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First Look

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May Revision Calls for a State EITC and Invests in Education, but Leaves Some Key Supports Diminished

On May 14, Governor Jerry Brown released the May Revision to his proposed 2015-16 state budget. With increased state revenues – partly the result of the Proposition 30 tax increases approved by voters in 2012 – and a growing economy, the Governor proposes to spend $115.3 billion from the state's General Fund in 2015-16. The May Revision estimates $6.7 billion in higher General Fund revenues across the three-year "budget window" (2013-14, 2014-15, 2015-16) compared to January's forecast.

In a significant advance for Californians, the Governor's revised budget calls for creating a state Earned Income Tax Credit (EITC) as an "add on" to the successful federal EITC. The state credit targets individuals and families with very low incomes, reducing economic hardship for up to 2 million Californians.

The May Revision also reflects increases in funding to meet certain constitutional obligations. The revised budget includes $68.4 billion for schools and community colleges in 2015-16, which reflects the minimum funding guarantee under Proposition 98. This is $2.7 billion above January's projections and represents a significant increase from the post-recession low point of $47.3 billion in 2011-12. Under Proposition 2, the rainy day fund measure approved by voters last year, the May Revision sets aside $3.7 billion in 2015-16 for paying down budgetary debt and building the state's reserve.

The Governor's revised budget also holds tuition levels flat at the state's universities, while providing some additional funding for CSU and UC, and calls for providing health care and other safety net services to eligible undocumented immigrants who qualify for "deferred action" status under President Obama's executive actions.

While the May Revision moves the state forward in some important ways, there is much that it does not do in terms of rebuilding essential public services battered by prior years' cuts. As the Governor and legislators work toward a final budget, they could pursue various options: continuing to increase support for subsidized child care and preschool, boosting assistance for low-income seniors and people with disabilities, strengthening the state's welfare-to-work program, and reversing prior cuts to Medi-Cal.

The following sections summarize key provisions of the May Revision. In the upcoming days and weeks, the Budget Center will prepare in-depth analyses of major proposals contained in the revised budget. Please check the Budget Center's website (calbudgetcenter.org) for our latest information and analysis.

Revenue Projections Even Higher in May Revision

The May Revision projects $6.7 billion more in General Fund revenues over the three-year "budget window" from 2013-14 to 2015-16 than had been projected in the Governor's January budget proposal. In particular, 2014-15 revenues are now projected to be significantly higher than previously forecast, due in large part to higher-than-expected personal income tax (PIT) receipts, but also to higher corporate income tax and sales tax receipts.

Higher PIT revenues have resulted from strong growth in tax withholding, as well as growth in capital gains and partnership income. The Administration notes that withholding growth was significantly stronger than overall wage growth in 2014, indicating that more of the wage gains have likely gone to high-income earners, who pay higher tax rates. The May Revision also extends by one year, to 2017, the point at which the Administration assumes capital gains' share of personal income will come down to "normal levels."

California's Economy Is Improving Faster Than Anticipated, but Still Leaving Many Behind

The state's improving revenue outlook is partly a reflection of an economy that is improving faster than anticipated. The Administration forecasts that the state's average unemployment rate will be 6.5 percent in 2015, lower than the average 6.9 percent unemployment rate forecast one year ago. As this year's May Revision notes, job growth is stronger in California than in the nation as a whole, and the state's economy is expected to continue adding jobs at a steady pace.

This improved economic outlook is welcome news, but California's economy still faces substantial challenges. The May Revision notes a number of risks to future economic growth, including an uncertain stock market and the potential for further economic slowdowns for California's trade partners, such as European nations and China.

On top of these risks to "the fundamentals" of the California economy, many workers still face a persistently difficult labor market. While California's overall unemployment rate was 6.5 percent as of March 2015, this state average masks substantial variation across California regions. Colusa County's unemployment rate was 20.5 percent, and counties throughout the San Joaquin Valley have unemployment rates in the double digits. Moreover, poverty remains high (see text box on page 9), and wage and income growth continue to be unevenly shared.

May Revision Estimates $3.7 Billion for Rainy Day Fund and Debt Repayment

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. Proposition 2 requires an annual set-aside equal to 1.5 percent of estimated General Fund revenues. An additional set-aside is required when capital gains revenues in a given year exceed 8 percent 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").

The May Revision estimates $3.7 billion in Proposition 2 transfers – $1.85 billion to the BSA and $1.85 billion to repaying budgetary debt. This is an increase from the Governor's January proposal, which assumed the Proposition 2 set-aside would total $2.4 billion ($1.2 billion to the BSA and $1.2 billion to repaying budgetary debt). The additional revenues that are available for repaying budgetary debt in 2015-16 would go toward repaying loans from special funds ($537 million on top of the Governor's January proposal of $965 million) and helping the University of California (UC) pay down its unfunded pension liability ($96 million).

Prior to the passage of Proposition 2, the BSA had grown to $1.6 billion. The addition of $1.85 billion in Proposition 2 transfers would bring the rainy day fund balance to nearly $3.5 billion by the close of 2015-16.

May Revision Includes a Refundable Tax Credit for Low-Income Californians

The May Revision includes a targeted state Earned Income Tax Credit (EITC) designed to reach families with very low incomes. The proposed state credit would be an "add on" to the successful federal EITC, which reduces economic hardship for more than 3 million low- and moderate-income households in California. This new state credit would be refundable, meaning that families would receive the credit even if they do not earn enough to owe state income taxes. Eligibility for the credit and the size of the credit would both be determined by income and family size.

This state credit would be limited to families with very low incomes, up to $13,869 for some families, and reach only a portion of the families who receive the federal EITC, which reaches some households with incomes up to $53,266. Families would receive a state credit worth a percentage of their federal credit, and that percentage would be determined during the annual budget process. The

Administration proposes that for 2015, the state credit would be worth up to 85 percent of the federal credit at a cost of $380 million. They estimate that this percentage would result in eligible families receiving, on average, a credit worth $460 on top of what they would receive from the federal EITC.

The Administration estimates that this state EITC will reach 2 million Californians. Importantly, because the maximum income threshold ($13,869) is less than what a full-time minimum wage worker would earn in 2015 ($18,270), this credit targets workers who face substantial obstacles to finding or keeping full-time work. Families may be unable to work full-time for a number of reasons, including child care or caregiving responsibilities, a disability or illness, or because they are unable to find full-time work in a difficult hiring environment.

There are a number of issues that policymakers will need to address in establishing a state EITC. The Administration's proposal to allow lawmakers to adjust what percentage of the federal credit the state credit would be during the annual budget process raises concerns. This provision could mean that this new credit would be scaled back to address budget challenges during down periods in the economic cycle, which is when low-income families would need the credit the most. This provision could even mean that in some future year no credit would be provided at all, which could result in confusion for those trying to claim the credit.

Increased Revenue Boosts 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. The May Revision assumes a Proposition 98 funding level of $58.9 billion in 2013-14, $66.3 billion in 2014-15, and $68.4 billion in 2015-16 – a net increase of $6.1 billion over this three-year period. Because changes in state General Fund revenues tend to affect the Proposition 98 guarantee, the Proposition 98 funding levels included in the May Revision largely reflect increases in revenue estimates compared to the Governor's budget proposal in January. The May Revision assumes the outstanding maintenance factor obligation to schools and community colleges – the amount the state must restore for prior-year reductions to the Proposition 98 funding level – will be $772 million at the end of 2015-16, compared with the $1.9 billion in outstanding payments assumed in the January budget proposal.

Compared to the Governor's January budget, the May Revision proposes to significantly increase the amount provided for the state's new education funding formula. Consistent with the January proposal, and as required by the 2014-15 budget agreement, the May Revision also eliminates $897.2 million in outstanding debt owed to schools.

Also within K-12 education, the May Revision:

- **Provides an additional $2.1 billion, for a total of $6.2 billion, to continue implementation of the state's new education funding formula.** As part of the 2013-14 budget agreement, the Local Control Funding Formula (LCFF) restructured the state's education finance system. The LCFF provides school districts 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.
- **Provides an additional $2.5 billion in one-time funding, for a total of $3.6 billion, to reduce mandate debt the state owes to schools.** The Governor's January budget proposal indicated this one-time funding would be distributed statewide on a per pupil basis to school districts, charter schools, and county offices of education (COEs) to support implementation of the Common Core State Standards, English Language Development Standards, and California's Next Generation Science Standards, and to support new responsibilities required under the LCFF. However, to the extent any educational entities have existing mandate reimbursement claims, the Governor's January proposal intended to reduce those claims by the amount of funding they receive for standards implementation and new LCFF-related responsibilities. 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. The state owed K-12 education $5.3 billion for unpaid mandate reimbursement claims as of April 1, 2015, according to the State Controller's Office.
- **Reduces General Fund Proposition 98 spending by $347 million due to increased local property tax revenues.** The May Revision decreases Proposition 98 General Fund support for school districts, special education local plan areas, and COEs by $123.3 million in 2014-15 and $224 million in 2015-16 as a result of higher-than-anticipated local property tax revenues.
- **Allocates $313.4 million from Proposition 39 revenues to K-12 school districts for energy efficiency project grants, a reduction of $6.7 million due to revised revenue estimates.** The Governor's January proposal allocated $320.1 million in Proposition 39 revenues to school districts. Proposition 39, the California Clean Energy Jobs Act approved by voters in 2012, increased state corporation tax revenue by requiring multistate corporations to use the "single sales factor" method of apportionment in calculating their taxable income.
- **Maintains $273.4 million in one-time funding to eliminate the state's remaining obligation to schools under the *Williams v. California* settlement agreement.**
- **Increases LCFF funding by $267.9 million due to increases in average daily attendance (ADA).** The May Revision provides school districts, charter schools, and COEs with $94.4 million in 2014-15 and $173.5 million in 2015-16 for increased LCFF funding due to higher ADA projections for 2014-15 and 2015-16.

- **Provides $150 million in additional one-time 2015-16 Proposition 98 funding to support a transitional Career Technical Education (CTE) Incentive Grant Program.** The Governor's January budget proposed $250 million in Proposition 98 funding annually for three years for the CTE Incentive Grant Program. In addition to the May Revision's proposed $150 million increase in 2015-16 one-time funding, the revised budget proposes $50 million in additional 2016-17 funding and a reduction of $50 million in 2017-18 for the CTE Incentive Grant Program. The Governor's January budget proposed that the new competitive grant program would require school districts, COEs, or charter schools receiving funding to match the grant dollar-for-dollar (that is, at a 1-to-1 ratio). The May Revision proposes to increase the required local match to a 1.5-to-1 ratio in 2016-17 and a 2-to-1 ratio in 2017-18. In addition, the revised spending plan proposes to eliminate the Career Pathways Trust Program from the list of allowable sources for local matching funds and to direct the California Department of Education and the State Board of Education to prioritize funding for applicants that administer programs located in rural districts or areas with high student dropout rates.
- **Revises the cost-of-living adjustments (COLAs) for certain non-LCFF programs.** The May Revision funds a 1.02 percent COLA, a decrease of $25 million from the 1.58 percent COLA ($71.1 million) proposed in the Governor's January budget.

California's community colleges (CCCs) help prepare approximately 2.3 million full-time students to transfer to four-year institutions as well as obtain training and skills for immediate employment. Consistent with the Governor's January proposal, and as required by the 2014-15 budget agreement, the May Revision eliminates $94.5 million in outstanding debt the state owes to CCCs. The May Revision also builds upon the Governor's January proposal to increase funding for CCC operating expenses and general-purpose apportionments.

Specifically, the May Revision:

- **Provides an additional $274.7 million in one-time funding, for a total of $626.0 million, to reduce mandate debt the state owes to community colleges.** The revised budget plan would provide an additional $13.5 million in 2013-14 funding and $261.2 million in 2014-15 funding. The $626.0 million in mandate debt repayments would be distributed on a per full-time-equivalent student basis and could be used by CCCs to "address various one-time needs, such as curricula redesign, start-up costs for new career technical education programs, and other one-time costs." However, to the extent CCCs have existing mandate reimbursement claims, the Governor's proposal would reduce those claims by the amount of funding they receive for these one-time costs. Mandate debt reflects the cost of state-mandated services that CCCs provided in prior years, but for which they have not yet been reimbursed. The state owed community colleges $564.9 million for unpaid mandate reimbursement claims as of April 1, 2015, according to the State Controller's Office.

- **Increases apportionment funding by $49.7 million, for a total of $156.5 million.** The proposed increase in apportionment funding, which provides general purpose dollars for CCCs, reflects 3 percent enrollment growth, whereas the Governor's January budget reflected 2 percent enrollment growth.
- **Reduces General Fund Proposition 98 spending by $156.1 million in 2015-16 due to increased local property tax revenues.** The May Revision decreases Proposition 98 General Fund support for CCCs as a result of higher-than-anticipated local property tax revenues.
- **Increases funding by $148 million for deferred maintenance and instructional equipment.** The May Revision provides one-time Proposition 98 funding that CCCs can use to reduce their backlog of deferred maintenance or to purchase instructional equipment. The revised budget indicates that CCCs will not be required to provide matching funds for deferred maintenance in 2015-16.
- **Increases base allocation funding by $141.7 million, for a total of $266.7 million, to pay for CCC operating expenses.** The May Revision provides additional funding, on top of the $125 million included in the Governor's January budget proposal, to pay for increased costs in facilities, retirement benefits, professional development, converting faculty from part-time to full-time, and other CCC expenses.
- **Provides $75 million to increase the number of full-time faculty at CCCs.** The May Revision proposes that this funding would be allocated based on full-time-equivalent enrollment to all CCC districts, but districts with relatively low proportions of full-time faculty would be required to increase their full-time faculty more than would districts with relatively higher proportions.
- **Revises the COLA for CCC apportionment funding.** The May Revision provides $61 million to fund a 1.02 percent COLA, a decrease of $31 million from the 1.58 percent ($92.4 million) proposed in the Governor's January budget. The revised budget also provides an increase of $2.5 million to provide a COLA for the Disabled Student Programs and Services program, the Extended Opportunity Programs and Services program, the Special Services for CalWORKs Recipients program, and the Child Care Tax Bailout program.
- **Increase funding by $60 million for the Basic Skills and Student Outcomes Transformation Program.** The May Revision proposes that this increased funding would be used to assist CCCs in delivering basic skills instruction. The revised budget also provides an increase of $2 million for a pilot program to provide incentives to CCCs and the California State University (CSU) to coordinate in their efforts to provide basic skills instruction to incoming CSU students.
- **Allocates $38.7 million from Proposition 39 revenues to community college districts for energy efficiency project grants, a reduction of $825,000 due to revised revenue estimates.**

The Governor's January proposal allocated $39.6 million in Proposition 39 revenues for energy efficiency project grants.

- **Increases funding by $30 million for "student success and outcomes" at the CCCs.** The May Revision provides an additional $15 million to "further close achievement gaps in access and achievement in underrepresented student groups, as identified in local Student Equity Plans." The revised spending plan also provides an additional $15 million "to implement strategies to improve college performance in student success and outcomes."

May Revision Reflects Funding Agreement With the University of California

Governor Brown and University of California (UC) President Janet Napolitano have reached an agreement on UC funding levels, presented in the May Revision. Under this agreement the state would provide $119.5 million in General Fund support for the UC for 2015-16, as included in the Governor's January proposal, with the expectation that tuition for California residents would remain frozen through 2016-17. In addition, the agreement calls for UC to adopt the lower cap on salary that is eligible for new employees' pensions as set by the Public Employees' Pension Reform Act of 2013 ($117,020 instead of UC's current $265,000). In exchange for these conditions, the state would use a total of about $436 million of Proposition 2 funds over three years to pay for unfunded UC pension obligations. The state would pay $96 million in 2015-16, and around $170 million in both 2016-17 and 2017-18.

Also under the agreement, UC will:

- **Simplify and clarify transfer requirements** to improve opportunities for community college students, toward UC's existing goal of having one-third of new students be transfers from community colleges; and
- **Reduce course requirements where possible and develop three-year degree pathways**, thereby saving students money and opening up admissions to more students.

Funding for the California State University (CSU) remains largely the same as the Governor proposed in January, with the May Revision providing an additional $38 million to CSU to reduce the time to degree completion and enroll about 1,500 more transfer students by spring of 2016.

All Californians Benefit From Investments That Reduce Poverty and Economic Insecurity

Everyone stands to benefit from public investments that provide all Californians with opportunities to succeed. In recent years, however, California's investments have fallen short of the amount needed to ensure that the state's economic prosperity is broadly shared. Recession-era cuts to many of California's core public supports largely remain in place at a time when millions of residents lack economic security. Around 6 million Californians have incomes below the official federal poverty line, and within this population, more than 2.5 million live in even greater despair, with incomes below *half* the poverty line, commonly referred to as "deep poverty." Children make up roughly one-third of both of these groups, even though they comprise less than one-quarter of the state's population. Allowing poverty to persist, particularly among children, could weaken California's future workforce and economy, threatening prosperity for all state residents.

Although poverty and economic insecurity are significant challenges, state policymakers have the tools to address these problems. New research using the US Census Bureau's Supplemental Poverty Measure – which factors in a broader array of resources that boost families' economic well-being – shows that public supports lift many families out of poverty. Supports including the federal Earned Income Tax Credit (EITC), food assistance, and unemployment insurance lifted 4.9 million Californians – including 1.4 million children – out of poverty each year, on average, between 2009 and 2012. State policymakers can further reduce economic hardship by strengthening California's public supports, such as by establishing a refundable *state* EITC (see discussion on page 3), increasing working parents' access to affordable child care (see page 9), and fully reversing recession-era cuts to CalWORKs and SSI/SSP (see page 10). These investments not only would increase economic security for millions of families and individuals, but also would strengthen our state's communities and economy by contributing to a better future for the next generation.

May Revision Makes Only Minor Investments in Subsidized Child Care and the State Preschool Program

Funding for California's child care and development system was cut dramatically during and after the Great Recession. Despite modest funding increases in recent years, annual funding for subsidized child care and the state preschool program remains over $1 billion lower than 2007-08 funding levels, after adjusting for inflation. As a result, the state is currently offering 90,000 fewer child care and preschool slots for working families struggling to make ends meet. Despite a greatly improved fiscal outlook, the

May Revision makes only minor investments in subsidized child care and the state preschool program. Specifically, the May Revision:

- **Increases the reimbursement rate for the state preschool program by 1 percent.** In order to better serve children with exceptional needs, the Governor's revised spending plan increases the reimbursement rate for state preschool program providers by 1 percent ($6 million Proposition 98). This rate increase is for preschool teachers' professional development and for parental outreach regarding resources for the screening and treatment of developmental disabilities.
- **Reflects a 1.7 percent increase in the number of slots for the state preschool program.** The May Revision includes an additional $12.1 million in Proposition 98 funds to increase the number of part-day preschool slots by 2,500. Priority for the new slots is to be given to children with exceptional needs.
- **Revises the size of the COLA proposed by the Governor in January.** The January proposal included a modest COLA for child care and preschool provider payment rates – the first COLA for these providers since 2007-08. However, the May Revision reduces the proposed COLA from 1.58 percent to 1.02 percent for savings of $7.2 million ($3.1 million Proposition 98).
- **Reflects additional federal funding in 2015-16 for the subsidized child care and development system.** The May Revision includes an increase of $17.7 million in federal funds for the 2015-16 fiscal year. Of the $17.7 million, $9 million are ongoing federal funds. In addition, the remaining $8.7 million will be carried over from 2014-15, of which $5.5 million are for one-time general purpose spending and $3.2 million are for one-time quality spending. Additional federal funds may create an opportunity for new investments in the child care and development system.
- **Increases funding for young children with special needs.** The revised budget increases funding by $30 million, for a total of $119 million, in Proposition 98 funds for the Early Education Program for Infants and Toddlers with Exceptional Needs. This program, implemented by local education agencies, provides early identification and interventions for children from birth through age two who have special needs.

May Revision Fails to Boost Support for Low-Income Families, Seniors, and People With Disabilities

Even after several years of economic recovery following the Great Recession, many Californians still face serious economic hardship in the aftermath of the downturn (see text box on page 9). Yet, the May

Revision – like the Governor's January proposal – calls for no major reinvestment in two key programs that are intended to help families and individuals make ends meet. The May Revision:

- **Leaves CalWORKs grants at deep-poverty levels, with no COLA.** The California Work Opportunity and Responsibility to Kids (CalWORKs) program provides modest cash assistance while helping parents find and keep jobs. More than 1.2 million Californians, nearly 80 percent of whom are children, benefit from CalWORKs. During and after the Great Recession, state policymakers reduced the level of support for families participating in CalWORKs, including reducing grant levels, eliminating the COLA, reducing time limits, and establishing more restrictive work requirements. Despite modest investments made in the program in the two most recent budget agreements, CalWORKs cash grants remain below the deep poverty cut-off of 50 percent of the poverty line. Currently, CalWORKs grants are $180 per month lower than they would be if they had been adjusted for inflation each year, beginning in 2007-08. The Governor's May Revision does not increase funding for the CalWORKs program.
- **Leaves SSI/SSP grants unchanged, with no COLA.** Supplemental Security Income/State Supplementary Payment (SSI/SSP) grants help 1.3 million low-income seniors and people with disabilities to pay for rent, food, and other necessities. State support for SSI/SSP grants – which are funded with both federal (SSI) and state (SSP) dollars – has been significantly reduced in recent years. State policymakers eliminated the annual state COLA and cut the SSP portion of the monthly grant to the minimum levels allowed by federal law ($156 for individuals and $396 for couples). Consistent with the Governor's January proposal, the May Revision does not call for reinstating the COLA or otherwise increasing SSP grant levels in 2015-16.

May Revision Includes Funding for Undocumented Immigrants Who May Qualify for Key State Services

In contrast to the Governor's January proposal, the May Revision acknowledges that certain undocumented immigrants living in California would qualify for key state-funded services as a result of recent federal actions. Specifically, last November, President Obama announced a new federal policy allowing several million undocumented immigrants throughout the nation to apply to temporarily remain in the US and work legally without fear of deportation. (This is known as "deferred action.") Under California law, individuals who obtain this federal status may enroll – if they are otherwise eligible – in three programs: Medi-Cal, the state's health coverage program for residents with low incomes; In-Home Supportive Services (IHSS), which helps seniors and people with disabilities remain safely in their own homes; and the Cash Assistance Program for Immigrants (CAPI), which provides monthly grants that help low-income seniors and people with disabilities meet basic living expenses. The costs associated with undocumented immigrants who receive these services are funded entirely with state dollars.

While the President's executive actions have not been implemented due to a federal court order, the May Revision includes state funding of about $43 million for Medi-Cal, IHSS, and CAPI in 2015-16, reflecting the partial-year costs associated with increased enrollment that is anticipated to occur in these programs if the President's actions are ultimately upheld by the federal courts. In addition, the May Revision projects partial-year state costs of roughly $19 million in the CalWORKs welfare-to-work program and the CalFresh food assistance program. While undocumented immigrants are not eligible for CalWORKs or CalFresh, the Administration assumes that some undocumented adults who qualify for deferred-action status would enroll their eligible children in these two programs in 2015-16.

In a related proposal, the May Revision includes $4.8 million for nonprofit organizations – funding that would be used to provide assistance to undocumented immigrants who are eligible to apply to remain legally in the US under the President's deferred action policies.

May Revision Continues Implementation of Health Care Reform, but Maintains Key Prior-Year Cuts to Medi-Cal

Medi-Cal, California's Medicaid program, provides health care services to approximately 12 million Californians who have low incomes. Enrollment in Medi-Cal has increased by 4 million over the past two years, due primarily to the implementation of federal health care reform and to the elimination of the Healthy Families Program (HFP), which shifted hundreds of thousands of children from the HFP to Medi-Cal. While the May Revision continues the implementation of health care reform, it also leaves in place significant cuts to Medi-Cal that were made to help close state budget shortfalls during and following the Great Recession. Specifically, the May Revision:

- **Maintains a 10 percent cut to payments for certain types of doctors and other Medi-Cal providers.** The Administration began implementing this reduction in September 2013, with the cut being retroactive to 2011. The original reduction – passed by the Legislature in 2011, but delayed due to litigation – was later modified to exempt certain providers and services from the cut and/or from the retroactive recoupment of prior payments. Yet, even with the partial rollback of the payment reduction, the remaining cut could still discourage some providers from participating in Medi-Cal, potentially hindering access to services for Californians who rely on the program to meet their health care needs.
- **Does not propose to reinstate any of the Medi-Cal benefits that were eliminated in 2009.** These include the full range of dental services for adults, optician/optical lab services, and

incontinence cream and washes. (Dental benefits for adults were *partially* restored beginning in May 2014.)

In addition, the May Revision estimates state savings of $381 million in 2015-16 due to a recent federal policy change related to the Children's Health Insurance Program (CHIP), which pays for health care services provided to certain children enrolled in Medi-Cal. This change significantly *increases* the federal government's share of the cost – and *decreases* the state's share of the cost – for children who receive CHIP-funded health care services through Medi-Cal. The May Revision does not specifically allocate this $381 million to other spending priorities. However, on a May 14th conference call with stakeholders, Administration officials suggested that these savings are being used to pay for higher-than-anticipated costs in other parts of the Medi-Cal budget.

May Revision Maintains Governor's Commitment to Fully Restore IHSS Consumers' Hours of Care

Many seniors and people with disabilities rely on the In-Home Supportive Services (IHSS) Program, which helps more than 440,000 people with low-incomes remain safely in their own homes, preventing the need for more costly out-of-home care. The May Revision:

- **Maintains the Governor's plan to roll back the current 7 percent cut to IHSS consumers' authorized hours of care on July 1, 2015.** In January, the Governor proposed to pay for these additional hours using some of the proceeds from a new tax on managed care organizations (MCOs), pending approval by the Legislature. On a May 14th conference call with stakeholders, Administration officials indicated that they are continuing to pursue an MCO tax, but are also considering other possible revenue sources in order to fund the additional hours, which "will be restored on July 1."
- **Continues to delay the implementation of new labor regulations regarding home care workers.** In 2013, the federal government issued rules mandating overtime pay for home care workers – including IHSS providers – and requiring that workers be paid for time spent in transit between multiple consumers, at medical appointments, and in mandatory trainings. The 2014-15 budget agreement provided state funding to implement these changes – along with new restrictions on overtime – starting on January 1, 2015. However, a federal court prevented the new federal rules from going into effect and, as a result, the Governor delayed implementing the rules in California pending a final court decision, which is not expected before the end of the current fiscal year (June 30). Delaying implementation of these rules reduces state General Fund spending by $184 million in 2014-15. The May Revision proposes to use these funds to "partially offset" higher-than-projected baseline costs for IHSS. These new costs – which exceed

the spending levels assumed by the Governor this past January – total $326.7 million for 2014-15 and 2015-16 combined, according to the Administration. The full-year cost of implementing the new labor rules in IHSS in 2015-16 would be $316 million, according to the Administration.

May Revision Includes a Plan to Reduce Use of Out-of-State Prisons

The May Revision allocates $10.2 billion for state corrections, excluding spending on infrastructure and on corrections responsibilities that were transferred to counties under the 2011 realignment. This spending level is $60.8 million less than assumed in the Governor's January proposal.

Due to voter approval of Proposition 47 last November, California's prison population has declined substantially, and the state now incarcerates about 111,300 people in state prisons designed to house about 82,700. This puts the prison population level below a federal court-ordered cap. The May Revision projects further reductions in 2015-16, but indicates the reduced population level may not be sustainable in the long term. The May Revision:

- **Reduces the use of out-of-state private prisons, vacating about 4,000 beds by June 2016 for General Fund savings of $73.3 million in 2015-16.** There are approximately 8,100 Californians currently serving their sentences in private prisons in other states.
- **Includes $51.8 million in 2014-15 and $60.6 million in 2015-16 to provide new Hepatitis C treatments to incarcerated adults.** There are higher rates of contagious diseases, such as hepatitis, in correctional facilities, causing significant health risks to incarcerated adults and the communities they return to.
- **Modifies a proposed debt amnesty program to reduce barriers to payment for low-income Californians.** The Governor's proposed budget in January included an 18-month amnesty program that would allow certain people with overdue court-ordered fines to pay off the debt at a reduced rate. However, this proposal did not address the fact that individuals with overdue debt face an additional penalty: the suspension of their driver licenses. Under the Governor's revised proposal, eligible people would be allowed to have their driver licenses reinstated as part of the program. Additionally, the revised amnesty program would waive the current $300 court-imposed assessment fee and replace it with a $50 administrative fee.

May Revision Includes $2.2 Billion in "Cap and Trade" Spending on Programs Related to Climate Change

The May Revision includes revenues already received or expected to be received from "cap and trade" auctions organized by the Air Resources Board, and the Administration estimates $2.2 billion in revenue for 2015-16, $1.2 billion above what was estimated in the Governor's January budget proposal. Major components of the "cap and trade" expenditure plan for 2015-16 are $500 million for high-speed rail; $400 million for the "Affordable Housing and Sustainable Communities Program," half of which must be spent on affordable housing projects; $350 million for transportation projects; and $128 million for water conservation efforts.

May Revision Maintains Plan for Reducing Unfunded Liability for Retiree Health Care

The Governor's proposed budget in January established a goal of addressing the state's unfunded liability for retiree health care. This liability results from the state not setting aside enough funds to pay for the health benefits accrued by current and future retired state workers. The state currently faces a $72 billion unfunded liability for the costs of these benefits, a liability that will grow substantially over time if not addressed. The May Revision elaborated on the Governor's January proposal, with a three-part approach to dealing with the state's unfunded retiree health care liability that includes:

- Requiring state employees to share in the costs of prefunding retiree benefits going forward, switching from a pay-as-you-go funding model to one that holds state and employee contributions in a trust fund that earns investment income (similar to how pensions are funded);
- Controlling costs by reducing the employer subsidy for retiree health care for future state employees and requiring state employees to work longer to qualify for retiree health care benefits; and
- Adding reporting requirements about state and employee retiree health plans to increase oversight of the state's health care administrator – the California Public Employees' Retirement System (CalPERS) – and adding lower-cost health care plans to the benefits menu.

The Administration's proposed changes would have to be negotiated through collective bargaining processes with state employees.