CALIFORNIA SENATE REPUBLICANS

Highlights and Analysis of the 2024-25 Governor's Budget

January 22, 2024

SENATE REPUBLICAN
FISCAL OFFICE

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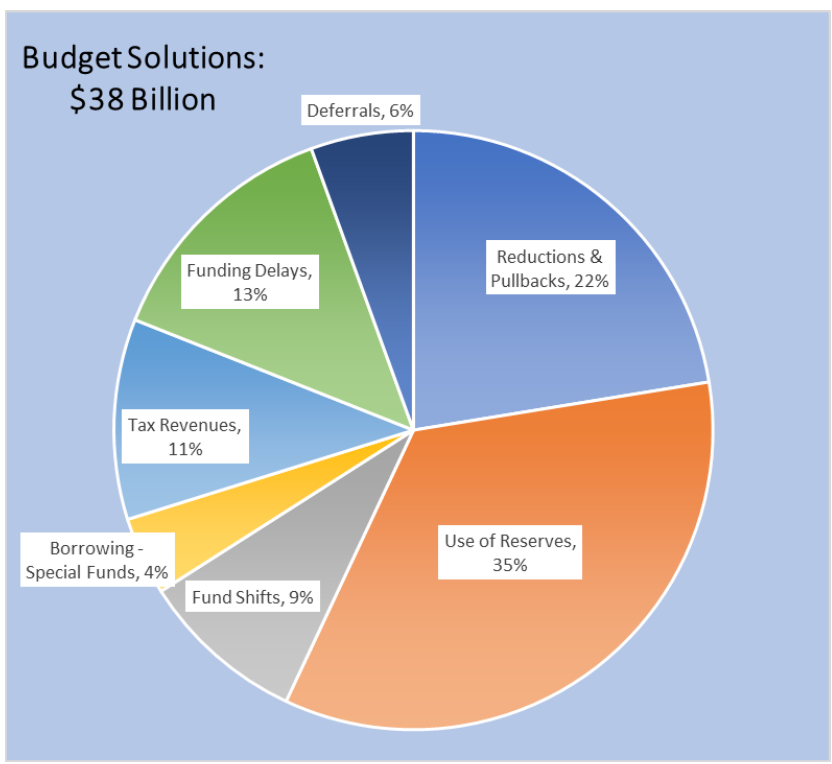
Executive Summary

Governor's Deficit Substantially Lower Than Nonpartisan Estimate. The Governor's January budget package projects a deficit of $38 billion by the end of 2024-25. This is $30 billion lower than the $68 billion deficit estimated by the nonpartisan Legislative Analyst's Office (LAO) in December. The most significant part of the difference results from the Governor's projection that tax revenues will be higher by $15 billion compared to the LAO estimate. Much of the remainder is the result of differing assumptions regarding whether to treat Proposition 98 education adjustments as part of the baseline or as a solution that the Legislature needs to adopt.

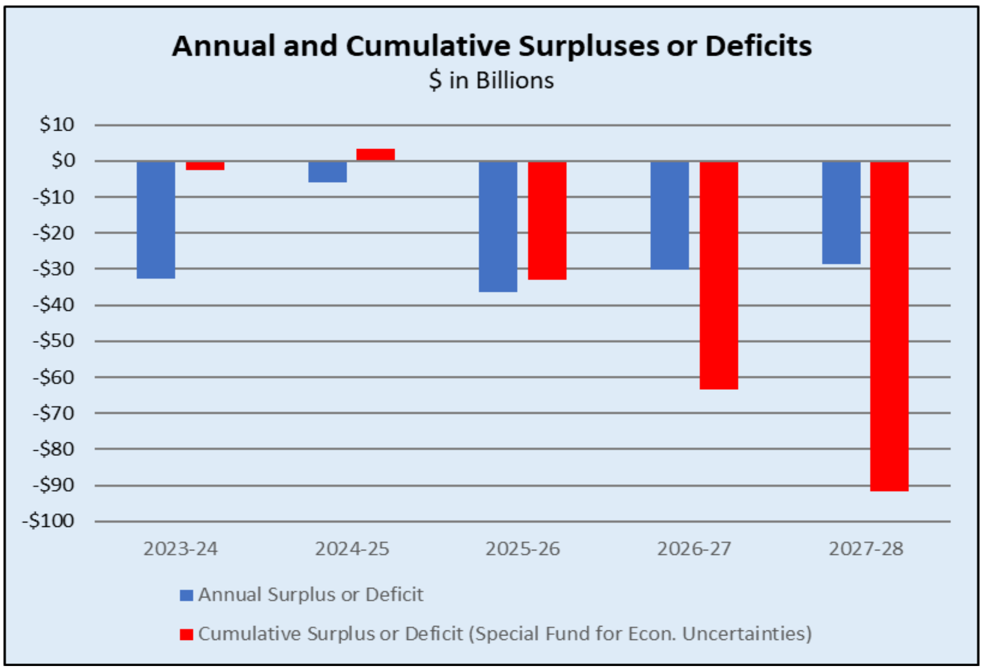
Short-Term Solutions Despite Long-Term Deficits. In order to address the deficit, the Governor proposes a mix of solutions totaling $38 billion that largely use one-time actions and budget gimmicks, rather than actual, on-going reductions that would create a truly sustainable budget. The solution categories are summarized in the chart and descriptions below.

- **Reserves.** $13 billion by drawing down budget reserves, including $12 billion from the state Rainy Day Fund and $900 million from the Safety Net Reserve.
- **Reductions and Pull-Backs.** $8.5 billion from various reductions and pull-backs of previously approved increases, most significantly including $2.9 billion for various climate programs, $1.2 billion for housing programs, and $350 million for previously approved local projects.
- **Delays.** $5.1 billion to delay previously scheduled spending, including $1 billion for transit and inner city rail and $613 million for developmental services payment rate increases.



- **Fund Shifts.** $3.4 billion by shifting General Fund expenses to state special funds, including $1.8 billion to the Greenhouse Gas Reduction Fund (cap and trade) and $1.3 billion in state retirement contributions to Proposition 2 debt payments.
- **Revenue Changes.** $4.1 billion by increasing the state's share of the managed care organization tax ($3.8 billion) and $300 million through greater limits on corporate net operating loss (NOL) deductions.
- **Deferrals.** $2.1 billion through various deferrals, most notably by shifting $1.6 billion in state payroll from 2024-25 to the following year (a cash accounting shift that is a "savings" on paper only). This category also includes $499 million to postpone increases for the University of California and California State University. Note that "deferrals" differ from "delays" ostensibly by including a higher level of obligation to actually provide the funds in the future.
- **Internal Borrowing.** $1.6 billion by authorizing the General Fund to borrow more money from state special funds, such as the AIDS Drug Assistance Rebate Fund ($500 million). This adds to last year's borrowing, when the state borrowed $2.7 billion from special funds to close that deficit.

Massive Deficits Persist Throughout Forecast. The Governor's multiyear forecast also indicates the state will have operating deficits each year through 2027-28, as illustrated in the chart below. Because the proposed solutions are largely one-time in nature, expenditures never adjust to match revenues in the Governor's budget forecast.



Revenues Fall Far Short. California's tax revenue outlook remained more uncertain than usual at the time of the 2023-24 budget's passage last summer, a result of the federal government shifting the tax filing deadline to November. Even so, the LAO had projected that tax revenues would be lower than assumed in the enacted budget. The Governor's January budget reflects revenues of $198 billion in 2023-24, lower than budgeted by $10 billion, which would grow slightly to $204 billion in 2024-25. Altogether, the Governor's budget estimates that revenues will be lower by nearly $43 billion combined through the 2024-25 budget year than assumed in last summer's enacted budget.

Expenditures Remain Unsustainable. General Fund expenditures under the Governor's proposal would reach a revised total of $231 billion in 2023-24, which, surprisingly, remains about $5 billion above the enacted budget level of $226 billion. Expenditures would then decline by about 10 percent to $209 billion in 2024-25 before starting to grow again. Because the Governor's deficit solutions rely heavily on one-time delays and shifts, as described above, expenditures remain above revenue in each year of the Governor's forecast through 2027-28.

Some Reserves Remain After Budget Solution. The proposed budget would utilize $13 billion from the state's reserves, maintaining an estimated $18 billion in total reserves. The proposed withdrawals and remaining reserve balances include the following categories:

- Withdrawal of $10.4 billion from the mandatory balance, and $1.8 billion from the discretionary balance of the state's Rainy Day Fund. This would leave $11.1 billion in the Rainy Day Fund.
- Withdrawal of $5.7 billion from the Proposition 98 Rainy Day Fund, leaving a balance of $3.8 billion.
- Withdrawal of $900 million from the Safety Net Reserve Fund, zeroing out the balance.
- A $3.4 billion balance in the discretionary reserve (the Special Fund for Economic Uncertainty).

Housing and Homelessness

Significant Reduction in Funding for Housing Production. The budget proposes to eliminate $1.2 billion in funding provided to various housing programs in previous years. A few notable reductions include $300 million from the Regional Early Action Planning Grant program, $250 million from the Multi-Family Housing Program, and $200 million from the Infill Infrastructure Grant program.

Delays in Homelessness Funds. The Governor's budget proposes various delays for homelessness programs including $260 million for the Homeless Housing, Assistance, and Prevention Program. What remains lacking is an acknowledgement that throwing billions of dollars at this problem is not working. Recent counts show an increase of 11,000 homeless in the last 12 months, putting the state at about 181,400 homeless Californians, despite spending billions on the problem.

K-12 Education

Proposition 98 Education. The Budget includes $127 billion ($76 billion General Fund and $50 billion other funds) for all K-12 education programs. The revised Proposition 98 funding for K-12 schools and community colleges is about $99 billion in 2022-23, $106 billion in 2023-24, and $109 billion in 2024-25. These revised levels reflect decreases of $9.1 billion in 2022-23 and $2.7 billion in 2023-24 compared to the 2023 budget act. Proposition 98 General Fund spending per pupil would be $17,653 in 2024-25 and $23,519 per pupil from all funding sources.

Local Control Funding Formula. The budget notes a $1.4 billion decrease in the Local Control Funding Formula (LCFF). This reflects a 0.76 percent cost-of-living adjustment (COLA) and population growth adjustments. The budget proposes withdrawing $2.8 billion from the Proposition 98 reserve in 2023-24 and $2.2 billion in 2024-25 to support LCFF costs. The budget also uses $39 million in re-appropriation and reversion funding.

Proposition 98 Reserve. The budget reflects a revised final balance in the Public School System Stabilization Account of $3.8 billion at the end of 2024-25. This decrease reflects a revised deposit of

$339 million in 2022-23 and net withdrawals of about $2.8 billion in 2023-24 and $1.9 billion in 2024-25. The account balance would be $5.7 billion in 2023-24, triggering the previously authorized (but ill-advised) local school district reserve cap.

School Facility Funding Cuts and Delays. The budget proposes cutting the School Facilities Program funding in 2024-25 by $500 million one-time General Fund. There would also be a delay of $550 million from 2024-25 to 2025-26 for the California Preschool, Transitional Kindergarten and Full-Day Kindergarten Facilities Grant Program. This is the second delay of this funding, which was delayed from 2023-24 to 2024-25 in the 2023 budget act.

Literacy Screening. The budget includes $25 million ongoing Proposition 98 General Fund in the K-12 Mandate Block Grant to support training educators to screen students in kindergarten through second grade for reading difficulties, including dyslexia. The screenings are to be rolled out by 2025-26.

Charter School Funding Eligibility. The budget proposes statutory changes that would make charter schools eligible for funding from the Education Revenue Augmentation Fund (ERAF). The ERAF was created in 1992 and redirects a share of property taxes statewide from cities, counties and special districts to K-14 schools. Charter schools were established the same year as ERAF, and it has never been clarified if they are eligible for this funding.

Higher Education

Compact Increase Deferrals. As part of the Governor's deficit solution package, the budget would defer the five percent increases previously agreed upon through the compacts, including $240 million to the California State University and $228 million to the University of California to 2025-26. Notably, the CSU trustees recently voted to approve a 6 percent tuition increase to help plug a budget deficit.

Resident Undergraduate Enrollment Growth Deferral. As an additional part of the Governor's deficit solution package, the budget would defer $31 million General Fund to offset revenue reductions associated with replacing 902 nonresident undergraduate students enrolled at three UC campuses.

Health

Getting More from the Managed Care Organization (MCO) Tax? The Governor's budget scores an additional $3.8 billion in General Fund relief from the MCO tax approved by the Legislature in 2023. The tax was officially approved by the federal government in December 2023, but the Governor is now seeking early action by the Legislature to request that the federal government approve a new smaller MCO tax only on Medi-Cal managed care plans that would add $1.5 billion in General Fund proceeds above the 2023 Budget Act estimates. In addition, the administration will also accelerate the use of an additional $2.3 billion that had been set aside for Medi-Cal provider rate increases in future fiscal years for additional General Fund budget relief in 2024-25. The administration claims that the proposed Medi-Cal provider rate increases will be funded as planned but that in future fiscal years the General Fund will have to cover more of the cost of the higher rates. More details will come when the draft trailer bill language is released.

$4.1 Billion to Continue Medi-Cal Eligibility Expansion to the Undocumented. Despite the obvious need to help at-risk hospitals stay open and build more mental health treatment beds for the homeless, the Governor's budget maintains $4.1 billion in General Fund for the last phase of the planned expansion of full-scope Medi-Cal eligibility to all low-income undocumented individuals. On January 1, 2024, an estimated 700,000 undocumented individuals aged 26-49, became eligible for full-scope

Medi-Cal. The state currently spends an estimated $2 billion annually for the previous expansions to those undocumented individuals age 25 and under and age 50 and above.

Regret on Health Care Minimum Wage Bill? Just months after signing the costly health care minimum wage bill (SB 525), Governor Newsom is now asking the Legislature for immediate action to change the law to add an annual “trigger” to make the minimum wage increases subject to General Fund revenue availability and to exempt state-run facilities such as University of California healthcare facilities. Details are unknown at this time, but this action will likely save more than $2 billion in 2024-25.

Delayed Funding for Mental Health Beds. Despite the overwhelming need to treat our growing homeless population, the Governor is proposing to delay $375 million in General Fund for mental health infrastructure, including funds for long-term treatment beds and short-term crisis beds. The administration is banking on the voters approving Proposition 1 on the March 2024 ballot, which would allow for a $6.38 billion bond to expand the capacity of mental health treatment beds.

Developmental Services

Breaking a Promise to the Developmentally Disabled. The Governor proposes to break a promise to the families and service providers of the developmentally disabled by slowing down, by one year, the planned implementation of service provider rate increases. Despite the Governor finding enough funding for the undocumented Medi-Cal expansion and for abortion industry subsidies, the Governor is proposing to delay $613 million General Fund in 2024-25. This delay will hamper the delivery of needed services to one of the state’s most vulnerable populations.

Human Services

In-Home Supportive Services Expansion. The 2024 budget continues the expansion of In-Home Supportive Services (IHSS) to undocumented immigrants of all ages, with costs of approximately $383 million General Fund for benefits and $15 million for administration. It will take a few years to reflect the full costs of this expansion as more individuals enroll.

CalWORKs Cuts and Reversions. The budget includes a reversion of $336 million General Fund from the 2022-23 CalWORKs Single Allocation, plus $41 million in 2023-24, and a cut of $41 million in 2024-25. The budget also cuts funding for employment services intensive case management by $47 million General Fund in 2024-25 and ongoing. Expanded subsidized employment is also reverted by $134 million in 2023-24 and reduced by $134 million in 2024-25 and ongoing.

Social Services Housing Program Funding Delays. The budget delays a combined $195 million General Fund to 2025-26 across several housing programs, including the Bringing Families Home Program, Home Safe Program, and the Housing and Disability Advocacy Program.

Foster Youth Housing Supplement Cut. The budget reflects a cut of $195,000 in 2024-25 and $19 million General Fund in 2025-26 and ongoing to the housing supplements provided in the 2023-24 budget for foster youth in Supervised Independent Living Placements.

Child Care

Child Care Slot Expansion and Rate Increases. The Governor's budget would continue to fund the expansion of slots, initiated in previous budgets, and includes $2.1 billion for about 146,000 child care slots to be filled in 2024-25. The 2021 budget act set a goal of creating 200,000 new slots by 2026-27. The rate increases initiated by the current bargaining agreement with Child Care Providers United will also continue to be implemented at about $724 million GF in 2024-25.

Public Safety

Cannabis Enforcement Funding Subsidizes General Fund Program Spending. Holding true to the relatively low priority the Governor places on public safety, his 2024-25 budget proposes a $100 million loan to the General Fund from the cannabis tax revenues earmarked for public safety (i.e., enforcement) by Proposition 64 (2016). This is despite continued complaints from the cannabis industry that one of the most significant challenges for legal operators is the continued existence of the illegal cannabis industry.

Corrections Costs Continue to Climb Despite Shrinking Population. Despite nearly $300 million in actual and projected General Fund savings in 2024-25 from the June 30, 2023 closure of the Division of Juvenile Justice, the expected termination of the California City Correctional Facility contract in March 2024, and the planned closure of Chuckawalla Valley State Prison beginning in 2024-25, the Governor's budget proposes General Fund expenditures for the Department of Corrections and Rehabilitation of $14.1 billion in 2024-25. This is an increase of more than $90 million above the enacted 2023-24 spending level. The most significant factors contributing to this continued cost growth are employee salaries and benefits ($620 million) and various inmate medical cost increases (totaling $130 million).

More Slush from Attorney General's Slush Fund. The 2023-24 Budget Act authorized a $400 million loan to the General Fund from the Litigation Deposit Fund (LDF), which is referred to by some as the Attorney General's slush fund due to its general lack of transparency. The Governor's budget proposes to loan an additional $100 million from the LDF to the General Fund. Apparently there is more slush in the slush fund than was originally acknowledged.

Energy and Utilities

Clean Energy and Reliability Investments. The Governor proposes to reduce spending on clean energy and reliability by $312 million with partial reductions across various programs. The largest single reduction is $196 million in the Equitable Building Decarbonization program. The proposal also includes funding delays of $670 million and fund shifts of $144 million across various programs to lessen the burden on the General Fund. These changes come after modest program reductions in the prior budget left $7.3 billion to be spent over six years.

Defers Some Broadband Investments Again. The Governor proposes to defer $100 million for last-mile broadband infrastructure grants from 2024-25 to 2026-27. Last year's budget included shifting funds into 2024-25, 2025-26, and 2026-27. While these deferrals do not reduce overall funding, they slow the progress to close the digital divide.

Reduces Local Financing Funds for Broadband Infrastructure. The Governor proposes to cut $250 million for the Loan Loss Reserve Fund, used to finance local broadband infrastructure development. After this reduction $500 million would remain in the program, with $150 million available in 2024-25.

Resources and Environment

Changes to Overall Climate Spending. The budget proposes $6.7 billion in General Fund adjustments for climate-related programs. These adjustments aim to maintain a balanced budget by reducing spending by $2.9 billion, delaying $1.9 billion in expenditures to subsequent fiscal years, and shifting $1.8 billion to other funds, predominantly the Greenhouse Gas Reduction Fund (GGRF).

Continuing Multiyear Wildfire Funding Commitments. Since 2021, the budget has committed $2.8 billion for forest health and fire prevention through multiyear budgeting. The Governor's budget upholds $2.7 billion of these commitments for fire prevention and response. However, it reduces $101 million from the General Fund, affecting programs such as the Biomass to Hydrogen/Biofuels pilot ($43.5 million) and High-Risk Region Conservancy Projects ($27.7 million), focusing on fuel reduction efforts with direct benefits. Recent budget investments in wildfire prevention are a welcome change from budget years past, and this proposed budget provides a prudent solution to get more bang for our buck by focusing funding on fuel reduction efforts with immediate benefits.

New Spending for Flood Protection. The budget proposes $94 million from the General Fund for flood safety efforts. This includes $33 million for Corps of Engineers and Urban Flood Risk Reduction projects, $31 million for ongoing Central Valley flood risk projects, and $30 million for repairs due to 2023 storm damage at flood control facilities and state-owned Delta lands. While the funding is not nearly enough to address the billions needed for water infrastructure improvements across the state, these projects remain essential despite the deficit.

Reevaluating Methane Reduction Programs. The budget proposes $46 million in General Fund adjustments, temporarily shifting and delaying $24 million to the Greenhouse Gas Reduction Fund for the Livestock Methane Reduction Program and reallocating $23 million for the Enteric Methane Incentives Program. These are welcome adjustments to the budget as the necessity and effectiveness of these programs have been under scrutiny since their introduction in the previous year's budget.

Proposal to Increase the Mill Assessment Returns. The budget includes a proposal to change the flat fee model currently used to purchase pesticides and move to a phased-in increase over the next three years. Revisions of this fee would require a two-thirds vote by the legislature. Additionally, the budget proposes allocating $33 million ongoing from the Greenhouse Gas Reduction Fund and special funds to support the Department of Pesticide Regulation's efforts in managing pesticides and transitioning to more climate-friendly pest management practices in California.

Cannabis

Revised Allocation Of The Cannabis Tax Fund. The budget estimates $586.9 million will be available to meet the requirements of Chapter 56, Statutes of 2022 (AB 195). This legislation mandates allocating funds to "Allocation 3 Programs," focusing on youth education, environmental protection, and public safety. The estimated budget includes $341.3 million for youth substance use disorder programs, $113.8 million for addressing environmental impacts from illegal cannabis cultivation, and another $113.8 million for public safety-related activities.

Tax Policy

Overall Tax Policy Change Effects. The Governor's budget proposes six tax policy changes that would provide $400 million in revenue in 2024-25. In some cases the Administration labels the changes as "conforming" to federal policy, but in reality the state can choose whether or not to conform to federal policy. The majority party has chosen not to conform in other areas in the past, and the current proposals are choices as well.

Changes to Net Operating Loss for California Businesses. The largest revenue-generating tax policy change in the Governor's budget is the proposal to limit Net Operating Loss (NOL's) that are carried forward from prior years to 80 percent of any subsequent year's net income, restricting NOL usage to 80 percent or less of taxable income. This change would apply to all businesses and is projected to generate $300 million in revenue from California businesses in 2024-25.

Business, Workforce Development and Employment

New Funding for CalCompetes Grant Program Even Without Performance Review. The budget proposes $50 million General Fund to extend the recently established CalCompetes Grant program through 2024-25, even though the program is in the early stages of implementation and outcome data is not available yet, leaving the Legislature unable to determine whether the program is actually achieving results.

Shifts Portion of UI Interest Payment to Special Fund. The Governor proposes a payment of $331 million to pay the annual interest payment on the state's Unemployment Insurance (UI) loan from the federal government. Of this amount, $100 million would come from the Employment Training Fund and the remainder would be paid by the General Fund. Although this is an allowable use of the Employment Training Fund, the purpose of the fund is to invest in a skilled and productive workforce and the money in the fund comes from employers.

Employment Development Department (EDD) Problems. The proposed budget includes $327 million ($163 million General Fund) for EDD IT systems, improved service for claimants, and fraud prevention. This money would fund the third year of a five-year modernization plan which began in 2022-23.

Apprenticeship and Workforce Training Programs. The Governor proposes reductions of approximately $100 million General Fund and delayed funding of $735 million for various apprenticeship and workforce development programs. The largest single cut is $45 million to the High Road Training Partnerships Program. Notably, the Displaced Oil and Gas Worker Pilot program is reduced by $10 million, from $40 million to $30 million.

Transportation

Gas Taxes Increase Again. The Governor proposes no changes to existing law, which would continue the automatic annual tax increases to gasoline and diesel fuels. Gasoline taxes would increase by 2 cents per gallon (cpg), or 3.5 percent, to 59.9 cpg, and diesel fuel taxes would increase by 1.3 cpg, or 2.9 percent, to 45.4 cpg on July 1, 2024.

Transit Bailout. The Governor proposes a one-year delay of half of the $2 billion in transit bailout funding planned for 2024-25. The proposal also includes shifting $261 million of the remaining bailout funding from the General Fund to the Greenhouse Gas Reduction Fund.

Transportation Infrastructure. The Governor proposes a cut of $200 million General Fund previously planned for projects promoting walking and biking, leaving $850 million General Fund for these projects, which was one-time funding largely included in prior budgets. The proposed budget would also shift $530 million for transit and rail projects from the General Fund to the Greenhouse Gas Reduction Fund.

Zero-Emission Vehicles. The Governor proposes to modify spending on zero-emission vehicle (ZEV) subsidies, infrastructure, and equity projects by cutting $38 million General Fund, shifting $475 million from the General Fund to the Greenhouse Gas Reduction Fund, and delaying $600 million from 2024-25 to 2027-28. Despite the cuts, shifts, and delays, a total of $10 billion remains for ZEV programs over a seven-year period.

Local Government

City of Fresno Infrastructure Funding Delay. The budget proposes to delay $200 million in funding provided in the 2023 Budget Act for the City of Fresno's Public Infrastructure plan, leaving $50 million available in 2023-24, and $100 million available in both 2025-26 and 2026-27.

Local Projects Pulled Back. The 2023-24 budget package included roughly $750 million for a list of local projects requested by various legislators. The Governor's budget proposes to withdraw funds for any project for which the state has not yet sent out the money, an estimated total of $350 million. A list of which projects are included in this proposal is not yet available.

Overall Revenues, Expenditures, and Deficits

Key Points

- **Governor's Revenues Higher Than Nonpartisan Estimate.** Reflects multiyear revenues that are $15 billion higher than the recent nonpartisan estimate, though still $43 billion below those assumed in the 2023 Budget Act, with minimal growth moving forward.
- **Spending Beyond Our Means Leads to Annual Deficits.** Authorizes ongoing expenditures that would outpace revenue growth, leading to operating deficits in the range of $33 billion or more each of the next several years.
- **Solutions Include Taxes and Borrowing, Few Actual Reductions.** Largely rejects real reductions to ongoing programs, and instead relies on reserves, borrowing, fund shifts, and the managed care tax for most of the deficit solutions.
- **Reserves Tapped as Largest Deficits Solution.** Withdraws $13 billion from general reserves to address the deficit, leaving $14 billion available in future years.

Governor's Deficit Substantially Lower Than Nonpartisan Estimate. The Governor's January budget package projects a deficit of $38 billion by the end of 2024-25. This is $30 billion lower than the $68 billion deficit estimated by the nonpartisan Legislative Analyst's Office (LAO) in December. The most significant part of the difference results from the Governor's projection that tax revenues will be higher by $15 billion compared to the LAO estimate. Much of the remainder is the result of differing assumptions regarding whether to treat Proposition 98 education adjustments as part of the baseline or as a solution that the Legislature needs to adopt.

The LAO's $68 billion deficit more accurately reflects the reality that the Legislature would need to vote to adopt lower Proposition 98 expenditures, while the Governor assumes a $15 billion reduction up front, thus prematurely lowering the deficit amount. The remaining differences, which generally offset each other, are smaller and involve different assumptions in automatic spending changes and a small balance in the discretionary reserve balance.

Short-Term Solutions Despite Long-Term Deficits. In order to address the budget year's deficit, the Governor proposes a mix of solutions totaling $38 billion that largely use one-time actions and budget gimmicks, rather than actual, on-going reductions that would create a truly sustainable budget. The solution categories are summarized in the descriptions below and the chart on the next page.

- **Reserves.** $13 billion by drawing down budget reserves, including $12 billion from the state Rainy Day Fund and $900 million from the Safety Net Reserve.
- **Reductions and Pull-Backs.** $8.5 billion from various reductions and pull-backs of previously approved increases, most significantly including $2.9 billion for various climate programs, $1.2 billion for housing programs, and $350 million for previously approved local projects.
- **Delays.** $5.1 billion to delay previously scheduled spending, including $1 billion for transit and inner city rail and $613 million for developmental services payment rate increases.
- **Fund Shifts.** $3.4 billion by shifting General Fund expenses to state special funds, including $1.8 billion to the Greenhouse Gas Reduction Fund (cap and trade) and $1.3 billion in state retirement contributions to Proposition 2 debt payments.
- **Revenue Changes.** $4.1 billion by expanding the managed care organization tax and shifting a portion of it to earlier years, thus increasing the General Fund offset ($3.8 billion), plus $300 million through greater limits on corporate net operating loss (NOL) deductions.

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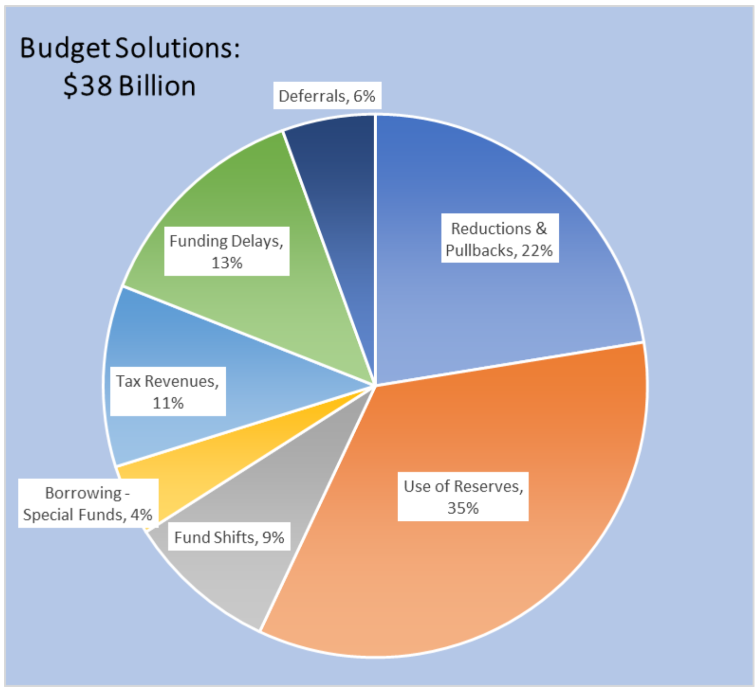
- **Internal Borrowing.** $1.6 billion by authorizing the General Fund to borrow more money from state special funds, such as the AIDS Drug Assistance Rebate Fund ($500 million). This adds to last year’s borrowing, when the state borrowed $2.7 billion from special funds to close that deficit.



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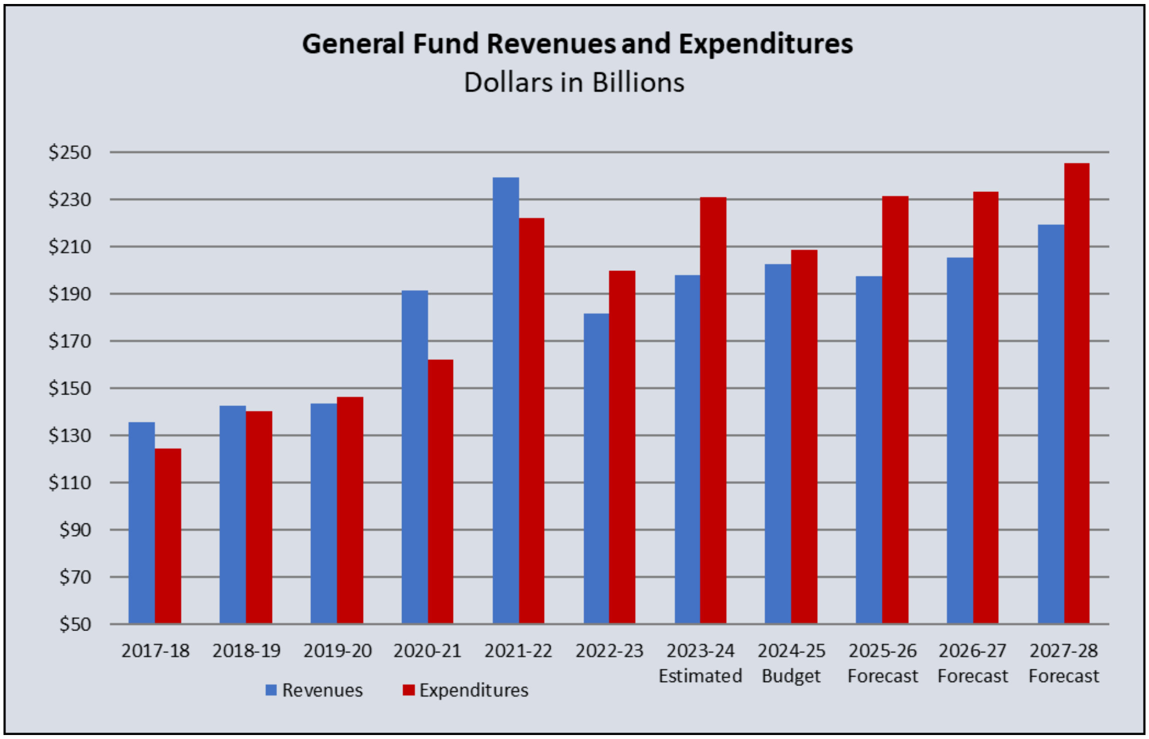
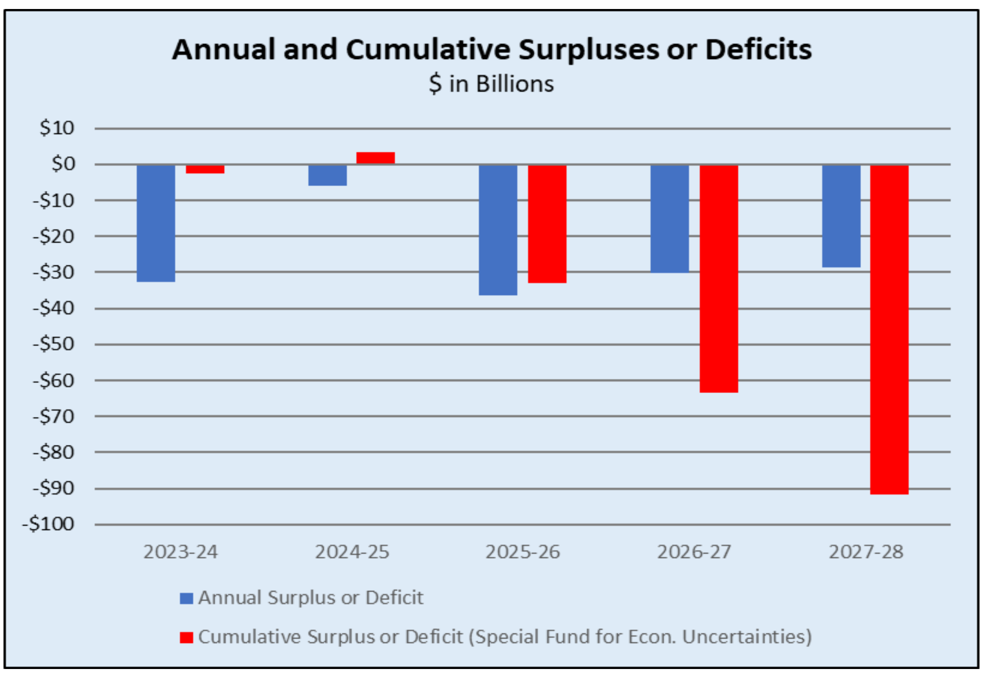
Expenditures Remain Unsustainable. General Fund expenditures under the Governor’s proposal would reach a revised total of $231 billion in 2023-24, which, surprisingly, remains about $5 billion above the enacted budget level of $226 billion. This appears to be the result of shifting some expenditures from 2022-23, when the actual spending came in about $35 billion below expectations. Expenditures would then decline by about 10 percent to $209 billion in 2024-25 before starting to grow again. Because the Governor’s deficit solutions rely heavily on one-time delays and shifts, as described above, expenditures remain above revenue in each year of the Governor’s forecast through 2027-28.

Massive Deficits Persist Throughout Forecast. The Governor’s multiyear forecast also indicates the state will have an ongoing imbalance between revenues and expenditures, as illustrated in the first chart on the next page. Expenditures (shown by the red bars) exceed revenues (blue bars) every year through 2027-28.



The ongoing imbalance under the Governor's budget means that operating deficits would occur each year in the Governor's forecast, beginning with a $33 billion deficit in 2025-26. By the end of the forecast period in 2027-28, California would have a cumulative deficit of $91 billion. The state cannot pass an unbalanced budget under the constitution, but this forecast indicates that the state would have to enact solutions to address those deficits in each year.



Threshold Met to Use Reserves for Future Deficits. Under the rules of Proposition 2, the state can withdraw funds from the Rainy Day Fund only in the case of a "budget emergency," defined as a situation in which General Fund resources are not sufficient to cover the highest enacted budget level of the past three years. The proposition only permits the Governor to declare a budget emergency. The Legislature would then need to pass a bill to withdraw funds from the reserve for use in the budget. Proposition 2 limits the withdrawal to 50 percent of the reserve balance in the first year of withdrawal. The 2024-25 budget would be $21 billion below the enacted 2022-23 budget, so the condition for a "budget emergency" has technically been met.

Some Reserves Remain After Budget Solution. The proposed budget would utilize $13 billion from the state's reserves, maintaining an estimated $18 billion in total reserves. The proposed withdrawals and remaining reserve balances include the following categories:

- Withdrawal of $10.4 billion from the mandatory balance, and $1.8 billion from the discretionary balance of the state's Rainy Day Fund. This would leave $11.1 billion in the Rainy Day Fund.
- Withdrawal of $5.7 billion from the Proposition 98 Rainy Day Fund, leaving a balance of $3.8 billion.
- Withdrawal of $900 million from the Safety Net Reserve Fund, zeroing out the balance.
- A $3.4 billion balance in the discretionary reserve (the Special Fund for Economic Uncertainty).

As the Governor now proposes to use reserves, it is worth noting that the state unwisely spent $8 billion from the reserves in the recent past. In June 2020, the state believed it faced a deficit of $54 billion as the pandemic took hold, and that budget implemented the $8 billion withdrawal. By May 2021, however, a turnaround had already occurred. The Governor estimated a $76 billion surplus for the 2021-22 budget and could have replaced the $8 billion withdrawal that was no longer needed. However, the Governor and legislative Democrats chose to spend the withdrawn funds anyway.

Economic Concerns Loom Large. With the exception of Silicon Valley and a few other high-profile industries, California faces greater challenges than the rest of the country on two fronts, which may make the road back to a sustainable budget more difficult. As reported by the Governor's Department of Finance:

- ***Higher Unemployment Rate:*** California's rate of 4.9 percent is significantly higher than the national rate of 3.7 percent (as of November 2023).
- ***Workforce Has Not Recovered.*** In California, only 77 percent of the 1 million people who left the labor force at the start of the pandemic have returned. In the nation as a whole, the labor force fully recovered by August 2022 and has grown by 3 million people since that time.

Taxes

<u>Key Points</u>

- **California Businesses to Provide New Tax Revenue.** Proposes several tax changes that would increase revenue by $400 million in 2024-25, and $293 million thereafter.
- **Restricts Use of Net Operating Losses (NOLs).** Proposes to limit businesses' use of NOLs and restrict carry-forward amounts, increasing revenue by $350 million in 2024-25.
- **Caps Deductions for Charitable Easement.** Includes $55 million in revenue from capping the allowable tax deduction for property owners who give up development rights.
- **Bad Debt Deduction.** Proposes to increase both state and local sales and use tax revenue by eliminating the use of the "bad debt" deduction and refund.
- **Revises Several Tax Policies Aimed at Oil and Gas Producers.** Proposals include disallowing accelerated expenses, eliminating a cost recovery credit, and eliminating special depletion rules.

Overall Tax Policy Change Effects. The Governor's budget proposes six different tax policy changes totaling $400 million in revenue in 2024-25, as described in the following paragraphs. In some cases the Administration labels the changes as "conforming" to federal policy, but in reality the state can choose whether or not to conform to federal policy. The majority party has chosen not to conform in other areas in the past, and the current proposals are choices as well.

Net Operating Loss Conformity. The January budget includes $300 million in revenue as a result of limiting businesses' ability to carry forward Net Operating Losses (NOLs), restricting carry-forward amounts from the current 100 percent to 80 percent, beginning with the 2024 tax year. An NOL occurs when a business has deductions that exceed taxable income in a given year. Under both state and federal law, these NOLs can be carried forward and applied to offset tax payments in future years. The proposal would conform state law to federal law that limits the prior year carry forward allowance for NOLs to 80 percent of income, and would apply to all businesses. The budget assumes revenue of $200 million annually thereafter.

Charitable Conservation Easements. The budget assumes revenue of $55 million General Fund in 2024-25 as a result of capping the deduction amount allowed for businesses claiming the charitable easement deduction. Currently, property owners who give up development rights on lands are allowed a deduction equal to the value of the property. In 2023, federal tax law was amended and capped the deduction to two and a half times the value of the taxpayer's investment. The Governor's proposal would conform state law to federal law for the treatment of this deduction, and would generate $25 million annually thereafter.

Elimination of the "Bad Debt" Deduction. The budget assumes state sales and use tax revenue of $24 million General Fund in 2024-25 with the elimination of the "bad debt" deduction and refund, effective January 1, 2025. Currently, state law allows retailers, lenders, and their affiliates to deduct or claim a refund for sales and use tax paid for taxable goods that turn out to be worthless. Lenders can currently claim the deduction or refund even if a profit was realized. The bad debt deduction/refund is unusual in that it is allowed to lenders even though sales tax due related to purchases made on credit is paid by the retailer, not the lender. The proposed budget eliminates this refund or deduction for non-retailer lenders. The Administration projects additional state revenue of $51 million in subsequent years. The proposal would also generate sales and use tax revenue of $60 million for local governments.

Disallowance of Accelerated Expenses for Intangible Drilling Costs. The budget includes $7 million in General Fund revenue annually from the proposed disallowance of accelerated expenses for oil and gas intangible drilling costs. Under current law, and in conformity with federal law since 1987, the state law allows 70 percent of intangible oil and gas drilling costs (such as survey work and ground preparation, among others) to immediately be deducted as a business expense in the year the cost is incurred, with the remainder spread over five years. Independent oil producers can fully expense 100 percent in the year that costs are incurred. Normal tax law generally requires that expenses be deducted only once their benefit is realized. The budget would, beginning in tax year 2024, eliminate the special accelerated deduction schedule for oil and gas intangible drilling costs, applying standard tax law that allows expenses to be deducted when their benefit is realized.

Percentage Depletion Rules for Fossil Fuels. The budget includes $15 million in General Fund revenue in 2024-25, $10 million annually thereafter, with the elimination of the increased depletion percentage allowance for fossil fuel minerals, including oil, gas, and coal. Percentage depletion rules allow independent oil companies to deduct about 15 percent of the gross revenue generated from a well, on a property-by-property basis, even if that amount exceeds the well's total value. These special depletion rules are unique because the allowance does not end when the property has paid for itself, as with depreciation on buildings and machinery. Instead, it goes on as long as production continues. The budget proposes to eliminate these depletion rules, which could provide consistency on the tax treatment of cost-depletion methods across businesses.

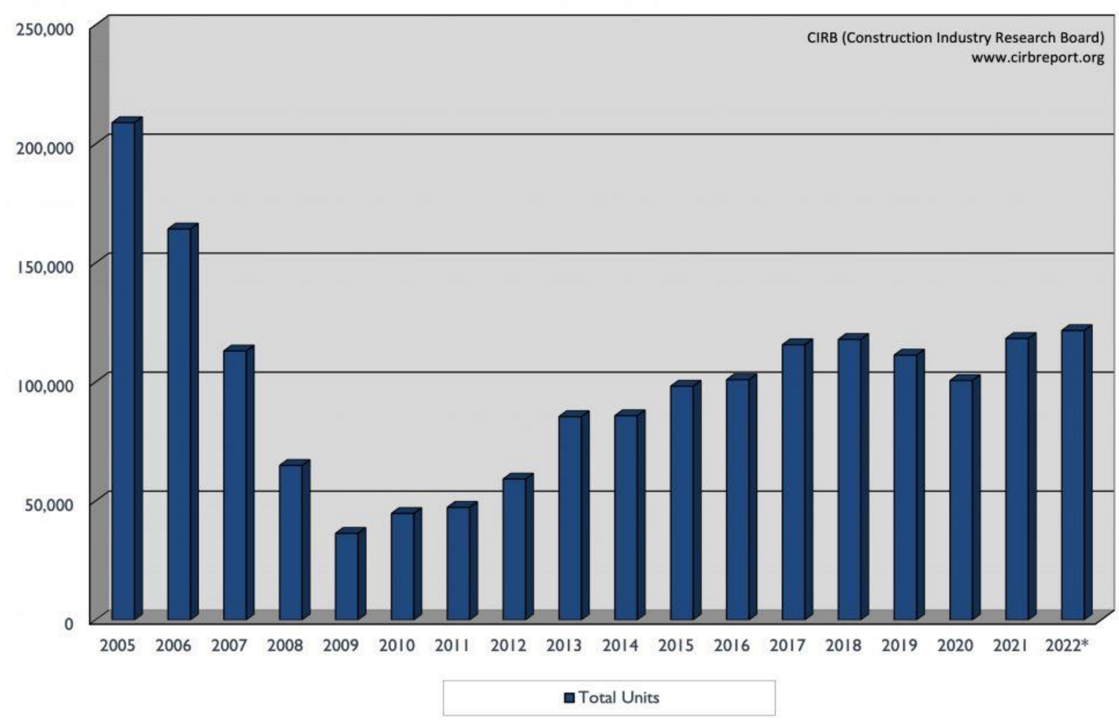
Enhanced Oil Recovery Costs Credit. The budget proposes to eliminate the enhanced oil recovery cost credit, which can be claimed by oil producers only if oil prices increase above a certain threshold. The credit is intended to encourage producers to extract domestic oil that can only be recovered using more expensive unconventional methods. Due to the threshold requirements, the cost of this credit is limited and uncertain, and it is common for this credit to yield no costs to the state budget. The Administration indicates that this credit is inconsistent with the priority to decrease greenhouse gas emissions, and as a result, has proposed the elimination of this tax credit.

Housing

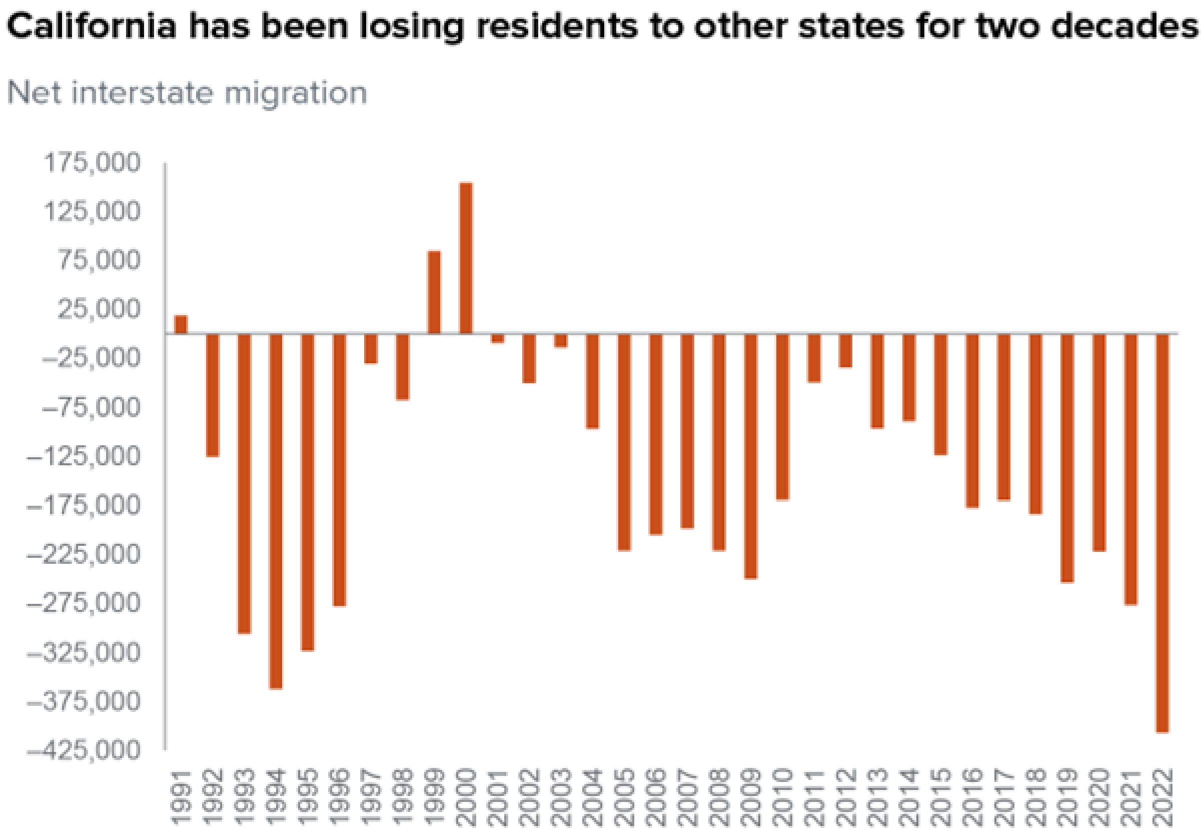
Key Points

- **Governor's Budget Continues to Reflect Policy and Campaign Failures.** The Governor fails to deliver on promise of building millions of new homes, despite tens of billions of dollars in housing subsidies.
- **Includes Reductions of $1.2 billion for Housing Programs.** Proposes $1.2 billion in reduced spending for housing programs, including Infill Infrastructure and Multi-Family Housing.

Governor Struggles to Fulfill Campaign Promise on Housing. In 2017, the Governor made a campaign promise to build 3.5 million homes by 2025, but between 2018 and 2022 the state has permitted less than 570,000 single and multi-family housing units (see chart below for permit data through 2022). In the years following the Governor's election, the state will have achieved less than 20 percent of the Governor's pledge. Facing this daunting reality, the Governor has recently walked back this pledge, and now is asking cities to *plan* for a combined 2.5 million homes by 2030. So the goal now is a million fewer homes that merely need to be *planned for*, not built, over a longer period of time. This lack of progress comes despite the state spending nearly $40 billion between 2018 to 2022 on various housing subsidies.



Cost of Housing a Factor in Continued Out-Migration. California has been losing residents for decades, as the chart below reflects. The cost of housing in California has been a contributing factor to the continued decline in the state's population. In recent years, data has shown large numbers of Californians headed towards Texas and Florida, among other states. A recent KTLA 5 news article cited data from U-Haul showing that Texas netted the largest number of movers in 2023. Florida ranks right behind Texas among growth states for the third year in a row. Moreover, for the fourth year in a row, California showed the largest net loss of one-way movers. Both of these states have one thing in common: they have both built significantly more housing since 2018 than California. Between 2018 and 2022 (the last year data is available) Texas has permitted a whopping 1.2 million new homes, and Florida has permitted 888,000, far surpassing California.



SOURCE: California Department of Finance estimates. Net flows are from July 1 to June 30th.
FROM: PPIC Blog, March 2023.

Unsurprisingly, the Governor continues to take a back seat on this pressing issue, as the budget again does not identify or include critical housing reforms, such as reducing exorbitant fees imposed by local governments, minimizing lengthy bureaucratic approval delays, or eliminating abusive legal challenges that force home construction to stall, sometimes indefinitely. Until these vital housing reforms are in place, any hope that California could once again become a top-destination for people wishing to live and work here will be unfulfilled.

Significant Reduction in Funding for Housing Production. The budget proposes to eliminate $1.2 billion in funding provided to various housing programs, as follows:

- **Regional Early Action Planning Grants 2.0.** A reduction of $300 million in regional planning grants for local jurisdictions, leaving a balance of $300 million available for program expenditures.

- **Multifamily Housing Program**. A reduction of $250 million, leaving $75 million in 2023-24 for the program.

- **Infill Infrastructure Grant Program.** A reduction of $250 million, leaving $25 million in 2023-24 for the program.

- **CalHome.** A reduction of $152.5 million, eliminating all the funding for the program.

- **Veterans Housing and Homelessness Prevention Program.** A reduction of $50 million, leaving no further funding available for the program.

- **Foreclosure Intervention Housing Preservation Program**. A reduction of $248 million over three years, which includes reductions of $85 million in 2024-25, $100 million in 2025-26, and $63 million in 2026-27.

- **Housing Navigators Program**. A reduction of $14 million in ongoing funding. This is a base reduction and would result in the elimination of this program.

Homelessness

Key Points

- **Homeless Population Continues to Grow.** New federal data released by the U.S. Department of Housing and Urban Development shows California now has a homeless population reaching 181,400, an increase of six percent over the past year.

- **More Delays in Mental Health Infrastructure Funding**. Delays funding to counties to construct much-needed treatment bed facilities.

- **Delays Funding for Social Services Housing.** Delays a cumulative $195 million General Fund to the 2025-26 budget year, meant to provide housing and homelessness assistance for individuals being served by social services programs.

- **No Housing Support for Foster Youth.** Cuts about $19 million General Fund over the next two budget years and ongoing for additional housing supplements recently approved for foster youth in the 2023 budget act.

Democrats' Homelessness Strategy Failing So Far. Democrats' massive spending in recent years to combat homelessness has failed to achieve any results. The state has committed nearly $22 billion since 2018-19, yet new federal data released by the U.S. Department of Housing and Urban Development show the problem is only getting worse. California now has a homeless population reaching 181,400, an increase of six percent, or about 10,000 homeless Californians in the last 12 months.

Democrats' insistence on only using the "Housing First" approach, combined with a lack of accountability for homeless individuals engaged in substance abuse, are key factors in this failure. Rather than continue to throw good money after bad, the state needs to re-evaluate its approach to addressing homelessness, increasing coordination efforts and data requirements, as well as enhancing tools local jurisdictions can utilize in their efforts to reduce the number of homeless living on the streets.

Homeless Housing, Assistance and Prevention Program (HHAP). The Governor's proposed budget delays allocation of $260 million in HHAP funding until 2025-26, and would also revert $101 million General Fund intended to support administration of the program. While the budget would maintain $1.1 billion General Fund for the Homeless Housing, Assistance and Prevention program (HHAP) in 2023-24, the Governor's proposed 2024-25 budget would not provide any new funding or statewide strategies for local jurisdictions, leaving the front-line providers with fiscal and program uncertainty as the state minimizes ongoing support at the same time the homeless population continues to explode.

More Delays in Funding for Mental Health Beds. Despite the overwhelming need to treat the growing mentally ill homeless population, the Governor is proposing another delay of $375 million in General Fund for mental health infrastructure, including funds for treatment and locked psychiatric beds and short-term crisis beds. This funding was to be allocated to county behavioral health departments and non-profit community partners to construct, acquire, or rehabilitate properties in order to increase mental health treatment bed capacity. The funding would also cover the rehabilitation and/or construction of tiny homes or small multi-bed facilities in locations where wrap-around behavioral health treatment can be administered. This new delay comes just after a budget delay of $480 million in grant funding in the 2023 Budget Act. The new timeline will now wait until 2025-26 to allocate those funds to the counties.

Given the recent federal data showing a substantial increase in California's seriously mentally ill homeless population, funding for treatment beds should be an elevated priority. When the state had a $98 billion surplus, Senate Republicans called for $10 billion to provide new treatment facilities. The Governor and legislative Democrats chose to spend funds on other programs. A bond proposal for mental health treatment beds and housing will appear on the March 2024 ballot. Should voters approve it, the Governor's May Revision could elevate those mental health infrastructure funds as a priority.

Pushes Funding for Housing Support Down the Road. As part of the Governor's "solutions" for addressing the budget shortfall, the 2024-25 budget proposes delaying a cumulative $195 million in one-time housing and homelessness investments to 2025-26. These funds serve individuals on social services programs at risk of or experiencing homelessness, including families in the child welfare system, individuals served by adult protective services, and those who are likely eligible for disability benefits. The *Human Services* section of this report provides more detail on these programs.

Cuts New Additional Housing Support for Foster Youth. The budget proposes cutting $200,000 General Fund (GF) in 2024-25 and about $19 million GF in 2025-26 and ongoing for a newly established housing supplement for foster youth in Supervised Independent Living Placements (SILPs). These SILPs are placement options for individuals ages 18 to 21 participating in extended foster care. Cutting this funding shows a lack of prioritization for this especially vulnerable foster youth population and makes a miniscule dent in the massive budget shortfall. The Human Services section provides more detail on this program.

Health

Key Points

- **Questionable Use of Safety Net Reserve.** The Governor sweeps all $900 million in the reserve despite the fact that he does not project an economic downturn, which is a requirement in the law.
- **Getting More from the Managed Care Organization (MCO) Tax?** Proposes to ask the federal government for additional funding and to sweep more of the funds to help balance the budget.
- **$4.1 Billion to Continue the Medi-Cal Expansion to the Undocumented.** Governor fully funds major expansion despite cuts to other areas of the budget, such as services to the developmentally disabled.
- **Regret on Health Care Minimum Wage Bill?** Governor wants immediate changes to the costly $25-an-hour health care minimum wage law he just signed.
- **Delay to Healthcare Workforce Funding.** Delays funding for healthcare workforce initiatives to increase the number of nurses, social workers, and behavioral health professionals in California.

Use of Safety Net Reserve Contrary to Intent. The Governor proposes sweeping the entire $900 million in the legislatively-created safety net reserve in order to "maintain existing program benefits and services for the Medi-Cal and CalWORKs programs." The reserve was created to help cover the costs of *increasing* caseloads in a recessionary economic climate. In 2024-25, the Governor is not forecasting a recession. Furthermore, the Medi-Cal caseload is projected to *decrease* from an estimated 14.8 million enrollees in 2023-24 to 13.8 million in 2024-25 due to the post-pandemic restarting of eligibility redeterminations. In addition, the Governor is still proposing real cuts in CalWORKs (see Human Services section). These factors raise questions whether the use of the safety net reserve is consistent with the law. As the Legislative Analyst's Office notes, "withdrawing the entirety of this reserve many not be consistent with its original design."

More Funding from the Managed Care Organization (MCO) Tax. The 2023 Budget Act included a new MCO tax, effective from April 1, 2023 through December 31, 2026, on both commercial and Medi-Cal managed care plans. The MCO tax, which was just officially approved by the federal government in December 2023, was estimated to provide an additional $19.4 billion in budget resources over the life of the tax, with $11.1 billion intended to support additional Medi-Cal provider rate increases and $8.3 billion for General Fund budget relief.

With the new projected deficit in the 2024-25 budget, the Governor is proposing two actions related to the MCO tax in order to gain $3.8 billion in additional General Fund relief this budget year:

- **A New $1.5 Billion Tax on Medi-Cal Managed Care Plans**. The Governor is asking the Legislature to act before March 31, 2024 to adopt an additional smaller MCO tax only on Medi-Cal Managed Care Plans. This would generate $1.5 billion in General Fund relief and would not fund additional Medi-Cal provider rate increases. While this may be an easy opportunity to obtain more federal funds, it is unfortunate that these funds will be siphoned off to plug the budget hole rather than to bolster our healthcare system. Draft trailer bill language on the new tax is not yet available.

- **Acceleration of $2.3 Billion of Future MCO Tax Proceeds**. The Governor is proposing to use $2.3 billion more of the total MCO tax proceeds in 2024-25 in order to maintain the new ongoing Medi-Cal provider rate increases as promised in the 2023 Budget Act. While keeping our promise to Medi-Cal providers this budget year is a good thing, this acceleration of MCO Tax proceeds for use in 2024-25 will either result in the need for more General Fund spending in future years to maintain those provider rates or will result in unfortunate provider rate cuts.

These actions would result in a revised estimate of $20.9 billion in total MCO tax proceeds through 2026, with $8 billion scheduled for new Medi-Cal provider rate increases and $12.9 billion for General Fund relief. With large future year deficits on the horizon, and with another MCO tax option off the table for several years, it will become even more tempting for the Democrats to break their promises to Medi-Cal providers and raid the provider set-aside in future budgets.

No Proposition 56 Tobacco Tax Supplemental Payments for Physician Services. A fund the Democrats frequently choose to raid is the Proposition 56 tobacco tax fund for Medi-Cal provider supplemental payments. This year, the Governor proposes to stop the funding for physicians that currently receive Proposition 56 supplemental payments for services. This action results in savings of $77 million in tobacco tax funds and $116 million in General Fund. The Administration claims that the new Medi-Cal provider rates funded through the MCO tax are sufficient to reimburse doctors for their services to Medi-Cal beneficiaries. In essence, the Governor gives through one program while taking away through another. With Medi-Cal reimbursement rates still far below the rates within the federal Medicare system, the Administration's claims are laughable, but its proposed grab of tobacco tax funds away from doctors is less so.

Medi-Cal Eligibility Redeterminations Lowering Medi-Cal Caseload. The Governor's budget projects that 38 percent of Californians (14.8 million individuals) will be enrolled in Medi-Cal, at a cost of $158 billion ($37 billion General Fund), in the 2023-24 fiscal year. In fiscal year 2024-25, the Administration projects a decline in Medi-Cal caseload to 13.8 million individuals (6.8 percent decrease), at a cost of $157 billion ($36 billion General Fund, a 3.8 percent decline).

Projected Medi-Cal Caseload and General Fund Costs			
	2023-24	2024-25	Change
Caseload (millions)	14.8	13.8	-6.80%
General Fund (billions)	$37.3	$35.9	-3.80%

The large projected caseload decline is mostly attributable to the end of the federal COVID emergency requirement to keep all enrollees on Medi-Cal through the length of the pandemic. Since the end of designated federal emergency in early 2023, counties have resumed redeterminations of Medi-Cal eligibility for every enrollee. It is estimated that 2 million Medi-Cal enrollees will eventually be disenrolled due to income or other ineligibility.

Despite this sizable caseload drop, General Fund Medi-Cal costs are only projected to decline by $1.4 billion in 2024-25. This is because of the growing enrollment of undocumented individuals of all age cohorts, which are almost exclusively a state financial responsibility, and the implementation of CalAIM, the Medi-Cal delivery system reform initiative. In 2024-25, the General Fund cost for both these initiatives is more than $7 billion, and will grow to more than $10 billion by the end of the decade.

$4.1 Billion to Continue Medi-Cal Eligibility Expansion to the Undocumented. Ignoring the realities of California's fiscal instability and other pressing healthcare priorities, the Governor's budget maintains $4.1 billion in General Fund spending ($1.2 billion in 2023-24 and $2.9 billion in 2024-25) for the last phase of the expansion of full-scope Medi-Cal eligibility to all low-income undocumented individuals. On January 1, 2024, an estimated 700,000 undocumented individuals aged 26-49, became eligible for full-scope Medi-Cal. Of that population, nearly 90 percent are estimated to be currently enrolled in restricted-scope Medi-Cal due to pregnancy or emergency care. Therefore, these enrollees will administratively transition to full-scope Medi-Cal over the new few months. Counterintuitively, the Administration does not project any caseload or cost impact from the recent influx of migrants at the border. The administration estimates that $3.2 billion General Fund annually will be needed to fund Medi-Cal for the age 26-49 population. This is on top of the estimated $2 billion annually for the previous expansions to the undocumented populations age 25 and under and age 50 and older.

Abortion Industry Support with Federal Funds. The Governor's budget includes $200 million ($100 million General Fund) in grants to abortion providers in order to offset service costs for the uninsured, update infrastructure, and provide the abortion clinic workforce with scholarships and loan repayments. The Administration plans to submit a waiver to the federal government to obtain an additional $85 million annually in federal funds for this program. While current federal law prevents federal funds to directly pay for abortions, the funds in this program will cover costs for all services provided at an abortion clinics other than abortions, an obvious indirect subsidy.

No New Funding for Distressed Hospitals. While the Governor found funds for the undocumented and for abortion clinics in a deficit year, the proposed budget contains no additional funding for the Distressed Hospital Loan Program to keep at-risk hospitals open. In 2023, the Legislature allocated $300 million to help those hospitals most at risk of closure. On August 24, 2023, the state issued $292 million in awards to 17 distressed hospitals. 13 additional hospitals applied, but were awarded no funding. In addition, many at-risk hospitals are closing specialty wards in order to reduce their costs. Of note is the closure of 35 labor and delivery wards in California since 2012, with 16 of those closures taking place since 2020. Senate Republicans will continue the fight to secure more funding for at-risk hospitals, knowing that Democrats' "healthcare for all" statement is hollow if there is nowhere to obtain healthcare.

Regret on Health Care Minimum Wage Bill? Just months after signing SB 525, the bill to increase the minimum wage to at least $25 per hour for all health care facility workers starting June 1, 2024, Governor Newsom is now asking the Legislature for immediate action to change the law. Specifically, the change would add an annual "trigger" to make the minimum wage increases subject to General Fund revenue availability and to exempt state-run facilities such as the University of California hospital systems. Draft trailer bill language is not yet available to review at this time.

It is understandable that Governor Newsom would regret signing SB 525, since he ignored the fiscal projection by his Department of Finance that the bill would result in a $2 billion General Fund impact in 2024-25, largely from increased Medi-Cal managed care rates. And he continues to ignore it in this proposed budget, since the budget does not include costs for the bill. Signing an irresponsible bill is one thing. Failing to publicly acknowledge its fiscal reality is another.

Delays in Funding for Health Care Workforce. The Governor's budget delays $140 million General Fund for the Nursing and Social Work Initiatives until the 2025-26 fiscal year. In addition, as a result of dramatically lower Mental Health Services Act revenue, the Administration is planning to delay $189 million (Mental Health Services Act funds) for various behavioral health workforce investments, including the social work initiative, addiction psychiatry fellowships, college and university grants for behavioral health professionals, expanding Master of Social Work slots, and the local psychiatry behavioral health program.

This funding was originally appropriated in the 2022 Budget Act to be spent over five years to address the sizable healthcare workforce shortages in California, such as the estimated shortage of 2,200 psychiatrists, 4,100 primary care clinicians, 44,000 nurse practitioners, and 600,000 home care workers, as outlined by the California Future Healthcare Workforce Commission's 2019 report.

Maintains Great Recession-era Budgeting Gimmick. The Governor's budget undoes a 2022 agreement to discontinue a Great Recession-era Medi-Cal accounting gimmick. To achieve one-time General Fund relief in the 2008 Budget Act, Medi-Cal provider reimbursement checks were delayed by two weeks in order to shift costs from the 2008-09 fiscal year to the 2009-10 fiscal year. This two-week check withhold for Medi-Cal providers has remained law ever since. The 2022 Budget Act included trailer bill language to "buy back" the two-week check withhold in 2023 at a one-time General Fund cost of $378 million, but the 2023 Budget Act delayed it until the 2024-25 fiscal year. Now in order to avoid an estimated $533 million in costs to implement the "buy back," the Administration is choosing to keep the two-week check withhold in law permanently.

Mental Health

Key Points

- **Dramatic Decline in Millionaires' Tax Revenue for Mental Health.** Significant drop in Personal Income Tax revenues decreases the amount of funding available for the Mental Health Services Act.
- **Another Mental Health Infrastructure Delay.** Governor slows down county grants for mental health treatment bed construction by an additional year.
- **New Wellness Coach Benefit in Medi-Cal**. Despite the deficit, the Governor adds a new Medi-Cal benefit for wellness coaches.

Drop In Millionaires' Tax Revenue Decreases Available Mental Health Services Funding. The Mental Health Services Act (MHSA), passed as Proposition 63 in 2004, imposed a 1 percent tax on personal income in excess of $1 million in order to fund state and county mental health programs. The forecast within the Governor's proposed budget displays a dramatic decrease in MHSA revenues as compared to the June 2023 Budget Act, as shown in the following chart.

Drop in Projected Proposition 63 (MHSA) "Millionaires" Tax Revenue			
(In Billions)	**2022-23**	**2023-24**	**2024-25**
2023 Budget Act	$3.2	$2.7	$3.0
Governor's 2024-25 Budget	$2.6	$2.4	$2.6

Because of the decrease in MHSA revenue, the Governor's budget proposes a substantial decrease in MHSA-funded expenditures as well, as shown in the chart below. Much of the decrease, roughly $600 million in 2023-24 and $300 million in 2024-25, is in local assistance to the counties for mental health services. The other notable area of impact is an ill-timed delay of $189 million in behavioral health workforce incentives funded by MHSA. In addition, the Governor proposes to shift $265 million in spending that would have been from MHSA revenue to the General Fund. Given the mental health care need on California's streets, these actions show how ill-prepared the Democrats were for a revenue downturn impacting the mental healthcare budget.

Decrease in Mental Health Services Act spending			
(In Billions)	**2022-23**	**2023-24**	**2024-25**
2023 Budget Act	$5.5	$3.2	$3.2
Governor's 2024-25 Budget	$3.0	$2.4	$2.5

More Delays in Funding for Mental Health Beds. Despite the obvious need to treat our growing mentally ill homeless population, the Governor proposes another delay of funding for mental health infrastructure in order to save $375 million in General Fund. This includes funds for locked psychiatric beds, outpatient treatment, and short-term crisis care. This funding was to be allocated to county behavioral health departments and non-profit community partners to construct, acquire, or rehabilitate properties in order to increase mental health treatment bed capacity. The funding would also cover the rehabilitation and/or construction of tiny homes or small multi-bed facilities in locations where wrap-around behavioral health treatment can be administered.

This new delay comes just as the 2023 Budget Act delayed $480 million in infrastructure grant funding. The new timeline will now delay allocation of those funds to the counties until 2025-26. Given the recent data showing the homeless population in California grew by 6 percent to an estimated 181,000 individuals, funding for treatment beds is overdue. In 2022 Senate Republicans proposed to fully fund this program with the then- $98 billion surplus, but Democrats chose to spend elsewhere. The voters may soon decide these services are a priority as Proposition 1 on the upcoming March 2024 ballot authorizes a $6.4 billion bond for mental health treatment beds and housing. The administration claims that, if approved by the voters, the bond funding will result in more than 10,000 new mental health beds. However, ignoring the previous opportunity to use surplus state funds means that implementation will be significantly delayed and will cost far more over time due to interest payments on the debt.

Department of State Hospitals' Caseload Increases, but Still Not Enough Beds. The Department of State Hospitals (DSH) is responsible for the daily care and mental health treatment of more than 9,000 patients in five main hospital campuses and in dozens of contracted facilities throughout the state. Over the last decade, the population demographic has shifted from primarily civil court commitments to a forensic population committed through the criminal court system. While the proposed 2024-25 budget estimates that caseload will increase to 9,314 patients at a cost of $3.4 billion ($3.2 billion General Fund), the department estimates that 952 individuals are currently on a waitlist for a DSH treatment bed. The department is actively pursuing contracts with counties for more bed space, a consequence of years of inadequate attention to this growing problem.

Improvement in the Incompetent to Stand Trial Waitlist. The Governor's budget projects a dramatic decline in the number of patients waiting for DSH competency restoration services from 804 in 2023-24 to 501 in 2024-25, a 38 percent decline. These patients are mentally ill individuals charged with a felony but deemed incompetent to stand trial. Without restoration of competency these individuals do not have the wherewithal to stand in defense in a court of law. The state is currently under a court order to reduce the wait time for restoration of competency services to just 28 days by March 2025. The administration also states that of the 501 individuals on the waitlist, 172 are receiving substantive treatment service through a new early access treatment program, which will stabilize the patients' conditions before they embark on competency restoration services.

Adding a Wellness Coach Benefit in Medi-Cal. Despite tens of billions of dollars in deficits for years to come, the Governor chooses this budget as the time to add a new wellness coach benefit within Medi-Cal at a cost of $4.1 million General Fund in 2024-25 and $34 million General Fund annually thereafter. Under this proposal, starting January 1, 2025, Medi-Cal will cover the addition of wellness coaches on staff at public schools. The certified, but not licensed, coaches will be in addition to any social workers, therapists, or psychologists already on school district staff and will be tasked with "guiding" students into making proper life choices. While this benefit may slightly help the delivery of behavioral health care in schools, the state's fiscal condition is not in a place to add new ongoing entitlement expenditures, especially one that isn't critical to the delivery of health care to low-income Californians.

Human Services

Key Points

- **Additional CalWORKs Grant Increase.** Provides $27 million for an additional 0.8 percent increase to CalWORKs Maximum Aid Payment levels.
- **Reduces Supports for Foster Youth and Families.** Cuts about $38 million General Fund in 2024-25 and ongoing for the Family Urgent Response System, and Child Welfare Services Public Health Nurses.
- **Eliminates Housing Support for Foster Youth.** Reduces $19 million General Fund over the next two budget years and ongoing for foster youth housing support.
- **Continues IHSS Undocumented Immigrant Expansion.** Continues the expansion of In-Home Supportive Services to undocumented immigrants of all ages at a projected cost of $398 million General Fund.
- **Defers Funding for Vulnerable Populations.** Delays $195 million in housing and homelessness assistance for needy Californians by one year.

Department of Social Services

The 2024-25 budget for Department of Social Services (DSS) programs is projected to be nearly $49 billion ($22 billion General Fund). This is approximately $278 million (total funds) less than the 2023-24 revised budget, but about $1.3 billion more in General Fund costs. The chart below highlights caseload projections for major programs at DSS.

Department of Social Services Caseload Projections

Program	2023 Budget Act	2023-24 Revised	2024-25 Projected	Change From 2023-24 Revised	
				Amount	Percent
CalFresh	2,966,760	3,054,619	3,085,183	30,564	1.0
SSI/SSP	1,108,625	1,110,779	1,094,642	(16,137)	-1.5
IHSS	645,217	660,497	691,075	30,578	4.6
CalWORKs	340,743	348,599	354,117	5,518	1.6
CalWORKs Child Care	137,273	149,044	169,857	20,813	14.0
Child Welfare Services	117,525	122,841	124,256	1,415	1.2
Adoption	85,569	86,738	86,862	124	0.1
CFAP	43,661	51,491	56,648	5,157	10.0
Foster Care	50,103	48,374	47,681	(693)	-1.4
Kin-GAP	18,179	17,965	18,053	88	0.5
CAPI	14,532	15,447	15,915	468	3.0

California Work Opportunity and Responsibility for Kids (CalWORKs)

CalWORKs Budget and Caseload. The budget proposes $7 billion overall in 2024-25 for CalWORKs program expenditures, and estimates an average monthly caseload of 354,117 families. This represents a 1.6 percent increase over the revised 2023-24 caseload of 348,599.

CalWORKs Grant Increase. The 2024-25 budget includes a 0.8 percent increase to CalWORKs Maximum Aid Payment levels, estimated to cost $27 million in 2024-25. This increase is supposed to be funded entirely by the Child Poverty and Family Supplemental Support Subaccount, a fund source that the state previously realigned to counties. While this expansion has not yet used General Fund, the nonpartisan Legislative Analyst's Office (LAO) raised concerns last year that while an increase included in the 2023-24 budget could be covered by the subaccount in 2023-24 and 2024-25, General Fund would likely be needed to pay for the increase starting in 2025-26. Providing an increase with the knowledge that General Fund will be needed in the near future contrasts with tens of billions of dollars in deficits.

CalWORKs Single Allocation Reduction. The budget proposes several reversions and ongoing cuts to the CalWORKs Single Allocation, including reverting $336 million General Fund in 2022-23, about $41 million GF in 2023-24, and reducing the allocation by around $41 million GF in 2024-25 and ongoing. The single allocation is meant to cover most costs outside of the cash assistance provided, such as eligibility administration, employment services, and the Cal-Learn Intensive Case Management.

Program Eliminations. The budget also proposes several reversions and reductions to services provided under CalWORKs that essentially eliminate the programs:

- $55 million General Fund reversion in 2023-24, and a cut of $71 million GF in 2024-25 and ongoing for the Family Stabilization program, which provides intensive case management services and crisis intervention for families. Examples of services provided include non-medical outpatient drug treatment, emergency shelter, rehabilitative services, and movement to transitional housing.

- $47 million GF reduction in 2024-25 and ongoing for Employment Services Intensive Case Management. This service is provided to individuals needing extra support from county staff to address barriers to employment.

- $134 million GF reversion in 2023-24, and $134 million GF reduction in 2024-25 and ongoing for Expanded Subsidized Employment.

In-Home Supportive Services (IHSS)

Enrollment and Cost Growth in IHSS. The budget includes $24.3 billion ($9 billion General Fund) in 2024-25 for the IHSS program, and reflects a $1.9 billion ($665 million General Fund) increase compared to the 2023-24 revised budget. Major reasons for the substantial increase in costs are the continued expansion of full-scope Medi-Cal to undocumented immigrants of all ages, projected caseload growth, minimum wage/cost per hour increases, and increases in the number of hours per case. Estimates put the projected caseload at 691,075 in 2024-25, representing a 4.6 percent increase over 2023-24. The 2023-24 projected provider cost per hour is $20.01, increasing to $20.52 per hour in 2024-25, and the hours per case are 122 in 2023-24 and expected to increase to 122.8 in 2024-25. For context, the previously projected cost per hour for 2023-24 was $19.12 at the Governor's January budget in 2023, and the hours per case were projected at 115.9.

Undocumented Services Expansion. The 2024 budget continues the expansion of IHSS to undocumented immigrants of all ages, reflecting projected benefits costs of $383 million General Fund and about $15 million GF for administration. It will take a few years to reflect the full costs of this expansion as more individuals enroll. The revised 2023-24 budget also reverts approximately $650 million GF previously allocated to cover the rollout of benefits to undocumented individuals 50 and over, due to a lower-than projected-caseload.

Supplemental Security Income/State Supplementary Payment (SSI/SSP)

Maintains SSP Increase. The 2024-25 budget includes $292 million General Fund for the continuation of a 9.2 percent increase to SSP grants included in the 2023-24 budget. There is also a 3.2 percent federal SSI cost-of-living increase. Effective January 2024, the maximum SSI/SSP grant levels are $1,183 per month for individuals and $2,023 per month for couples. Even with these increases, the maximum grant for SSI/SSP individual recipients will still be below the federal poverty level. Those who receive SSI/SSP benefits are blind, disabled, or at least 65 years old. The funds are meant to help recipients provide for basic living expenses such as food, clothing, and shelter.

Children and Family Services

The budget includes $690 million General Fund in 2024-25 for Children and Family Services programs. Including federal and realignment funds, the total funding is more than $9.4 billion. Children and Family Services programs include Child Welfare Services (CWS), Adoption Assistance, Foster Care, Kinship Guardian Assistance Payment (Kin-GAP), and relative caregiver programs.

The Governor's budget makes several cuts to children and family services including:

- $30 million General Fund in 2024-25 and ongoing for the Family Urgent Response System (FURS), which provides hotline support for current and former foster youth, and caregivers who are dealing with emotional, behavioral, or other difficulties that require immediate support.

- $8.3 million General Fund in 2024-25 and ongoing for the Los Angeles County Child Welfare Services Public Health Nursing Program. The program is meant to maximize the use of county public health nurses in the field to provide families, whose children are at risk of being placed in the child welfare system, with preventative services to meet their medical, mental, and behavioral health needs.

- $195,000 General Fund in 2024-25 and $26 million ($19 million GF) in 2025-26 and ongoing for housing supplements for foster youth in Supervised Independent Living Placements. See the housing and homelessness programs section below for more details.

Rate Reform for Foster Care. The budget also proposes $12 million General Fund in 2024-25 to implement automation changes to reform the foster care payment structure. The new system is supposed to focus more on an individual child's need and strengths versus their placement type.

Housing and Homelessness Programs

Delays Funding for Californians at Risk of Homelessness. The budget proposes delaying $195 million to 2025-26 in one-time housing and homelessness investments meant to serve those at risk of or experiencing homelessness. The delays include:

- $80 million for the Bringing Families Home Program, which serves families in the child welfare system and seeks to prevent foster care placements and keep families together.
- $65 million for the Home Safe Program that provides housing supports for individuals in adult protective services, usually as a result of elder abuse, neglect, or financial exploitation.
- $50 million for the Housing and Disability Advocacy Program, which provides housing supports, among other services, for individuals that are likely eligible for disability benefits and struggling with housing or homelessness.

The budget also proposes extending the expenditure deadline for one-time funding provided in the 2021 budget act for these programs to June 30, 2025.

Eliminates Housing Support for Foster Youth. The 2024-25 budget proposes cutting $200,000 General Fund (GF) in 2024-25 and about $19 million GF in 2025-26 and ongoing for a housing supplement for foster youth in Supervised Independent Living Placements (SILPs). The 2023 budget act created this supplement to the basic rate paid for a non-minor dependent placed in a SILP, with an expected rollout on July 1, 2025. These SILPs are placement options for individuals aged 18 to 21 participating in extended foster care. Providing an additional housing supplement was meant to help fill the gap between housing costs and the basic rate paid. The proposed cuts to this funding essentially eliminates the program.

Other Human Services Programs

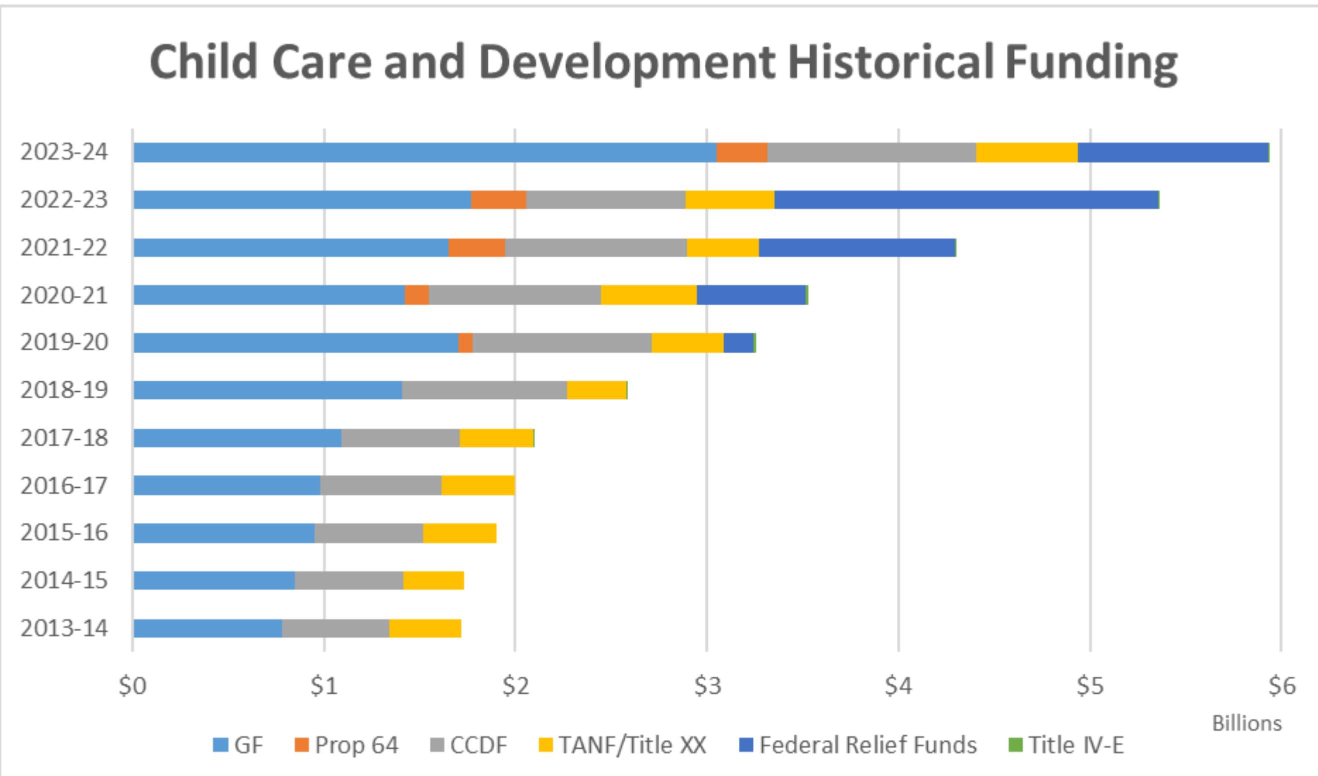
EBT Benefit Theft Reimbursement. The 2024-25 budget proposes $45 million ($34 million GF) in reimbursements for stolen cash and food benefits. This is a decrease from the revised 2023-24 reimbursement total of $215 million ($168 million GF). DSS assumes that reimbursements will decrease as a result of the implementation of new EBT security card technology improvements. The 2023-24 budget made investments to begin enabling EBT cards with Chip/Tap technologies, with full implementation anticipated to be complete in 2025-26.

Child Care and Early Education

Key Points

- **Child Care Slot Expansion.** Includes $2.1 billion for the continued expansion of subsidized child care slots.
- **Alternative Methodology for Rate Reimbursements.** Notes that a state plan will be submitted to the federal government for approval of an alternative methodology by July 2024.
- **Maintains Funding for Bargaining Agreement.** The budget maintains funding for the provisions of the bargaining agreement reached with Child Care Providers United in the 2023 budget and continues to provide funding for parity provisions that apply to State Preschool Providers.

The 2024-25 budget proposes $6.6 billion ($4.6 billion General Fund) for child care programs administered by DSS, including CalWORKs Stages One, Two, and Three, Alternative Payment Programs, Migrant Child Care, General Child Care, Child Care for Children with Disabilities, the Emergency Child Care Bridge Program, and local supports for the programs. This reflects an increase of about $1.5 billion General Fund over the revised 2023-24 budget. Below is a chart showing historical child care and development funding by source. An exact breakdown of funding figures for 2024-25 was not available at the time this report was written.



CCDF is the federal Child Care and Development Fund, Tittle IV-E is federal funding related to Foster Care, Proposition 64 is Marijuana Tax Funding, and TANF/Title XX is the federal Temporary Assistance for Needy Families and Social Services funding.

Child Care Transition, Expansion and Rates History. The Budget Act of 2020-21 transferred Child Care and Development from the California Department of Education (CDE) to DSS effective July 2021.

In addition to the department transition, the state has significantly increased spending in recent budget cycles to for additional child care slots.

- The 2021-22 budget set a goal of adding 200,000 new subsidized child care slots, with a full rollout in 2026-27.
- The 2024-25 budget is projected to add 28,000 new slots and includes $2.1 billion to fund roughly 146,000 total slots added since 2021-22.

The chart below shows how many slots have been added each year and the cost of those slots.

Total Number and Cost of New Child Care Slots Added Since 2021-22 ***(in Millions)***

	2021-22		2022-23		2023-24	2024-25	
Program	Slots	Full Year Slot Funding	Slots	Full Year Slots Funding		Additional Slots	Annualized Costs for New Slots
Alternative Payment (CAPP)	62,620	$ 734	32,000	$ 330	No new slots added	16,000	$ 278
General Child Development (CCTR)	8,804	$ 273	12,390	$ 279		12,000	$ 184
Migrant Alternative Payment (CMAP)	1,300	$ 17	-	$ -		-	$ -
Emergency Child Care Bridge	500	$ 4	-	$ -		-	$ -
Total by Fiscal Year	73,224	$ 1,028	44,390	$ 609		28,000	$ 462
Cummulative Total Slots Added from 2021-22 to 2024-25							145,614
Cummulative Yearly Cost of Total Slots Added from 2021-22 to 2024-25							$ 2,099

In addition to the new slots, numerous subsidies and rate increases have been provided to child care providers since the 2021-22 budget. The most sweeping of these changes was included in the 2023-24 budget, which ratified a new bargaining agreement between the state and Child Care Providers United (CCPU), whose members are not state employees. The agreement had a projected total cost of about $2 billion over 2023-24 and 2024-25, and this budget continues those expenditures. Major provisions of the agreement included:

- $915 million for a temporary monthly “cost of care plus rate” per child for all subsidized child care providers. These payments range from $98 for license-exempt providers in the Central Region to $211 for licensed providers in the Bay Area.
- $229 million for one-time add-on payments to providers who were reimbursed for subsidized child care or state preschool services in April 2023. The one-time payments are $500 for license-exempt providers, $2,500 for licensed small family daycare homes, and $3,000 for licensed large family daycare homes.

- $200 million for the CCPU Workers Health Care Fund. This funding reflects the maximum for potential annual deposits.
- $160 million for the establishment of the CCPU Retirement Trust to provide access to retirement benefits for family child care providers. This funding reflects the initial deposit and maximum for potential annual deposits.
- $155 million to extend the COVID-era "hold harmless" policies until June 30, 2025 for child care reimbursements. This policy inexplicably continues to pay providers as though they still had higher numbers of children in their care, irrespective of the actual attendance.
- $104 million to re-define “part-time” care as care certified for a child for less than 25 hours per week, and “full-time” care as 25 hours or more per week. The previous “part-time” definition was less than 30 hours per week.

Continues to Pursue an Alternative Methodology for Rate Reimbursements. The 2023-24 budget directed DSS, in collaboration with the State Department of Education (CDE), to develop and conduct an alternative methodology for setting reimbursement rates for state-subsidized childcare and preschool services. The 2024-25 budget, apparently ignoring California’s years of projected multibillion dollar deficits, unwisely continues a previous state plan to ask the federal government for approval of an alternative methodology by July 2024. Preliminary estimates put the cost to fully fund the methodology at $12 billion. Although there is no requirement to actually implement the alternative methodology, it is the majority party’s intent to use it to inform future rate-setting. With a major deficit and bleak future fiscal outlook, it brings to light the improbability that these rates will be realized in the near future.

State Preschool Program. The 2024 proposed budget includes about $54 million General Fund, previously supported by one-time federal stimulus funding, to continue the implementation of reimbursement rate increases included in the 2023 budget. These rate increases were included in the recently negotiated collective bargaining agreement with CCPU. The state extended provisions of the agreement to State Preschool providers to ensure provider parity, with the exception of the health, retirement, and training funds. The $54 million is in addition to about $141 million General Fund and $206 million Proposition 98 General Fund appropriated in the 2023-24 budget. Those funding levels reflect one-time savings of $172 million General Fund and $446 million Proposition 98 General Fund.

Developmental Services

Key Points

- **Breaks Promise to Developmentally Disabled Community.** Instead of fully implementing the much-needed service provider rate reform in 2024-25 as promised, the budget would pull the rug out from providers and delay the last year of funding.
- **General Fund Budget Higher by $1.7 Billion, Spurs Master Plan on the Developmental Services.** With the regional center caseload on a significant rise, the department's General Fund budget increases by 11.7 percent from 2023-24, spurring a soon-to-be developed "master plan" that could include future cost control changes.
- **Costly "Warm Shutdown" of Fairview Developmental Center Continues.** Despite plans to use the property for public and private sector alternatives, the department spends millions for facility to sit vacant.
- **Another Preschool Inclusion Grants Delay.** The budget delays again, for two years, support funding for preschools to adapt their facilities for toddlers with intellectual/developmental disabilities.

Growing Caseload Served by Regional Centers Could Lead to Dramatic Cost Control Measures. The Department of Developmental Services (DDS) is responsible for administering the Lanterman Act, which provides services and supports through a network of regional centers to enable people with intellectual and developmental disabilities to lead more independent and integrated lives. The Governor's budget proposes that the overall 2024-25 budget for DDS will be $15.3 billion total funds, of which $9.6 billion is General Fund, an increase of 11.7 percent from 2023-24. This increase is attributable to the rapidly growing regional center caseload. The number of individuals served by regional centers is expected to reach 458,228 in 2024-25, a 6.7 percent increase from 2023-24. In addition, 302 individuals are projected to be served in state-operated facilities as of July 1, 2024.

The substantial rise in caseload and associated costs is spurring DDS to convene a workgroup of stakeholders in the creation of a Master Plan for Developmental Services. Details on this proposed master plan are limited, but the department has stated that establishing a more "quality-driven" and "consumer friendly" experience are the main goals. In the end, the department desires to implement a new "program management system" to "maximize the effectiveness" of investments. These vague statements have been taken by many advocates as a call for a more Medi-Cal-managed-care-like capitated rate payment model rather than a per-service payment structure in order to average out the per client annual costs and to more effectively draw down federal funding.

Breaks 2022 Promise to Developmentally Disabled Community by Slowing Necessary Provider Rate Increase. The Governor's budget removes $613 million General Fund in 2024-25 and imposes a one-year delay in implementing the final year of the long-awaited service provider rate increases. This was to be the fourth and final year of a multi-year roll-out of the rate reforms, under the timeline Governor Newsom endorsed in the 2022 Budget Act. Delaying the last year of funding in 2024-25 breaks the promise to the developmentally disabled community and creates a disruptive impact in delivery of services to individuals. Service providers may have already made hiring decisions reliant on the July 2024 scheduled rate increase, and thus may have insufficient resources to maintain adequate levels of staff.

Senate Republicans have long advocated for improving rates for services, but while tax revenues have rapidly increased over the past decade, two successive Democratic governors have repeatedly delayed the inclusion these funds for years, choosing to create and fund new programs in other areas of the budget instead (like billions allocated for newly expanded undocumented healthcare, for example). Senate Republicans believe that keeping rate reform implementation on schedule is a priority in order to maintain and improve service to families with developmentally disabled individuals.

Preschool Inclusion Grants Delay. The budget delays yet again, for two years until 2026-27, the implementation of a $10 million General Fund annual grant program to support preschool inclusion efforts such as facility modifications or staff training. This program was included as part of the Early Start to special education transition process for toddlers with intellectual and/or developmental disabilities.

Continues Warm Shutdown of Fairview Developmental Center. The budget proposes an another extension of the warm shutdown funding for Fairview Developmental Center in Costa Mesa at a cost of $11.3 million General Fund to maintain 52 staff there. The last resident moved out of Fairview in January 2020, but the administration is choosing yet again to maintain the warm shutdown status for potential needs like homeless shelter if necessary. The use of this much money in a deficit year to maintain empty facilities, especially when tens of thousands currently live on the streets, should be a concern to the public. There are a number of better public and private uses of the valuable property, and the state should consider ways to use this asset to help close our budget deficit.

K-12 Education

Key Points

- **Proposition 98 Minimum Drop.** The Proposition 98 constitutional minimum is down $14.3 billion over the 2022-23 to 2024-25 budget period. Most of the drop, $9.1 billion, is in 2022-23.

- **Lack of Detail on an $8 Billion Funding Decrease.** The budget notes that statutory changes will be proposed to address an $8 billion Proposition 98 funding decrease in 2022-23, but fails to provide substantial details.

- **Reduces School Facility Funding.** The budget proposes a cut of $500 million General Fund for the School Facility Program.

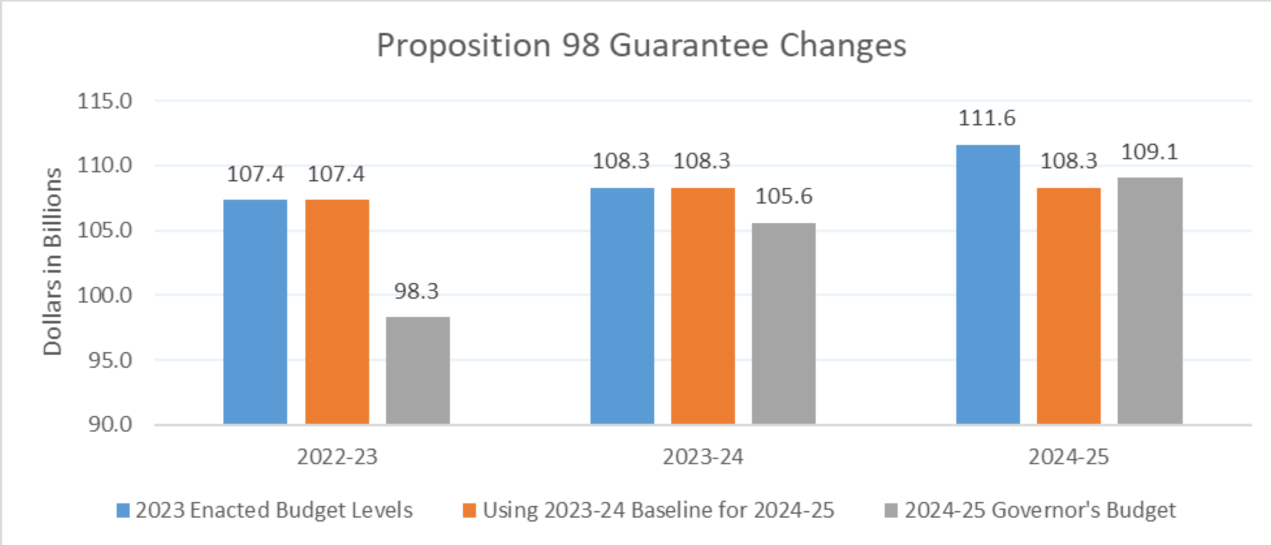
- **Charter School Funding Eligibility.** The budget proposes statutory changes that would make charter schools eligible for funding from the Education Revenue Augmentation Fund (ERAF).

- **Absenteeism Solutions and Attendance Recovery.** The budget proposes statutory changes to allow Local Education Agencies (LEAs) to add attendance recovery time to data submitted for funding and chronic absenteeism reporting.

- **Zero Emission Buses, Despite Deficit.** The budget maintains $500 million in one-time Proposition 98 General Fund for zero-emission buses.

Overall K-12 Education Funding. The Budget includes $127 billion ($76 billion General Fund and $50 billion other funds) for all K-12 education programs. Under this budget proposal, ongoing K-12 Proposition 98 per pupil expenditures are $17,653 in 2024-25, and $23,519 per pupil when accounting for all funds. The Legislative Analyst's Office (LAO) estimates $18,160 per pupil in Proposition 98 spending. The LAO's estimate is higher as they include the Proposition 98 reserve withdrawal (discussed below) and $500 million in Proposition 98 funding allocated for electric school buses, which the Administration does not include in its figures.

Proposition 98 K-14 Funding. The Proposition 98 constitutional minimum is down $14.3 billion over the 2022-23 to 2024-25 budget period, compared to the 2023 budget act, due to the revised General Fund revenue estimates. The Governor's budget claims a decrease of only $11.3 billion by using the 2023-24 Proposition 98 funding level as the starting point for 2024-25. Most of the drop, $9.1 billion, is in 2022-23. The revised Proposition 98 funding levels are $98.5 billion in 2022-23, $105.6 billion in 2023-24, and $109.1 billion in 2024-25. The table on the next page summarizes these comparisons.



Proposition 98 Funding by Segment and Source
(Dollars in Millions Except Funding Per Student)

	2022-23 Revised	2023-24 Revised	2024-25 Proposed	Change From 2023-24 Amount	Change From 2023-24 Percent
K-12 Education					
General Fund[a]	$60,591	$68,959	$70,093	$1,133	1.6%
Local property tax	25,882	26,917	27,975	1,057	3.9%
Subtotals	**$86,473**	**$95,877**	**$98,068**	**$2,191**	**2.3%**
California Community Colleges					
General Fund	$7,634	$8,425	$8,679	$255	3.0%
Local property tax	3,860	4,036	4,210	175	4.3%
Subtotals	**$11,494**	**$12,460**	**$12,890**	**$430**	**3.4%**
Reserve Deposit/Withdrawal (+/-)[b]	$339	-$2,751	-$1,878	$873	-31.7%
Totals	**$98,306**	**$105,586**	**$109,080**	**$3,493**	**3.3%**
Enrollment					
K-12 attendance	5,396,404	5,401,820	5,400,244	-1,576	0.0%
Community college FTE students	1,100,681	1,100,417	1,098,591	-1,826	-0.2%
Funding Per Student					
K-12 Education	$16,024	$17,749	$18,160	$411	2.3%
California Community Colleges	10,442	11,323	11,733	410	3.6%

[a] Includes funding for instruction provided directly by state agencies and the portion of State Preschool funded through Proposition 98.
[b] Accounts for required and discretionary changes to the Proposition 98 Reserve. Amounts consist entirely of General Fund.

FTE = full-time equivalent.

$8 Billion in Unknown Statutory Solutions. The budget proposes to reduce the Proposition 98 General Fund spending in 2022-23 by $8 billion. The entire 2022-23 reduction is $9.1 billion, but $1.1 billion of this is addressed through changes in the required reserve deposit. The Governor's budget claims that the $8 billion decrease will be done with "statutory changes", and the changes will avoid impacting Local Education Agency (LEA) and community college budgets. Administration officials have stated informally that the solutions include supplemental payments to be made over a five-year period from 2025-26 through 2029-30, plus a fund swap. However, specific details on the implementation have not been provided. With the lack of information on this proposal, it is not clear how, or even if, the Governor's proposal would work.

Proposition 98 Rainy Day Fund. The 2024 budget estimates a $3.9 billion balance in the Public School System Stabilization Account (school reserve) at the end of 2024-25. This is a decrease of about $7 billion compared to the projected balance at the 2023 budget act. This decrease reflects a revised deposit of $339 million in 2022-23 and net withdrawals of about $2.8 billion in 2023-24 and $1.9 billion in 2024-25.

Under current law, there is a cap of 10 percent on school district reserves in fiscal years immediately succeeding those in which the school reserve balance is equal to or greater than 3 percent of the total K-12 share of the Proposition 98 guarantee. The balance of $5.7 billion in 2023-24 continues to trigger school district reserve caps in 2024-25. Senate Republicans have raised concerns on these district-level caps, which reduce local control and force schools to spend more. This law is especially concerning considering the fiscal situation facing the state, and the potential need for schools to utilize reserves in case of further deficits.

Local Control Funding Formula (LCFF). The budget includes a 0.76 percent cost-of-living (COLA) adjustment for the LCFF, that when combined with population growth adjustments, will result in a $1.4 billion decrease in additional discretionary funds for schools. The budget proposes withdrawing $2.8 billion from the Proposition 98 reserve in 2023-24 and $2.2 billion in 2024-25 to fully fund LCFF costs and offset the decrease. The budget also uses $38.6 million in re-appropriation and reversion funding for LCFF costs in 2024-25.

The budget also provides $65 million ongoing Proposition 98 General Fund for COLA adjustments for categorical programs such as Special Education, State Preschool, Youth in Foster Care, Child Nutrition, the Charter School Facilities Grant Program, and the LCFF Equity Multiplier.

Delays the Full-Day Kindergarten Program Again. The 2023-24 budget delayed a $550 million one-time General Fund investment in the Preschool, Transitional Kindergarten, and Full Day Kindergarten Facility Grant (FDK) program to 2024-25. The 2024-25 proposed budget further delays that investment to 2025-26. The FDK program provides funding to retrofit existing school facilities or construct new facilities for transitional kindergarten, preschool classrooms, and full-day kindergarten. With no change to the rollout of universal TK, and the push for universal preschool and mandatory kindergarten, it could be seen as inconsistent to delay funding meant to provide adequate facilities. On the other hand, the LAO previously noted that facilities for these programs are less of a concern to LEAs, and that staffing needs are the more pressing issue. Time will tell if these repeated delays have a negative impact on the state's early education push.

School Facility Grant Cut. The Governor's budget proposes cutting the School Facilities Program funding in 2024-25 by $500 million one-time General Fund. This would bring the planned allocation from $875 million to $375 million. The 2023 budget also reduced funding for this program by $100 million. The state auditor released a report in January 2022 that found California will need $7.4 billion in state funding to meet projected modernization requests over the next five years. The last approved facilities bond, Proposition 51 in 2016, authorized $9 billion in State General Obligation bonds to support K-12 and community college facility construction. The budget notes that the Administration expects to enter into negotiations with the Legislature this spring to reach an agreement on a bond proposal to be considered in the November 2024 election.

Instructional Stability and Student Support. The budget proposes several statutory changes to provide students with enhanced instructional stability and support, to help minimize learning loss, and reduce the fiscal impacts of absenteeism. These proposals include:

- Providing LEAs with the option to add attendance recovery time to attendance data submitted to the Department of Education (CDE) for Average Daily Attendance (ADA) reporting and chronic absenteeism. This change has the potential to mitigate funding impacts related to ADA, and could encourage LEAs to provide students with more attendance recovery programs. Some of the programs that would qualify are Saturday school, before/after school programs, and intersessional school.

- Requiring that during emergencies lasting 5 or more days, LEAs provide students with remote access or support students to enroll at a neighboring LEA.

- Encouraging LEAs to provide hybrid and remote learning opportunities to students unable to attend school.

The budget also proposes $6 million one-time Proposition 98 General Fund to research existing and develop new models for hybrid and remote learning. This includes providing resources to LEAs on how to develop their own programs. The funding will also be used to investigate local student information systems to allow for the submission of absence data that can, among other things, isolate and identify absences related to emergency events.

Proposition 28 and Arts Career Education. The budget includes $931 million to fund Proposition 28, passed by voters in 2022. The measure requires an amount equivalent to one percent of the prior year's Proposition 98 funding received by local education agencies to be directed to schools for arts education. The budget also includes a proposal for the Commission on Teacher Credentialing to create a new Elementary Arts and Music Education authorization for career technical education (CTE) teachers. The intention is to create additional pathways for artists to provide arts instruction in elementary schools and provide CTE instruction in grades 7 through 12.

Charter School Funding Eligibility. The budget proposes statutory changes that would clarify that charter schools are eligible for funding from the Education Revenue Augmentation Fund (ERAF). The ERAF was created in 1992, and redirects a share of property taxes statewide from cities, counties and special districts to K-14 schools. ERAF offsets funding K-14 schools would otherwise receive from the state General Fund. Charter schools were established the same year as ERAF and it has never been clarified if they are eligible for this funding.

Educator Workforce Investments. The budget includes several investments and statutory proposals related to educator workforce development, including:

- $25 million ongoing Proposition 98 General Fund through the K-12 Mandate Block Grant to support training teachers to begin administering reading difficulty screenings, including for dyslexia, by 2025-26 for students in kindergarten through second grade.

- $20 million one-time Proposition 98 General Fund for a County Office of Education to work with the University of California Subject Matter Projects to develop and provide training for mathematics coaches and leaders. These coaches/leaders will provide training and support to help math teachers provide instruction based on the new Mathematics Framework adopted by the State Board of Education in 2023. The budget also proposes statutory changes to allow the use of Learning Recovery Emergency Block Grant funding for professional development associated with the new mathematics framework.

- Proposes recognizing the completion of a bachelor's degree as satisfying the basic skills requirement for a credential and improving how transcripts are reviewed. These changes are intended to simplify the process and reduce the cost for a prospective teacher to become credentialed.

- Finally, the budget proposes changes that will enable school staff to be better equipped and offer mental health supports to students. These supports will be aligned with other state investments in the mental health space, and professional development opportunities are also indicated.

Additional K-12 Budget Adjustments. The budget also includes the following changes.

- **Local Property Tax Adjustments.** The budget includes a decrease of $113 million Proposition 98 General Fund for school districts and county offices of education in 2023-24, and a $996 million decrease of ongoing Proposition 98 General Fund in 2024-25 as a result of increased offsetting property taxes.

- **Zero-Emission Bus Funding.** The budget proposes to continue a $500 million one-time Proposition 98 General Fund investment in 2024-25 for efforts to convert school bus fleets to zero-emission through programs operated by the California Air Resources Board and the California Energy Commission.

- **Continued Support for School Nutrition.** The budget proposes an increase of $122 million ongoing Proposition 98 General Fund to fully fund the universal school meals program in 2024-25. It is projected that over 845 million meals will be served in 2024-25.

Higher Education

Key Points

- **Total Higher Education Funding Increases.** Proposes total funding of $26.7 billion General Fund for universities, community colleges, and financial aid, a slight increase of $364 million.
- **University Compact Increase Deferrals.** Defers the five percent increases previously agreed upon through the compacts, including $240 million to the California State University and $228 million to the University of California to 2025-26.
- **Resident Undergraduate Enrollment Growth Deferral.** Defers $31 million General Fund to offset revenue reductions associated with replacing 902 nonresident undergraduate students enrolled at three UC campuses.
- **Suspending Student Housing Revolving Loan Fund Program.** Suspends $300 million one-time General Fund previously intended to be appropriated each year from 2024–25 to 2028–29.
- **Student Aid Reduction.** Proposes to forego $289 million one-time General Fund for Middle Class Scholarships.

Higher Education Expenditures

(Dollars in Millions)

	2022-23	2023-24	2024-25	Change from 2023-24	
				Dollars	Percent
University of California					
Ongoing General Fund	4,377.0	4,722.2	4,739.3	$17.1	0.4%
One-Time General Fund	532.5	148.0	1.1	-	-
Total Funds[1/]	$10,398.4	$10,560.3	$10,643.5	$83.2	0.8%
California State University					
Ongoing General Fund	5,041.1	5,409.1	5,472.8	$63.7	1.2%
One-Time General Fund	268.4	35.5	0.0	-	-
Total Funds[1/]	$8,600.4	$8,713.6	$8,914.4	$200.7	2.3%
California Community Colleges					
General Fund & Property Taxes	12,148.2	12,991.9	13,566.2	$574.3	4.4%
Total Funds[2/]	$21,091.1	$21,255.3	$21,611.3	$355.9	1.7%
California Student Aid Commission					
General Fund[3/]	2,880.5	3,055.2	2,946.9	($108.3)	-3.5%
Total Funds	$3,299.8	$3,481.3	$3,373.3	($108.1)	-3.1%
General Fund	**$25,247.8**	**$26,361.9**	**$26,726.3**	$364.3	1.4%
Total Funds	**$43,389.8**	**$44,010.6**	**$44,542.4**	$531.8	1.2%

[1/] These totals include tuition and fee revenues and other funds the universities report as discretionary.

[2/] Withdrawals from the Public School System Stablization Account are reflected in this row.

[3/] General Fund expenditures for the Cal Grant program are offset by reimbursements, including approximately $400 million in federal Temporary Assistance for Needy Families (TANF) funds received through an agreement with the Department of Social Services.

Source: Department of Finance

University Compact Increase Deferrals. As part of the Governor's deficit solution package, the budget defers the five percent increases previously agreed upon through the compacts, including $240 million to the California State University (CSU) and $228 million to the University of California (UC) to 2025-26. The budget indicates the compacts with CSU and UC will continue to be maintained by providing the 2024-25 base increases a year later in 2025-26. The Governor argues that CSU and

UC could draw down their reserves or borrow internally or externally as a way to manage the one-year deferral. However, given the state's ongoing deficits of $33 billion or more, it appears unlikely that UC and CSU will actual receive those funds a year later.

Also noteworthy is that in September 2023, the CSU Board of Trustees approved annual tuition rate increases over five academic years, starting with a six percent increase in fall 2024. In November the UC board submitted a request to the state for $273 million in ongoing funds, plus another $1.2 billion for capital projects. The Governor's budget deferrals move in the opposite direction instead.

California Community Colleges. The community college budget is part of the state's Proposition 98 education obligation and often includes similar adjustments to K-12 education. Adjustments in the Governor's budget include:

- An increase of $69 million ongoing Proposition 98 General Fund to provide a 0.76 percent cost-of-living adjustment (COLA) for Student-Centered Funding Formula apportionments and $30 million ongoing Proposition 98 General Fund for 0.5 percent enrollment growth.

- An increase of $9 million ongoing Proposition 98 General Fund to provide a 0.76 percent COLA for select categorical programs and the Adult Education Program.

- An increase of $60 million one-time Proposition 98 General Fund to expand nursing programs and Bachelor of Science in nursing partnerships.

Community College Housing Projects. Last year's budget shifted 19 community college student housing projects from being funded with cash to debt financing. Three of these are to enter into intersegmental projects with the UC system. Of the remaining 16 projects, three have now been deemed unsuitable for a statewide lease revenue bond, and the Governor's budget proposes to return to funding these three projects with $51 million in non-Proposition 98 General Fund from last year. These campuses are in Napa, Santa Rosa, and Imperial Valley. The Administration indicates more detail on the statewide lease-revenue bond will be available in the May Revision.

Additional University of California Adjustments. In addition, the Governor's budget proposes the following reductions:

- *Resident Undergraduate Enrollment.* Delays planned funding of $31 million ongoing General Fund to 2025-26 for increasing resident undergraduate enrollment by 902 students across three UC campuses.
- *UCLA Research Center.* Forgoes a planned investment of $300 million for the UCLA immunology institute. The Governor recently announced giving UCLA the first $200 million for that project, which also expects to receive funds from philanthropists and corporate interests like Google.

Despite the reductions, the Governor's budget would maintain a previously planned increase of $15 million in ongoing General Funds to support the Medical School Project at UC Merced.

California Student Aid Commission. The Governor's budget proposes financial aid expenditures totaling $3.3 billion, $2.5 billion of which supports the Cal Grant Program, and $636 million of which supports the Middle-Class Scholarship program. The state's Cal Grant program is estimated to provide over 377,000 financial aid awards to students who meet specified eligibility criteria in 2023-24. In light of the state's deficit, the budget forgoes a planned one-time Middle Class Scholarship investment of $289 million.

Suspending the Student Housing Revolving Loan Fund Program. Another part of the Governor's deficit solution package suspends $300 million one-time General Fund previously intended to be appropriated each year from 2024–25 to 2028–29. In addition, $194 million of $200 million one-time General Fund appropriated in 2023–24 would be reverted.

College of the Law, San Francisco (Formerly UC Hastings). The Governor's budget includes an increase of $2 million in ongoing General Funds to support operating costs at the law school's discretion, representing a 3 percent increase in base augmentation. Although this amount is small, it is unclear why a law school would receive an increase when the UC and CSU would see significant delays under the Governor's budget.

California State Library. The Governor's budget includes multiple pullbacks to the California State Library to address the deficit, including $34 million of the $35 million provided to expand statewide library broadband services.

Labor and Workforce Development

Key Points

- **Shifts Portion of Unemployment Interest Payment to Special Fund.** Proposes $331 million to pay the annual interest payment on the federal Unemployment Insurance (UI) loans. Of this amount, $100 million would come from the Employment Training Fund and the General Fund would pay the remainder.
- **Employment Development Department (EDD) Modernization.** Includes $327 million in funding for EDD IT systems, improved service for claimants, and fraud prevention, continuing a five-year modernization plan initially funded in 2022-23.
- **Reductions, Delays to Workforce Programs.** Proposes reductions of $95 million General Fund and delayed funding of $735 million for various apprenticeship and workforce development programs.

California Unemployment Debt Continues to Challenge Employers. California remains one of only two states to have neglected to pay off its unemployment insurance (UI) debt to the federal government following the pandemic. (New York is the other.) California's debt balance of $20 billion as of January 4, 2024, has actually grown by about $3 billion since May of 2023, moving in the wrong direction. Employers must pay down the debt principal through increased federal employer taxes, which will ratchet up each year until the debt is paid off. Governor Newsom likes to claim he does not support broad tax increases, but by refusing to pay off California's UI debt when a surplus was available, the Governor and other Democrats chose to let those tax increases go into effect.

Shifts Portion of UI Interest Payment to Special Fund. While increased federal employer taxes pay down the principal on the federal Unemployment Insurance (UI) loans, the state is responsible for the interest payments. The Governor proposes $331 million to pay the annual interest payment. Of this amount, $100 million would come from the Employment Training Fund and the General Fund would pay the remainder. Although this is an allowable use of the Employment Training Fund, the purpose of the fund is to invest in a skilled and productive workforce, and the money in the fund comes from employers. Since employers must already pay the principal of the UI debt through higher taxes, this fund shift would double down on making employers pay for the state's policies.

Continues Funding to Modernize the EDD. The budget provides $327 million ($163 million General Fund) for the third year of EDDNext, a five-year plan to modernize the EDD. This includes efforts to modernize EDD's benefit systems, improve customer service delivery, simplify forms and notices, develop anti-fraud analysis tools, and speed up application processing. This work is long overdue. The majority party knew over a decade ago that EDD's systems were inadequate for its mission, but Democrats prioritized many other programs in the budget. This neglect set the stage for EDD's horrendous performance and billions in fraudulent claims paid during the pandemic.

Apprenticeship and Workforce Training Programs. The Governor proposes reductions of $95 million General Fund and delays of $735 million for various apprenticeship and workforce development programs. The largest single cut is $45 million to the High Road Training Partnerships Program. Notably, the Displaced Oil and Gas Worker Pilot program is reduced by $10 million, from $40 million to $30 million.

Of the amounts delayed $140 million General Fund for the Nursing and Social Work Initiatives is delayed to 2025-26. Additionally, as a result of lower than anticipated Mental Health Services Act revenue, the proposal includes a delay of $189 million (Mental Health Services Fund) for various workforce investments at the Department of Health Care Access and Information.

The chart below displays the program reductions and delays.

Workforce Development Reductions and Delays
($ in millions)

Department	Program	Prior Budget Packages	General Fund Reduction	Delayed Funding	Amount Remaining
Department of Health Care Access and Information	Nursing and Social Work Initiatives	$446		$140	$446
	Various Healthcare Workforce Investment Programs	$351		$189	$162
Department of Industrial Relations	Apprenticeship Innovation Fund	$135		$40	$135
	Women in Construction Unit[1]	$15	$5		$10
	California Youth Apprenticeship Program	$65		$25	$65
Employment Development Department	Emergency Medical Technician Training	$40	$20		$20
	California Jobs First	$600		$300	$600
	Displaced Oil and Gas Worker Pilot Fund	$40	$10		$30
California Workforce Development Board	High Road Training Partnerships	$135	$45		$90
	Goods Movement Workforce Training Facility	$70		$40	$70
	Low Carbon Economy Program	$45	$15		$30
Total		**$1,496**	**$95**	**$734**	**$1,401**

[1] Amounts for this program are allocated annually.

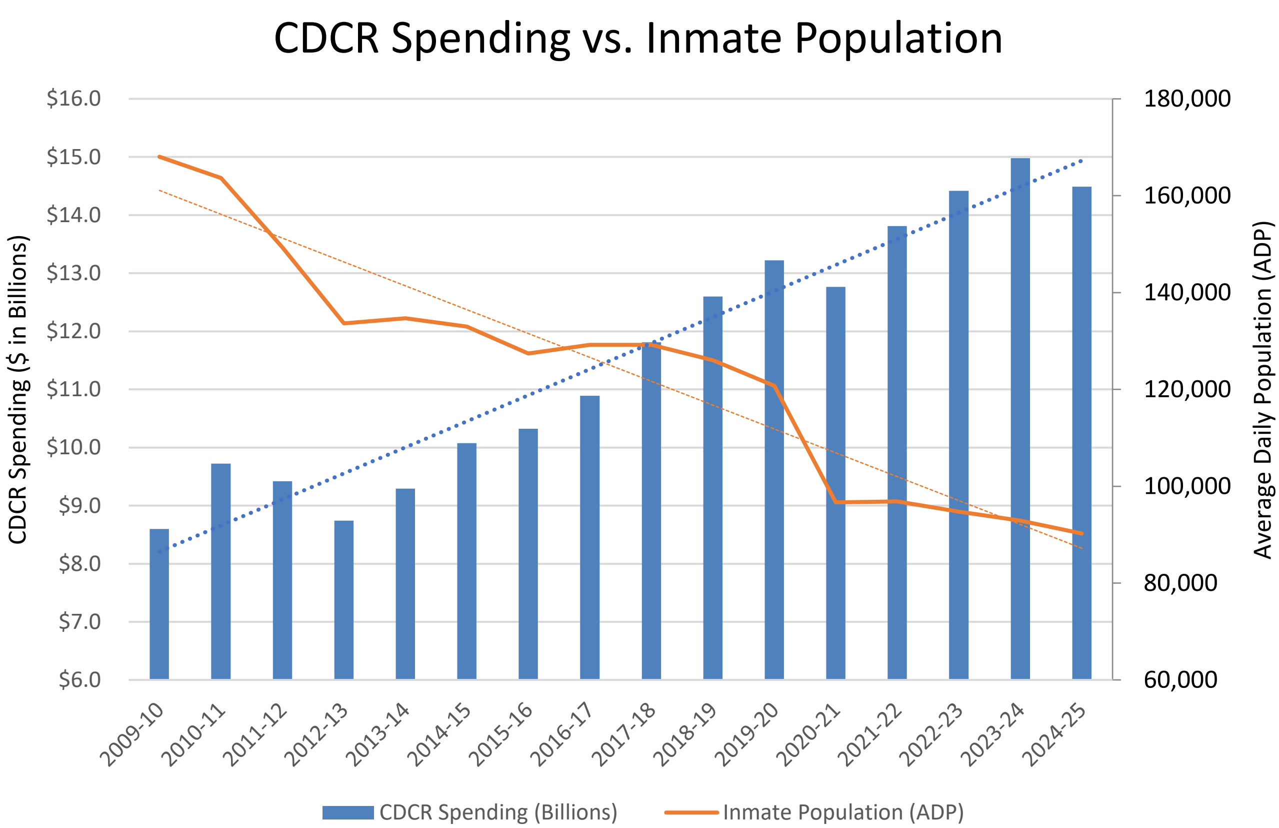
Public Safety and Judiciary

Key Points

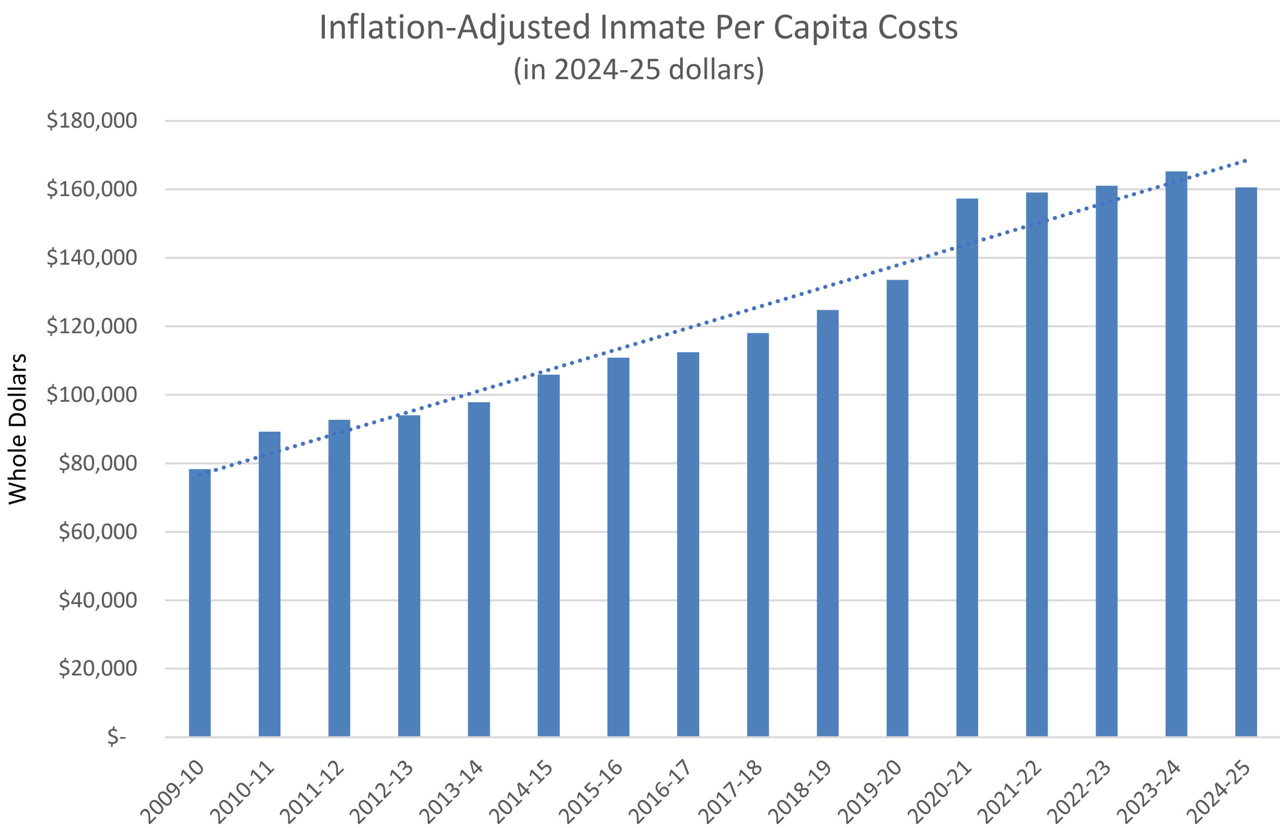
- **Budget Solutions Provide Only Temporary Relief.** $526 million in 2024-25 solutions from Department of Corrections and Rehabilitation, Department of Justice, Office of Emergency Services, and Judicial Branch combine for only $22 million in ongoing relief.
- **Governor Continues to Ignore Violent Crime Trends.** Budget includes no new funding to combat rising violent crime. Majority of recent public safety increases slated to expire.
- **Litigation Fund Loans More Money for General Fund Programs.** Rather than putting lawsuit settlement funds to work for Californians immediately, Attorney General accumulates billion-dollar balance. Half will prop up General Fund spending under Governor's proposal.

Department of Corrections and Rehabilitation (CDCR)

The Governor's budget includes total funding of $14.5 billion ($14.1 billion General Fund) for CDCR in 2024-25. This is an increase of more than $90 million over the 2023-24 budget at enactment (although lower than the revised 2023-24 total), despite projections that the inmate population will decrease in 2024-25. Contributing to this spending increase are rising costs for employee pay and benefits ($620 million) and inmate health care ($130 million), which more than offset hundreds of millions of dollars in savings related to the shrinking prison population. The chart below compares CDCR spending with the inmate average daily population (ADP) since the end of the Great Recession. While there were a few years in which CDCR's spending decreased, the general trend has been about 5 percent average annual growth, far exceeding inflation, despite the fact that the ADP has been declining steadily.



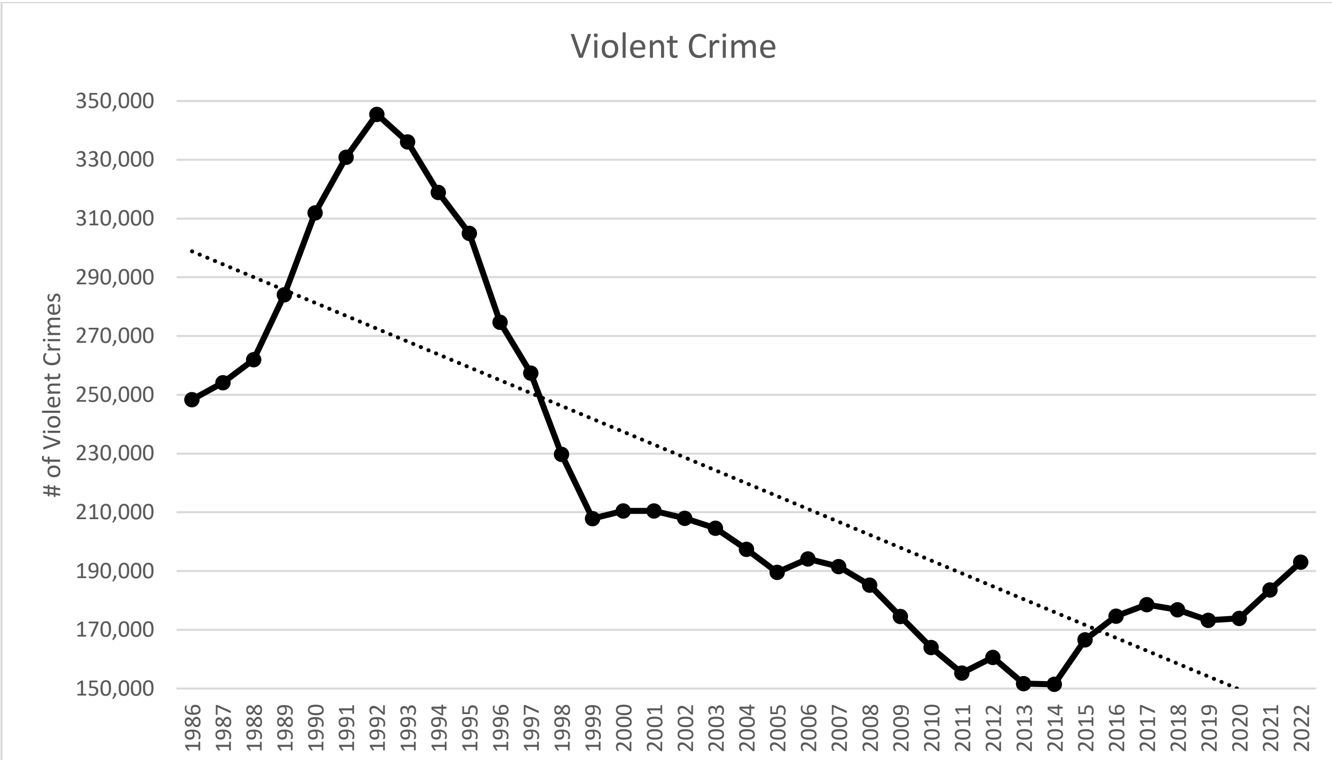
The inflation-adjusted average annual cost per inmate more than doubled over the same period, as shown in the next chart. This means that CDCR is spending more per capita than ever before to house and provide programming to offenders. Unfortunately, the dramatic increase in spending has not yielded commensurate results in terms of reducing recidivism. The three-year reconviction rate for the cohort of CDCR inmates released in 2008-09 was 49.1 percent, compared to 44.6 percent for the cohort released in 2017-18 (the most recent cohort for which data is available). Similarly, the three-year re-arrest rate only decreased from 75.3 percent to 68.4 percent.

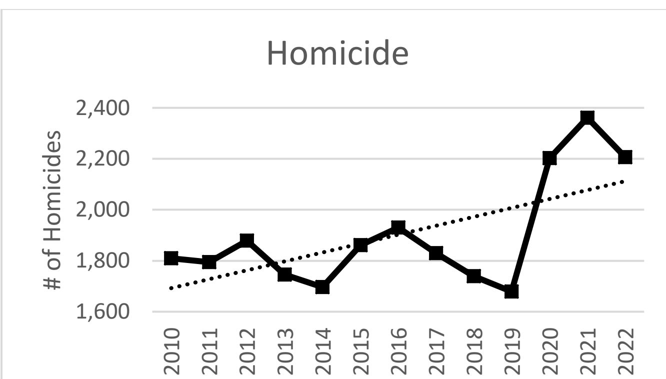


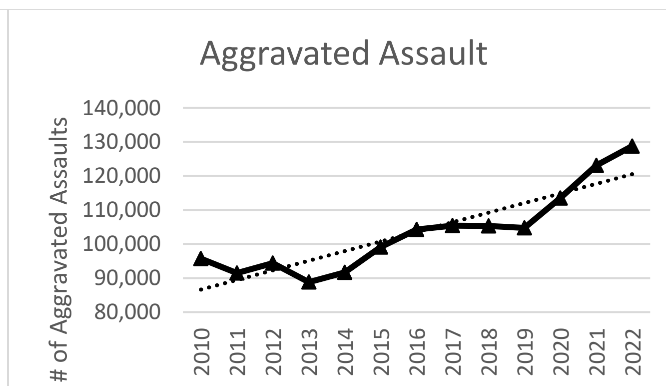
CDCR Budget Solutions. To help address the General Fund deficit, the Governor proposes a meager $109 million in solutions within CDCR's budget, which equates to about three quarters of one percent of CDCR's annual expenditures. Of this amount, $87 million are one-time reductions, leaving only about $22 million in ongoing solutions. The one-time solutions include delaying several video surveillance installation projects, reverting budgeted COVID-19 funds that would likely be unspent and revert on the natural anyway, and abolishing an unused CDCR special fund and transferring the balance to the General Fund. Ongoing solutions include a $15 million unallocated administrative reduction and right-sizing a handful of programs and contracts to align them with actual utilization. At one tenth of one percent of CDCR's annual expenditures, the $15 million unallocated administrative reduction appears to be the only actual permanent cut proposed by the Governor. CDCR spends more than $690 million per year on rehabilitative programs that produce lackluster results. Surely there are at least a few of these programs that could be reduced or eliminated in light of the massive deficit the state is facing.

<u>Crime Trends and Governor's Response</u>

Violent Crime. Violent crime is on the rise after nearly three decades of steady decreases, led by significant increases in homicides and aggravated assaults (see charts below). The costly and ineffective soft-on-crime policies of the ruling party are not working and are beginning to take a toll on our communities.







Data Source: CA Department of Justice, OpenJustice Portal

Property Crime. For the most part, property crime continued its decades-long decrease in the years following the Great Recession, although recent upticks in larceny and burglary and continuing increases in motor vehicle theft since the 2011 Public Safety Realignment are cause for concern.

Governor's Response. While the Governor vociferously claims to be making massive investments in public safety, he fails to propose any new funding in 2024-25 to combat violent crime, despite the continued increases discussed above. Furthermore, the vast majority of recent public safety spending increases are slated to expire. Of the $426 million in 2022-23 "public safety investments" touted by his most recent budget proposal, only $71 million would remain in the budget by 2025-26.

Department of Justice (DOJ)

The 2024-25 budget includes total funding of $1.3 billion ($487 million General Fund) for DOJ, an increase of $9 million above the 2023-24 enacted budget.

Additional Litigation Deposit Fund (LDF) Loan to General Fund. The LDF is a special fund established to receive proceeds from litigation conducted by DOJ. As of June 30, 2023, the balance in the LDF was more than a billion dollars. The Budget Act of 2023 authorized a $400 million loan from the LDF to the General Fund. The Governor proposes to loan another $100 million from the LDF to the General Fund to prop up General Fund spending for 2024-25. Since about half of the entire balance in the LDF would be loaned to the General Fund, it leaves one to wonder about the intended purpose of those funds and why are there no near-term plans to use them as intended.

Office of Emergency Services (OES)

The Governor's proposed 2024-25 budget includes $3 billion ($2.2 billion federal funds, $530 million General Fund) for OES, a decrease of approximately $112 million from the 2023-24 enacted budget.

OES Budget Solutions. To help address the General Fund deficit, the Governor proposes one-time solutions totaling $217 million General Fund within OES's budget – no ongoing solutions are provided. These include the following adjustments to 2023-24 spending:

- Transferring $76 million from the California Emergency Relief Fund (CERF) to the General Fund in 2023-24. The CERF was established in 2022 to provide emergency resources or relief relating to states of emergency proclaimed by the Governor. Revenues in the CERF were transferred there from the General Fund. The Governor proposes transferring some of the remaining balance back.
- Reverting $48 million General Fund in 2023-24 for flexible cash assistance to victims of crime and their families.
- Reverting $45 million General Fund in 2023-24 for community hardening grants.
- Reverting $27 million General Fund in 2023-24 for seismic retrofitting and home hardening grant programs.
- Reverting $21 million General Fund in 2023-24 for an ill-advised gun buy-back program that both Senate and Assembly Republicans argued against.

Board of State and Community Corrections (BSCC)

Cannabis Enforcement Funds Prop Up General Fund Spending. Holding true to the relatively low priority the Governor places on public safety, his 2024-25 budget proposes to loan $100 million from the Cannabis Tax Fund to the General Fund. Specifically, these funds would come from the portion of cannabis tax revenues that Proposition 64 (2016) directs to the BSCC for public safety activities (i.e., enforcement). Since the commercial cultivation and distribution of recreational cannabis was legalized in 2016, one of the most significant hurdles the industry has faced has been competition from the illegal market. The high tax and regulatory burden borne by licensees makes it virtually impossible for them to provide competitively-priced products, while the state's failure to adequately address unlawful production and distribution results in a thriving illicit market that undercuts licensees. Rather than using these cannabis tax revenues as intended to combat illegal cannabis, the Governor would instead use the funds to avoid making real reductions to General Fund programs.

Judicial Branch

The Governor's budget essentially maintains current operations for the Judicial Branch, proposing total funding of $5.1 billion ($3.2 billion General Fund) in 2024-25. This includes $4 billion to support the trial courts. Relative to the 2023 Budget Act, proposed 2024-25 Judicial Branch spending levels are about $80 million higher, with funding for the trial courts approximately $51 million higher.

Judicial Branch Revenue Backfills Continue. For more than a decade, revenues to various Judicial Branch special funds have been declining for a number of reasons, including an increasing inability of court users and defendants to pay fees and fines, plus new state policies that seek to reduce the financial impact of the criminal justice system on defendants and their families. The Governor's 2024-25 budget proposes to continue backfilling two of these special funds with General Fund to allow the courts to maintain current operations. These backfill amounts include $83 million for the Trial Court Trust Fund (down from $105 million in 2023-24) and $80 million for the State Court Facilities Construction Fund (up from $56 million in 2023-24).

Maintains Funding for Self-Help Centers. Every court in the state has a self-help center, the purpose of which is to assist unrepresented litigants in being prepared for court, thus relieving pressure on limited court resources and calendars. The current annual funding level for self-help centers is $30 million, of which $19 million is limited-term and set to expire in 2024-25. The Governor's budget proposes to continue the $19 million and make it a permanent part of the baseline budget for self-help centers.

Judicial Branch Budget Solutions. To help address the General Fund deficit, the Governor proposes one-time solutions totaling $100 million General Fund within the Judicial Branch's budget – no ongoing solutions are provided. These include the following adjustments:

- A $75 million transfer in 2024-25 from the Trial Court Trust Fund to the General Fund. High judicial officer vacancies have resulted in an unrestricted balance in the Trial Court Trust Fund with no mechanism for these funds to revert to the General Fund on the natural.

- A transfer in 2024-25 of $5 million from the Trial Court Trust Fund State-Level Emergency Reserve to the General Fund. This is an annual $10 million set-aside managed by the Judicial Council to help maintain individual trial court operations during times of emergency, revenue shortages, or budget imbalances. To rip off these funds during a state budget crisis defies the very nature of the reserve and calls into question its usefulness if the Administration can simply grab it to bail out the General Fund in the midst of the very scenario for which it was established.

- A reversion of $20 million from the $40 million provided in the Budget Act of 2022 for a three-year program to remove firearms from individuals prohibited from possessing them via civil actions, like certain types of restraining orders, at the time the prohibition is imposed. If the Governor plans to reduce front-end funding for enforcing firearms prohibitions, a balanced approach would suggest that he refuse to sign any legislation that is punitive toward law-abiding gun owners or that makes it more difficult to lawfully own a firearm.

- To enable individual trial courts to better plan and prepare for operational needs and emergency expenses, the Governor proposes trailer bill language to increase the cap on each trial court's reserves (the amount a court is allowed to carry forward into the next budget cycle) from three percent of annual expenditures to five percent. If enacted early enough, this change could allow courts to manage their current-year operations to provide additional flexibility in 2024-25, where the fiscal outlook is less certain.

Resources & Environmental Protection

Key Points

- **Overall Climate Spending.** The budget allocates $6.7 billion from the General Fund to climate-related programs, but also reduces $2.9 billion, delays $1.9 billion, and shifts $1.8 billion to other funds.
- **New Spending for Flood Protection.** The budget allocates $94 million from the General Fund for vital flood safety initiatives, a positive step toward addressing statewide water infrastructure needs.
- **Maintains Most Multiyear Wildfire Funding Commitments.** The 2023-24 budget sustains $2.7 billion of $2.8 billion in previous commitments, aiming to enhance fire prevention, mitigate the risk of catastrophic wildfires, and bolster fire protection and response resources.
- **Delays Unnecessary Methane Reduction Programs.** The budget incorporates $26 million from the General Fund for programs targeting agricultural methane emissions, which are currently unnecessary.
- **Proposal to Increase the Mill Assessment Returns.** The budget proposes transitioning from the current flat fee model for pesticide purchases to a phased-in increase over the next three years.

Overall Climate Budget

The budget proposal allocates $6.7 billion from the General Fund for existing commitments in climate-related programs. Changes to address the deficit include reducing spending by $2.9 billion, postponing expenditures of $1.9 billion to future years, and reallocating $1.8 billion to various funds, primarily the Greenhouse Gas Reduction Fund (GGRF).Specifically, these General Fund solutions incorporating the following adjustments:

Watershed Climate Resilience Programs:

- Reversion of $88.4 million General Fund and a reduction of $350 million over the next two years.
- Maintains $56 million previously allocated to these programs.

Water Recycling:

- Reversion of $174.4 million General Fund and a delay of $100 million until 2025-26.
- Maintains $348 million previously allocated to this program.

Per- and Polyfluoroalkyl Substances:

- Reversion of $71.6 million General Fund and a reduction of $30 million in 2024-25.
- Maintains $53 million previously allocated to this program.

Dam Safety:

- Reversion of $50 million General Fund for dam safety investments.
- Maintains $50 million previously allocated to this program.

State Water Efficiency and Enhancement Program:

- Shift of $20.6 million General Fund to the Greenhouse Gas Reduction Fund (GGRF).
- Funding for the program is delayed to 2024-25.

Relief for Small Farmers:

- Reversion of $12.9 million California Emergency Relief Fund for drought relief to small farms.

- Maintains $17 million previously allocated to this program.

Forecasted Informed Reservoir Operations/Snow Surveys:

- Reduction of $6.75 million General Fund ongoing for Forecast Informed Reservoir Operations.
- Maintains $10 million ongoing in baseline support for the program.

On-Farm Water Use and Agriculture Technical Assistance:

- Reversion of $6 million California Emergency Relief for on-farm water use and agriculture technical assistance.
- Maintains $9 million previously allocated to this program.

<u>Flood Risk Reduction and Water Supply</u>

In January 2023, the dangers stemming from the state's negligence of water infrastructure investment became evident during the onslaught of atmospheric rivers, saturating the drought-affected region. Despite ongoing severe weather events and a rising death toll, coupled with billions in damages to struggling communities, this budget falls short. While allocating $94 million from the General Fund for crucial flood safety endeavors, it recognizes the inadequacy in addressing the extensive billions required for statewide water infrastructure improvements. Nevertheless, it signifies a commendable start by strategically investing in projects like supporting the state cost share for Corps of Engineers and Urban Flood Risk Reduction initiatives, funding ongoing flood risk projects in the Central Valley, and earmarking funds for repairs related to 2023 storm damage at flood control facilities and State-owned Delta lands. The details of these spending proposals include:

- $33 million from the General Fund to bolster the state's cost share in ongoing U.S. Army Corps of Engineers and Urban Flood Risk Reduction projects, dedicated to flood risk reduction, along with covering associated state operations costs for project implementation.

- $31.3 million from the General Fund to sustain ongoing multi-benefit flood risk reduction projects in the Central Valley.

- $29.6 million from the General Fund allocated for addressing storm damage at State Plan of Flood Control facilities and state-owned Delta lands, specifically earmarked for critical repairs stemming from the impact of the 2023 storms.

<u>Wildfire and Forest Resilience</u>

The 2023-24 budget upholds $2.7 billion in commitments to advance fire prevention, mitigate the risk of catastrophic wildfires, and enhance fire protection and response resources. However, it trims $100.7 million from the General Fund, as specified below. While recent budget investments in wildfire prevention are a positive shift, this proposed budget offers a sensible approach to maximize effectiveness by focusing on fuel reduction efforts with immediate benefits. Though Democratic leaders acknowledge the need for billions annually over the next decade to clean up California's forests, they have not prioritized sufficient funding to effectively reduce the risk of catastrophic wildfires.

<u>Wildfire Reductions</u>—In response to the anticipated shortfall, the budget outlines General Fund strategies to attain fiscal balance. These encompass:

Expenditure Reductions—A reversion of $100.7 million General Fund from various programs with indirect benefits to fuel treatment or limited-term projects.

- $43.5 million: Biomass to Hydrogen/Biofuels pilot
- $27.7 million: Conservancy Project Implementation in High-Risk Regions
- $12 million: Home Hardening Pilot
- $5.7 million: Monitoring and Research
- $5.3 million: Prescribed Fire and Hand Crews
- $3.6 million: Forest Legacy
- $2.9 million: Interagency Forest Data Hub

Fund Shifts—A reallocation of $162.5 million General Fund to the Greenhouse Gas Reduction Fund (GGRF) across 2023-24 and 2024-25. This aims to sustain crucial investments in direct fuel treatment programs, fostering forest health, enhancing wildfire resilience, and curbing Greenhouse Gas emissions from catastrophic wildfires. Notable shifts include:

- $82 million within 2023-24: Fire Prevention Grants
- $34.5 million allocated to 2024-25: Stewardship of State-Owned Land
- $26 million earmarked for 2024-25: Department of Forestry and Fire Protection Unit Fire Prevention Projects
- $20 million shift to 2024-25: Regional Forest and Fire Capacity

Unnecessary Programs Get Delayed

The budget allocates $26 million from the General Fund towards addressing unnecessary programs focused on reducing agricultural methane emissions, at least for the present. This involves reallocating and postponing $24 million from the General Fund to the Greenhouse Gas Reduction Fund (GGRF) for the Livestock Methane Reduction Program and reverting $23 million from the General Fund for the Enteric Methane Incentives Program. While both programs aim to assist farmers in adopting more sustainable agricultural practices, their merits and necessity came under question during their presentation to the Legislature in last year's budget.
Other notable changes include:

Urban Waterfront Funding
- Reversion of $12.3 million General Fund for various projects in urban areas adjacent to rivers and waterways throughout the state.
- Maintains $142 million General Fund previously allocated for this program.

Pesticide Notification
- Reversion of $2.6 million General Fund related to the Pesticide Notification Network previously appropriated in the 2021 Budget Act.
- Maintains $7.3 million previously allocated for this purpose.

Proposal to Increase Fees Returns

Amid a fiscal deficit, the budget revisits a proposal to revamp the flat fee model for pesticide purchases, opting for a phased-in increase over the next three years. Notably, these revisions require a two-thirds vote by the legislature.

In 2021, the Budget Act initiated an independent mill assessment study engaging stakeholders to evaluate the Department of Pesticide Regulation's (DPR's) long-term resource needs. The study recommended a phased-in increase of the mill assessment for stable, long-term funding. The budget embraces this suggestion, allocating $33.3 million ongoing from the DPR Fund and Greenhouse Gas Reduction Fund (GGRF) phased in over three years.

The DPR Fund, mainly supported by the mill assessment, faces a structural imbalance. The budget suggests a mill assessment increase over three years: 5 mills in FY24/25 (26 mills total), 1.5 mills in FY25/26 (27.5 mills total), and 1.1 mills in FY26/27 (28.6 mills total). DPR may consider future increases up to 33.9 mills. CDFA's mill assessment for agricultural use products is currently 0.75 mills. Due to increased workload since 2018, CDFA proposes raising its mill assessment limit to 1.04 mills for essential pesticide regulation analyses, contingent on spending existing reserves before any increase.

The budget also proposes using the revenues collected from the increased mill assessment to implement the below changes to promote the following goals:

Streamline Processes and Support Alternatives:
- Increase of $17.9 million ongoing in the DPR Fund.
- Accelerate pesticide evaluation and registration timelines.
- Support innovative alternatives research and adoption.
- Develop and implement a public, stakeholder-engaged, and scientifically based priority pesticide process.
- Provide general administrative support.

Strengthen Statewide Services:
- Increase of $8.6 million ongoing in the DPR Fund and $592,000 ongoing in GGRF.
- Support statewide and cross-jurisdictional enforcement and compliance.
- Facilitate pesticide monitoring, data evaluation, and risk mitigation.
- Contribute to regulation development.

Provide Critical Support for Local Partners and Communities:
- Increase of $6.1 million ongoing in the DPR Fund and $125,000 ongoing in GGRF.
- Offer training and compliance support for County Agricultural Commissioners.
- Facilitate local engagement and transparency efforts.

Energy and Utilities

Key Points

- **Strategic Energy Reliability Reserve.** Proposes to retain funds promised in prior multi-year packages, but delays $55 million by one year, leaving $20 million for 2024-25.
- **Clean Energy Incentive Programs Modestly Reduced, Delayed.** Proposes to reduce programs by $419 million and delay $505 million to future years.
- **Clean Energy Reliability Investment Plan (CERIP).** Proposes to delay $800 million for CERIP from 2024-25 and 2025-26 to instead be allocated in future years.
- **Broadband Investments.** Proposes an additional $1.5 billion General Fund over two years to complete the development of the statewide middle-mile network. Also proposes a reduction of $250 million General Fund for the financing of local broadband projects, and a delay of $100 million for last-mile projects.

Strategic Energy Reliability Reserve. The 2022-23 budget included $2.37 billion General Fund over a five-year period for a Strategic Reliability Reserve (Reserve). The proposed budget retains all the planned funding, but delays $55 million by one year, leaving $20 million in 2024-25. The bulk of the initial funding was allocated in prior budgets.

Under the Reserve, the Department of Water Resources will utilize power plants previously scheduled for retirement to generate electricity during extreme events, purchase additional temporary natural gas generators, and enter new power purchase agreements, in an effort to avoid rolling blackouts during California's hasty energy transition. The Reserve is only funded through 2025-26 but new renewable resources have been delayed and California's electricity transmission grid is in need of major investments. There is also uncertainty surrounding the offshore wind industry. These issues suggest that Reserve resources may be needed beyond 2025-26.

The Reserve also includes incentivizing the installation of air emission reduction technologies on fossil-fueled backup power generators, deployment of new zero- or low-emission backup generation, upgrades at existing generation facilities that yield additional generation capacity, and load reduction during extreme events.

While these measures increase reliability during the transition to clean energy, it is unknown if they are sufficient. Rolling blackouts were only narrowly avoided in summer of 2022, and the state's policies continue to place more demand on the grid. It would be prudent to slow down and let supply catch up with demand, or it will literally be lights out for parts of California again.

Clean Energy Incentive Programs Modestly Reduced, Delayed. The Governor proposes $216 million in 2024-25 to incentivize various types of clean energy projects. The 2021 and 2022 budgets included multi-year packages for these programs and projects, which were adjusted in last year's budget. As of the 2023-24 budget, these packages totaled $7 billion. Overall, this proposed budget decreases the packages by $419 million and delays $505 million to future years.
Various programs are proposed for modest cuts or delayed funding, as follows:

- ***Industrial Grid Support and Decarbonization Program ($22 million reduction):*** Incentivizes projects that enable participation in utility load reduction programs, electrify existing fossil fuel processes, incorporate energy storage or renewable resources, increase energy efficiency, or develop and deploy new decarbonization technologies. Specifically prohibits geologic storage of captured carbon.

- ***Food Production Investment Program ($19 million reduction):*** Incentivizes projects that enable participation in utility load reduction programs, electrify existing fossil fuel processes, incorporate solar, energy storage, or other renewable resources, increase energy efficiency, or develop and deploy new decarbonization technologies at food production and processing facilities. Specifically prohibits carbon capture projects. *This program was reduced by $10 million last year.*
- ***Equitable Building Decarbonization Program-Rebates ($283 million reduction over two years):*** Incentivizes installation of low-carbon building technologies, such as heat pumps, space and water heaters, and other efficient electric technologies. This program also includes funds for accelerating the adoption of lower polluting refrigerants in grocery and convenience stores.
- ***Carbon Removal Innovation Program ($40 million reduction):*** Incentivizes research, development, and deployment of direct air carbon capture technologies. Specifically excludes projects that would benefit petroleum or gas production, processing, or refining, through enhanced oil or gas recovery.
- ***Hydrogen Grants ($35 million reduction):*** Incentivizes in-state projects for the demonstration or scale-up of the production, processing, delivery, storage, or end use of clean hydrogen. These projects aim to reduce sector-wide emissions.
- ***Capacity Building ($20 million reduction):*** Grants to California Native American Tribes and community-based organizations for participation in California Public Utility Commission (CPUC) decision-making processes and supporting activities.

Clean Energy Reliability Investment Plan (CERIP). Separate from the investments detailed above, the proposed budget delays $400 million for CERIP from each year in 2024-25 and 2025-26, and instead plans to spend the funds in future years. SB 846 (Ch. 239, Stats. 2022, Dodd) provided that upon appropriation by the Legislature, a total of $1 billion would be available over a three-year period for the CERIP, to accelerate the deployment of clean energy resources, support demand response, assist ratepayers, and increase energy reliability. Notably, the proposed delays would spread the funds over five years rather than three. At this time, it is unknown how the proposed delays will affect existing projects and programs or the state's overall climate goals.

Summary of Energy Investments. As described above, the proposed budget includes various reductions and delays in energy programs. These are as summarized in the table on the next page.

<u>Broadband</u>

Middle Mile. The Governor's January budget includes $1.5 billion General Fund over two years ($250 million in 2024-25 and $1.25 billion in 2025-26) for the Department of Technology to complete the development of the statewide middle-mile network. The Administration indicates additional funds would be needed to complete the project in subsequent years, but fails to include any further data or justification for that assumption.

Last Mile. The Governor proposes a cut of $250 million to the Loan Loss Reserve Fund, used to finance local broadband infrastructure development. Additionally, the Governor proposes to defer $100 million for last-mile broadband infrastructure grants from 2024-25 to 2026-27.

Specifically, for the Loan Loss Reserve Fund, $150 million is reduced from 2024-25 and $100 million is reduced from 2025-26. The proposal retains $150 million in 2024-25 and $175 million in 2025-26. These cuts result in less funds available for local governments, tribes, and non-profits to finance last-mile public broadband networks.

Energy Package Reductions and Delays ($ in millions)					
Department	**Program**	**Package Amounts at 2023-24 Budget Act**	**General Fund Reductions**	**Delayed Funding**	**New Proposed Energy Totals**
Energy Commission	Incentives for Long Duration Storage	$330			$330
	Hydrogen Grants	$100	$35		$65
	Industrial Grid Support and Decarbonization	$90	$22		$68
	Food Production Investment Program	$65	$19		$46
	Equitable Building Decarbonization	$922	$283		$639
	Offshore Wind Infrastructure	$45			$45
	DOE Grid Resilience Match	$5			$5
	Energy Modelling Support	$7			$7
	Distributed Electricity Backup Assets	$595			$595
	Demand Side Grid Support	$295			$295
	Carbon Removal Innovation	$75	$40		$35
	Energy Data Infrastructure & Analysis	$5			$5
California Air Resources Board	Ultra Low Global Warming Potential Refrigerants	$40			$40
Department of Water Resources	Oroville Pump Storage	$240		$200	$240
	Support Resources for Reliability	$3			$3
	Distributed Electricity Backup Assets	$100		$50	$100
	Investments in Strategic Reliability Assets	$2,370		$55	$2,370
California Public Utilities Commission	Residential Solar + Storage	$630		$200	$630
	Capacity Building	$30	$20		$10
	Distributed Energy Workload	$5			$5
	Equitable Building Decarbonization	$145			$145
IBank/GO Biz	Transmission Financing	$225			$225
	Hydrogen Hub	$5			$5
Department of Community Services & Development	California Arrearage Payment Program	$651			$651
Various	AB 525 Implementation	$4			$4
	Clean Energy Reliability Investment Plan	$1,000		$400	$1,000
Total		**$7,982**	**$419**	**$905**	**$7,563**

(Source: Compiled with information from the Department of Finance)

Transportation

Key Points

- **Gasoline Taxes Increase Again.** The automatic annual gas tax increase will raise the price of gas by 2 cents per gallon as of July 1, 2024.
- **Transit Bail Out.** Proposes a one-year delay for half of the $2 billion in transit bailout funding planned for 2024-25. The proposal also shifts $261 million of the remaining bailout funds from the General Fund to the Greenhouse Gas Reduction Fund (GGRF).
- **Zero-Emission Vehicle Subsidies and Infrastructure.** Proposes $807 million for zero-emission vehicle (ZEV) subsidies, infrastructure, and equity projects. Delays $600 million previously planned to future years and shifts $475 million from the General Fund to the GGRF.
- **High-Speed Rail Office of the Inspector General**. Proposes $3 million for the High-Speed Rail Office of the Inspector General.
- **High-Speed Rail.** In addition to spending previously appropriated bond funds, the proposed budget includes $928 million in 2024-25 from Cap and Trade funds.

Gasoline and Diesel Taxes Rise Again. Pursuant to SB 1, the 2017 gas and car tax bill, gas, and diesel taxes are adjusted for inflation each year on July 1. This July 1, the tax on gasoline is estimated to increase by 2 cents per gallon, and the diesel excise tax to increase by 1.3 cents per gallon. These increases will generate about $301 million in tax revenues, bringing total gas and diesel tax revenue to an estimated $9.3 billion for 2024-25.

Transit Bail Out Partly Delayed. The Governor proposes to delay $1 billion in promised funding for struggling transit operators by one year and shift $261 million of that delayed funding from the General Fund to the GGRF, which receives funds from cap-and-trade auctions. The 2023-24 budget included $2 billion General Fund to bail out public transit, with an additional $2 billion planned for 2024-25. Delaying a portion of the funding by one year would only kick the can down the road, even though the budget forecasts deficits through at least 2027-28. Additionally, continuing to bail out these entities makes little sense, due to a lack of demand for service and outdated business models.

However, if California insists on continuing to bailout transit, additional state oversight is necessary. A budget trailer bill enacted last year (Chapter 54, Statutes of 2023 (SB 125)) makes the bailout funds contingent upon compliance with new accountability measures. The California State Transit Agency is reviewing submitted reports and will allocate initial funds by April 30, 2024. Senate Republicans will continue to remain engaged in oversight of this money.

Zero-Emission Vehicle Subsidies and Infrastructure. The proposed budget includes $807 million ($500 million General Fund, $230 million GGRF, and $77 million federal funds) for zero-emission vehicle (ZEV) subsidy, infrastructure, and equity projects. In prior budgets, the Governor committed $10 billion over five years to transition Californians to ZEVs, aligning with state regulations to ban the sale of gasoline cars by 2035. This proposal maintains that commitment by providing $10 billion over seven years. This continues to be a hefty price tag for California taxpayers, with little return on investment. Despite billions in subsidies, the share of passenger ZEVs registered in California remains under 4 percent, based on the most recent data available on the state's dashboard. Proposed changes to multi-year program allocations are displayed in the table on the next page.

Zero-Emission Vehicle Investments (Dollars in Millions)							
Investment Category	**Program**	**Agency**	**Package Amounts at 2023-24 Budget Act**	**General Fund Reductions**	**Delayed Funding**	**New Proposed ZEV Totals**
Passenger Vehicles	Clean Vehicle Rebate Project	CARB	$525	$0	$0	$525
	Clean Cars 4 All & Other Equity Projects	CARB	$656	$0	$45	$656
	ZEV Fueling Infrastructure Grants	CEC	$870	$0	$120	$870
	Equitable At-home Charging	CEC	$300	$0	$80	$300
Big ZEVs	Drayage Trucks & Infrastructure	CARB	$445	$0	$48	$445
		CEC	$500	$0	$50	$500
	Drayage Trucks & Infrastructure Pilot Project	CARB	$40	$14	$0	$26
		CEC	$25	$9	$0	$16
	Transit Buses & Infrastructure	CARB	$140	$0	$0	$140
		CEC	$60	$0	$0	$60
		CalSTA	$910	$0	$0	$910
	School Buses & Infrastructure	CARB	$1,390	$0	$0	$1,390
		CEC	$410	$0	$0	$410
	Clean Trucks, Buses and Off-Road Equipment	CARB	$1,100	$0	$0	$1,100
		CEC	$670	$0	$137	$670
	Ports	CARB	$185	$0	$0	$185
		CEC	$130	$0	$0	$130
	Near-Zero Heavy Duty Trucks	CARB	$45	$0	$0	$45
Other	ZEV Consumer Awareness	GO-BIZ	$5	$0	$0	$5
	ZEV Manufacturing Grants	CEC	$250	$7	$0	$243
	Community-Based Plans, Projects and Support / Sustainable Community Strategies	CARB/CalSTA	$339	$0	$100	$339
	Emerging Opportunities	CARB	$100	$0	$0	$100
		CEC	$100	$7	$0	$93
	Hydrogen Infrastructure	CEC	$0	$0	$0	$0
	Charter Boats Compliance	CARB	$100	$0	$20	$100
	Transportation Package ZEV	CalSTA	$790	$0	$0	$790
		Totals	**$10,085**	**$38**	**$600**	**$10,047**

(Source: Compiled with data from the Department of Finance)

California High-Speed Rail

High-Speed Rail Office of the Inspector General. The budget proposes $3 million (Public Transportation Account) and 11 positions for the operation of the High-Speed Rail Office of the Inspector General (OIG) to oversee the high-speed rail project. The HSR OIG, established by SB 198 (Committee on Budget and Fiscal Review, 2022), has broad authority to initiate audits and reviews, conduct independent fiscal analysis, identify best practices, recommend efficiencies, and evaluates contracts. The OIG is still in its infancy and has yet to conduct any audits. It is unknown if the proposed resources are sufficient to provide any meaningful oversight. Time will tell if this is another fig leaf maneuver by the Governor and Legislative Democrats to give the appearance that something is being done to rein in the out-of-control train to nowhere.

High-Speed Rail Authority. The 2022-23 budget included $4.2 billion in remaining Proposition 1A (2008) bond funds for the High-Speed Rail Authority to continue the construction of the Merced to Bakersfield high-speed rail line. While previously appropriated, these funds will be spent over several years. For context, $1.2 billion in Prop 1A funds were spent in 2022-23, and updated projects reflect over $1 billion being spent in the current year. In addition to previously appropriated bond funds, the budget proposes $928 million in Cap and Trade revenues for the project in 2024-25.

The 2023 Project Update Report indicated the total costs of completing HSR is up to $128 billion, with no estimated completion date, though much of the data remains based on operations from San Francisco to Los Angeles beginning in 2033. In December 2023, the federal government announced an award of $3.1 billion to the High-Speed Rail Authority. Despite these additional funds, California remains more than $100 billion short of the total needed to build a San Francisco-to-Los Angeles train. Despite this outlook and years of criticism, Democrats have yet to offer any plausible plan for how to obtain funds to complete the project. Instead, they continue to throw good money after bad in their HSR fantasyland and call on California taxpayers to foot the bill.

The federal government also awarded $3 billion to the Brightline West high-speed rail line from Los Angeles to Las Vegas. That effort is largely funded by private investors who are willing to put up their own money, indicating a much stronger underlying business case. In contrast, the state's project has received no private investment.

General and Local Government

Key Points

- **Governor's Office of Policy and Research (OPR).** In the Governor's tenure, OPR has gone from a $54 million research unit to a $1.1 billion state bureaucracy.
- **Reduces Drought Relief For Small Farmers.** Reduces available grant funds intended to provide relief to small farmers by nearly half.
- **Continues Cal Competes Grant Program.** Includes $60 million for the California Competes grant program in 2024-25.
- **Delays Funding for the City of Fresno Infrastructure Plan.** Provides $50 million in 2024-25 and shifts $100 million to both 2025-26 and 2026-27 for the project.
- **Reverts Member Request Funding.** Reverts any funds approved in the 2023-24 budget for member request projects that have not yet been sent to local agencies.
- **Excludes Funds for Signed Legislation.** Excludes funds needed for legislation enacted in 2023 until the May Revision, potentially allowing for delays in those programs.

Office of Planning and Research (OPR) Department Reorganization. The Governor's January budget includes some acknowledgement of the shocking growth within OPR, which was once just a small group of researchers intended to support the Governor's Office. Prior to the beginning of Governor Newsom's tenure in 2018, OPR's budget was $54 million General Fund, with less than 40 employees. Fast forward to the proposed 2024-25 budget, and OPR is now a full-on bureaucracy, with a proposed budget of $1.1 billion and 330 positions, all in just six years.

The Governor intends to review OPR programs for possible reassignment to other departments, which acknowledges Senate Republicans' concerns in recent years that OPR was tasked with new programs outside of its expertise. Unfortunately, the Governor does not propose to reduce OPR, but instead proposes to reassign some of the programs, which could help disguise the past and likely future growth of a redundant and unnecessary state department.

While the budget does not include details on a reorganization plan, the budget does include the following budget adjustments within OPR programs:

- **California Environmental Quality Act (CEQA) Judicial Streamlining.** The January budget would provide $2.3 million ongoing General Fund for OPR's role in implementing recently adopted judicial streamlining provisions for infrastructure and environmental development projects.

- **Office of Community Partnerships and Strategic Communications (OCPSC).** The proposed budget would revert $5 million from the 2023-24 budget, and would reduce base spending by $8 million in 2024-25 and 2025-26 for community engagement and awareness campaigns associated with public education efforts such as COVID-19 vaccination, water conservation, and extreme heat. The program would retain $60 million in 2023-24 and $57 million in 2024-25 and 2025-26, respectively. Given the budget constraint facing the state, prioritizing General Fund resources for outreach campaigns should be reconsidered.

- **California Experience Corps**. The Governor's proposed budget reverts $8.8 million from the California Experience Corps (CEC) program, which provides grant funding to volunteer programs that engage older adults in volunteer service. The CEC was established in the 2021 Budget Act and provided $10 million General Fund. The reversion of nearly all of the program funding validates Senate Republican concerns that the program did not address mission-critical needs within communities as nearly all of the funding will be reverted three years later.

Taking Back Relief for Small Farmers*.* The Governor's budget proposes to revert $13 million California Emergency Relief Fund within the Governor's Office of Business and Economic Development (GO-Biz) for drought relief to small farms, maintaining $17 million previously provided in 2022-23.

CalCompetes Grant Program. The Governor's budget continues the CalCompetes grant program in 2024-25, providing $50 million General Fund, as well as shifting $10 million from the 2023-24 budget to 2024-25. The CalCompetes program provides financial subsidies to business that agree to stay in, or relocate to, California in exchange for investment and job creation commitments. In addition to $180 million in annual tax credit allocations to CalCompetes provided through 2027-28, the 2022 and 2023 Budget Acts each provided $120 million in one-time General Fund for the grant program, with recent priority given to the semiconductor industry.

City of Fresno Infrastructure Plan. The 2023 Budget Act allocated $250 million in General Fund to support infrastructure development projects in downtown Fresno. The Governor's budget maintains the General Fund prioritization, but would shift $100 million into 2025-26 and $100 million into 2026-27. The rationale for providing special treatment to Fresno with these funds has never been clear.

Infrastructure State Revolving Fund. The Infrastructure State Revolving Fund at the California Infrastructure and Economic Development Bank (IBank) helps local governments to finance clean energy, water, and other environmental infrastructure projects. The Governor's budget provides $50 million in one-time General Fund to recapitalize the Fund.

Capitol Annex Project. The January budget proposes an additional $50 million budgetary loan from the State Project Infrastructure Fund (SPIF) to the General Fund, bringing the total loan amount to $550 million between the 2023 Budget Act and the Governor's proposed 2024-25 budget. The 2022 Budget Act provided a $917 million transfer from the General Fund to the SPIF to fund the remaining design, pre-construction, and construction activities for the State Capitol Annex project. The Administration indicates the loan would be repaid as needed in 2025-26 and 2026-27.

Reverts Member Request Funding. The 2023-24 budget approved over $700 million General Fund for a long list of member-requested local projects. The Governor's budget assumes savings of $350 million by reverting funds for projects that have not yet been sent out to local agencies. The Administration has not provided a list of which specific projects are included in the reversion estimate.

Excludes Funds for Signed Legislation. The Governor signed a long list of bills in 2023 that require funds to implement, despite vetoing some on budgetary grounds. The January budget excludes any funds needed to implement that legislation until the May Revision, potentially allowing for reductions or delays in those programs. The Administration has not provided a specific estimate for these savings. The most notable of these bills is the SB 525 health facility minimum wage law, which the *Health* section describes in further detail.

State Employee Compensation and Retirement

Key Points

- **Contributions for State Retirement.** Proposes $6.9 billion in state contributions for state pension costs, a decrease of $1.6 billion compared to last year, but an overall increase of $2.3 billion compared to a decade ago.
- **Upcoming Pay Increases for State Employee Unions Still Unknown.** Includes a set-aside for employee compensation for two bargaining units. Includes a confidential amount as a placeholder for unknown pay increases subject to negotiations between the state and employee bargaining units.
- **Proposition 2 Debt Repayment.** Proposes $885 million in one-time Proposition 2 debt repayment funding for 2023-24 to reducing the unfunded pension liabilities, the minimum required under law.
- **Payroll Deferral Gimmick.** Proposes to defer roughly $3.2 billion in state employee payroll costs from June 30, 2025 to the next day as a gimmick to address the deficit.

State Employee Growth Outpaces Population Dramatically. Over the past decade, the state population has grown by only 1 percent, to about 39 million people, and has been flat over the past seven years. Over the same period, the number of state employees has grown nearly 18 percent, to a projected 426,290 in 2024-25, including a jump of 12 percent, or about 44,000 employees, since the pandemic started. The number of state employees per 1,000 residents will be nearly 11 in 2024-25, the highest level for at least 50 years. This is particularly notable considering that the state “realigned” significant prison and human services responsibilities to counties roughly a decade ago, which should have decreased the number of state employees per resident.

Employee Compensation and Collective Bargaining Costs. The budget includes $1.3 billion ($676 million General Fund) for previously agreed-upon collective bargained pay increases, other increased employee compensation, health care costs for active state employees, and retiree health care prefunding contributions for active employees.

The state will negotiate this year with two bargaining units representing Highway Patrol Officers and Firefighters, whose contracts expire in summer 2024. The budget includes an unknown set-aside amount for employee compensation for the two bargaining units. The Administration argues that the amount should be kept confidential because it is subject to bargaining.

Proposed Telework Stipend Savings. The budget proposes to negotiate with each bargaining unit for the elimination of the telework stipend, which was first offered to state employees in 2021-22. The budget assumes savings of an estimated $51 million ($26 million General Fund) from this change, but since it is unclear what bargaining units might ask in return, these savings may not materialize.

Unknown Vacant Position Savings. The budget states that $763 million in savings would be achieved through vacant positions in 2024-25, but that funding for those positions would be restored in future budget years. Given the growth in state staff, as described above, and future deficits, it would be justifiable to permanently delete vacant positions.

Payroll Deferral Gimmick Proposed. In an attempt to address the projected budget deficit, the budget proposes to defer state employees’ payroll costs from June 30, 2025 to July 1, 2025. This estimated $3.2 billion ($1.6 billion General Fund) deferral would shift payroll costs from 2024-25 to 2025-26. However, this change would only be reflected in accounting and would not affect the timing of payments issued to state employees. This one-time gimmick appears to help solve the deficit on paper, but does nothing to truly bring spending in line with revenues.

CalPERS Pension Costs Continue to Grow. The budget authorizes $6.9 billion in total funds ($3.5 billion General Fund) in employer contributions to Public Employee Retirement System (PERS) for state employees' retirement costs, and $615 million General Fund for California State University employees. This is up $2.3 billion compared to ten years ago, an increase of 50 percent.

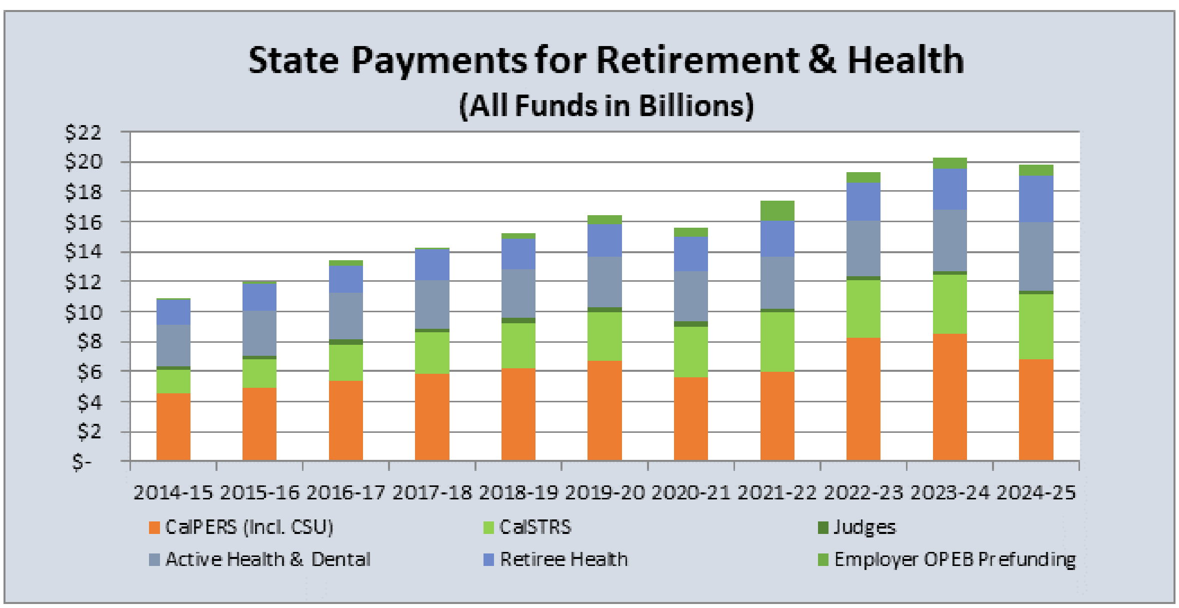
As part of the Governor's deficit solution package, $1.3 billion of the mandatory Proposition 2 repayment funding would be used to make currently required state pension contributions, thus reducing the non-Proposition 2 General Fund portion. This shift makes pension costs appear to be lower than the previous year, as illustrated by the orange bar in the chart on the next page.

Teacher Pension Costs Also Grow. The budget includes $4.2 billion General Fund for state contributions to CalSTRS, the teachers' pension fund. This is roughly a $300 million increase from 2023-24.

Retiree Health Care Benefits. The budget includes approximately $3.2 billion ongoing for health care benefits for state retirees, California State University retirees, and dependents. Retiree health care benefits continue to be paid out mainly on a "pay-as-you-go" approach, which has created a $96 billion unfunded liability. It also includes $375 million in one-time Proposition 2 debt repayment funding in 2024-25 for the employer's share of contributions to pay for future retiree health benefits.

Total State Cost for Retirement and Benefits. To highlight the costs over time of various benefit actions, the graph below illustrates combined budgetary costs for employer contributions to PERS and STRS, along with costs for retiree health, active health, and other retirement prefunding over the past decade.

As shown in the graph on the next page, state pension, retiree health, and other benefit costs combined will drop just below $20 billion in 2024-25, still more than doubling over the past decade. During that same period the state's overall budget grew by slightly more than double as well, following the dramatic increase in General Fund spending in the past three years.



Statewide Debts and Liabilities

Key Points

- **Special Fund Borrowing Increases to Close Budget Gap.** Budget adds $1.4 billion in borrowing from special funds to pay for budget year spending.
- **Partially Shifts Payment on Unemployment Insurance (UI) Debt.** Proposes $331 million in one-time funding ($231 million General Fund) to meet the annual interest payment on the state's UI debt, but takes $100 million from a special fund

Expanding Special Fund Borrowing. Now facing another year of a budget deficit, the Governor's budget proposes more borrowing to close the budget gap. The budget proposes $1.4 billion in loans from special funds to the General Fund. This is in addition to $2.7 billion that the state borrowed in the 2023-24 budget. It is not clear what effect the loans would have on programs supported by those special funds.

Unemployment Insurance (UI) Debt. As described more fully in the *Labor and Workforce Development* section of this report, the budget proposes $331 million in one-time funding ($231 million General Fund) to meet the annual interest payment on the state's UI debt. Of this amount, $100 million would be funded by the Employment Training Fund. The default course of action under federal law is for this debt to be repaid by a surcharge on employers beginning in 2023. The state General Fund is responsible for the interest on the UI debt, but various other states used federal stimulus funds to pay off their debts. California is one of only two states that did not pay off its pandemic UI debt balance, and California's $20 billion current balance is far higher than the other state, New York, at $7 billion.

Bond and Proposition 2 Debt Payments. The Budget Act includes nearly $10 billion to pay down the state's current debts and liabilities. Debt payments include the following components:

- ***Normal Bond Debt Service.*** $6.5 billion to pay debt service costs for the state's outstanding and planned general obligation and lease-revenue bonds in 2023-24, as required by the constitution and debt covenants. Included as part of the GO bond debt payment is $2.3 billion that is required to be spent on infrastructure in 2023-24, part of the state' Proposition 2 requirement. According to the State Treasurer, the state currently has outstanding general obligation bonds totaling $70.6 billion and has authorization to issue nearly $24 billion more. Additionally, outstanding lease-revenue bonds total $6.5 billion.
- ***Required Proposition 2 Debt Repayments***. The budget would make the constitutionally-required Proposition 2 debt payment of $2.1 billion toward unfunded pension and health liabilities. Specifically, the budget allocates $885 million for CalPERS pension debt, $375 million for retiree health debt, and $836 million to pay a state pension loan previously authorized by SB 84 in 2017. Additionally, due to prior Proposition 2 repayment funding paid to CalPERS, combined pension contributions are lower than the previous year.

Total State Debt Estimate Declines to $243 Billion. The state continues to face voluminous debts from various sources, which are estimated to reach $243 billion, as shown in the table below. However, due to strong investment performance by pension funds in 2020 and 2021,

State and Other Public Debts and Liabilities			
(Dollars in Millions)	At Start of 2023-24	At Start of 2024-25	Difference
Special Fund Loans	$2,736	$1,422	-$1,314
State Retirement Liabilities			
State Retiree Health	$95,510	$82,413	-$13,097
State Employee Pensions	$70,818	$70,818	$0
Teachers' Pensions (state portion)	$10,256	$10,265	$9
Judges' Pensions	$2,771	$ 2,771	$0
SB 84 Loan from Surplus Money Invst. Fd.	$2,780	$2,857	$77
Deferred payments to CalPERS	-	-	$0
Subtotal	$182,135	$169,124	-$13,011
Other State Debts			
Long-Term Bonds - General Obligation & Lease-Revenue	$79,159	$70,600	-$8,559
Suspended Local Mandates	$ 486	$ 549	$63
Education Mandates	$ 1,100	$ 876	-$224
Subtotal	$ 80,745	$ 72,025	$ (8,496)
State - Total Debt	**$ 265,616**	**$ 242,571**	**-$22,821**
Other Related Public Debts			
Unemployment Insurance*	$18,002	$ 19,935	$ 1,933
Teachers' Pensions (Local Districts)	$75,547	$ 75,538	$ (9)
University of California Liabilities**			$ -
UC Employee Pensions	$ 21,800	$ 21,700	$ (100)
UC Retiree Health	$ 19,600	$ 19,600	$ -
UC Total	$ 41,400	$ 41,300	$ (100)
Total, State and Other Public	**$400,565**	**$379,344**	**-$21,221**

* The state pays the interest on the Unemployment Insurance debt, while employers pay the principal through higher payroll taxes. However, the state could chooose to pay down the debt

** UC liabilities technically belong to the UC system alone, not the State of California, due to UC's constitutional autonomy, but these liabilities are nonetheless included as eligible for repayment

revised actuarial estimates show declines in state worker and teacher pension liabilities compared to this time last year. These declines account for an overall reduction of $23 billion (10 percent) in estimated state liabilities from $266 billion last year to $243 billion. Note that some balances have not been updated for new actuarial estimates. These totals also do not count pension and other retiree debts faced by the University of California ($41 billion), teacher pension debts held by local school districts ($76 billion), or the Unemployment Insurance debt of nearly $20 billion, which is technically owed by employers.

Fund Shifts. As described earlier in this report, the budget proposes $3.4 billion in fund shifts from the General Fund as a deficit solution. Of that $3.4 billion, $1.3 billion reduces the state's retirement contributions using the mandatory Proposition 2 debt repayment, as described in the *Employee Compensation* section. This action may technically be allowed under the law, though it would violate the spirit of the Proposition 2 debt payment requirements. The budget also shifts $100 million in Unemployment Insurance Payments to the Employee Training Fund, as described in the *Labor and Workforce Development* section.

Senate Republican Fiscal Staff Assignments

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K-12 Education and Social Services	Megan De Sousa
Public Safety, Judiciary, Corrections	Matt Osterli
Natural Resources & Environment	Emilye Reeb
Health & Veterans Affairs	Anthony Archie
Revenue, General Government & Housing	Chantele Denny
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