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Budget Proposal Misses Opportunity to Invest in Californians, Focuses Instead on Adding to Reserves

On January 7, Governor Jerry Brown released his proposed 2016-17 state budget, forecasting annual revenues that are $3.5 billion higher than previously projected for the current fiscal year (2015-16) and $2.4 billion higher for 2016-17. Despite this stronger-than-expected revenue growth, the Governor's proposed budget misses a chance to boost investment in broadening Californians' economic opportunity and security while still saving for a rainy day and paying down state debts.

The Governor's proposal sets aside a portion of 2016-17 revenues – $3.1 billion – with half deposited in the state's rainy day fund and half used to pay down state debts, as required by Proposition 2 (2014). However, the Governor also proposes to deposit an additional $2 billion in the rainy day fund *beyond* Proposition 2's requirements, leaving significantly less funding for other priorities.

While heavily emphasizing growing the reserves, the Governor's proposal misses several opportunities to strengthen vital public services and systems. It includes only modest increases for higher education – a key to the state's economic future – no significant reinvestment in child care, and no additional investment in a welfare-to-work system that was deeply cut in recent years. Meanwhile, the proposal does not include a plan to tackle systemic issues – including over-reliance on incarceration – that contribute to ongoing prison overcrowding and persistently high corrections spending.

The Governor's proposal takes a number of positive steps, including continuing support for the state's new Earned Income Tax Credit (EITC); advancing a new proposal to revise and extend a tax on managed care organizations (MCOs) that, if left unaddressed, would result in a $1 billion General Fund shortfall; and providing the first state cost-of-living adjustment (COLA) since 2006 for cash grants for low-income seniors and people with disabilities. The Governor's proposal also reflects a sizeable boost in funding for K-12 schools due to a growing economy and the temporary tax increases put in place by Proposition 30 (2012).

Despite a strong revenue outlook, the Governor's budget proposal falls short of presenting a plan that adequately prepares the state for future growth by striking a balance between saving for a rainy day and addressing the state's biggest challenges: stagnating wages for low- and middle-income Californians, widening income inequality, and public supports weakened by years of disinvestment.

The following sections summarize key provisions of the Governor's proposed 2016-17 budget. Please check the Budget Center's website (calbudgetcenter.org) for our latest commentary and analysis.

California's Job Market Is Expected to Continue Improving, but Millions Still Struggle to Meet Basic Needs

The Administration forecasts that California's labor market will continue to improve. The state's unemployment rate is expected to further decline to an annual average of 5.7 percent in 2016, down by more than half since its peak annual average of 12.2 percent in 2010, and California is expected to see continued growth in personal income as well as the labor force. In addition, the Administration expects wages to rise amid a more competitive job market as high-skilled young workers enter the workforce.

Although an improved economic outlook is welcome news, several years of job market gains have yet to translate into broadly shared prosperity throughout the state, and economic hardship remains one of the most significant challenges facing California. Millions of Californians cannot adequately support themselves and their families, suggesting that greater state investments are needed to ensure that a high quality of life is within everyone's reach. Nearly 1 in 6 state residents – more than 6 million people – struggle to meet their basic needs as measured by the federal poverty line, which is about $19,000 in annual income for a family of three. California's official poverty rate – 16.4 percent in 2014 – remained a full 4.0 percentage points higher than in 2007, the year the national recession began, in spite of a steady decline in the state's unemployment rate. In fact, poverty rates in most California counties were still higher in 2014 than they were seven years earlier, even in several San Francisco Bay Area and southern California counties with booming job markets. And yet these facts substantially *understate* the extent of economic insecurity throughout the state. A better indicator of economic well-being shows that about 4 in 10 state residents (40.8 percent) lived in or near poverty in 2013. This indicator, the California Poverty Measure, improves on the official poverty measure by accounting for how California's high cost of living makes it challenging to make ends meet and by factoring in how public supports, such as food assistance, can help families get by.

Again This Year, Governor's Proposal Projects Higher Revenues Than Previously Assumed

Along with continued growth in California's economy, the Administration projects General Fund revenues in 2015-16 and 2016-17 that are higher than previously assumed in the 2015-16 budget agreement. Before accounting for transfers, such as to the rainy day fund, General Fund revenue is projected to be $3.5 billion higher in 2015-16 and $2.4 billion higher in 2016-17. Over the three-year "budget window," from 2014-15 to 2016-17, pretransfer General Fund revenue is now projected to be $5.9 billion higher than assumed in the 2015-16 budget agreement.

The Administration attributes this growth to high-income earners' continuing to do well economically, with high capital gains and strong growth in wages, resulting in higher taxes owed. Overall wage growth is forecast to be higher than previously anticipated, but because growth in wage withholding has been stronger than overall wage growth, the Administration notes that "increases in wages are likely more concentrated among high-income taxpayers."

The long-term revenue picture forecast by the Governor is significantly improved from last January's projection. However, the Administration now projects that the expiration of the high-income tax rate increases in Proposition 30, at the end of 2018, will result in a small but outright decline in General Fund revenue in 2018-19 from the "big three" taxes: the personal income, sales, and corporate income taxes. Last year, the Administration projected that the final expiration of Proposition 30 would result in a slow-down of General Fund revenue growth from the "big three," but not a year-to-year decline.

The Governor's Proposal Sets Aside Billions 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 Governor's proposed 2016-17 budget, reflecting higher-than-anticipated revenue collections, projects that by the end of the current fiscal year (2015-16) the BSA account will total $4.5 billion. Based on the Governor's revenue projections for 2016-17, Proposition 2 would constitutionally require the state to set aside an additional $3.1 billion ($1.56 billion to the BSA and $1.56 billion to repaying budgetary debt). Beyond the constitutional requirements of Proposition 2, the Governor proposes an additional transfer to the BSA of $2 billion, bringing the state's rainy day fund to just over $8 billion by the close of 2016-17.

The BSA is not California's only reserve fund. Each year, the state deposits unspent funds into a "Special Fund for Economic Uncertainties." For 2016-17, the Governor's proposes to allocate $2.2 billion to this fund. Including this fund, the Governor's proposal would build state reserves to a total of $10.2 billion in 2016-17.

The choice to allocate additional General Fund revenues to the BSA, beyond what is required by Proposition 2, means that significant funding is not available to invest in other vital public systems and services.

Governor Calls for Revising and Extending the "MCO Tax" as Part of a Broader Tax Reform Package

In recent years, California has imposed a tax on managed care organizations (MCOs) that operate Medi-Cal managed care plans. This tax allows the state to bring in additional federal funding for Medi-Cal, which provides health care services to more than 13 million Californians with low incomes. The MCO tax also reduces – or "offsets" – state spending on Medi-Cal by roughly $1 billion. In turn, these General Fund savings are used to support other state priorities.

The MCO tax expires on July 1. Without an extension, the General Fund offset will end, leaving a roughly $1 billion shortfall in the 2016-17 state budget. Despite months of negotiations, state policymakers and health plans have not been able to reach an agreement on extending this tax, an action that requires a two-thirds vote of each house of the Legislature.

The Governor's proposed budget assumes that the Legislature will approve a revised, "federally allowable" MCO tax that would take effect on July 1, 2016, and remain in place for three years. Budget documents indicate that the revised MCO tax would be part of a broader "tax reform package." During a January 7 press conference, an Administration official stated that this package would encompass the MCO tax, the corporate income tax, and the gross premiums tax and would result in a $90 million net benefit to the private managed care industry. Health plans would also be allowed to charge "differential rates" for Californians enrolled in Medi-Cal managed care plans compared to other health plan enrollees, according to the Administration. In addition to maintaining the annual $1 billion General Fund offset, the Governor's MCO tax proposal would provide funding for the In-Home Supportive Services Program and could be used to increase payments for services provided to people with developmental disabilities.

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. The Governor's proposed budget assumes a 2016-17 Proposition 98 funding level of $71.6 billion, $2.4 billion above the revised 2015-16 minimum funding level. The Proposition 98 guarantee tends to reflect changes in state General Fund revenues, and estimates of 2014-15 and 2015-16 General Fund revenue in the proposed budget are higher than those in the 2015-16 budget agreement. As a result, the Governor's proposed 2016-17 budget reflects increases in prior-year Proposition 98 funding levels above those assumed in the 2015-16 budget agreement. The Governor's proposed budget assumes a 2015-16 Proposition 98 funding level of $69.2 billion, $766 million more than the level assumed in the 2015-16 budget agreement, and a $66.7 billion 2014-15 Proposition 98 funding level, $387 million above the level assumed in the 2015-16 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. Specifically, the Governor's proposed budget:

- **Provides $2.8 billion 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 2016-17 LCFF funding level would "bring total formula implementation to 95 percent."
- **Provides $1.3 billion 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 cost-of-living adjustments (COLAs) for non-LCFF programs.** The Governor's proposed budget funds a 0.47 percent COLA ($22.9 million) for several categorical programs that remain outside of the LCFF, including special education, child nutrition, and American Indian Education Centers. The Governor proposes to use the increases in LCFF grants proposed for school districts and charter schools to fund the COLA for non-LCFF programs.

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. The Governor's proposed budget provides funding to increase access to career technical education programs, increases funding for CCC general-purpose apportionments, and reduces mandate debt the state owes to CCCs. Specifically, the Governor's proposed budget:

- **Increases CCC funding by nearly $250 million to support career technical education.** In 2015, the CCC Board of Governor's Task Force on Workforce, Job, Creation, and a Strong Economy (the Strong Workforce Task Force) made a series of recommendations to enhance the capacity of the CCCs to prepare students for high-value jobs in regions throughout California. The Governor's proposed budget provides $200 million to support the "Strong Workforce Program, which will enable community colleges to expand access to additional career technical education courses and programs and to implement a regional accountability structure that is aligned with the Task Force's recommendations." The Governor's proposal also increases funding by $48 million for the Career Technical Education Pathways Program to expand career technical education programs that build upon existing regional capacity to meet regional labor market demands.
- **Increases apportionment funding by $114.7 million.** The proposed increase in apportionments – which provide general purpose funding for CCCs – represents a 2 percent increase in full-time equivalent enrollment.
- **Provides $76.3 million in one-time funding to reduce mandate debt the state owes to CCCs.** Mandate debt is the cost of state-mandated services that CCCs provided in prior years, but for which they have not yet been reimbursed.
- **Provides $29.3 million to fund a 0.47 percent COLA for apportionments.** The budget agreement also includes an increase of $1.3 million to provide a 0.47 percent COLA for Disabled Student Programs and Services, Extended Opportunity Programs and Services, Special Services for CalWORKs Recipients, and the Child Care Tax Bailout program.

Administration Continues Modest Funding Increases for CSU and UC

The Governor's proposed budget continues a multiyear plan that modestly increases General Fund spending for the California State University (CSU) and the University of California (UC), with the expectation that CSU and UC will improve performance standards and avoid tuition and fee hikes. Specifically, the Governor's proposed budget:

- **Increases funding for CSU by $125.4 million in 2016-17.** The Governor's proposal states that the Administration expects that CSU will adopt a funding model in 2016-17 that is based primarily "on student success that targets additional resources to campuses that are successfully serving the students with the greatest needs."
- **Increases funding for UC by $125.4 million in 2016-17.** The proposed budget indicates that UC is expected to implement reforms and achieve outcomes specified in a 2015 agreement

between the Governor and the UC President, such as reducing student time-to-degree outcomes and improving instruction and operations through the utilization of data and technology.

Governor's Proposal Creates an Early Education Block Grant

California currently supports the educational needs of children ages 3 to 5 in a variety of ways. The California State Preschool Program (CSPP) provides full- and part-day preschool for three- and four-year-olds from low- and moderate-income families through a mixed-delivery system, which includes local education agencies (LEAs), colleges, and private organizations. California's Transitional Kindergarten (TK) program provides an additional year of kindergarten for four-year-olds turning five between September 2 and December 2, regardless of family income. In addition, the 2015-16 budget agreement clarified that schools could provide "expanded" TK for children turning five after the December 2 cutoff date with local funds, while drawing down state funds as soon as the child turns five.

The Governor proposes consolidating funding for these programs into an early education block grant. The state would create a single funding stream by reappropriating $726 million Proposition 98 General Fund for TK, $878 million Proposition 98 General Fund for the CSPP, and $50 million Proposition 98 General Fund for the CSPP Quality Rating and Improvement System. (These funding levels reflect an increase in funding for CSPP of $5.5 million Proposition 98 General Fund for growth and a COLA).

The Administration's stated goals for merging these funding streams include providing LEAs with improved financial flexibility to meet local needs, while prioritizing services for low-income and at-risk four- and five-year-olds. Early education block grant funding would be distributed based upon increases or decreases in the target populations, while ensuring that no LEA receives less funding than under prior models.

The Administration plans to engage stakeholders in the development of the block grant throughout the next few months. It is not yet clear whether the new block grant would maintain the mixed-delivery system, including both LEAs and non-LEA providers, such as private organizations, or how the new block grant would provide funding for three-year-olds currently participating in the CSPP. In addition, $140 million in General Fund dollars for non-LEA full-day preschool ("wraparound care") has not been included in the new block grant, but the proposal does not specify whether this funding would continue to provide wraparound care or if it would be used elsewhere. Finally, the proposal does not outline how the block grant will ensure that programs meet quality standards and are developmentally appropriate.

Governor's Proposal Does Not Significantly Reinvest in Child Care or Address New Federal Guidelines

California's child care and development system helps prepare children for school and provides affordable care so parents can find jobs and remain employed. State policymakers failed to maintain state support for this system during and after the Great Recession, cutting annual funding for programs by roughly 40 percent, after adjusting for inflation, and eliminating more than 100,000 child care and preschool "slots." Recent years' budget agreements have increased support for these programs, but 2015-16 funding for child care and preschool slots is more than 20 percent lower than that in 2007-08, after adjusting for inflation, and the number of subsidized slots remains far lower than prior to the recession.

In 2014, Congress reauthorized the Child Care and Development Block Grant (CCDBG), which provides federal funding for subsidized child care. Part of this reauthorization included new provisions aimed at boosting the quality of subsidized child care. The 2016 federal omnibus spending bill provides additional funding for the block grant, which is reflected in the Governor's proposed budget ($10.4 million federal funds). Yet, California's share of the federal funds is unlikely to cover the state's entire cost for coming into compliance with the new federal regulations.

The Governor's 2016-17 proposal does not significantly reinvest in the child care and development system, nor does it address CCDBG reauthorization. The proposal does propose other changes to the system. Specifically, the proposed budget:

- **Recommends the consolidation of the state's provider rate system.** Currently, eligible families can access subsidized child care through a provider that contracts directly with the state *or* by using a voucher to access care of their choice. Contract and voucher providers have different licensing requirements along with separate rate systems to reflect these requirements.
- **Provides additional funding for "growth" and a COLA.** The Governor's proposal provides a 0.13 percent increase in funding due to population growth, which will increase spending for subsidized child care by $1.0 million General Fund. The proposal also includes a COLA of 0.47 percent for non-CalWORKs child care programs, which will increase spending by $3.5 million General Fund.

Governor's Proposal Does Not Reinvest 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 failed to maintain core benefits to CalWORKs during and after the recession, substantially reducing cash aid for families and imposing a 24-month limit on the amount of time CalWORKs parents can access the full array of welfare-to-work activities available under state law before having to meet less flexible federal work participation requirements.

The Governor's proposed budget does not make any new investments in CalWORKs. Despite being modestly increased in recent years, CalWORKs grants remain below pre-recession levels and fail to lift most families out of "deep poverty," which is defined as having an income that is below half the federal poverty line ($10,045 for a family of three in 2015). Further, the CalWORKs grant is lower than analogous cash assistance in many other states when factoring in California's high cost of living. Finally, California has a family cap rule, known as the Maximum Family Grant (MFG), which is widely regarded as punitive and racist. The MFG only serves to plunge low-income children deeper into poverty by denying additional CalWORKs cash assistance when a child is conceived and born while any member of the family is already receiving assistance.

Proposed Budget Provides a State COLA for SSI/SSP Grants for the First Time Since 2006

Supplemental Security Income/State Supplementary Payment (SSI/SSP) grants help 1.3 million low-income seniors and people with disabilities to purchase food, housing, and other basic necessities. Grants are funded with both federal (SSI) and state (SSP) dollars. State policymakers made deep cuts to SSI/SSP cash assistance in recent years. SSP grants for couples and for individuals were reduced to federal minimums in 2009 and 2011, respectively. In addition, the annual state COLA for SSI/SSP grants was eliminated beginning in 2010-11, after being suspended for several years. Due to these changes, the maximum SSI/SSP grant for individuals dropped below the federal poverty line in 2009 – and remains below the poverty threshold today.

The Governor proposes to provide a state COLA "to the SSP portion of the grant" effective January 1, 2017, at a cost of $40.7 million in 2016-17. This increase – estimated to be 2.96 percent – would be the first state COLA provided for SSI/SSP grants since 2006, according to budget documents. In addition, the Administration estimates that the *federal* COLA for the *SSI* portion of the grant will be 1.7 percent effective January 1, 2017. As a result of these changes, under the Governor's proposed budget:

- **The maximum SSI/SSP grant for individuals would rise from the current level of $889 per month to $907 per month on January 1, 2017.** This grant level equals 92.5 percent of the current federal poverty line for an individual ($981 per month).
- **The maximum SSI/SSP grant for couples would increase from the current level of $1,496 per month to $1,527 per month on January 1, 2017.** This grant level equals 115.0 percent of the current poverty line for a couple ($1,328 per month).

Budget Proposal Implements New Rules for Home Care Workers, Allocates Some "MCO Tax" Revenues to IHSS

Many seniors and people with disabilities rely on the In-Home Supportive Services (IHSS) Program, which helps people with low incomes remain safely in their own homes, preventing the need for more costly out-of-home care. IHSS enrollment is projected to rise from nearly 464,000 in 2015-16 to roughly 490,000 in 2016-17, a 5.7 percent increase. The Governor's proposed budget:

- **Reflects the implementation, on February 1, 2016, of new federal labor rules affecting home care workers.** These new federal regulations mandate overtime pay for home care workers, including IHSS providers, and require that workers be paid for time spent in transit between multiple consumers and at medical appointments. IHSS providers will be paid overtime for working more than 40 hours per week, but under state law are limited to a 66-hour work week. The Administration estimates that implementing these regulations will increase General Fund spending by $331.3 million in 2015-16 and by $443.8 million annually in subsequent years. These rules initially were scheduled to take effect in January 2015, but the Governor postponed implementation after a federal court ruled that the regulations exceeded federal authority. A federal appeals court subsequently upheld the rules, paving the way for their implementation in California.
- **Proposes to use revenues from a revised tax on managed care organizations (MCOs) to fund some IHSS costs.** As noted in a previous section (see page 4), the Governor has proposed a revised MCO tax to replace the current version of the tax, which expires on July 1. The Governor proposes to use some revenues from the new MCO tax to pay for certain IHSS costs that are currently funded with General Fund dollars. Specifically, MCO tax revenues would be used to pay for 7 percent of IHSS consumers' authorized hours of care, at a cost of $236.2 million in 2016-17.

Proposed Budget Increases Corrections Spending, Projects Relatively Low State Savings From Proposition 47

Currently, the state incarcerates 127,500 people in prisons and other facilities. Of this total, 112,700 people are housed in state prisons designed to hold 82,700 – putting the prison system at 136.3 percent of its "design capacity." Although prisons remain overcrowded, the state is in compliance with a federal court order to reduce overcrowding to no more than 137.5 percent of prisons' capacity by February 28, 2016. California also incarcerates 14,800 people in facilities that are not subject to the court-imposed population cap, including fire camps, in-state "contract beds," and out-of-state facilities.

The total number of people incarcerated by the state has declined by more than one-quarter since peaking at 173,600 in August 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. These include voter approval of Proposition 47 in 2014, which reclassified several drug and property crimes as misdemeanors. Because of Proposition 47, state prison is no longer a sentencing option for these crimes, and the resulting state savings – as determined by the Governor's Department of Finance each year – must be allocated to local mental health and drug treatment programs (65 percent), services for at-risk youth (25 percent), and trauma recovery services for crime victims (10 percent).

The Governor's proposed budget does not include a plan to tackle the systemic issues, including the state's over-reliance on incarceration, that contribute to ongoing prison overcrowding and persistently high corrections spending. Instead, the Governor's proposal:

- **Provides $10.3 billion in General Fund support for the California Department of Corrections and Rehabilitation (CDCR) in 2016-17.** This is up from an estimated $10.1 billion in 2015-16.
- **Estimates that state savings from Proposition 47 in the current fiscal year (2015-16) will total $29.3 million.** Annual savings in subsequent years are expected to be approximately $57 million, according to the Administration. In contrast, last year the nonpartisan Legislative Analyst's Office (LAO) projected annual state savings in the range of $100 million to $200 million. The Governor's final savings calculation for 2015-16 is due on or before July 31.
- **Provides $328.7 million in General Fund support for the Board of State and Community Corrections (BSCC) in 2016-17.** This is up from an estimated $67.8 million in 2015-16. This substantial increase is largely due to the Governor's decision to set aside $250 million to renovate or replace jails, primarily in small counties, with counties required to provide up to a 10 percent match. In addition, the proposed budget includes $20 million for local police departments, with these dollars intended to "increase positive outcomes between city police and the homeless community, persons with mental health needs, and high-risk youth

populations," according to budget documents. The BSCC would administer both of these funding streams.

- **Projects that counties will receive $1.3 billion in special fund dollars in 2016-17 to support their role in supervising many adults convicted of "low-level" felonies.** This is up from an estimated $1.2 billion in 2015-16. Counties receive these funds as part of the 2011 transfer – or "realignment" – of certain public safety responsibilities from the state.

The Governor's Proposed Budget Does Not Contain Any New Major Investments in Affordable Housing

The high costs of housing remain a significant challenge for Californians. The state's affordable housing crisis is widely acknowledged, but recent legislative efforts to boost state support for affordable housing development have stalled. Despite these challenges, the Governor's proposed budget does not substantially increase the state's role in expanding access to affordable housing. While the proposed budget does continue the required allocation of "Cap and Trade" revenues to the Affordable Housing and Sustainable Communities Program ($400 million in 2016-17), which helps fund the construction of affordable housing, there are no other major proposals for affordable housing. In public remarks, however, the Administration noted that a recent major legislative proposal to reduce homelessness would be considered.

The Administration Expresses Tentative Support for a "Regional" Minimum Wage

As part of the 2016-17 budget release, the Administration clarified its position on additional increases to California's minimum wage, which rose to $10 an hour on January 1, 2016. The Governor's budget summary expresses skepticism about an additional increase to the statewide minimum wage, citing the fiscal impact on public employee salaries and the potential for private sector job losses as a result of higher business costs. Moreover, the Governor's budget says that any further statewide minimum wage increases should have appropriate "off-ramps" during an economic downturn, though it does not specify what those provisions would be and how they would affect workers.

While the Administration has concerns about an additional statewide minimum wage increase, Governor Brown did express, at his budget release press conference, a tentative openness to statewide legislation that sets different minimum wage levels *by region*. A regional minimum wage increase would likely vary based on differences in local economies, such as the cost of living. For instance, since Bakersfield has a much lower cost of living than San Francisco, its regionally-adjusted minimum wage would be lower than San Francisco's. Also, a statewide effort to implement regional minimum wages would reach workers living in higher-cost localities that are not currently pursuing their own increases.

While a regional minimum wage increase has merit, there are also practical concerns about implementation. These include how to define a region in California and what metrics should be used to determine minimum region-specific wage levels. This is especially important since the "formula" used to determine regional wage increases would play a powerful role in determining wage levels across California moving forward.

Governor Proposes Allocating $2.0 Billion for Maintenance and Improvement of State Facilities

As part of the Administration's 2016 Five-Year Infrastructure Plan, the Governor proposes to use $2.0 billion General Fund to renovate or replace "aged and inadequate" state office buildings in Sacramento and address deferred maintenance needs at various state facilities. This proposal diverges from the more common state practice of issuing lease-revenue bonds – money the state borrows and pays back over a number of years – to finance the construction and renovation of state facilities. The Governor's choice to use a one-time General Fund allocation for the renovation and replacement of buildings rather than issue bonds means that the costs of financing the projects identified in his budget proposal would be concentrated in the budget year, rather than spread out over time. As a result, fewer General Fund dollars would be available to support other investments in 2016-17. Specifically, the Governor's proposed budget:

- **Allocates $1.5 billion General Fund to renovate or replace certain state office buildings,** including the Capitol Annex building, the Natural Resources Agency building, and the Department of Food and Agriculture Annex.
- **Provides $500 million General Fund to address "the most critical statewide deferred maintenance needs,"** including at state parks, universities, community colleges, prisons, and state hospitals.

Governor Reiterates Last Year's Call for Reducing Unfunded Liability for Retiree Health Care

In January 2015, the Governor called for reducing 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. Like last year, the state faces a $72 billion unfunded liability for the costs of these benefits, and this liability will grow substantially over time if not addressed.

In this year's budget proposal, the Governor cites last fall's state agreement with Bargaining Unit 9 (professional engineers) as a model for how to reduce the liability while preserving retiree health benefits. The LAO summarizes the key points of how that agreement achieves the desired long-term savings as follows: "(1) require current and future employees and the state to begin contributing a specified percentage of pay toward an invested trust fund to prefund retiree health benefits beginning in 2017-18 and (2) significantly reduce the amount of subsidies that employees hired after January 1, 2016 will receive for health benefits after they retire." The Administration aims to reach this goal through labor contract negotiations with additional bargaining units in 2016-17.