



Date: January 24, 2018
To: State Legislative Committee
From: Patrick H. West, City Manager *PWest*
Subject: Governor's January Budget for FY 19

Introduction

The Governor introduced his FY 18-19 budget on January 10, 2018. The FY 19 Budget is projected to have a healthy one-time surplus. However, the Governor's January Budget does not factor in the recently enacted Federal tax bill, which may alter economic and revenue forecasts. Due to the uncertainty of the future, this Budget proposes to bring the Rainy Day Fund to 100 percent of its constitutional target by depositing \$5 billion in the fund. This fact sheet provides additional details on the Governor's January Budget.

Summary

The Governor's proposed FY 19 budget assumes \$135.1 billion in General Fund revenues, and expenditures totaling \$131.7 billion. Comparably, the FY 18 budget enacted in June 2017 included \$127.5 billion in expenses. The projected deficit for FY 19 is \$1.9 billion, as opposed to the previously anticipated deficit of \$5.8 billion. Many of the budget uncertainties are due to Federal tax changes including the limitation of ability to deduct state and local taxes from federal filings; Children's Health Insurance Program (CHIP) Reauthorization, which if not extended beyond March would increase state costs by hundreds of millions of dollars in FY19; and Federal cost shifting if Congress were successful in repealing the Affordable Care Act.

State Budget Items

Statewide Transportation Infrastructure Funding

For FY 19 the Budget includes \$4.6 billion in new transportation funding. In addition to traditional Highway Users Tax Account (HUTA) revenues, SB 1 revenues, which were approved in 2017, are allocated by statutory formula to the state for highways, to cities and counties for local roads, and to transit agencies for operations and capital expenditures.

In FY 19 Long Beach expects to receive \$8.2 million in Road Maintenance Rehabilitation funding with an increase each year until reaching \$11 million per year once all revenue mechanisms are in place. It is expected there will be an attempt to repeal SB 1 based on constitutional grounds. If voters choose to repeal SB 1 in November 2018, then future expected SB 1 revenues would no longer be allocated to Long Beach. However, the repeal would not impact State Highway Users Tax Account (HUTA) dollars currently allocated to cities for streets and roads. In FY 19, Long Beach is estimated to receive \$11.3 million from HUTA. City staff will continue to closely monitor SB 1 repeal efforts.

California Drought, Water, Parks, Climate, Coastal Protection Outdoor Access (SB 5)

Voters will have an opportunity to approve \$4 billion in general obligation bonds for California’s parks, water, and flood control infrastructure, ocean and coastal protection, safe drinking water, groundwater management and climate preparedness and resiliency. Should voters approve this measure, the Governor’s FY 19 budget proposes to appropriate \$1.02 billion for the first year of implementation. Below are the projected budget allocations:

**California Drought, Water, Parks, Climate, Coastal Protection and Outdoor Access
For All (SB 5)
(Dollars in Millions)**

| Investment Category | Department | Program | Amount |
|--|---|--|----------------|
| State and Local Park Improvements | Department of Parks and Recreation & Natural Resources Agency | Local and Regional Grant Programs for Neighborhood Parks and Greenway Trails | \$464 |
| | Department of Parks and Recreation | State Park System Enhancements | \$4 |
| | Department of Food and Agriculture | Deferred Maintenance for Fairs | \$4 |
| Ecosystem Restoration & Climate Resiliency | Multiple Departments & Conservancies | River Recreation, Creek, and Waterway Improvements | \$58 |
| | Natural Resources Agency | Salton Sea Restoration | \$30 |
| | Multiple Departments & Conservancies | Climate Adaptation & Resiliency | \$110 |
| | State Coastal Conservancy & Ocean Protection Council | Coastal Protection | \$13 |
| | California Conservation Corps | CCC Restoration and Rehabilitation Projects & Grants to Local Community Conservation Corps | \$10 |
| Water Action Plan | State Water Board | Safe Drinking Water Projects | \$63 |
| | Department of Water Resources & Natural Resources Agency | Flood Management | \$99 |
| | Department of Water Resources & State Water Board | Sustainable Groundwater Management Act | \$146 |
| | Department of Food and Agriculture | State Water Efficiency and Enhancement Program | \$18 |
| Total | | | \$1,019 |

Affordable Housing and Homelessness

The Governor’s January Budget addresses affordable housing and homelessness as issues that are interlinked. In 2017, the Governor and Legislature developed a housing package that contained 15 bills to collectively shorten the housing development approval process and limit local control, but which also enables a new mechanism to collect real-estate transaction fees, and enact a bond. The most notable revenue generating bills include the Building Homes and Jobs Fund Program (SB 2). SB 2 authorizes collection of fees from \$75 to \$225 on particular real-estate transactions. The bill is estimated to produce \$245 million annually. In addition to SB 2, SB 3 was adopted.

SB 3 enables voters to consider the Veterans and Affordable Housing Bond Act Programs (Bond), which includes a \$4 billion bond on the November 2018 ballot. Upon passage of the Bond, \$3 billion would be for existing housing programs and \$1 billion for veterans housing. Of the \$3 billion, \$277 million would go towards local assistance funding for the Multifamily Housing Program which assists with new construction, rehabilitation and preservation of permanent and transitional housing for lower income households.

Homelessness

The Governor's January Budget does not include new homeless services programs, but instead brings attention to continued investment in existing programs such as the No Place Like Home Program, for which \$262 million has been proposed, and the Homeless Youth and Exploitation Emergency Services Program, for which \$1 million has been proposed. Other State efforts towards affordable housing include funding for the Low-Income Housing Tax Credit program, which resulted in 20,847 units financed with federal tax credits in 2016 and support for multifamily lending with the California Housing Financing Agency, which provided \$369 million in financing in FY 17 for 2,100 affordable housing units. State funding in housing and homelessness is summarized in the chart below:

2018-19 Affordable Housing and Homelessness Funding
(Dollars in Millions)

| <i>Department</i> | <i>Program</i> | <i>Amount</i> |
|---|---|---------------------|
| Department of Housing and Community Development | Veterans and Affordable Housing Bond Act Programs (SB 3) | \$277 |
| | No Place Like Home Program | \$262 |
| | Building Homes and Jobs Fund Programs (SB 2) | \$245 |
| | Federal Funds | \$122 |
| | Housing for Veterans Funds | \$75 |
| | Office of Migrant Services | \$6 |
| | Various | \$54 |
| California Housing Finance Agency ^{1/} | Single Family 1st Mortgage Lending | \$1,500 |
| | Multifamily Conduit Lending | \$300 |
| | Multifamily Lending | \$200 |
| | Single Family Down Payment Assistance | \$108 |
| | Special Needs Housing Program | \$30 ^{2/} |
| Strategic Growth Council ^{3/} | Affordable Housing and Sustainable Communities | \$455 |
| Tax Credit Allocation Committee | Low Income Housing Tax Credits (Federal) | \$259 ^{4/} |
| | Low Income Housing Tax Credits (State) | \$97 |
| | Farmworker Housing Assistance Tax Credits | \$3 |
| Department of Veterans Affairs | CalVet Farm and Home Loan Program | \$264 |
| Department of Social Services | CalWORKS Housing Support Program | \$47 |
| | CalWORKS Homeless Assistance Program | \$35 |
| | CalWORKS Family Stabilization, Housing Component | \$3 ^{5/} |
| Office of Emergency Services | Transitional Housing Program, Victim of Crimes Act | \$12 |
| | Homeless Youth and Exploitation Program | \$1 |
| | Domestic Violence Housing First Program | \$6 |
| Department of Public Health | Housing Opportunities for Persons with AIDS (HOPWA) | \$3 |
| | Housing Plus Program | \$2 |
| California Department of Corrections and Rehabilitation | Integrated Services for Mentally-Ill Parolees | \$3 |
| | Specialized Treatment of Optimized Programming, Parole Service Center, Day Reporting Center, Female Offender Treatment and Employment Program | N/A ^{6/} |
| | Whole-Person Care Pilot Program, Health Homes Program, Mental Health Services Act Community Services and Supports, California Community Transitions Program | N/A ^{6/} |
| Total | | \$4,369 |

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, increased the excise tax rate by \$2 per pack of 20 cigarettes and other tobacco products, effective April 1, 2017, and July 1, 2017, respectively. This tax is also applicable to electronic cigarettes for the first time. Ten cents of the per pack tax is allocated to the General Fund. 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^{1f}</i> |
|-------------------------------------|---|--|------------------------------------|
| Enforcement | Department of Justice | Local Law Enforcement Grants ^{2f} | \$37.5 |
| | Department of Justice | Distribution and Retail Sale Enforcement ^{2f} | \$7.5 |
| | Board of Equalization | Distribution and Retail Sales Tax Enforcement ^{2f} | \$5.8 |
| | Department of Public Health | Law Enforcement ^{2f} | \$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 ^{2f} | \$50.0 |
| | Department of Public Health | State Dental Program ^{2f} | \$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 |

^{1f} 2017-18 figures include one quarter of 2016-17 revenue and four quarters of 2017-18 revenue.
^{2f} Annual amount specified in statute.

State Cap and Trade Program

In 2017, the Legislature expanded the State's Cap and Trade Program through 2030. As a result of the extension, auction proceeds have increased resulting in \$1.25 billion available for appropriation in FY 19.

The future of California's Cap and Trade Program impacts Long Beach in several ways:

- Residential utility rate payers who are serviced by investor-owned utilities, which in Long Beach is Southern California Edison, receive two annual Residential

Climate Credits that appear as a “credit” on individual rate payer accounts. Small businesses receive the climate credit monthly, as a credit related to the amount of electricity used. This credit, or savings, is intended to encourage utility users to invest in small energy efficiency upgrades in their homes and businesses, ie: replace old light bulbs with energy efficient options. With the dissolution of the State’s Cap and Trade Program, this credit could be discontinued.

- As a greenhouse gas reduction mechanism, the State’s Cap and Trade Program (Program) has increased costs at the State’s three waste-to-energy facilities, including City’s Southeast Resource Recovery Facility (SERRF). Long Beach was able to secure exemptions for SERRF during the Program’s first two compliance periods, but SERRF will fall under the Cap and Trade Program during the third compliance period. The third compliance period begins in 2018 and extends through 2020. At this time, the City is working on securing a cost-neutral agreement with respect to inclusion in the third compliance period. The City also continues to advocate for recognition for SERRF’s important functions as a greenhouse gas mitigation option from the perspective of waste disposal, as well as the function SERRF serves in the destruction of confiscated controlled substances.

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. The Department of Finance currently estimates net savings of \$64.4 million for Proposition 47 when comparing FY 18 to FY 14. 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.

Cannabis Excise Taxes

In November 2016 voters approved Proposition 64, the Adult Use of Marijuana Act which legalized the adult-use sale and production of cannabis to persons over the age of 21. As of January 1, 2018, the Adult Use Marijuana Act levies new excise taxes on the cultivation and retail sale of both adult-use and medical cannabis. The 15 percent State tax on the retail price of cannabis is expected to generate \$175 million in FY 18 and \$643 million in FY 19. Long Beach held a public lottery on September 28, 2017 to determine which Medical Marijuana Dispensary Business License applications were eligible to proceed in an application process, resulting in 32 medical marijuana dispensary licenses that could be issued in the City. As of November 14, 2017, the City of Long Beach has a temporary moratorium of 180 days on the issuance of any permit and entitlement, license, approval, operation, or activity relating to adult-use, non-medical commercial cannabis activity in the City. The City will continue to monitor State legislative proposals and regulations as the new market develops.

Continuing Health Care Expansion

The Affordable Care Act (ACA) was under revision by Congress in FY 17 but attempts to dismantle the ACA were unsuccessful. 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. It is not clear what changes, if any, will take place. Medi-Cal is projected to cover nearly \$13.5 million Californians in FY 19. The Budget continues to support Medi-Cal expansion and assumes costs of \$22.9 billion (\$1.6 billion General Fund) for the 3.9 million Californians in the optional Medi-Cal expansion program; this is an increase from FY 18, during which \$17.7 billion (\$1.4 billion General Fund) will be invested.

Next Steps

The Governor's next budget update will come in May 2018. 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 (562) 570-6506.

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