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Restrained Budget Proposal Reflects Uncertainty About Federal Commitments and Economic Conditions

On January 10, Governor Jerry Brown released a proposed 2017-18 budget that reflects both deep uncertainty about looming federal actions and a tempered economic and fiscal outlook for the state. The Governor forecasts revenues that are \$5.8 billion lower – over a three-year period – than previously projected and proposes taking steps to address a \$1.6 billion projected shortfall for 2017-18. The Governor’s proposal assumes current federal policies and funding levels, even as the Affordable Care Act and other federal programs face the prospect of cuts with President-elect Trump taking office.

As part of addressing the deficit that his Administration foresees, the Governor proposes to rescind several one-year spending commitments that had been part of the 2016-17 budget agreement, including \$400 million for affordable housing programs and \$300 million for renovation of state office buildings. The Governor also proposes to “pause” a multiyear plan for reinvesting in the state’s child care system.

The Governor’s proposal calls for continued funding of the California Earned Income Tax Credit (CalEITC) and also reflects the state’s increased minimum wage. However, this restrained budget proposal contains no additional investments in the welfare-to-work system (CalWORKs) or in basic income support for low-income seniors and people with disabilities (SSI/SSP). In addition, the Governor’s budget does not include proposals to address California’s affordable housing crisis.

The Governor’s proposal continues modest increases in funding for the California State University and University of California, but also reduces certain student aid programs. Lower revenue projections also mean slower growth in the Proposition 98 minimum guarantee for K-14 education spending.

The Governor’s proposal includes setting aside \$2.3 billion as constitutionally required by Prop. 2 (2014), with half deposited in the state’s rainy day fund and half used to pay down state debts. Under the Governor’s proposal, state reserves would total \$9.5 billion by the end of 2017-18.

With the near-term state budget facing many uncertainties, it is critical that California’s Congressional delegation and state lawmakers seek to protect the Affordable Care Act and the social safety net, and that state lawmakers ensure that California is well positioned to invest over the long term in education, child care, affordable housing, and other public services that help Californians advance economically.

The following sections summarize key provisions of the Governor’s proposed 2017-18 budget. Please check the Budget Center’s website (calbudgetcenter.org) for our latest commentary and analysis.

Administration Expects Economic Growth to Continue, but Notes Several Risks

The US economy is now in its seventh year of expansion since the Great Recession ended, and California's economy has grown at a healthy clip in recent years, with the state's job growth outpacing that of the nation. The Governor's proposed budget assumes that economic growth will continue at a moderate pace over the next few years given that gains have slowed recently as the expansion has matured and the job market has neared full recovery from the recession. However, the Administration highlights several "risks to consider" that could weaken gains going forward. These include the possibility that the national economy could fall into another recession; that federal policy changes could disrupt the economy; and that California's ongoing housing crisis could limit economic growth. While it is important to keep these potential risks in mind, it is worth noting that a recession in the next few years is not inevitable. The Administration states that "it would be a historical anomaly for there not to be a recession before 2020" given that the current economic expansion has lasted longer than the typical expansion. However, the Legislative Analyst's Office (LAO) and other experts have pointed out that this fact does not in and of itself mean that another recession is likely soon because expansions "do not die of old age."

Governor Projects a Budget Shortfall Partly Due to a Lower Revenue Forecast

The Governor's proposed budget projects that California will face a budget shortfall of \$1.6 billion in 2017-18, absent action by policymakers to address this gap. The projected deficit reflects two key factors: lower General Fund revenue projections and a shortfall in the Medi-Cal budget for the current fiscal year (2016-17). According to the Administration, state revenues have fallen short of expectations in most months since the 2016-17 budget was enacted. As a result, the Governor now projects that General Fund revenues (before transfers) over the three-year "budget window," from 2015-16 to 2017-18, will be \$5.8 billion lower than the projections included in the 2016-17 budget agreement. Specifically, the Governor expects personal income tax (PIT) revenues during this three-year period to be \$2.1 billion lower, sales and use tax (SUT) revenues to be \$1.9 billion lower, and corporation tax (CT) revenues to be \$1.7 billion lower than expected when the budget for the current fiscal year was signed into law.

By comparison, the LAO forecast, published in November 2016, expected modestly lower revenues in 2015-16 and 2016-17 relative to projections in the 2016-17 budget agreement, but followed by "healthy revenue growth" in 2017-18. One of the major differences between these forecasts is that the LAO assumes higher growth in wages and salaries and capital gains than does the Administration, which

contributes to higher PIT revenues, particularly in 2017-18. The LAO's November forecast projected that the three largest revenue sources (PIT, SUT, and CT) would increase by 5.4 percent between 2016-17 and 2017-18, driven by a nearly 7 percent increase in PIT revenues, which comprise around 70 percent of General Fund revenues.

To address the projected budget shortfall and rebuild the state's discretionary reserve, the Governor proposes to:

- **Rescind certain one-year spending commitments included in the 2016-17 budget.** These include:
 - **\$400 million set aside for affordable housing programs.** These dollars were to be provided only if lawmakers modified the local review process for certain housing developments, as proposed by the Governor. The Legislature did not adopt the Governor's proposal.
 - **\$300 million that was intended to begin the process of renovating or replacing certain state office buildings.**
 - **\$45 million for the Housing and Disability Advocacy Program.** The purpose of this program, established in the 2016-17 budget, was to help people who are homeless or at risk of homelessness and who have a disability to access appropriate benefits.
- **Delaying a multiyear plan adopted in 2016 to reinvest in the state's child care and development system,** including by updating provider payment rates and further boosting the number of full-day state preschool slots.
- **Beginning the phase out of the Middle Class Scholarship program** by not providing grants to any new students.

In addition, the Governor assumes a lower Proposition 98 minimum guarantee in 2015-16 and 2016-17, which reduces K-14 education spending over the two years by about \$886 million.

The Administration notes that it is possible that the revenue forecast will improve by the time the Governor releases his revised 2017-18 budget in May, just after California's final personal income tax receipts come in, in which case the state could possibly avoid making some or all of these cuts. Indeed, the revenue picture will likely remain "murky" until at least April, according to recent LAO publications. The LAO points out that lower-than-expected PIT revenue collections late in 2016 may reflect changes in taxpayers' behavior in anticipation of potential federal tax changes. Specifically, the LAO suspects that some personal income tax filers with high incomes are deferring capital gains to calendar year 2017 in order to delay tax payments with the hope that they will owe less in taxes if federal policymakers lower tax rates beginning this year.

Under Prop. 2 (2014), which made changes to California’s constitutional rainy day fund – the Budget Stabilization Account (BSA) – the Governor has the authority to declare a “budget emergency” under certain conditions, allowing the state to suspend or reduce annual transfers into the BSA or withdraw funds from the BSA. A “budget emergency” is defined as resulting from either a disaster or extreme peril, as defined in the state Constitution, or from 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. (For a fuller discussion of Prop. 2, see the following section.) The Governor’s proposed budget does not indicate whether the projected budget shortfall would constitute a budget emergency as defined under Prop. 2. Were the Governor to declare a budget emergency, it would allow the state to suspend or reduce the deposit into the BSA and/or withdraw reserve funds, freeing up revenue to help close the projected shortfall.

Governor’s Proposal Emphasizes the Importance of Reserves

California voters approved Prop. 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 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 Governor’s proposed 2017-18 budget projects that the BSA will total \$6.7 billion by the end of the current fiscal year (2016-17). Based on the Governor’s revenue projections for 2017-18, Prop. 2 would constitutionally require the state to deposit an additional \$1.2 billion in the BSA (as well as use \$1.2 billion to repay budgetary debt), bringing the BSA total to \$7.9 billion by the end of fiscal year 2017-18.

The BSA is not California’s only reserve fund. Each year, the state deposits additional funds into a discretionary reserve called the “Special Fund for Economic Uncertainties.” For 2017-18, the Governor projects \$1.6 billion for this fund. Including this fund, the Governor’s proposal would build state reserves to a total of \$9.5 billion in 2017-18.

Governor Proposes No Changes to the CalEITC

The California Earned Income Tax Credit (CalEITC) is a refundable state tax credit designed to boost the incomes of low-earning workers and their families and help them afford basic expenses. The credit was established by the 2015-16 budget agreement and became available to claim in the 2015 tax year.

In its first year, the CalEITC provided an average credit of slightly more than \$500 to over 385,000 households.

The Governor's proposed budget makes no changes to the CalEITC. Unlike state EITCs in other states, the CalEITC is not automatically provided each year like a typical tax expenditure. Instead, California policymakers must specify in each year's state budget how large a credit to provide. Specifically, they must set the state credit at a particular percentage of the federal EITC, referred to as the "adjustment factor." The 2015-16 budget and 2016-17 budget set the state EITC adjustment factor at 85 percent, and the Governor proposes to maintain the adjustment factor at this percentage in the 2017-18 budget. Additionally, the Governor projects that the CalEITC will reduce state General Fund revenues by \$240 million in 2016-17 and by \$264 million in 2017-18, slightly more than the \$200 million cost of the credit in 2015-16. When the CalEITC was first proposed, the Governor projected that it would reach 825,000 households at a cost – in terms of lower revenues – of \$380 million annually. However, because claims in the credit's first year were considerably lower than expected, the projected cost of the credit is also lower.

Raising awareness of the CalEITC could help boost the number of low-earning workers benefiting from the new tax credit. The 2016-17 budget agreement included \$2 million to provide grants to community-based organizations and other entities to expand education and outreach efforts in order to increase CalEITC claims. It does not appear that the Governor's proposed 2017-18 budget includes any funding to maintain these efforts beyond the current year.

Lower Revenue Estimates Slow Growth in the Minimum Funding Level for Schools and Community Colleges

Approved by voters in 1988, Prop. 98 constitutionally guarantees a minimum level of funding for K-12 schools, community colleges, and the state preschool program. The Governor's proposed budget assumes a 2017-18 Prop. 98 funding level of \$73.5 billion for K-14 education, \$2.1 billion above the revised 2016-17 minimum funding level. The Prop. 98 guarantee tends to reflect changes in state General Fund revenues, and estimates of 2015-16 and 2016-17 General Fund revenue in the proposed budget are lower than those in the 2016-17 budget agreement. As a result, the Governor's proposed 2017-18 budget reflects decreases in prior-year Prop. 98 funding levels compared to those assumed in the 2016-17 budget agreement. The Governor's proposed budget assumes a 2016-17 Prop. 98 funding level of \$71.4 billion, \$506 million less than the level assumed in the 2016-17 budget agreement, and a \$68.7 billion 2015-16 Prop. 98 funding level, \$380 million below the level assumed in the 2016-17 budget agreement.

California's school districts, charter schools, and county offices of education (COEs) provide instruction to approximately 6.2 million students in grades kindergarten through 12. The Governor's proposed budget increases funding for the state's K-12 education funding formula – the Local Control Funding Formula (LCFF) – and pays off outstanding obligations to school districts. Voter approval of Prop. 51 in November 2016 authorized \$7 billion in state general obligation (GO) bonds for K-12 school facilities. However, the Governor's proposed budget notes shortcomings in the State Facilities Program and suggests that until measures are in place to verify that state GO bond funds "are appropriately used," the Administration will not support the expenditure of Prop. 51 dollars. The Governor also proposes to engage stakeholders in discussions during the spring budget process to respond to recommendations made to improve the current special education finance system.

Additionally, the Governor's proposed budget:

- **Increases funding by \$744.4 million in 2017-18 to continue implementation of 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 Governor's proposal to increase LCFF funding may reduce the amount of time it takes to fully implement the LCFF, which depends on funding sufficient for all districts to reach a target base grant (all COEs reached their LCFF funding targets in 2014-15). According to the Administration, the proposed 2017-18 LCFF funding level "maintains formula implementation at the current-year level of 96 percent." In addition, the Governor's proposed budget defers \$859.1 million in 2016-17 LCFF funding to 2017-18 due to a reduction in 2016-17 Prop. 98 funding compared to the 2016-17 budget agreement.
- **Provides \$287.3 million in one-time funding 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.
- **Provides \$200 million for the Career Technical Education Incentive Grant Program.** The proposed spending plan reflects the final installment of a three-year program that began with the 2015 Budget Act.
- **Provides cost-of-living-adjustments (COLAs) for non-LCFF programs.** The Governor's proposed budget funds a 1.48 percent COLA (\$58.1 million) for several categorical programs that remain outside of the LCFF, including special education, child nutrition, and American Indian Education Centers.

California's community colleges (CCCs) help prepare approximately 2.4 million full-time students to transfer to four-year institutions as well as obtain training and skills for immediate employment. The

Governor's proposed budget provides CCCs with \$150 million in one-time funding for grants to develop and implement "guided pathways" programs, an institution-wide approach to support student success. Participating CCCs can use guided pathway grants for activities such as targeted advising and support services and designing "academic roadmaps and transfer pathways that explicitly detail the courses students must take to complete a credential or degree on time."

Administration Continues Modest Funding Increases for CSU and UC and Reduces Student Aid Programs

The Governor's proposed budget includes modest increases in General Fund spending for the California State University (CSU) and the University of California (UC), with the expectation that CSU and UC implement new practices that reduce the cost of instruction and expand access to higher education for California students. At the same time, the Governor's budget proposal notes that the UC Office of the President will propose a 2.5 percent tuition increase to the UC Board of Regents later in January and that the CSU Chancellor's Office will propose a 5 percent tuition increase to the CSU Board of Trustees in March. The Governor's proposal notes that these tuition increases would boost the 2017-18 Cal Grant costs for UC and CSU students by \$17.7 million and \$24.9 million, respectively. However, the Governor's proposed budget does not include funding to pay for these increased costs and states "any tuition increases must be viewed in the context of reducing the overall cost structure at UC and improving the graduation rates at the CSU."

Specifically, the Governor's proposed budget:

- **Increases funding for CSU by \$161.2 million in 2017-18.**
- **Increases funding for UC by \$131.2 million in 2017-18.** The Governor's proposal represents a 4 percent increase in funding consistent with the existing agreement between the Administration and the UC President. The Governor's proposed budget also includes a one-time increase of \$169 million in Prop. 2 funds to help pay down unfunded liabilities of the UC Retirement Plan, which reflects the final installment of \$436 million provided over a three-year period.
- **Phases out the Middle Class Scholarship Program (MCSP).** The Governor's proposal would provide \$74 million to the MCSP in 2017-18, but would only renew scholarships for the approximately 37,000 students who received them in the 2016-17 academic year.
- **Reduces funding for the Cal Grant Program by \$76.9 million.** The Governor's proposal would decrease Cal Grants by \$24.5 million in 2017-18 and \$52.4 million in 2016-17 "to reflect estimated costs."

Governor's Proposal "Pauses" Modest Reinvestments in Early Care and Education Programs

California's child care and development system is composed of a variety of programs that allow parents with low and moderate incomes to find jobs and remain employed while caring for and preparing children for school. State policymakers dramatically cut support for these programs during and after the Great Recession, and overall funding in the current fiscal year remains nearly 20 percent below pre-recession levels, after adjusting for inflation, even with reinvestments made in recent years. Despite tremendous unmet need, the state currently provides about 70,000 fewer slots than in 2007-08.

The 2016-17 budget agreement called for implementation of a multiyear plan to reinvest in the state's child care and development system, including by updating provider payment rates in order to keep pace with the state's rising minimum wage and further boosting the number of full-day state preschool slots. Yet due to the projected decrease in revenue, the Governor's proposed 2017-18 budget now "pauses" these proposed reinvestments until the 2018-19 fiscal year.

Proposed Budget Highlights Impact of Proposition 57, Which Provides New Tools for Reducing Incarceration

Currently, more than 129,200 people who have been convicted of a felony offense are serving their sentences at the state level. Most of these individuals – just over 114,000 – are housed in state prisons designed to hold slightly more than 85,000 people. This level of overcrowding is equal to 134 percent of the prison system's "design capacity," which is below the prison population cap – 137.5 percent of design capacity – established by federal court order. In addition, California houses roughly 15,200 individuals in facilities that are not subject to the court-ordered population cap, including fire camps, in-state "contract beds," out-of-state prisons, and community-based facilities that provide rehabilitative services.

The total number of people incarcerated by the state has declined by more than one-quarter since peaking at 173,600 in 2007. This substantial reduction resulted largely from a series of policy changes adopted by state policymakers and the voters in the wake of the 2009 federal court order requiring the state to reduce overcrowding in state prisons.

California voters added a new reform this past November by approving Prop. 57, which gives state officials new policy tools to address ongoing overcrowding in state prisons. Prop. 57 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. The measure also gives the California Department of

Corrections and Rehabilitation (CDCR) – which is part of the Governor’s administration – broad new authority to award sentencing credits to reduce the amount of time that people spend in prison. Prop. 57 requires the CDCR to adopt regulations implementing both of these provisions. In addition, Prop. 57 requires juvenile court judges to decide whether a youth should be tried in adult court.

The CDCR is currently drafting regulations that will implement the new parole process and outline how the Administration will use its new authority to award sentencing credits. With respect to the new parole process, the Governor’s budget summary does not indicate how the new regulations will define a “nonviolent felony offense.” With respect to credits, the summary states that the “current credit-earning structure is convoluted” and suggests that the new regulations will aim to increase the amount of credits earned and “provide more equality in the credit structure.”

The CDCR’s new regulations are expected to be in place by October 1, 2017. The Governor estimates that in 2017-18, Prop. 57 will reduce the number of incarcerated adults by nearly 2,000 below the level that was otherwise projected (130,118). This annual drop in the inmate population is projected to grow to about 9,500 by 2020-21. According to the Administration, the combination of Prop. 57 and other population-reduction measures already in place would allow the CDCR to end the use of out-of-state prison facilities by 2020. Moreover, Prop. 57 would result in estimated net state savings of \$22.4 million in 2017-18, rising to about \$140 million by 2020-21.

Proposed Budget Emphasizes the Uncertainty Over the Fate of the Federal Affordable Care Act

The Governor’s proposed budget highlights the uncertainty surrounding the federal Affordable Care Act (ACA), also known as Obamacare. Under the umbrella of the ACA, state policymakers expanded Californians’ access to health care coverage, cutting the state’s uninsured rate in half. President-elect Trump campaigned on repealing the ACA, and Republicans in Congress have begun the process of dismantling the law. However, it is unclear how much of the ACA will ultimately be repealed, when any such repeal would actually take effect, and what the Republicans’ replacement for the ACA – if any – would look like.

California would lose well over \$20 billion in federal funding *each year* if Republicans succeed in repealing two key components of the ACA:

- **The Medicaid expansion.** California and 30 other states expanded eligibility for Medicaid health care coverage to low-income adults under age 65 who previously were excluded from the program. (Medicaid is called Medi-Cal in California.) Slightly more than 4 million Californians

are expected to be enrolled in Medi-Cal in 2017-18 as a result of this expansion. Moreover, California is projected to receive more than \$17 billion in federal funding in the upcoming fiscal year to support health care services for this population, according to the Governor's budget summary.

- **Federal subsidies for private coverage purchased through online health insurance marketplaces, such as Covered California.** Nearly 1.4 million Californians who earn too much to qualify for Medi-Cal but lack access to affordable job-based insurance get their coverage through Covered California. Nearly 9 in 10 of these individuals – 1.2 million – receive federal subsidies to reduce the cost of their coverage, with these subsidies totaling roughly \$5 billion per year.

The Governor's budget summary points out that "a complete repeal of the Affordable Care Act, without a companion replacement program, would not only affect millions of Californians' health benefits, but would also disrupt the private insurance market."

In addition, the Governor's budget proposal:

- **Projects total Medi-Cal enrollment of 14.3 million in 2017-18.** This is up from 7.9 million in 2012-13, an increase that is due primarily to California's full implementation of federal health care reform.
- **Projects total Medi-Cal spending of \$102.6 billion in 2017-18, which is comprised primarily of federal dollars.** Federal support for Medi-Cal is projected to be \$66.8 billion in 2017-18, roughly two-thirds of total funding for the program. State General Fund support for Medi-Cal is projected to be \$19.1 billion in the upcoming fiscal year, with other non-federal funds providing the remaining \$16.7 billion.
- **Identifies a \$1.8 billion General Fund shortfall in the Medi-Cal budget for the current fiscal year (2016-17).** According to the Governor's budget summary, this significant gap is primarily due to "a one-time retroactive payment of drug rebates to the federal government and miscalculation of costs" related to the Coordinated Care Initiative, which coordinates health care and other services for certain seniors and people with disabilities.
- **Uses certain tobacco tax revenues raised by Prop. 56 to fund "increased General Fund health care costs in the Medi-Cal program."** Approved by voters this past November, Prop. 56 increases the state's excise tax on cigarettes by \$2 per pack starting on April 1. The measure also boosts the tax on other tobacco products by an equivalent amount and – for the first time – applies the state excise tax to electronic cigarettes that contain nicotine. Prop. 56 requires that the vast majority of revenues raised by the measure go to Medi-Cal. The Administration projects that Prop. 56 will generate \$1.7 billion between April 1, 2017, and June 30, 2018, with

\$1.2 billion of this amount allocated to Medi-Cal. The Governor does not propose to use any of these new revenues to support payment increases for doctors and others who provide health care services to Medi-Cal enrollees.

- **Assumes that Congress will reauthorize the Children’s Health Insurance Program (CHIP) in 2017, but that the federal share of CHIP funding will be reduced.** In California, federal and state funding for CHIP is used primarily to support health care services for certain children enrolled in Medi-Cal. (These children previously would have been enrolled in the Healthy Families Program, which was eliminated in 2013.) Since late 2015, the federal government has paid 88 percent of CHIP costs in California, with the state covering the remaining 12 percent. Previously, the federal share was set at 65 percent. With CHIP currently authorized only through September 2017, the Governor assumes that Congress will reauthorize the program this year, but revert to the prior sharing ratio (65/35) effective October 1, 2017. This change would increase the state’s General Fund costs for CHIP by \$536.1 million, according to Administration estimates.

Governor’s Proposal Shifts Additional Costs for In-Home Supportive Services to Counties

Under the Coordinated Care Initiative (CCI), California integrates health care and other services – including In-Home Supportive Services (IHSS) – for certain seniors and people with disabilities. The Administration indicates that because the CCI is not cost-effective, it will be discontinued in 2017-18, pursuant to current law. One key outcome of discontinuing the CCI is that the counties’ share of the non-federal costs for IHSS would go up (and the state’s share would go down). This is because the current funding formula – which is tied to the CCI and significantly limits counties’ share of IHSS cost increases – would end. In its place, the state would reestablish – effective July 1, 2017 – the prior funding formula, which requires counties to pay 35 percent of the non-federal portion of IHSS costs, with the state paying the other 65 percent. The Administration anticipates that counties would lack sufficient funding to cover their increased share of IHSS costs in 2017-18, likely creating a “financial hardship and cash-flow problems.” As a result, the Governor proposes to “work with counties to mitigate, to the extent possible,” the financial impact of increasing counties’ share of costs for IHSS.

Governor’s Proposal Does Not Make Any New Investments in CalWORKs

The California Work Opportunity and Responsibility to Kids (CalWORKs) Program provides modest cash assistance for nearly 1 million low-income children while helping parents overcome barriers to employment and find jobs. State policymakers made a historic advance last year when they repealed

the punitive Maximum Family Grant (MFG) or “family cap” rule, which only served to drive families with children deeper into poverty. The Governor’s proposed budget does not make any additional investments in CalWORKs, although this would be necessary to restore cuts made to the program during and after the Great Recession. Currently, CalWORKs grants fail to lift most families out of “deep poverty,” which is defined as having an income that is below half of the federal poverty line (\$10,080 for a family of three in 2016). With the minimum wage increase scheduled for January 1, 2018, CalWORKs spending is expected to decrease by \$5.3 million General Fund as more families earn an income that is above the eligibility limit but far below the level needed to make ends meet.

Governor Does Not Provide a State Cost-of-Living Increase for SSI/SSP Grants in 2017-18

Supplemental Security Income/State Supplementary Payment (SSI/SSP) grants help well over 1 million low-income 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 made deep cuts to the SSP portion of these grants in order to help close budget shortfalls that emerged following the onset of the Great Recession in 2007. SSP grants for couples and for individuals were reduced to federal minimums in 2009 and 2011, respectively, and the annual state COLA for SSI/SSP grants was eliminated beginning in 2010-11, after being suspended for several years. However, California took a step toward reinvesting in SSI/SSP during the current fiscal year (2016-17). Effective January 1, 2017, the state increased the SSP portion of the grant by 2.76 percent. This raised the monthly SSP grant to \$160.72 for individuals (an increase of \$4.32) and to \$407.14 for couples (an increase of \$10.94).

The Governor does not propose to provide a new state COLA for SSI/SSP grants during 2017-18. However, the Administration projects that the federal government will provide a 2.6 percent COLA to the SSI portion of the grant effective January 1, 2018. As a result of the federal SSI COLA:

- **The maximum monthly SSI/SSP grant for individuals would rise from the current level of \$895.72 to \$915.72 on January 1, 2018.** The projected 2018 grant level equals 92.5 percent of the current federal poverty guideline for an individual (\$990 per month).
- **The maximum monthly SSI/SSP grant for couples would increase from the current level of \$1,510.14 to \$1,539.14 on January 1, 2018.** The projected 2018 grant level equals 115.3 percent of the current poverty guideline for a couple (\$1,335 per month).

Changes to State Retirement Systems Reflected in the Governor's Budget Proposal

The Governor's proposed 2017-18 budget incorporates contributions to three state-run retirement systems: the California Public Employees' Retirement System (CalPERS), the California State Teachers' Retirement System (CalSTRS), and the Secure Choice Retirement Savings Program that was authorized in 2016.

CalPERS and CalSTRS, like many retirement systems, are not funded at levels that will keep up with future benefits, resulting in the state needing to make higher annual contributions in order to pay down unfunded liabilities. Both systems are evaluating long-term investment assumptions, including the "discount rate" that is used to estimate the level of contributions from the state and employers. The Governor's proposed 2017-18 budget includes \$5.3 billion (\$2.8 billion General Fund) for state contributions to CalPERS for state pension costs, and \$672 million General Fund for CSU retirement costs. A recent CalPERS Board decision to reduce the discount rate from 7.5 percent to 7.0 percent over the next three years (that is, to adjust downward slightly its expected rate of return on the CalPERS investment portfolio) is reflected in these estimates, resulting in additional state contributions of \$172 million (\$105 million General Fund) in 2017-18.

The Governor's proposed 2017-18 budget assumes that CalSTRS will also lower its discount rate, along with changes in other investment assumptions, requiring \$153 million in additional state contributions from the General Fund. State contributions to CalSTRS are expected to total \$2.8 billion from the General Fund in 2017-18.

In 2016, Senate Bill 1234 created the California Secure Choice Retirement Savings Program, a state-administered retirement savings program for private-sector employees in California who are not provided with retirement savings plans at their workplace. Approximately 6.8 million private-sector workers in California do not have access to a retirement savings plan. Secure Choice provides these workers with a low-cost option for investing in their retirement security. The proposed 2017-18 budget includes a \$15 million loan from the General Fund for startup and administrative costs to implement the program, which would be repaid in future years with administrative fees.

Governor Again Proposes a 10-Year Transportation Funding and Reform Package

California's expansive transportation infrastructure includes 50,000 lane-miles of state and federal highways, 304,000 miles of locally owned roads, Amtrak intercity rail services, and numerous local

transit systems, all of which are intended to facilitate the efficient movement of people and goods across the state. The state's largest category of deferred maintenance is for its existing transportation facilities.

The Governor's proposed 2017-18 budget includes a 10-year, \$43 billion transportation funding and reform package that would provide \$1.8 billion in fiscal year 2017-18. The package was first introduced in 2015 and includes a mix of new revenues, additional investments of "cap and trade" auction proceeds, accelerated loan repayments, and efficiencies in the California Department of Transportation (Caltrans).

The Governor's 10-year plan would be funded through a series of new revenue sources and redirected savings from efficiencies, including:

- \$2.1 billion from a new \$65 fee on all vehicles, including hybrids and electrics.
- \$1.1 billion from the state gasoline excise tax, which would be set at the 2013-14 rate of 21.5 cents, with the broader gasoline tax adjusted annually for inflation.
- \$425 million from an 11-cent increase in the diesel excise tax, adjusted annually for inflation.
- \$500 million in additional cap-and-trade proceeds.
- \$100 million from cost-savings reforms in Caltrans.

It is likely that the new or increased revenue sources would require a two-thirds vote in each house of the Legislature.

These revenues, split evenly between state and local governments, would be used for investments in repairing and maintaining existing infrastructure, particularly state highways, local roads, and public transit.

Administration Acknowledges Housing Crisis, but Proposes No New Funding to Address the Problem

The Governor's proposed budget includes numerous references to California's housing crisis and its implications for families and individuals as well as employers and the economy. The Governor notes that California's lack of affordable housing means that many people have less income to spend on taxable goods, which weakens sales and use tax revenues – a key revenue source for the state budget. In addition, high and rising housing costs make it harder for employers to attract skilled workers in certain areas of the state, and if businesses cannot relocate to lower-cost areas, the state's job growth could

stall. In fact, the Governor identified the state's housing crisis as a key threat to the state's economy over the next few years.

Although the Administration views the housing crisis as one of the major challenges facing California, the proposed budget includes no new funding to address the problem. Instead, the Governor eliminates \$400 million set aside for affordable housing programs in the 2016-17 budget agreement. These dollars were to be allocated only if lawmakers modified the local review process for certain housing developments, as proposed by the Governor last year. The Legislature did not adopt the Governor's so-called "by-right" proposal, and so these funds will not be available for affordable housing. The Governor also eliminates \$45 million for the Housing and Disability Advocacy Program, established in the 2016-17 budget agreement. The purpose of this program was to help people who are homeless or at risk of homelessness and who have a disability to access appropriate benefits.

Budget documents state that the Administration is "committed to working with the Legislature on the development of a legislative package to further address the state's housing shortage and affordability pressures." However, the Governor makes clear that he is not willing to provide resources through the state budget to finance any solutions, as he states that this legislative package "should not rely on the General Fund." Instead of proposing concrete solutions, the Governor outlines several principles for housing policy, which include reducing local barriers that prevent, slow down, or drive up the cost of housing developments.

Governor Makes \$2.2 Billion Allocation Plan for Cap-and-Trade Revenues Dependent on Legislative Action Affirming Program

Established by the California Global Warming Solutions Acts of 2006 (Assembly Bill 32), California's "cap and trade" program sets a statewide limit on the emission of greenhouse gases (GHGs) and authorizes the Air Resources Board to auction off emission allowances. Proceeds from these auctions are invested in activities that seek to reduce GHG emissions.

Since cap-and-trade auctions began in 2012, the state has allocated more than \$3 billion in proceeds from them. However, the revenues from individual auctions have varied widely over the past the year, a predicament that the Administration attributes in part to "perceived legal uncertainty" about the program beyond 2020.

The Governor's budget proposal calls on the Legislature to confirm, by a two-thirds vote in both the State Senate and the Assembly, the Air Resources Board's authority to administer the cap-and-trade

program beyond 2020. Contingent on this legislative action, the Governor proposes a \$2.2 billion Cap and Trade Expenditure Plan for 2017-18, with the dollars allocated to high-speed rail and other transit investments, affordable housing, pollution-reduction projects, and other activities aimed to promote sustainability and energy efficiency.