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First Look

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# May Revision Includes Some Key Advances, but There Is Still Significant Room for Additional Investment

On May 11, Governor Jerry Brown released the May Revision to his proposed 2018-19 state budget. The Governor forecasts revenues $8.0 billion higher – over a three-year window – than projected in January, mostly reflecting higher tax collections due to strong economic growth and stock market gains.

Most of the additional revenues are set aside to build up reserves, pay down budgetary debts, and make one-time investments in infrastructure. The May Revision provides $6.1 billion for reserves and paying down debt – $3.5 billion as constitutionally required by Proposition 2 (2014), with half deposited in the rainy day fund and half used to pay down debts – and an additional, discretionary $2.6 billion deposit to the rainy day fund. The Administration also sets aside $3.2 billion for other uncertainties in a separate reserve fund. State reserves would total $17.0 billion by the end of 2018-19. The May Revision also provides $2 billion in one-time investments in deferred maintenance of infrastructure.

The May Revision makes several improvements over the January proposal. It expands eligibility for the California Earned Income Tax Credit (CalEITC) to young adults and seniors who are currently excluded, broadening the reach and impact of this important credit. Other notable improvements include allocating some of the higher-than-expected revenues to one-time spending for addressing homelessness and providing mental health services. Like the January proposal, the May Revision calls for funding to fully implement the Local Control Funding Formula for K-12 education.

However, and especially in light of the significant discretionary funds available due to strong revenues, the May Revision leaves much room for additional investments in individuals, families, and communities across California. The revised budget does not include new proposals to address housing affordability or the large unmet demand for subsidized early care and education – two areas that make up the largest share of many household budgets. It also continues to underinvest in the welfare-to-work system (CalWORKs) and basic income support for low-income seniors and people with disabilities (SSI/SSP). And, while the revised budget maintains marginal increases for the state's higher education systems, it does so against a backdrop of increasing needs and decades of state disinvestment.

As the Governor and the Legislature work toward a budget agreement in the coming weeks, there is ample room to strike a better balance between saving for a rainy day and investing in Californians.

The following sections summarize key provisions of the Governor's revised 2018-19 budget. Please check the Budget Center's website (calbudgetcenter.org) for our latest commentary and analysis.

# May Revision Reflects an Improved Fiscal Outlook

The Governor's revised budget reflects an improved fiscal outlook, with General Fund revenues over the three-year "budget window," from 2016-17 to 2018-19, expected to be about $8.0 billion *higher* than projected in January. After accounting for transfers, which include loan repayments as well as required and *discretionary* transfers to the state's rainy day fund (the Budget Stabilization Account), General Fund revenues are expected to be $7.6 billion higher than projected in January.

The May Revision projects that all three major sources of General Fund revenues will be higher than in January, with personal income tax (PIT) revenues up by about $4.4 billion, sales and use tax (SUT) revenues up by $744 million, and corporation tax (CT) revenues up by over $2.5 billion. Higher PIT revenues reflect the combination of higher projected capital gains and wages, particularly among highly paid workers. Increased SUT revenues reflect, in part, greater business investment due to recent federal tax law changes, while higher CT revenues are due to several factors, including higher projected corporate profits and the repatriation of foreign earnings as a result of recent federal tax changes.

The Legislative Analyst's Office's (LAO) updated fiscal outlook projects significantly higher revenues than the Administration. Specifically, the LAO projects that General Fund revenues over the three-year budget window will exceed the Governor's January forecast by $10.8 billion – $2.7 billion higher than the Administration's May Revision projection. After accounting for transfers, the LAO projects that General Fund revenues will exceed the Governor's January forecast by $10.2 billion – $2.6 billion higher than the Administration's May Revision projection. These differences largely reflect the fact that the LAO expects PIT revenues to be $3.7 billion higher than does the Administration, largely due to higher capital gains and wages. The LAO's higher PIT revenue projection is offset by lower projected SUT and CT revenues (by $757 million and $88 million, respectively).

The Governor's revised budget continues to caution that the state's improved fiscal outlook is subject to a number of risks that the Administration believes pose greater threats now than in January. These include the risk of a national recession coming at a time when many people have yet to fully recover from the prior downturn; the risk of an increase in import tariffs, which could hit California particularly hard since many of the state's businesses depend on international trade; and the risk of a stock market correction, which could disproportionately affect California since stock market gains over the past decade have been driven by technology companies in the state. In addition, the Administration notes that while its forecast assumes that recent federal tax changes will temporarily boost the national economy, these gains will likely come at a cost over the long-term by dampening future economic growth and exacerbating income inequality.

# The Governor's Revised Proposal Continues to Maximize the State's Rainy Day Fund and Build Up State Reserves

California voters approved Proposition 2 in November 2014, amending the California Constitution to revise the rules for the state's Budget Stabilization Account (BSA), commonly referred to as the rainy day fund. Prop. 2 requires an annual set-aside equal to 1.5% of estimated General Fund revenues. An additional set-aside is required when capital gains revenues in a given year exceed 8% of General Fund tax revenues. For 15 years – from 2015-16 to 2029-30 – half of these funds will be deposited into the rainy day fund, and the other half will be used to reduce certain state liabilities (also known as "budgetary debt").

Based on the Governor's revenue projections for 2018-19, Prop. 2 would constitutionally require the state to deposit $1.75 billion into the BSA (and to use an additional $1.75 billion to repay budgetary debt). In addition, the Governor proposes to make an optional, one-time supplemental transfer of $2.6 billion from the General Fund to the BSA. (The total transfer to the BSA would be $4.4 billion: $1.75 billion as required by the state Constitution, plus the $2.6 billion supplemental transfer.) As a result, the BSA would grow to a total of $13.8 billion by the end of the 2018-19 fiscal year.

Under the scenario outlined by the Governor, the BSA could reach its constitutional maximum of 10% of General Fund tax revenues in 2018-19. When this limit is reached, Prop. 2 requires that any additional dollars that would otherwise go into the BSA be spent on infrastructure, including spending on deferred maintenance. In other words, Prop. 2 prohibits these additional dollars from being allocated to ongoing programs and services.

The BSA is not California's only reserve fund. Each year, the state deposits additional funds into a "Special Fund for Economic Uncertainties" (SFEU). For 2018-19, the Governor proposes to leave $3.2 billion in this fund. Including this fund, the Governor's proposal would build state reserves to a total of $17.0 billion in 2018-19.

One additional implication of the Governor's proposal is that the $2.6 billion supplemental transfer to the BSA may not be readily available to help the state meet needs created by future developments, such as federal budget cuts. In order to access the BSA funds, the Governor would need to declare a "budget emergency," defined by Prop. 2 as a disaster or extreme peril, or insufficient resources to maintain General Fund expenditures at the highest level of spending in the three most recent fiscal years, adjusted for state population growth and the change in the cost of living. After a budget emergency has been declared, a transfer to the BSA could be suspended or reduced only through a bill passed by a majority vote of each house of the Legislature.

## May Revision Prioritizes One-Time Infrastructure Investments

The Governor's revised budget calls for $2 billion in one-time infrastructure investments to address deferred maintenance of state facilities. The Administration estimates that the state has $20 billion in liabilities for deferred maintenance, not including roads and highways. The proposed funding includes $630 million for improvements to state office buildings in Sacramento; allocations for state higher education systems – the California Community Colleges system ($143.5 million), the California State University ($100 million), and the University of California ($100 million); $174 million for state corrections facilities; $100 million for flood control and levee improvements; $100 million for courts; $100 million for state hospitals; and $100 million for state park facilities, in addition to other allocations across a range of state agencies and facilities.

## May Revision Strengthens the CalEITC

The Governor's May Revision proposes to strengthen the California Earned Income Tax Credit (CalEITC) – a refundable state tax credit that boosts the incomes of low-earning workers and their families, helping them afford necessities. Specifically, the revised budget:

- **Extends the CalEITC to low-earning young adults and seniors who are currently ineligible for the credit.** Since the CalEITC was created in 2015, it has conformed to the age requirements of the *federal* EITC. This means that workers with incomes low enough to qualify for the state credit and who are not living with qualifying children cannot benefit from the CalEITC if they are younger than age 25 or older than age 64. The May Revision eliminates this age requirement, allowing childless adults and non-custodial parents who are just starting out in the workforce, as well as those who are working beyond the traditional retirement age, to qualify for this state tax credit beginning in tax year 2018. Last year, Minnesota lowered the age requirement for that state's EITC to 21, and last month Maryland's Legislature approved, and the Governor is expected to sign, legislation to lower the age limit for that state's EITC to 18. In addition, several federal proposals in recent years have called for changing the federal EITC age requirements for childless workers and noncustodial parents.
- **Raises the income limit to qualify for the CalEITC.** The 2017-18 budget increased the income limit to qualify for the CalEITC for workers with qualifying children to about $22,300 – equivalent to just over a full-time, year-round salary at a $10.50-per-hour minimum wage. This minimum wage applied to workers at large businesses in 2017 and has applied to workers at small businesses since January 2018. The May Revision further raises the CalEITC income limit for workers with qualifying dependents to $24,960 – the equivalent of a full-time, year-round

salary at a $12-per-hour minimum wage, which will apply to workers at large businesses in 2019 and at small businesses in 2020. Last year's budget also increased the CalEITC income limit for workers without qualifying children to about $15,000, and the May Revision further boosts this limit to $16,800. Both of these changes also would go into effect beginning in tax year 2018.

Together, these two changes to the CalEITC are expected to benefit over 700,000 households and reduce General Fund revenues by about $60 million in 2018-19, according to the Administration.

As in January, the Governor's proposal does not provide any additional funds to maintain or expand community-based efforts to promote the CalEITC in order to boost credit claims. The May Revision also does not appear to provide any state funds to expand free tax preparation services for low-income tax filers.

## May Revision Proposes New Funding to Address Homelessness

California has nearly 25% of the nation's population of homeless individuals, with an estimated 135,000 homeless residents as of January 2017. More than two-thirds of California's homeless residents are unsheltered, sleeping in locations such as in a vehicle, in a park, or on the street.

The Governor proposes using some of the higher revenues reflected in the May Revision to address homelessness, including significant new one-time investments as well as some smaller new ongoing expenditures. Specifically, the May Revision:

- **Allocates $250 million General Fund to one-time Emergency Homeless Aid Block Grants.** These grants would be administered through existing Continuum of Cares (local homelessness planning bodies) and would be available to localities that declare a local shelter crisis. Grants could be used for activities such as emergency housing vouchers, rapid re-housing, construction of emergency shelters, or use of armories to house homeless individuals.
- **Increases funding for two CalWORKs programs that assist homeless families.** CalWORKs is California's welfare-to-work program. The CalWORKs Housing Support Program, which helps families secure permanent housing, would receive an additional $24.2 million General Fund in 2018-19 (for total funding of $71.2 million), increasing to an additional $48 million in 2019-20 and beyond (for total ongoing funding of $95 million annually). The CalWORKs Homeless Assistance Program, which provides up to 16 days per year of temporary housing for homeless CalWORKs participants via vouchers for temporary shelter or hotels/motels, would also receive an additional $8.1 million General Fund in 2018-19, increasing in 2019-20 to an additional $15.3

million in ongoing funding. This increased funding would be used to raise the daily voucher rate, so that a family of four would be allowed $85 per night rather than the current $65 per night, beginning January 1, 2019.

- **Dedicates $15 million General Fund in one-time funding over three years for a pilot program to prevent and address homelessness among seniors.** The Home Safe Pilot Program would be housed within Adult Protective Services and would be available to counties that provide local matching funds.
- **Increases General Fund dollars on a one-time basis to address homelessness among domestic violence survivors and youth.** The Office of Emergency Services would receive an additional $10 million to support domestic violence shelter services and an additional $1 million to support homeless youth shelters.
- **Makes a one-time $50 million General Fund allocation to the Department of Health Care Services for services for homeless individuals with mental illness.** Counties would be able to use the funds for multi-disciplinary teams providing intensive outreach, mental health treatment, and related services, modeled on the types of programs that the state funded in earlier years through Assembly Bill 2034 of 2000 and its precursor Assembly Bill 34 of 1999. (Note: This allocation also is discussed in the later section on funding for mental health.)

The Governor's revised budget also proposes $500,000 General Fund to expand staffing and provide ongoing support for the Homeless Coordinating and Financing Council, which was created in 2016 to identify and oversee implementation of homeless programs at the state level. The Council would be elevated from its current location within the Department of Housing and Community Development to its own department-level status within the Business, Consumer Affairs, and Housing Agency.

A final homelessness proposal in the May Revision does not allocate new funding, but rather proposes that the No Place Like Home program be placed on the November 2018 ballot for voter validation. This program was developed as a legislative proposal and dedicates $2.0 billion in bond proceeds, to be repaid with funds from the Mental Health Services Act (MHSA), for permanent supportive housing for individuals with mental illness who are homeless or at risk of homelessness. Though the Governor signed the legislation in July 2016, it has not been implemented due to a legal challenge asserting that MHSA funds cannot be used for this purpose. Voter validation of this use of MHSA funds would allow the program to proceed. The Governor further proposes a $1.2 million General Fund loan to the Department of Housing and Community Development in order to issue an initial Notice of Funding Availability prior to November so that if voters approved the No Place Like Home measure, the first funding awards could be announced by December. The November ballot will also include the $4 billion bond for affordable housing that was part of the legislative housing package signed in September 2017.

With the No Place Like Home proposal on the ballot as well, voters will be asked to approve two major housing-related bond measures in November.

Homelessness is a key area the Governor identifies for investment of additional revenues in the May Revision, with a total of $358.8 million General Fund in increased spending proposed for 2018-19 as well as a $64.1 million proposed increase in ongoing spending for 2019-20 and beyond, in addition to the No Place Like Home proposal. While representing a significant boost over current state spending on homelessness, the Governor's proposal falls short of the investment proposed by the Legislature, where proposals to dedicate up to $1.5 billion (in the Assembly) and $2.0 billion (in the Senate) to address homelessness and develop affordable housing are pending. Notably, the Governor does not propose increased state investment in affordable housing more generally, despite noting that California's median home price is now more than twice the national price.

## Governor's Revised Budget Proposes No New Funding to Address Needs of Immigrants

California has the largest share of immigrant residents of any state, and immigrants make up a third of the state's workforce. Given the prominence of immigrants in California's population and the state's economy, recent and ongoing federal actions to limit immigration and aggressively enforce immigration laws particularly impact California. The Governor's January budget included a continuation of increased funding for legal services for immigrants, to assist undocumented unaccompanied minors, and for the Attorney General's office to address federal actions. The May Revision retains these expenditures but proposes no additional new spending to address the needs of immigrants. This contrasts with the priorities of the Legislature, which has proposed several important expansions of services and supports for undocumented immigrants, including extending Medi-Cal eligibility to undocumented young adults and extending eligibility for the CalEITC to immigrant workers who file taxes with an Individual Taxpayer Identification Number (ITIN).

## Increased Revenues Boost the Minimum Funding Level for Schools and Community Colleges

Approved by voters in 1988, Proposition 98 constitutionally guarantees a minimum level of funding for K-12 schools, community colleges, and the state preschool program. Changes in state General Fund revenues tend to affect the Prop. 98 guarantee, and the May Revision's estimates of 2016-17, 2017-18, and 2018-19 revenues are up compared to those made in January's budget proposal. As a result, the May Revision assumes a 2018-19 Prop. 98 funding level of $78.4 billion, $68 million above the level assumed in the Governor's proposed budget. The May Revision also assumes Prop. 98 funding levels of

$75.6 billion in 2017-18 and $71.6 billion in 2016-17, up $407 million and $252 million, respectively, from the levels assumed in January.

The May Revision proposes to change how the final funding level guaranteed under Prop. 98 is certified. Despite the requirement under current law to certify a final calculation of the annual Prop. 98 guarantee within nine months of the end of a fiscal year, the final Prop. 98 funding level has not been certified since 2008-09. The May Revision proposes establishing "a revised certification structure" that would include certifying the Prop. 98 guarantee for 2009-10 through 2015-16 as well as creating a new mechanism intended to certify the final Prop. 98 funding level more quickly to "increase certainty around the payment of future certification settlements, and provide the state with additional budgeting flexibility."

The largest share of Prop. 98 funding goes to California's school districts, charter schools, and county offices of education (COEs), which provide instruction to approximately 6.2 million students in grades kindergarten through 12. The May Revision proposes to increase funding for the state's K-12 education funding formula – the Local Control Funding Formula (LCFF) – and, like the January proposal, would provide sufficient dollars to reach the LCFF's target funding level in 2018-19. The revised budget also increases funding to pay off outstanding state obligations to school districts. The May Revision:

- **Provides an additional $320 million, for a total of $3.2 billion, to fully implement the LCFF.** The LCFF provides school districts, charter schools, and COEs a base grant per student, adjusted to reflect the number of students at various grade levels, as well as additional grants for the costs of educating English learners, students from low-income families, and foster youth. The May Revision's proposal to increase LCFF funding is sufficient for all K-12 school districts to reach a target base grant in 2018-19 (all COEs reached their LCFF funding targets in 2014-15).
- **Boosts one-time funding by $286 million, for a total of $2.0 billion, to reduce mandate debt the state owes to schools.** Mandate debt reflects the cost of state-mandated services that school districts, charter schools, and COEs provided in prior years, but for which they have not yet been reimbursed.
- **Increases funding by $27.3 million for the English Language Proficiency Assessment for California (ELPAC).** The May Revision proposes to use these one-time dollars to convert the ELPAC to a computer-based assessment from one that is paper-based as well as to develop a computer-based alternative for children with exceptional needs.
- **Provides $15 million in one-time funding to expand the state's Multi-Tiered Systems of Support (MTSS).** The revised budget provides funding to the Orange County Department of Education jointly with the Butte County Office of Education to contract with a to-be-identified

California higher education institution to expand the state's MTSS with the goal of fostering positive school climate in both academic and behavioral areas.

- **Provides $13.3 million in one-time funding to create the Community Engagement Initiative.** The May Revision proposes to create this new initiative to build the capacity of communities and school districts to deepen community engagement with the goal of improving student outcomes.
- **Increases the cost-of-living adjustment (COLA) for non-LCFF programs.** The revised budget provides an additional $10.6 million to fund a 2.71% COLA for several categorical programs that remain outside of the LCFF. This is an increase from the 2.51% COLA proposed in the January budget.

## Administration Proposes Adjustments to New Funding Formula for California Community Colleges and Offers Details on Online Community College

A portion of Proposition 98 funding provides support for California's community colleges (CCCs), which help prepare over 2 million students to transfer to four-year institutions as well as obtain training and employment skills. The Governor's January budget proposal called for a new funding formula for CCC general-purpose apportionments and the establishment of a fully online community college. The May Revision proposes several adjustments to the new CCC funding formula and provides more details on the online community college proposal. The updated spending plan:

- **Provides an additional $104 million for the new CCC funding formula and adjusts apportionments.** The May Revision includes a revised "hold harmless" provision that maintains funding for all CCC districts during 2018-19 and 2019-20 at no less than the amount of funding received in 2017-18, and provides $104 million in one-time discretionary funds for districts whose year-over-year increase in general-purpose apportionment funding would be less than 2.71%. The proposal also adjusts the apportionments to the three grant components: the base grant, the supplemental grant, and the student success incentive grant. The revision allocates funding as follows:
  - A 60% *base grant* for each district would be calculated using a three-year rolling average of the per-Full-Time Equivalent Student (FTES) funding rate. The January proposal had called for allocating 50% of the funding to the base grant.
  - A 20% *supplemental grant* would include considerations for: the number of low-income College Promise Grant fee waiver recipients over the age of 25; specified undocumented students qualifying for resident tuition; and all Pell grant recipients. The

January proposal had called for allocating 25% of the funding to the supplemental grant.
  - A 20% *student success incentive grant* would consider the outcomes of economically disadvantaged students, student transfer rates to four-year institutions, wages of students who have completed a degree or certification program, and other factors. The January proposal had called for allocating 25% of the funding to this grant.

- **Outlines several provisions for the fully online community college.** The May Revision offers more detail regarding the online college's governance, collective bargaining, student success measures, and curriculum. The May Revision notes that the CCC Board of Governors would serve as the governing board of the online community college and that faculty and classified employees of the college would be represented by an existing CCC district for the purposes of collective bargaining. The plan also indicates that in the third year of operation, the online college would provide policymakers with a status report on student outcomes and outreach efforts for working adults. The revised spending plan also clarifies that the intent of the online college is to offer unique content that is not available at local campuses.
- **Decreases one-time funding for deferred maintenance and other CCC expenses by $131.7 million.**
- **Increases apportionments for CCCs by $73.7 million.** This increased Prop. 98 funding includes $46.9 million for FTES funding earned back by districts that had declining enrollment in the previous three-year cycle, $14.9 million to reflect unused enrollment growth funding in 2016-17, and $11.9 million to reflect a 2.71% cost-of-living adjustment (COLA) for apportionments.
- **Consolidates the Student Success and Support Program, the Student Success for Basic Skills Program, and the Student Equity Program into a single block grant.** These three categorical programs, which target similar communities of students, would be integrated with the intent of increasing program flexibility.

## Governor Maintains Modest Funding Increases for CSU and UC

The Governor's revised budget maintains the funding levels proposed in January for the California State University (CSU) and the University of California (UC). The revision also proposes a new stipulation for addressing potential tuition increases at both institutions. Specifically, the revised spending plan:

- **Maintains the Governor's January proposal to increase CSU funding by $92.1 million.** The Administration expects the CSU to use these funds to make progress toward the CSU Graduation Initiative, which aims to increase graduation rates and eliminate opportunity and achievement gaps. The CSU is requesting a $283 million increase – $191 million higher than what the Governor proposes.

- **Maintains the Governor's January proposal to increase UC funding by $92.1 million.** UC is requesting $140 million above the Governor's proposal for 2018-19. In addition, the 2017-18 budget package conditioned the release of $50 million in funding on the University providing evidence of meeting several budget and enrollment expectations by May 1, 2018. The Governor's May Revision assumes the release of those funds, pending the UC Board of Regents approval of several remaining report items demonstrating that the expectations have been met.
- **Proposes a new stipulation for addressing the potential impact of tuition increases on Cal Grant and Middle Class Scholarship programs.** The Governor's January proposal did not reflect funding to cover increased Cal Grant costs that would result from potential tuition hikes at the CSU and the UC. The May Revise suggests reducing the primary appropriations for each system by the amount of estimated Cal Grant and Middle Class Scholarship program cost increases if tuition is increased in 2018-19.
- **Increases admission goals for private nonprofit institutions to maintain the maximum Cal Grant tuition awards.** The Governor's proposal maintains the maximum award for new students attending private nonprofits at $9,084, but adjusts the annual admissions goal for students who have earned an Associate Degree for Transfer (ADT) required to maintain the maximum award level. The revised spending plan requires the private nonprofit sector to admit at least 2,000 ADT students in 2018-19. The May Revision proposes increasing the admission goals in 2019-20 and 2020-21 to 3,000 students and 3,500 students, respectively – 500 more than the January proposal.

## Revised Budget Boosts State Investments in Mental Health Services

Federal, state, and county support for mental health services in California totals about $8 billion per year. Even with this substantial funding, "many challenges remain in the mental health system," the May Revision notes. To help address these challenges, the revised budget includes new state funding aimed at strengthening efforts to improve outcomes for people living with a mental illness. Specifically, the May Revision:

- **Proposes to repay $253.9 million, plus interest, that is owed to counties – an amount that the Governor "expects" counties to use to support mental health services for youth, "with an emphasis on teens."** This payment would settle a state debt related to certain mental health services for children that counties provided – as required by the state – from 2004 to 2011. The state failed to reimburse the counties for these services at the time.

- **Provides one-time funding of $55 million to support psychiatric graduate medical education programs.** This funding would support programs serving Health Professional Shortage Areas or Medically Underserved Areas in rural areas of the state.
- **Provides one-time funding of $50 million to support county outreach and treatment for homeless persons with mental illness.** These efforts would be "expected to result in earlier identification of mental health needs, prevention of criminal justice involvement, and improved coordination of care for this population at the local level," according to the May Revision. Counties would be encouraged to match these state dollars with local as well as federal dollars, where appropriate.

## Revised Budget Includes No Major Changes to State Health Policy

Recently, state lawmakers have expressed interest in expanding health care coverage options for undocumented immigrants as well as in boosting the affordability of coverage for middle-income families who purchase health plans on the individual market and face high premiums and cost-sharing. The Governor's revised budget does not address either of these issues and focuses instead on maintaining the state's existing health care commitments. Nonetheless, the May Revision does highlight two notable changes from the Governor's initial budget proposal in January. The revised budget:

- **Reflects reduced General Fund costs for CHIP.** The Children's Health Insurance Program (CHIP) is a joint federal-state program that supports health insurance for almost 9 million children throughout the US during the course of a year, including over 2 million in California. Since late 2015, the federal government has paid 88% of CHIP costs in California; previously, the federal share was set at 65%. In January, the Governor assumed that Congress would immediately revert to the 65/35 sharing ratio when it reauthorized CHIP. However, Congress ultimately struck a 10-year deal that maintains the 88/12 sharing ratio through federal fiscal year (FFY) 2019 (which ends September 30, 2019). The federal share of CHIP costs will step down to 76.5% in FFY 2020 and then to 65% from FFY 2021 through FFY 2027. Compared to the Governor's January proposal, the May Revision estimates combined General Fund savings of nearly $900 million in 2017-18 and 2018-19 due to Congress' decision to temporarily extend the more generous federal sharing ratio.
- **Provides an increase of $70.4 million ($21.8 million General Fund) in 2018-19 to authorize treatment for all Medi-Cal patients ages 13 and older with Hepatitis C.** The May Revision

indicates that treatment would be provided "regardless of liver fibrosis stage or co-morbidity," except for people who are expected to live less than one year.

## Governor Maintains Proposal for CalWORKs Home Visiting Pilot Initiative, but Does Not Expand Eligibility

The California Work Opportunity and Responsibility to Kids (CalWORKs) program provides modest cash assistance for 830,000 low-income children while helping parents overcome barriers to employment and find jobs. CalWORKs is the state's version of the federal Temporary Assistance for Needy Families (TANF) program.

In January, the Governor proposed allocating $158.5 million in one-time TANF funds for a new CalWORKs home visiting pilot initiative, with $26.7 million in TANF dollars allocated in the 2018-19 state budget year and the remaining $131.8 million to be available through calendar year 2021. The proposed initiative would provide up to 24 months of home visiting for first-time CalWORKs parents under age 25, who would have to be either pregnant or parenting a child under age 2. (Participation in this new program would be voluntary.) These eligibility requirements would exclude many families, as the average CalWORKs household has two children and is headed by a 34-year-old caregiver. In the May Revision, the Governor does not propose expanding eligibility, as has been proposed by advocates.

## May Revision Does Not Provide Funding for Additional Subsidized Child Care Slots With State or Federal Funds

State policymakers have taken steps in recent years to restore funding to California's child care and development system, which was cut dramatically during and after the Great Recession. Despite these incremental increases, in the current fiscal year (2017-18) overall funding for these programs remains more than $500 million below pre-recession levels, after adjusting for inflation. As a result, the state is currently providing about 67,000 fewer subsidized slots for working families struggling to make ends meet.

The May Revision does not increase funding to provide additional families with subsidized child care, despite the state's higher-than-expected revenues. The proposal maintains provisions included in the Governor's January proposal, such as boosting reimbursement rates for providers that contract directly with the state; creating a "hold harmless" provision for voucher-based providers to ensure that they would not see a decrease in payment rates; and adding 2,959 full-day state preschool slots for Local

Education Agencies (LEA), as stipulated in a multiyear plan included in the 2016-17 budget agreement. In addition, the May Revision:

- **Provides $104 million General Fund for CalWORKs Stage 2 and Stage 3 caseload adjustments.** The 2017-18 budget agreement included $25 million to increase the decade-old income eligibility limits and implement a 12-month eligibility period. Based on communication with the Administration, the May Revision adjusts funding for CalWORKs Stage 2 and Stage 3 child care to reflect a larger-than-expected increase in caseload due to these provisions.
- **Adjusts funding for the proposed Inclusive Early Education Expansion Program by $42.2 million Proposition 98.** The Governor's initial budget proposal included one-time funding for a new grant program to increase access to inclusive subsidized early care and education programs by funding "infrastructure costs" such as facilities renovation or professional development. The January proposal included $42.2 million in Temporary Assistance for Needy Families (TANF) funds, which the state may not have been able to use for this type of program. The May Revision maintains the proposed funding of $167.2 million by backfilling TANF funds with Proposition 98 funds. This means that only LEAs are eligible to apply for the grant program, but the Administration is encouraging partnerships with non-LEAs. Grant funds would not be available to provide additional subsidized slots.

Finally, the May Revision does not reflect increased federal funding for subsidized child care that was part of the omnibus spending legislation for the 2018 federal fiscal year, signed by President Trump this past March. California is expected to receive about $232 million in additional federal funds. The Administration does not plan to include these funds in the 2018-19 budget agreement, but will instead conduct a stakeholder process in order to determine how to best use the funding in the future.

## Revised Budget Makes No Investments in CalWORKs or in SSI/SSP Cash Assistance for Low-Income Californians

The Governor's revised budget includes no new investments in two key programs that provide basic income support to help low-income families, seniors, and people with disabilities pay for basic living expenses, such as housing. Specifically, the May Revision:

- **Does not increase CalWORKs grants.** The California Work Opportunity and Responsibility to Kids (CalWORKs) program provides modest cash assistance for 830,000 low-income children while helping parents overcome barriers to employment and find jobs. The May Revision does not propose to reinstate the annual state cost-of-living adjustment (COLA) or otherwise increase CalWORKs grants – though such changes would be needed in order to reverse the state cuts that were made during and following the Great Recession. The maximum CalWORKs grant for a family of three is equal to just 41% of the federal poverty line (FPL), leaving it well below the deep-poverty threshold (50% of the FPL).

- **Does not increase the state (SSP) portion of SSI/SSP grants.** Supplemental Security Income/State Supplementary Payment (SSI/SSP) grants help well over 1 million seniors and people with disabilities to pay for housing, food, and other basic necessities. Grants are funded with both federal (SSI) and state (SSP) dollars. State policymakers deeply cut the SSP portion during and following the Great Recession and have provided only one COLA in recent years – a modest 2.76% boost that took effect in January 2017. The state has not provided an increase since then, and the Governor's revised budget would freeze SSP grants at their current level for another year.

## May Revision Highlights Modest Decline in Incarceration, Includes New Funding to Expand Hepatitis C Treatment

Currently, more than 129,200 people who have been convicted of a felony offense are serving their sentences at the state level – down from a peak of around 173,600 in 2007. Most of the individuals who are currently incarcerated – over 114,600 – are housed in state prisons designed to hold slightly more than 85,000 people. This level of overcrowding is equal to 134.7% of the prison system's "design capacity," which is below the prison population cap – 137.5% of design capacity – established by a 2009 federal court order. (In other words, the state is in compliance with the court order.) In addition, California houses over 14,600 individuals in facilities that are not subject to the court-ordered cap, including fire camps, in-state "contract beds," out-of-state prisons, and community-based facilities that provide rehabilitative services.

The sizeable drop in incarceration has resulted largely from a series of policy changes adopted by state policymakers and the voters in the wake of the federal court order. The most recent reform was Proposition 57, a 2016 ballot measure that provided state officials with new tools to address ongoing overcrowding in state prisons. Prop. 57:

- Gave the California Department of Corrections and Rehabilitation (CDCR) broad authority to award sentencing credits to reduce the amount of time that people spend in prison.
- Requires parole consideration hearings for state prisoners who have been convicted of a nonviolent felony and have completed the full term for their primary offense.
- Requires juvenile court judges to decide whether a youth accused of a crime should be tried in adult court.

With the implementation of Prop. 57, the average daily number of incarcerated adults is projected to drop from 130,197 in 2017-18 to 126,890 in 2018-19 (a 2.5% decline), according to May Revision estimates. Moreover, the Administration anticipates that by reducing the number of incarcerated adults, Prop. 57 – along with other recent criminal justice reforms – will allow the state to end the use of out-of-state prison facilities by the end of January 2019. Currently, more than 3,200 Californians are housed in facilities in Arizona and Mississippi because there is no room for them in state prisons given the court-imposed prison population cap.

The May Revision contains a significant proposal to spend $317.4 million General Fund over the next three years, starting in 2018-19, to expand Hepatitis C treatment to all state prisoners who are infected with the virus. Currently, about 22,000 incarcerated adults carry the virus, with approximately 2,300 receiving treatment in the current year. The May Revision proposal would allow the remaining 19,700 prisoners to receive treatment over the next three years, at a state cost of $105.8 million per year.