's computer electronics industry is the number of skilled foreign worker visas authorized under the legal immigration bills. Consideration is being given to restricting the number of these workers permitted to enter the United States annually. The computer electronics industry, in order to remain globally competitive, must be able to hire skilled foreign engineers and technicians for employment in the United States when U.S. workers with the same skills are unavailable. Restricting the number of visas available for these workers may eventually be a factor in a company's decision whether to retain or expand a manufacturing operation in the U.S., or move production abroad.

The recently passed welfare reform bill will also have a significant impact on immigrants in California. For a detailed discussion of the changes this bill makes to the eligibility of legal immigrants for welfare and other benefits, see below. In addition to banning immigrants from some benefits, the welfare reform bill extends the "deeming" period for several categories of benefits. Currently, depending on the specific program, for three to five years after a legal immigrant has entered this country, the income of that immigrant's sponsor -- the U.S. citizen who has recommended that immigrant's entry -- is "deemed" to be added to the immigrant's income for purposes of calculating whether the immigrant is eligible for certain benefits. The welfare reform bill extends the deeming period to in effect deny most benefits to immigrants until they have become citizens or worked ten years in the United States. Other legislation under consideration by Congress, including student aid revision, also contemplates lengthening the deeming period and otherwise restricting legal immigrants' access to federal benefits. Since California's share of the nation's legal immigrants is triple our share of the nation's population as a whole, such measures would likely have a pronounced impact on the state. The impact might be somewhat mitigated, however, depending on to what extent eligible immigrants elect to become citizens, which would exempt them from most deeming proposals.

Immigration issues are of significant importance to California, and the Institute has been actively involved in the debate over these issues since 1994. As the Congress continues to address these issues, the Institute will continue to analyze their impact from California's unique perspective and provide the delegation with the best information possible.

B. WELFARE

In August, Congress finalized its sweeping welfare reform legislation and President Clinton signed it into law. Replacing the Aid to Families with Dependent Children (AFDC) program with Temporary Assistance to Needy Families (TANF), the law eliminates the entitlement nature of cash benefits and other welfare assistance. Instead, the states will now receive block grants of federal dollars to run the system their way, with some restrictions placed on them by federal law. Recipients will have to work within two years of receiving benefits and a

lifetime five year limitation is placed on the receipt of benefits. States may set stricter restrictions than this, and may exempt up to 20 percent of recipients from these restrictions due to hardship. The states are required to maintain their own spending on welfare at 75 percent of their 1994 level.

The bill strictly limits the welfare assistance available to legal immigrants. Legal immigrants who arrive in the United States after enactment of the bill will be ineligible for most assistance programs until they become citizens. Legal immigrants currently residing in the country lose their eligibility to receive Supplemental Security Income (SSI) payments for the elderly, blind, and disabled, and food stamps. The individual states will decide whether to continue to provide Medicaid to legal immigrants already in the U.S., although emergency medical services will be provided. Under the bill, illegal immigrants are denied most federal and state assistance, with the exception of some emergency benefits, such as short-term disaster relief and emergency medical services.

These provisions will have their greatest impact on California, which is home to about 40 percent of the legal immigrants living in the U.S. The state's Department of Health Services has estimated that 260,400 immigrants in California receive SSI and Medi-Cal. The New California Coalition, a group affiliated with the National Immigration Law Center, has estimated that as many as 425,000 legal immigrants in California, half of them children, could lose food stamp benefits. What is not known, however, and is one reason why the group's estimates have been criticized by proponents of the legislation, is how many of these immigrants are eligible, and will become, citizens in order to preserve their benefits.

The Institute will continue to closely follow the impact of the welfare reform bill as it is implemented in California. One of the most important concerns will be the financial burden on the state's counties if and when they are called on to provide General Assistance to those individuals, citizens and immigrants alike, who lose benefits because of the legislation.

C. MEDICAID FUNDING

Throughout the budget debates, the savings that changes in the Medicaid program could realize were hotly contested by both sides. The Institute was actively involved in providing the delegation with the most up-to-date information regarding how the many proposals would affect California's share of federal Medicaid dollars. It also prepared an opinion editorial warning of the dire consequences to the state if certain formula factors were included. In the end, it may have been at least a partial victory for California that Medicaid reform was not included in the final 1996 budget agreement, though the rapidly increasing cost to the federal treasury will likely necessitate addressing the issue in the future.

California's perspective on the Medicaid formula debate is unique. California has been a "donor state" for nearly 10 years, sending billions more dollars into the federal treasury than it receives back. So it was no surprise that as budget balancers attempted to negotiate an overhaul of the Medicaid program, California again was being asked to subsidize medical care for the poor of other states. None of the numerous proposals on the balanced-budget negotiating table would have rectified the disparity between California's federal Medicaid receipts and our large numbers of poor patients.

In purely percentage terms, the Congressional Republicans' block grant proposal would have given California a larger share than the other proposals. California's share of federal

Medicaid funds would grow from 9.5% in 1996 to 10.8% in 2002 under the Congressional conference agreement, according to the General Accounting Office. However, because California now houses 15% of the nation's persons in poverty and 14% of the nation's Medicaid-eligible population, this level is still well short of "fair."

Three other major proposals were aired -- one from the Clinton Administration, another from a coalition of conservative House Democrats (the Blue Dog Democrat plan), and a third from a bipartisan group of 21 Senators (the Breaux-Chaffee plan). Each would have retained the entitlement status of Medicaid, but would have done so by locking states into their current receipts per beneficiary with a "per capita cap." Since California now receives only 9.5% of federal Medicaid funds, that low share would have been fixed in place permanently.

While preferable on a percentage basis, the Republican Congressional proposal might well have resulted in fewer total federal Medicaid dollars to California in the long run. By converting the program from an open-ended entitlement to a block grant, the plan would no longer allow for added growth during economic hard times. Yet this impact was distributed evenly among all states. The other plans allowed for such emergencies, and would have adjusted more for inflation, features which would have reduced those plans' savings, or at least the certainty of them. Under the Republican plan, California would have received \$80.3 billion of the nation's \$790 billion federal Medicaid block grant dollars between fiscal years 1996 and 2002. (For the same period, the Urban Institute predicted that California would receive \$95.7 billion of the nation's \$954 billion under the existing Medicaid program.)

According to a GAO source, the per capita cap concept, used in all bills except the House Republican leadership plan, would favor states already providing high levels of medical service to a relatively narrow range of patients. Since more federal funds would be provided only if Medicaid enrollment increases, such states could simply expand coverage and rake in federal dollars at a high matching rate. Since California now provides more limited service to a broad range of patients, our potential for growth would be severely limited. According to GAO, California ranks 51st (50 states plus D.C.) in level of service, yet we are 6th in breadth of patient coverage.

California receives a small relative share of federal Medicaid dollars. While we serve nearly twice as many indigent patients as New York, the next largest state, California receives roughly 9.5% of Medicaid funds compared to New York's 13%. New York spends more than three times as much to care for each patient as does California. In 1993, California served 4.8 million persons with combined state-federal funding of \$9.6 billion, while New York served 2.7 million persons with \$17.6 billion. Thus, California spent \$2,000 per patient, while New York spent \$6,500. (The national average was \$3,100.) To lock in these inequitable distribution levels would unfairly penalize California and other states which have worked hard to control excess spending on medical care, and it would reward inefficient states for their exorbitance.

During the debate, the Institute argued that there should be per capita parity -- or at least real progress toward it -- rather than a per capita cap. California manages to serve more Medicaid patients with fewer federal dollars, and it should not be punished for doing so. Allocating Medicaid funds according to numbers of poor persons would be vastly more equitable.

Undoubtedly, significant changes in the Medicaid program will continue to be considered as Congress and the President continue to address the federal budget. The Institute will continue to

diligently analyze the proposals put forth to ensure that the delegation has the best and most accurate information regarding their impact on California.

D. NATURAL DISASTER INSURANCE

The Institute has actively supported the establishment of a national insurance program to protect against the damages caused by earthquakes and other natural disasters. No one questions the need to address how the federal government responds to natural disasters. The startling fact is that from 1979 to 1993, the federal government provided disaster assistance funding and loans of over \$130 billion. The issue of how to reform federal disaster assistance funding to ease the burden on the treasury, without sacrificing effective assistance, has occupied Congress for the last four years.

In 1995, H.R. 1856, the Natural Disaster Protection Partnership Act, was introduced by the late Rep. Bill Emerson (Mo.) and former Rep. Norman Mineta. The bill would establish a national system of disaster insurance operated primarily by private insurance companies, with federal government back-up. By the spring of 1996, the bill had garnered over 225 co-sponsors, including over 39 members of the bipartisan California congressional delegation. The Senate counterpart, S. 1043, also has broad, bipartisan support. During hearings on the bills in the House and Senate, concerns were raised that the insurance pool created by the bills would not be funded sufficiently to insure against a major disaster and that the federal government's exposure remains too great. As a result, Congress, the Administration, and interested parties have been negotiating a compromise bill that would address these and other concerns. To date, a satisfactory compromise has not been reached.

Earlier this year, Reps. David Dreier (San Dimas) and Bill McCollum (Fla.) gathered signatures from the California and Florida delegations on two letters requesting that the bill receive expedited consideration by the House Transportation Committee, and be made a legislative priority in this Congress by the House leadership. A bipartisan group of 24 members of the California congressional delegation signed the letters. The Institute disseminated information on these letters to the delegation and continues to support consideration of the bill this year. Unfortunately, with the end of the 104th Congress expected soon, it is unlikely that Congress will be able to pass a bill this year. The Institute will continue to make this legislation a high priority.

E. EDUCATION

Since its inception, the Institute has monitored education issues as they affect the state, particularly in ensuring that the formulas used to allocate federal education dollars do not shortchange California. Recently, the Institute has begun to increase its focus on K-12 education issues, and it will work with Congressional offices and the California-D.C. Education Alliance to further California's interests in the K-12 education arena.

Earlier this year, the House Subcommittee on Early Childhood, Youth and Families, chaired by Rep. Randy (Duke) Cunningham of San Diego, passed a bill to rewrite the Individuals with Disabilities Education Act (IDEA). The subcommittee proposed to replace the current funding allocation formula from one based on reported counts of disabled children (which can be subject to gaming of numbers and inconsistency of application by other opportunistic states) to a "bright-line" formula based simply on the number of children in the state as counted by the Census Bureau. In doing so, the proposal would significantly increase California's funding allocation. California now receives \$236 million from IDEA's primary grant, out of \$2.27 billion

nationwide. If fully implemented, the Cunningham subcommittee's proposal would raise California's allocation to \$286 million, assuming the total pot remains stable. Thus, California receipts would rise from the current 10.4% of the nation's total IDEA funds to 12.5% -- a share more reflective of our state's share of the nation's child population. Unfortunately, the shift to the new figures would take place over 10 years (10% per year), an unusually long phase-in period. The Institute will monitor the progress of these formula change proposals and assist where possible as Congress considers IDEA reauthorization next year.

On another education issue, Governor Pete Wilson reached an agreement with Education Secretary Richard Riley on the conditions for California's acceptance of \$42 million in Goals 2000 education funding. Wilson said his decision to accept the funds was based on assurances from Secretary Riley that participation in the Goals 2000 program would not interfere with the implementation of California education reforms such as home schooling, opportunity scholarships, and the creation of single-gender academies. Both the Governor and the California Superintendent of Instruction Delaine Eastin laid out the following additional requirements for the acceptance of Goals 2000 funding: (1) the members of the California State Board of Education will serve as the state Goals 2000 panel; (2) the federal peer review panel to be appointed by the U.S. Secretary of Education will consist of a majority of Californians, and will be advisory only, having no authority to impose any conditions on the state; (3) of the \$42 million available to California, \$11 million is to be allocated to local school districts that received planning grants from the first-year allotment, and the remainder will be expended by the state to provide funds for a major initiative focused on improving basic skills in reading and math in grades K-4; and (4) acceptance of the Goals 2000 funding does not obligate California to participate in the program in subsequent years.

A number of education issues will face the 105th Congress when it convenes, and several will be of particular importance to Californians. Among them will be whether updated census poverty data figures will be used for distribution of education formula funding, and how the revisions in and replacement of the AFDC program's child counts will impact education formulas.

F. EXPORT ADMINISTRATION ACT REAUTHORIZATION

Foreign trade is one of the most significant factors driving California's economic recovery. In 1995, California's exports rose to \$92 billion, an increase of almost \$24 billion since 1993. The export of computers, and industrial and electrical equipment account for \$47.1 billion, over half of all of California's exports by value. Silicon Valley, where a significant portion of the computer and electronics industry is located, accounts for at least one-third of California's foreign trade.

In July, the House passed by voice vote H.R. 361, the Export Administration Act of 1996. The bill replaces the Export Administration Act of 1979, which expired in August of 1994, and which was the statutory basis for the control of exports of dual-use commodities and technologies. The purposes of H.R. 361 are twofold: one, to strengthen the effective use of U.S. export controls in preventing international terrorism and the proliferation of weapons of mass destruction; and two, to improve U.S. export competitiveness by streamlining the U.S. export license process to eliminate unnecessary governmental regulations.

Dual-use commodities and technologies are non-munitions, civilian items that have potential military applications. Their export has been controlled for national security and foreign policy purposes, and to alleviate potential "short supply" problems in the United States if exports

are allowed to continue. The federal government controls exports under this system by requiring the issuance of an export license for dual-use commodities and technologies that have been placed on the Commodity Control List. The Department of Commerce has the primary role in approving or disapproving applications; however, many applications are also referred to the Departments of State and Defense, and other national security agencies for comments and recommendations. These referrals can cause significant delays in the issuance of an export license.

Members of the computer electronics industry have expressed concern that the House bill will not result in expediting licensing procedures or removing existing impediments to the export of computer technology and equipment. Under the bill as originally drafted, an industry negatively-affected by export controls could petition the government for relief if it could show that: 1) foreign availability of the controlled products are, or soon would be, adversely affecting U.S. market share; 2) the controls do not meet the stated objective; or 3) the controls are causing adverse economic impact on the affected industry. In order to ensure that the National Security Committee did not request sequential referral of the bill, the House International Relations Committee during mark-up deleted the second and third criteria, and removed the prospective factor from the foreign availability clause. The electronics industry believes these changes have made the unfair impact provision essentially meaningless.

In addition to this problem, the bill does not address the export of encryption devices, manufactured by U.S. computer electronics companies to ensure the security of financial and other transactions conducted electronically. Currently, the U.S. prohibits the export of these items because of the potential that terrorists and other criminal groups may use them to cover up their activities. This is an important issue for U. S. electronics companies, because foreign competitors are manufacturing and selling encryption devices abroad. The companies have been negotiating with the administration in an effort to develop a suitable compromise on the export of these devices. In addition, Congress will hold a hearing on the issue in late September.

During the committee mark-up of H.R. 361, Chairman Toby Roth (Wis.) allowed that the current system of controls on encryption devices was cumbersome and jeopardized the competitiveness of U.S. manufacturers. Although he pledged to work with the administration and interested companies to reach a regulatory solution, he expressed concern that dealing with the problem through legislative language would bring a request for sequential referral from the National Security Committee, a possibility he opposed because of the short time left on the legislative calendar for this year.

The Institute prepared a white paper analyzing H.R. 361, and pointing out the concerns expressed by the computer electronics industry. The paper was disseminated to the congressional delegation and other interested parties prior to floor action on the bill. Because of the limited time left in this Congress, it is unlikely that the Senate will take up the bill this year. The Institute will continue to follow the bill closely and ensure that the delegation is kept abreast of its impact on California's export industry.

G. FDA REFORM

An important issue to California's growing biomedical industry is the proposed reform of the Food and Drug Administration. The current process for approval of drugs and medical devices for public use can add significant costs to developing new products and delay marketing. The House Commerce Committee held hearings on three bills aimed at overhauling the FDA. The

three companion bills, as introduced, are: H.R. 3199 dealing with regulation and approval of new drugs and biological products; H.R. 3200, dealing with food and nutritional regulations; and H.R. 3201, dealing with biomedical devices. Since that time, Congress, the Administration, and interested parties have been negotiating in an attempt to reach a consensus on the best way to reform FDA. The Senate marked up a more limited version of FDA reform in late March.

The Institute is working with the California Health Care Institute and other interested parties to ensure that the congressional delegation is made aware of the importance of this issue to California. It intends to sponsor a briefing on FDA reform during the Congressional recess. At that time, members of the biotechnology industry, as well as congressional committee staff with expertise in the area, will be invited to brief the delegation. It is unlikely that there will be final action on this issue before the end of this Congress as so little time remains before the end of the session.

H. NORTH AMERICAN DEVELOPMENT BANK

The Institute has worked closely with Reps. Esteban Torres, Duncan Hunter, Ron Packard, and other Southern California members to ensure the full \$56.25 million funding for the North American Development Bank (NADBank) under the foreign operations appropriations bill. NADBank, created under NAFTA, will finance environmental clean-up projects along the U.S.-Mexican border. Several clean-up projects in the San Diego area are expected to be financed through the Bank.

As a result of the bipartisan support for the bill, the FY96 foreign operations appropriations passed earlier this year provided the full funding for NADBank. In the FY97 funding cycle, the House-passed bill decreases funding by ten percent to \$50.62 million. The Senate-passed bill, however, contains the full \$56.25 million. A conference committee is expected to resolve the difference in September. Under the agreement between the U.S. and Mexico, if U.S. funding falls short, Mexico will also reduce its matching contribution by a like amount. The Institute will continue to work to ensure that full funding is provided in conference.

In addition, in February, NADBank opened a U.S. Community Adjustment and Investment Office in Los Angeles. The Office will provide financial assistance to any U.S. communities and businesses that have experienced job losses related to NAFTA. The Bank will provide capital to help business start-ups, diversification, and retooling to create new job opportunities for workers in their communities.

I. ALAMEDA CORRIDOR PROJECT

The proposed Alameda Corridor would consolidate train traffic from the ports of Los Angeles and Long Beach onto a 20-mile high-speed, high capacity, and fully grade-separated transportation corridor, linking those ports with transcontinental rail yards near downtown Los Angeles. The project would also widen and improve the highway running parallel to the corridor. The total cost to design and build the corridor is estimated at \$1.8 billion. The Alameda Corridor Transportation Authority estimates that the project will be completed by 2001. The Institute is on record in support of the project and funding for the effort will continue to be a priority. Completion of the corridor would likely lead to large scale economic revitalization in the Los Angeles area and throughout the state. It is estimated that the Alameda Corridor will generate 700,000 permanent jobs by the year 2010.

In late March, the Clinton Administration announced its plans to seek Congressional approval for a \$400 million loan to fund the Los Angeles Alameda Corridor project. The Alameda Corridor Transportation Authority would utilize corridor user fees to repay the loan within the next thirty years. Payments on the loan would not begin until the railway is in use, estimated to be in 2001. The \$59 million appropriation to cover the government's start-up costs for the loan was approved by both the House and Senate, with the difference that the Senate earmarked the funds out of the new State Infrastructure Bank's \$250 million appropriation rather than the Direct Loan Financing Program. In conference on the spending bills, however, the conferees agreed to delete the funding from the appropriations bill and include it in the continuing resolution that is expected to be enacted before October 1.

J. DEFENSE / NASA PROCUREMENT

Among many others, two major DoD aircraft programs have been the subject of much Washington focus during the 104th Congress and are of particularly important to California: the B-2 Stealth Bomber and the C-17 Cargo Jet.

In February, administration officials announced President Clinton's decision to discontinue funding for the purchase of new B-2's. This year's defense budget already includes \$493 million, appropriated by Congress last December and signed by the President, for future production of the planes. According to the administration, the money will now be spent on upgrades and modifications to the existing fleet of 20 bombers. Furthermore, the President did not include funding for B-2 production in his FY97 budget request. It is believed that the decision came at the behest of senior Pentagon officials, who for some time have opposed the production of additional B-2's. The aircraft, produced by California-based Northrop Grumman, is estimated to support more than 20,000 California jobs. Representing 30 percent of defense dollars coming into Los Angeles County, the B-2 program is a core component of Southern California's high-technology aerospace industry. The only potentially good news came when a spokesperson for the President stated that the White House has ordered a study of the military's long range fighting capabilities and the role of the B-2, in relation to other weapons, in meeting these defense needs. The Institute communicated its research regarding the program to the congressional delegation, and will continue to assist efforts to identify a future for the program.

Last November, the Pentagon announced it would purchase 80 additional C-17 cargo jets, which McDonnell Douglas builds primarily in California. The C-17 military transport is designed to airlift heavy payloads over long distances without refueling. With a total price tag of about \$18 billion, the purchase should bolster the prospects for one of the state's largest aerospace firms. It is estimated that the order will preserve 8,700 jobs at the company's plant in addition to about 9,000 other aerospace jobs in Southern California. Officials from McDonnell Douglas said that the announcement will enhance their ability to sell the C-17's to foreign nations who were waiting for cues from Washington before making any decisions. More good news came this February when the President announced his decision to speed up production of the C-17, from its original ten-year schedule to an accelerated seven-year schedule. It is estimated that this move will bolster McDonnell Douglas' Southern California workforce by 2,300. The accelerated schedule is expected to result in production of as many as 15 aircraft per year. Faster production of the aircraft is expected to save the Pentagon \$893 million. Although the move will mean more jobs for the region in the short term, it also means that the project will be completed earlier, without assurances of continuing projects.

The Pentagon will soon narrow, from three to two, the number of potential contractors for the next generation of tactical strike aircraft. Known as JSF or the Joint Strike Fighter, the plane will be used jointly by branches of the armed services, and the winner of the contract may find itself well positioned to be a key force in the defense aerospace industry. While California firms will serve major roles in all three proposals as subcontractors, the prime contract competitors include Boeing, Lockheed Martin and Northrop Grumman. A decision on which two proposals will move to the prototype-development phase is expected around the end of this year.

In July, the administration announced that Lockheed Martin Skunk Works division in Palmdale won the race to build the X-33, a prototype reusable launch vehicle, or RLV. The selection of a contractor for the \$900 million, three-year contract begins the second phase of the X-33 program, during which Lockheed Martin will perform tests and compile data to determine RLV's viability. Several California companies will be key subcontractors for X-33 components. Major partners include the Rocketdyne division of Rockwell International (soon to become part of Boeing), Rohr Industries, Sverdrup, and Allied Signal. A primary goal of the X-33 program is to cut launch costs. Currently payload costs for space cargo can be as high as \$12,000 per pound; an RLV could cut costs to as low as \$1,000 per pound. Such cost efficiency would demonstrate commercial viability of an RLV. NASA intends to cut funding for the X-33 after three years, and leave the effort to private industry. A number of major California aerospace companies are expected to continue RLV research. The Institute helped publicize a briefing organized by Rep. Buck McKeon and Lockheed Martin on the X-33 in July.

Finally, as the Administration and Congress consider downsizing at NASA, the Institute has monitored the discussions. NASA is a significant factor in California, in terms of both procurement awards to California companies and NASA operations at such facilities as the Jet Propulsion Laboratory at Caltech in Pasadena and at NASA's Ames Research Center in Sunnyvale.

K. CENSUS UNDERCOUNTING AND USE OF OUTDATED POVERTY DATA

On March 20, the U.S. Supreme Court unanimously rejected a request from Los Angeles, New York and other major cities to force the Census Bureau to recalculate the 1990 census. Recalculation could have resulted in additional federal formula funding to California and, theoretically, perhaps an additional Congressional seat for the state. By the Census Bureau's own estimation, the 1990 census undercounted the population of California by 834,000 people. The Census Bureau determined that it undercounted the nation's population by 1.6% and California's by more than 2.7%. Because California was undercounted more than the rest of the nation, the decision not to recalculate cost California tens and perhaps hundreds of millions of dollars in unrealized formula grant funds. In 1991, then-Commerce Secretary Robert Mosbacher overruled his own Census Bureau's recommendation and declined to apply the adjusted figures. In 1994, a New York federal appeals court found that the 1991 decision violated Constitutional equal protection rules because the poor and minorities were disproportionately undercounted. The Supreme Court action overruled that decision. The Institute has worked actively on this issue since testifying before the Census Bureau several years ago.

The issue of whether "statistical sampling," as it is now called, will be permitted will be an increasingly important issue as the 2000 census nears. Already there are efforts to limit or prohibit statistical sampling methods.

Another important census data issue is poverty data currency. Because census information on income and poverty is collected only every ten years and has not been estimated between censuses, California and other growing states have been disadvantaged in the distribution of federal formula program dollars to the states.

In one potential bright spot, thanks largely to California Congressional delegation efforts in 1994, the Title One education program has been directed to use new intercensal poverty data now being developed. The Institute and the delegation will continue to work together to ensure these data are used, and that other formula grant programs which still rely on outdated census data are given the most current data possible.

For additional information on the poverty data subject, please refer to the California Institute publication entitled, *"Usage of Poverty Data in Federal Formula Programs: California Implications."*

L. TRANSPORTATION FUNDING

Last November, the President signed a bill designating 160,000 miles of U.S. highways as the National Highway System. The measure freed up \$6.5 billion in road funding to the states, which was unavailable until the National Highway System was adopted. According to Federal Highway Administration data, of the total \$15.6 billion apportioned under the bill, California will receive \$1.5 billion, or about 9 percent. Included in this figure is approximately \$253 million for the National Highway System and \$126 million for congestion mitigation and air quality control. California will also receive about \$101 million, or 23.5%, of "donor state bonus" dollars -- a fund created to reimburse states, such as California, which put more tax dollars into the system than they receive back in funding.

Also enacted as part of the National Highway System Designation Act were the newly created State Infrastructure Banks (SIBs). The SIBs are designed to support bond financed programs and to leverage state, local and private sources of capital to increase investment in the nation's surface transportation infrastructure. In July, Transportation Secretary Federico Peña recently announced that California will join nine other states in testing the use of SIBs as a method for financing transportation projects which would otherwise be without necessary funds. The SIBs will be created with federal seed money and will offer a selection of loan and credit enhancement assistance, including loan guarantees such as the one which was approved for the Alameda Corridor, to provide additional support of financing projects. The SIBs will use the repaid funds to make new loans or guarantees for other transportation projects.

On the legislative horizon is the reauthorization of the Intermodal Surface Transportation Efficiency Act (ISTEA). With the distribution of tens of billions of federal transportation dollars at stake, a favorable alteration of the spending distribution formulas will result in millions more dollars flowing to California for transportation projects. Under current law California is particularly disadvantaged with respect to federal transportation funding. In fact, California is one of the largest "donor states" to the Highway Trust Fund, putting in more monies annually than it receives. Other ISTEA reauthorization issues of particular significance to California are the development of innovative financing methods and the direction of funds towards border infrastructure projects. The Institute will continue to monitor and engage in the issues surrounding

ISTEA reauthorization. Additionally, it plans to produce a research paper and hold a delegation briefing on the subject later in the year.

M. TAX POLICY AND MICROELECTRONICS INDUSTRY ISSUES

Last year, the Institute organized a workshop between its Economic Advisory Council and representatives of the microelectronics industry in Silicon Valley. The EAC members were briefed on the importance of the industry and its beneficial impact on California's economy. As a result of that seminar, the EAC prepared a report, which was disseminated to the California congressional delegation, the news media, Institute supporters and others in the California-Washington community.

After analyzing the industry, the EAC made several recommendations for policy changes that would help ensure future growth of microelectronics companies in California. Among these recommendations were three dealing with tax policy: a targeted capital gains tax reduction; a permanent R&D tax credit using a realistic base year; and, a three-year depreciation schedule for semiconductor manufacturing equipment. The EAC found that each of these changes could encourage investment in the industry. In addition, a permanent extension of the R&D tax credit would help to compensate for the decline in federal funding for research.

As a result of the EAC's findings, the Institute took a position in support of each of these tax changes. Included in the recently enacted minimum wage bill was language extending the R&D tax credit for one year through June 1997. Unfortunately, the credit expired in 1995 and the new law did not apply the credit retroactively for the year 1995 through June 1996. Although the law does not change the base year, which has been very problematic for a large number of California companies, new language does allow for the use of an alternative credit calculation. This provision is expected to address the fact that some companies had been unable to take advantage of the tax credit as it was previously drafted.

The Institute will continue to work with the microelectronics industry regarding other tax provisions recommended by the EAC.

Another issue microelectronics industry issue this year was the continuation of the U.S.-Japan Semiconductor Trade Agreement. Working non-stop, the Administration and Japan reached a new agreement shortly after the self-imposed deadline of July 31, 1996. The semiconductor industry employs 60,000 people in California, and a renewed bilateral government-to-government agreement was very important for the U.S. semiconductor industry to maintain market access in Japan. Since the first agreement was reached, the foreign share of the Japanese market has increased from 8.5 percent in 1985 to 25.4 percent in 1995. However, the U.S. share of the world market outside of Japan is 50 percent, while the U.S. share of the Japan market remains at only 18 percent.

N. FEDERAL RESEARCH & DEVELOPMENT EXPENDITURES

An issue critical to retaining California's academic and intellectual prominence is federal funding for science, research and development. In its recent survey of research and development spending by ten federal agencies, the National Science Foundation determined that 22.6 percent of federal R&D funds are spent in California. Of \$65.7 billion spent nationally on federal R&D in FY 1993, \$14.9 billion was spent in California. (These data are for federally-funded R&D only,

and do not include significant non-federal research activities of California's universities and industries.) The federal government has spent roughly \$800 billion on research and development activities over the past 20 years. In each of those years, California has won between 21 percent and 27 percent of those funds. Since California's contributions to the federal government in taxes and other revenues have never exceeded 13.4 percent, federal R&D spending constitutes a good bargain for California. Nearly half of federal R&D dollars are spent at industrial firms. Of the \$30.3 billion spent at U.S. companies, nearly one-third (\$9.2 billion) went to firms in California. The level eclipsed the next highest state, Georgia, whose firms received \$2.6 billion, and number three Maryland, where companies took in \$2.2 billion.

California is likewise a big winner of federal research and development dollars spent at universities and colleges. Of the \$14.6 billion spent, California universities receive more than \$3.3 billion, or more than 22 percent of total U.S. university R&D. In this category, only New York (at \$1.2 billion) even breaks the \$1 billion level; total university R&D receipts in Massachusetts, New Mexico, Pennsylvania, Illinois, and Texas each exceeded \$500 million. The University of California alone receives close to 10 percent of general science expenditures for university research. Significantly, our state's major research universities and many companies take a unique high road by opting not to pursue special interest Congressional earmarking of project funds, preferring rather to compete fair-and-square solely on the merits. The Institute will continue to monitor California's share of R&D spending.

O. BAY-DELTA RESTORATION PROJECT

With California's growing population, manufacturing and agricultural industries, water management, and environmental quality is a major issue for the state. Recently, a bipartisan group of policymakers, environmentalists, developers, urban and agricultural users and northern and southern Californians developed the Bay-Delta water restoration program. The San Francisco Bay-Delta Estuary provides 2/3rds of California's water. This November, Proposition 204, a \$995 million bond initiative for state implementation of the restoration program will be on the ballot. In addition to these state funds, significant federal funds will also be needed over the next ten years. Rep. Bill Baker (Walnut Creek), joined by several other members of the delegation, recently introduced legislation to fund the first phase of the Bay-Delta restoration program. The bill would authorize \$143 million annually for fiscal years 1998 thru 2000 to be used for water quality and environmental improvements in the Bay-Delta. The Institute will continue to work with the delegation on this vitally important project.

P. BASE REUSE

Base closure, cleanup and reuse issues are critical to California. While California housed only 15 percent of the nation's military personnel as the recent base closure rounds began in 1988, our state took two-thirds of the nation's net cuts in base jobs during the four closure rounds. Consequently, California has one of the largest stocks of former military installations to be transferred to civilian usage and has a keen interest in ensuring that the federal focus remains on efforts to smooth that transition. In particular, environmental remediation efforts or other mitigation approaches will be vital to ensure appropriate civilian use of former military installations. Most closed bases have significant environmental cleanup problems, and a careful strategy, which could include the federal government, states, local communities, and various components of the private sector, will be required to smooth the transition.

Q. GIFT BAN RULES

Earlier in the year, the Institute provided the delegation and its Advisory Board members with information on the interpretation of the new House rules restricting members and staff from receiving anything of value, including meals, from outside organizations. The new rules went into effect in January, but the House Ethics Committee did not issue its written interpretation of the rules until late March, causing some confusion in members' offices.

The rules placed new, stringent limitations on the gifts, food, and events that members of Congress could accept or attend as part of their official duties. Under the rules, a member is allowed to accept free attendance at an event, including accepting a meal, if: (1) the event is "widely attended;" (2) the invitation comes from the event's sponsor; and (3) attendance is related to the member's official duties. The Ethics Committee's new guidelines define "widely-attended" as an event where: (1) there is a "reasonable expectation that at least twenty-five persons," other than members and congressional employees, will attend; and (2) attendance at the event is open to individuals from throughout a given industry or profession, or those in attendance represent a range of persons interested in a given matter. A "sponsor" is the primary organizer of an event, and does not include a person or group who just contributes money to an event. Meetings with constituent organizations do not have to meet the above requirements, but the meeting or event must be "regularly scheduled," for example, an annual meeting, related to the representative's official duties, and open to all members of the constituent organization, as opposed to just officers or board members. (With the advice of the Ethics Committee, the Institute was able to determine by February that its Member breakfasts are considered "widely attended.")

R. OTHER IMPORTANT ISSUES

The Institute has also followed a number of other issues of interest to Californians and -- at the request and on the advice of members of the Congressional delegation, the Advisory Board and the Institute's Economic Advisory Council -- is examining future issues of interest. Among these various other important California issues are:

- _ intellectual property protections for California's entertainment and software industries
- _ ensuring adequate continuing assistance to the state for the effects of natural disasters
- _ the establishment of another National Science Foundation (NSF) earthquake research center (a consortium of California universities will submit a proposal due to NSF on October 15, 1996)
- _ the rebidding of contracts for NSF supercomputing centers (the San Diego Supercomputing Center is one of four in the nation)
- _ continued funding for the flat panel display consortium
- _ development of a commercial spaceport at Vandenberg Air Force Base

- _ additional and expanded manufacturing extension centers in California
- _ resolution of a wheat quarantine dispute with USDA in Southern California
- _ ultimate disposition of the Ward Valley site for a low-level radioactive waste depository
- _ the impact on California's petroleum industry of exporting Alaska North Slope oil
- _ the National Ignition Facility to be constructed at Lawrence Livermore National Laboratory
- _ federal support for fusion energy research (for further information on fusion research, refer to Section II at page 17).

The Institute is also considering examining the reauthorization of fast-track provisions for international trade agreements; the importance of the mortgage interest deduction to the state in the context of proposed tax changes; and the impact of various proposals on California's health care market.

II. INSTITUTE PRODUCTS AND SERVICES

A. MEMBER BREAKFASTS

In 1995 the Institute began a breakfast series with members of the California congressional delegation. The Institute invites its Washington-based Advisory Board representatives to attend a breakfast at which one or two members of the delegation brief the attendees on federal issues of importance to California. Since its inception, 15 members of the House, as well as Senator Dianne Feinstein have been guests of the Institute. Recently, our supporters have heard from Reps. Frank Riggs, Bob Filner, Steve Horn, and Anna Eshoo. Other participants have included Reps. David Dreier, George Brown, Chris Cox, Bob Matsui, Jerry Lewis, Vic Fazio, George Radanovich, Calvin Dooley, Nancy Pelosi, Sam Farr, and Buck McKeon.

The breakfasts provide an excellent forum for the members and the Institute's supporters to exchange information and views on federal policy issues under consideration by the Congress. The member breakfasts have been a great success and are strongly supported by our contributors.

B. BRIEFINGS

This year the Institute has increased the number of briefings it sponsors for the Congressional delegation. The briefings provide the members with up-to-the-minute information on legislative topics, as well as other policy matters. In addition to briefings actually sponsored, the Institute has helped inform delegation members, the news media and other colleagues about other briefings of interest. Over the last several months, the Institute has organized briefings on the following subjects.

1. IMMIGRATION POLICY

On September 10, the Institute joined the Population Resource Center and the Sunbelt Institute in co-sponsoring a seminar on immigration issues. Approximately 57 congressional staff and other interested parties heard from three experts on immigration policy. The three panelists were: Philip Martin, Ph.D., Professor of Agricultural Economics and Chair, Comparative Immigration and Integration Program, University of California at Davis; Jeffrey S. Passel, Ph.D., Director, Program for Research on Immigration Policy, The Urban Institute; and Mark Krikorian, Executive Director, Center for Immigration Studies.

Dr. Martin focused on new immigration patterns in California. He pointed out that in the mid-1960s migration to California was at a rate of 1500 persons per day, with the vast majority of immigrants coming from other U.S. states. Currently, migration to California runs at 1,000 per day, but the majority are foreign-born nationals of Mexico and the Philippines. He pointed out that part of the assimilation problem in California is due to the fact that there is no "average" immigrant, as there is an "average U.S.-born citizen." Today's immigrants are more likely to have college degrees than the average U.S. citizen, but, in addition, other immigrants are also more likely to have less than a high school education. Thus, the California immigrant today is either more educated or less educated than the average U.S. citizen.

Dr. Martin also stated that he believed the Seasonal Agricultural Worker (SAW) program initiated in the 1980s has been a major factor in increasing California's immigrant population and the corresponding demand for services. Under that program, one million of the six million Mexican working-age males became SAWs and moved with their families to California. In general, these immigrants were poorly educated, with only about five years of schooling, and on average had five to six children in the family. This influx happened at the same time that the recession was first being felt in California. Thus, the demand for increased services, such as elementary schools, hit at the worst possible time for California.

Dr. Martin also cautioned that proposals to deny U.S. citizenship to the children born in the U.S. of immigrants may have unintended consequences. He pointed out that by the year 2050 in Germany, where citizenship is denied the German-born children of immigrants, 30 percent to 60 percent of the population of Germany's six largest cities will be non-German.

Dr. Passel then briefed the audience on the interpretation of several studies estimating the costs of providing education to immigrants. He pointed out that the vast differences in estimated costs result from different assumptions used by the specific studies, and he cautioned that use of the figures should be tempered by knowledge of the assumptions made.

He stated that on one area there is general agreement: in California, the cost of educating undocumented immigrant children is approximately \$1.5 billion per year. Four studies, two done by California officials, one by the General Accounting Office and one by the Urban Institute, all reached about the same estimate. But he also pointed out that these studies estimated average costs. Eliminating education to undocumented immigrant children would not save California \$1.5 billion per year, he said, because the estimates include the costs associated with buildings and salaries that might not necessarily be eliminated if the number of students were reduced.

Mr. Krikorian spoke on the impact of the pending immigration bill on migration to the U.S. He stated that, if the bill is enacted, it will only affect the symptoms of immigration and not its causes. He opined that jobs are the magnet for immigration to the United States and until there is an effective, national verification program designed to determine worker eligibility with a minimum intrusion on privacy, migration will continue to increase. He pointed out that high levels of legal immigration result in high levels of illegal immigration, because of family ties and national networks. Thus, he believes that legal immigration must be reduced in order to decrease illegal immigration.

2. IMMIGRATION AND MIGRATION

This briefing was the second of two on immigration that the Institute, the PRC, and the Sunbelt Institute have hosted this year. The first was held on March 1, 1996. At that briefing, Dr. Charles Keeley of Georgetown University discussed the supply and demand forces that drive migration to the United States. He pointed out that there are patterns of migration, based on networks of families and prior refugee migrations, that encourage immigrants to seek entry into the U.S.

Dr. Sidney Weintraub, of the University of Texas, Austin and the Center for Strategic and International Studies, spoke on current and future immigration pressures from Mexico and Latin America. Dr. Weintraub discussed the depression experienced by Mexico last year and the pressure that put on its citizens to migrate, legally and illegally, to the United States. He stated that the success of current efforts to stop the flow of undocumented immigrants can only be measured over time. He also pointed out that there may be unintended consequences if all illegal traffic is halted, because Mexico is a major U.S. trading partner, and there is significant legal cross-border traffic.

Finally, Dr. Thomas Espenshade of Princeton University discussed undocumented immigration to the United States, since passage of the 1986 Immigration and Reform Act. He pointed out that even though about 30 illegal immigrants out of 100 are apprehended at the border, they try again to re-enter, and the vast majority make it into the United States by the second or third attempt. Once in the U.S. and working, the chances of being apprehended drop to about one percent. The Institute plans to co-host a third briefing on other immigration issues with the Population Resource Center in the future.

3. THE CALIFORNIA ECONOMY

In another Institute-sponsored briefing, representatives of the Center for Continuing Study of the California Economy (CCSCE) and the Center for the New West (CNW) discussed their report *California: A Twenty-First Century Prospectus* with an audience of California members, staff, news media and other interested parties. Commenting on the future of the California economy were Philip Burgess, president of CNW; Stephen Levy, report author and director of CCSCE; and Mark Dowling, a California Economy Fellow with the CNW. The speakers relayed encouraging findings about the economic opportunities available to the state, particularly in the areas of foreign trade, high technology, professional services, and entertainment. They noted, however, that for the economic prosperity to persist, the state needs to rebuild its infrastructure foundation of quality schools, universities, airports, ports, other transportation infrastructure, and water supplies. The panelists also pointed out that federal policies that encourage foreign trade, such as market access and intellectual property rights, as well as those that support technology, R&D, and basic research, would help state reach its economic potential.

4. NETDAY 96

The Institute also sponsored a briefing in February on NetDay96 given by representatives of the White House and Sun Microsystems. NetDay96 was the effort of a broad cross-section of California companies, universities, unions, nonprofits, and government entities to mount a state-wide volunteer effort to wire thousands of California schools for connection to the Internet. NetDay96 was held all across California on March 9 and was successful in making many California schools Internet-ready.

5. FUSION ENERGY RESEARCH

The Institute hosted a briefing on federal fusion issues and their impact on California in March. California is a world leader in fusion energy research. Various institutions and companies across California participate in federally-supported fusion research activities, including Lawrence Livermore National Laboratory, General Atomics, Lawrence Berkeley Laboratory, UCLA, U.C. San Diego, SAIC, Lockheed-Martin, Varian Associates, Westinghouse (Sunnyvale), Rockwell International, and various other universities (including UC campuses at Berkeley, Davis, Irvine and Santa Barbara, as well as Cal Tech and Stanford). Supporters on the Hill are requesting that this year's appropriation for fusion energy research be at least \$275 million. Three California experts on fusion energy research outlined the importance of federal fusion research programs to the state. Dr. E. Michael Campbell, Associate Director of Lawrence Livermore National Lab for Laser Programs, outlined the National Ignition Facility (NIF), which is to be constructed at Livermore. The NIF would use powerful lasers to ignite small fuel capsules, resulting in massive energy output. The multiple missions of a NIF include retaining nuclear scientific expertise under a nuclear test ban, reproducing astrophysical conditions, and, eventually, electrical energy production. The entire project will cost \$1.07 billion, with 75% of those funds to be invested in U.S. industry. A recent report found that two-thirds of vendors currently supporting Livermore's projects are located in California, and that NIF will create 3,320 jobs in the Bay Area. Dr. David Baldwin of General Atomics Corporation outlined the federal magnetic fusion energy program and its significance to California. General Atomics runs the DIII-D fusion facility, which is the most flexible tokamak in the world. Baldwin noted that federal fusion funding to California exceeds \$200 million per year, which supports jobs in industry, at universities, and at the state's three National DOE Laboratories. Dr. Charles Baker, U.S. Home Team Leader for ITER (the International Thermonuclear Experimental Reactor) and Associate Director - Fusion at U.C. San Diego, discussed ITER. ITER is a 4-way collaboration among the U.S., Japan, the European Union, and the Russian Republic to develop a large reactor capable of creating and sustaining a fusion burn for several minutes, thereby demonstrating the viability of fusion as an energy source. Dr. Baker noted that California institutions lead the U.S. ITER effort and play a major role in the technical work.

6. IMPACT OF BASE CLOSURES AND DEFENSE DOWNSIZING

The Institute sponsored a briefing at which Kevin McCarthy, Coordinator for California Research for the RAND Corporation, discussed a recently released report on the economic impact of base closures and defense industry downsizing in California. The study, funded by the Pentagon, indicates that there were somewhat fewer negative economic consequences to the reduction of base, aerospace and defense-related positions in California than had previously been predicted.

To determine the impact on communities in which military bases were closed, RAND studied the economic impacts on three such areas: George Air Force Base in San Bernardino County, the Fort Ord Army base in Monterey County, and Castle Air Force Base in Merced County. In Monterey County, Mr. McCarthy stated, the report concluded that the Fort Ord base closure resulted in a three percent reduction in population, a figure below the anticipated 15 percent. Additionally, unemployment in the area increased one percent as opposed to the projected seven percent, according to the study. In contrast to economic predictions of drastically reduced retail sales following base closures, sales rose by two percent following the closure. And contrary to

early predictions, both George and Castle air bases experienced increases, some sizeable, in population, retail sales, housing purchases and school enrollments.

In explaining these outcomes, the report outlines factors which limited the negative impacts of base closures. In many cases, military retirees would no longer shop at base stores, thereby contributing to rising retail sales. The departure of some spouses of military personnel who had worked in the private sector resulted in job opportunities for local residents. Finally, the development of commercial uses for base property resulted in job creation and economic opportunities. The report stresses the difficulty in developing anticipatory impact studies and encourages federal and local agencies to focus on analysis of already closed bases to assess economic-impact patterns. Mr. McCarthy stressed that the report should not be read as stating that no economic injury occurred. On the contrary, the defense shifts caused significant hardship on a great many individuals. Nevertheless, the RAND study concluded that the painful dislocation that was felt on an individual level did not result in a severe economic dislocation in the aggregate.

C. POLICY PAPERS

The Institute has prepared several research papers this year on federal policy issues. These papers are disseminated to the congressional delegation, the Advisory Board, and the media. Recently, the Institute has prepared reports on export controls, federal formula grant allocations, and the California-federal government balance of payments. Several more papers, on such topics as patterns of federal spending in California and federal transportation issues are planned in the near future.

Papers released to date this year include:

— "Export Administration Act of 1996" --The paper examines the proposed Export Administration Act of 1996 with particular attention paid to the potential California impacts of the legislation.

— "Federal Formula Grant Program: California Implications" --This report offers a general review of primary data elements used to determine federal formula grant allocations by state and assesses their California-specific implications.

— "*Balance of Payments Between California and the Federal Government: Fiscal Year 1995*" -- This report provides a detailed description and analysis of California's share of both the U.S. tax burden and federal expenditures to states and offers a clear picture of California's continuing status as a donor state.

— "*California's Microelectronics Industries and Federal Technology Policy*" -- Prepared by the Institute's Economic Advisory Council the paper examines the importance of the industry to California's economy and suggests several changes to federal tax and trade laws that would ensure the industry's continued growth.

— "*The National Governor's Association Medicaid Proposal: Overview and California Implications*" -- This paper analyzes the Medicaid proposal proffered by the National Governor's Association and points out several areas, including the

proposed formula and the treatment of immigrants, that would have a significant impact on the State.

— *"Usage of Poverty Data in Federal Formula Programs: California Implications"* -- This recently completed paper examines poverty data collected through the census, and points out the adverse effect on California of using a single national poverty threshold in determining poverty levels for funding purposes. It also examines the impact of using poverty data from the outdated census on the formula funds received in the state.

D. CALIFORNIA CAPITOL HILL BULLETINS

Since the fall of 1994, the Institute has prepared a weekly report of current activity on Capitol Hill which directly impacts our state. The *California Capitol Hill Bulletin* is published weekly during sessions of Congress, and occasionally during other periods. Since the beginning of this year, Institute staff has worked hard to increase the coverage and quality of the reporting.

We view our *California Capitol Hill Bulletin* as an opportunity to discern, translate and relay California's federal priorities within the California-Washington community. The Institute welcomes suggestions for input. The *Bulletin* is faxed to roughly 350 recipients, and more than 400 readers now receive it by electronic mail.

E. ELECTRONIC PRODUCTS

Late last fall, Sun Microsystems generously donated a high-powered Internet server to the Institute, providing a wide range of future applications. Initially, it has allowed greater and more immediate Internet access to Institute staff, and it serves as a platform for our recently-enhanced Internet account.

Very soon, the Sun server will act as a host server for the California Institute-Economic Advisory Council home page which is currently being developed at "www.calinst.org." In addition to Institute reports and other written products, a key feature of the home page will be a searchable database of California economic and other data. In the future, the Sun server and the Institute-EAC home page can be the basis for a variety of potential opportunities, such as an interactive sounding board for discussion of California-federal issues or perhaps, with further enhanced line speed, a touchpoint for video conferencing and multimedia distribution of selected Washington activity.