



Date: February 7, 2017
To: State Legislative Committee
From: Patrick H. West, City Manager *T.M.*
Subject: Governor's January Budget for FY 18

Introduction

The Governor introduced his FY 18 budget on January 10, 2017. For the first time in four years, the Governor is projecting a deficit; in FY 18, the Governor is predicting a \$1.5 billion revenue shortfall. The Governor's January Budget proposal includes expenditure reductions to cover the anticipated shortfall, while protecting funding for education, the State's Earned Income Tax Credit, cost increases associated with the State's minimum wage increase to \$15 per hour, and healthcare expansion. This fact sheet provides additional details on the Governor's January Budget.

Summary

The Governor's proposed FY 18 budget assumes \$124 billion in General Fund revenues, and expenditures totaling \$122.5 billion. Compared to the FY 17 budget that was adopted in June 2016, the two main factors causing the State's project deficit in FY 18 are: (1) a revenue forecast that is \$5.8 billion lower than expected, and (2) a current-year shortfall in the Medi-Cal program. These projections already take into account tax increases that were approved by voters in the November 2016 election. While revenues have been trending downward, the Governor's Budget does leave room for revenue recovery in the coming months. If the downward trend reverses, then the May Revision will reflect the change, and proposed cuts can be avoided.

To close the budget deficit and rebuild the state's operating reserve, the Governor's Budget proposes \$3.2 billion in budget solutions. Rather than cut existing program levels, the cuts temper spending growth.

- Adjust Proposition 98 to schools (\$1.7 billion)
- Recapture 2016 Allocations (\$0.9 billion)—The 2016-17 Budget contained a large package of one-time spending. Much of that spending remains uncommitted at this point in time, and the Budget proposes to eliminate the authority to spend the dollars. The two largest components of this proposal are eliminating the \$400 million set-aside for affordable housing that was never allocated and a \$300 million transfer to modernize state office buildings planned for 2017-18.
- Constrain Spending Growth (\$0.6 billion)—The Budget limits spending proposals to keep spending flat. This involves pausing rate increases for child care, not providing Middle Class Scholarships to any new students,

and not submitting a variety of spending proposals (including those to implement new legislation) from state departments that otherwise were justified.

The Governor's January Budget also assumes the continuation of existing federal fiscal policy. The incoming presidential administration and leaders in Congress have suggested major changes to Medicaid, trade and immigration policy, and the federal tax structure. Many of the proposed federal changes could have significant impacts on the State's economy and budget. However, at this point, it is not clear what those changes will be or when they will take effect.

State Budget Items

Statewide Transportation Infrastructure Funding

The Governor's FY 18 January Budget re-introduces a transportation package, which the Governor first proposed in September 2015. This Statewide revenue package would provide \$4.2 billion annually to improve the maintenance of highways and local roads, expand public transit and strengthen trade corridors. The 10-year funding plan identifies new funding and redirected from:

- Road Improvement Charge—\$2.1 billion from a new \$65 fee on all vehicles, including hybrids and electrics.
- Stabilize Gasoline Excise Tax—\$1.1 billion by setting the gasoline excise tax at the 2013-14 rate of 21.5 cents and eliminating the current annual adjustments. The broader gasoline tax would then be adjusted annually for inflation to maintain purchasing power.
- Diesel Excise Tax—\$425 million from an 11-cent increase in the diesel excise tax. This tax would also be adjusted annually for inflation to maintain purchasing power.
- Cap and Trade—\$500 million in additional Cap and Trade proceeds.
- Caltrans Efficiencies—\$100 million in cost-saving reforms.

The Governor's proposal differs with the State Legislature's proposal in several ways. Whereas the Governor is proposing a \$4 billion package, the Legislature's proposal would provide \$6 billion annually. The Governor's proposal generally uses few fee increases, while the Legislature is proposing an \$38 increase to the Vehicle Registration Fee, and assess Zero Emission Vehicles.

With the Legislature's \$6 billion proposal, Long Beach would receive a higher direct allocation of \$16 million per year to be used for local streets and roads maintenance. If the Governor's proposal remains, cities will still receive a direct allocation, though the amount will be less. It is expected that healthy debate will be had on this matter.

The Governor's proposal would allocate funding as follows:

Governor's Transportation Package
 (Dollars in Millions)

<i>Investment Category</i>	<i>Program</i>	<i>2017-18 Amount</i>	<i>Annualized Amount^{1/}</i>
Local Streets and Roads / Partnership Programs	Active Transportation Program	\$100	\$100
	Local Road Maintenance & Repairs	\$206	\$1,163
	Local Partnership Grants ^{2/}	\$0	\$250
	SB 375 Local Planning Grants	\$25	\$25
	Corridor Mobility Program	\$275	\$275
Transit	Transit Capital ^{3/}	\$485	\$400
State Highway Repair and Maintenance ^{4/}	Pavement ^{3/}	\$129	\$997
	Bridges and Culverts	\$91	\$554
	Traffic Management Systems	\$12	\$100
	Maintenance	\$120	\$120
Trade Corridors	Improved Goods Movement ^{3/}	\$358	\$250
Total		\$1,801	\$4,234

^{1/} Excludes one-time loan repayments totaling \$706 million.

^{2/} Provides up to \$250 million per year beginning in 2018-19.

^{3/} The 2017-18 totals include anticipated loan repayments.

^{4/} Annualized amounts include \$100 million per year in Caltrans efficiency savings.

Continuing Health Care Expansion

It is estimated that 1.4 million people will be enrolled in Covered California during FY 18. Additionally, the expansion of the Medi-Cal program through the federal Affordable Care Act is expected to increase Medi-Cal caseloads from 7.9 million in FY 13 to a projected 14.3 million in FY 18; this covers over one-third of California's population. The incoming presidential administration and leaders in Congress have suggested major changes to the federal Affordable Care Act. Recent proposals have included reductions to federal funding for the expansion population, a block grant structure for Medicaid programs, capped per-beneficiary allotments to states, tax credits to enroll Medicaid beneficiaries in private insurance, and creation of high-deductible plans for the Medicaid program combined with health savings accounts. At this point, it is not clear what those

changes will be or when they will take effect. As such, the Budget assumes costs of \$20.1 billion (\$888 million General Fund) in FY 17 and \$18.9 billion (\$1.6 billion General Fund) in FY 18 for the 4.1 million Californians in the optional Medi-Cal expansion.

Proposition 47

Proposition 47, passed by the voters on November 4, 2014, requires misdemeanor rather than felony sentencing for certain property and drug crimes, and permits inmates previously sentenced for these reclassified crimes to petition for resentencing. Based on fall projections, Proposition 47 is expected to reduce the FY 17 adult inmate average daily population by 4,425, compared to 5,247 in FY 16. The FY 17 population reduction is attributable primarily to avoided new admissions. Proposition 47 requires state savings resulting from the proposition to be transferred into the Safe Neighborhoods and Schools Fund. The fund is used to reduce truancy and support drop-out prevention programs in K-12 schools, increase victim services grants, and support mental health and substance use disorder treatment services. The Governor's January Budget provides \$10.1 million to support investments aimed at improving outcomes for public school pupils in K-12 by reducing truancy and supporting pupils who are at risk of dropping out of school or are victims of crime, consistent with the provisions of Proposition 47.

CalGRIP

The Governor's January Budget proposes to eliminate the State's CalGRIP program. Over the last 3 years, Long Beach has used CalGRIP funding to reduce gang activity among at-risk youth, ages 8-24, by providing workforce training, evidence-based mentoring, civic leadership training, and evidence-based parent education. We have also used the funding to reduce female gang membership and commercial sexual exploitation of female youth, ages 10-24 by increasing community awareness about the nexus of gangs and human trafficking, increasing school attendance and providing training and education for at risk girls, providing comprehensive social services to victims of human trafficking, and police suppression of gangs using human trafficking as a for-profit venture. The elimination of this State program would eliminate services locally.

Tree Removal Funding

With the recent drought, California has seen a record number of dying and decaying trees. These trees can become a public safety concern if not removed when appropriate. In recognition of the unprecedented challenges with tree mortality, the Governor's January Budget proposes \$52.7 million in State General Fund revenues for the State Office of Emergency Services to provide assistance to counties through the California Disaster Assistance Act. This funding can be used to aid local agencies in the removal of dead or dying trees that are a direct threat to public safety.

Affordable Housing and Homelessness

The Governor's January Budget addresses affordable housing and homelessness as issues that are interlinked. Proposed State funding in both of these areas can be summarized by the chart below:

2017 18 Affordable Housing and Homelessness Funding
 (Dollars in Millions)

<i>Department</i>	<i>Program</i>	<i>Amount</i>
Department of Housing and Community Development	No Place Like Home Program	\$262
	Federal Funds	\$122
	Housing for Veterans Funds	\$75
	Office of Migrant Services	\$6
	Various	\$15
California Housing Finance Agency ^{1f}	Single Family 1st Mortgage Lending	\$1,250
	Multifamily Conduit Lending	\$300
	Multifamily Lending	\$200
	Mortgage Credit Certificates	\$165
	Single Family Down Payment Assistance	\$60
	Special Needs Housing Program	\$35 ^{2f}
Strategic Growth Council ^{3f}	Affordable Housing and Sustainable Communities	TBD
	Transformative Climate Communities	TBD
Tax Credit Allocation Committee	Low Income Housing Tax Credits (Federal)	\$241 ^{4f}
	Low Income Housing Tax Credits (State)	\$95
	Farmworker Housing Assistance Tax Credits	\$6
Department of Veterans Affairs	CalVet Farm and Home Loan Program	\$230
	Transitional Housing Program, Veterans Homes of California	\$2
Department of Social Services	CalWORKS Housing Support Program	\$47
	CalWORKS Homeless Assistance Program	\$29 ^{5f}
	CalWORKS Family Stabilization, Housing Component	\$12 ^{5f}
Office of Emergency Services	Transitional Housing Program, Victim of Crimes Act	\$18
	Homeless Youth Emergency Services	\$10
	Domestic Violence Housing First Program	\$5
	Homeless Youth and Exploitation Program	\$2
Department of Health Care Services	Whole-Person Care Pilot Program, Health Homes Program, Mental Health Services Act Community Services and Supports, Projects for Assistance in Transition from Homelessness	N/A ^{5f}
	Integrated Services for Mentally-Ill Parolees	\$2
California Department of Corrections and Rehabilitation	Specialized Treatment of Optimized Programming, Parole Service Center, Day Reporting Center, Female Offender Treatment and Employment Program	N/A ^{5f}
Total		\$3,189

^{1f} Amounts are the estimated lending activities from 2016-17 trends.

^{2f} This amount represents a voluntary allocation of Proposition 63 funds from 16 participating counties.

^{3f} The Affordable Housing and Sustainable Communities program will reflect 20 percent of Greenhouse Gas Reduction Fund revenues; however, amounts have not yet been determined for 2017-18. The Transformative Climate Communities program (\$140 million for 2017-18) funds various activities, including housing, as an eligible capital component; however, the investment in housing will not be determined until awards are made.

^{4f} This amount represents the 9 percent tax credits allocated in 2017-18 and an estimated figure for 4 percent credit awards based on 2014-2016 averages. This figure does not include the \$3.9 billion of tax exempt bond debt allocation that is available for award from the California Debt Limit Allocation Committee.

^{5f} This amount represents an estimate of the portion of the program associated with housing and homelessness activities.

^{6f} The state provides a number of wrap-around supportive services through these programs, including housing support, which cannot be separated from the Department of Health Care Services and Department of Corrections and Rehabilitation's general budgets.

While affordable housing and homelessness can be related, cities believe the dissolution of Redevelopment in 2011, State prison realignment (which was intended to reduce the State's prison population), and recent ballot initiatives such as Proposition 47 (2014) and Proposition 57 (2016) have also had an impact on the challenges surrounding homelessness in California.

Affordable Housing

The Governor's January Budget takes the perspective that local governments enact land-use and housing-related decisions that discourage housing construction and contribute to higher construction costs, which then lead to higher housing costs. It is true local governments retain the large majority of land-use and housing-related permitting authority. These types of decisions impact local neighborhoods and communities most, and therefore the decision making authority is appropriately placed with cities. The Governor's January Budget also contends that, "Throughout the development process, each local government is faced with factors that discourage housing development, including community opposition, incentives to approve sales-tax generating development over residential development, and market conditions, such as high land and construction costs." While noting the local economic challenges at hand, the Governor's Budget does not provide any significant new programs to support local governments in the quest for affordable housing.

Homelessness

The FY 18 budget does not propose new homeless services programs, but it does continue funding for existing programs such as the No Place Like Home Program, which authorized a \$2 billion bond secured by a portion of future Proposition 63 Mental Health Services Act revenues, and a \$149.4 million General Fund (\$100 million one-time) commitment for housing and homelessness programs, including \$35 million for the California Emergency Solutions Grant program and \$10 million for the Homeless Youth and Exploitation Emergency Services Pilot Projects to rapidly rehouse individuals, youth, and families experiencing homelessness.

Tobacco Tax Increase (Proposition 56)

The California Healthcare, Research and Prevention Tobacco Tax Act of 2016 (Proposition 56), passed by the voters in November 2016, increases the excise tax rate on cigarettes and tobacco products, effective April 1, 2017. This tax is also applicable to electronic cigarettes for the first time. The Governor anticipates Proposition 56 will generate \$1.7 billion in new revenues during FY 18. Although grant guidelines for tobacco prevention programs have not been released yet, the funding is proposed to be distributed in the following manner:

Proposition 56 Allocations
 (Dollars in Millions)

<i>Investment Category</i>	<i>Department</i>	<i>Program</i>	<i>2017-18 Amount^{1/}</i>
Enforcement	Department of Justice	Local Law Enforcement Grants ^{2/}	\$37.5
	Department of Justice	Distribution and Retail Sale Enforcement ^{2/}	\$7.5
	Board of Equalization	Distribution and Retail Sales Tax Enforcement ^{2/}	\$5.8
	Department of Public Health	Law Enforcement ^{2/}	\$7.5
Education, Prevention, and Research	University of California	Cigarette and Tobacco Products Surtax Medical Research Program	\$80.7
	University of California	Graduate Medical Education ^{2/}	\$50.0
	Department of Public Health	State Dental Program ^{2/}	\$37.5
	Department of Public Health	Tobacco Prevention and Control	\$178.5
	State Department of Education	School Programs	\$31.5
Health Care	Department of Health Care Services	Health Care Treatment	\$1,237.4
Administration and Oversight	State Auditor	Financial Audits	\$0.4
	Board of Equalization	Sales and Use Tax	\$1.1
Revenue Backfills	Proposition 99, Breast Cancer Research Fund, and Proposition 10		\$37.1
Total			\$1,712.5

^{1/} 2017-18 figures include one quarter of 2016-17 revenue and four quarters of 2017-18 revenue.

^{2/} Annual amount specified in statute.

Next Steps

The Governor's next budget update will come in May 2017. The City will continue to monitor these developments and provide updates as appropriate.

If you have questions or comments, please contact Diana Tang, Manager of Government Affairs, at 8-6506.

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