SENATE REPUBLICANS

Highlights and Analysis of the 2017-18 Budget

SENATE REPUBLICAN
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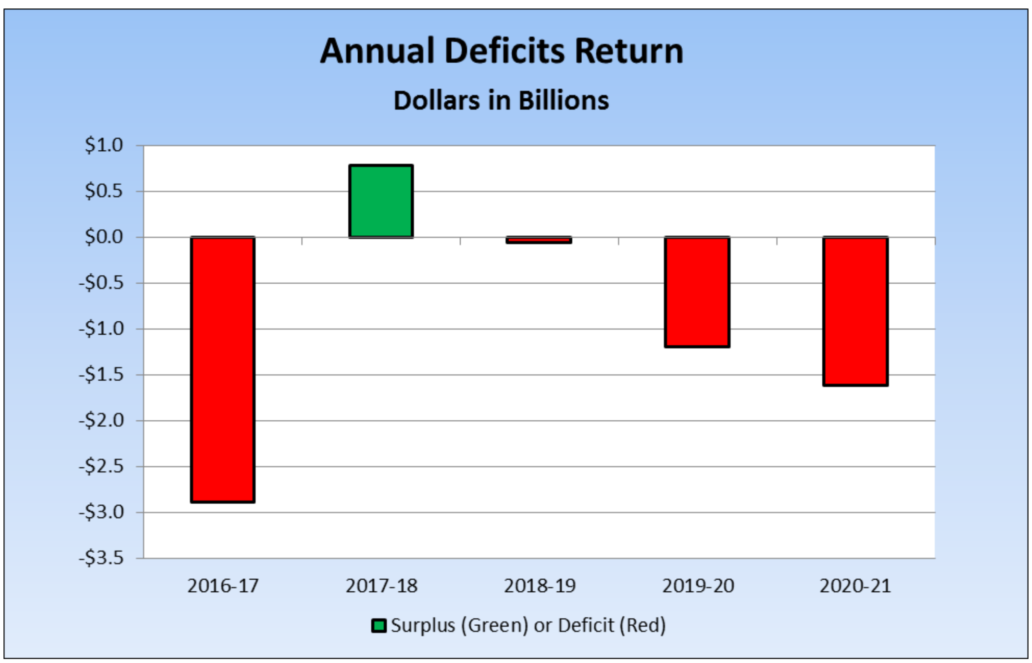
Executive Summary

Overview: Deficits and Missed Opportunities. It's no secret that California is becoming increasingly unaffordable for many of its residents, as costs for housing, energy, and gasoline are at or near national highs. Many Californians are not sharing in the current prosperity of those in a few coastal communities like Silicon Valley. Senate Republicans believe that if the state is smart about managing its budget, we can keep moving forward by prioritizing the things that matter to Californians: good schools, safe communities, and a more affordable quality of life in California.

The 2017-18 budget misses opportunities through misplaced priorities and too few efforts to make California more affordable, such as addressing the high cost of housing. The state remains in the unfortunate position of facing recurring deficits, despite receiving record-high tax revenues, as a result of unrelenting spending growth. As a result, the budget reflects $3.5 billion in savings actions over two years in order to avoid a deficit in 2017-18.

Revenues Reach New Record. The budget reflects total General Fund revenues and transfers of $127.7 billion for 2017-18, an increase of $6.1 billion (5 percent) from the previous year, to set another record high. Compared to expectations one year ago, revenues are projected to be lower, but despite this softening outlook, significant annual increases ranging from 3.1 percent to 3.7 percent per year are still projected through 2020-21.

Spending Growth Creates Deficits. Total General Fund spending would reach a record $125 billion in 2017-18, an increase of $3.7 billion compared to the prior year. Although Senate Republicans cautioned against spending beyond our means, billions of dollars in long-term spending commitments made by Sacramento Democrats over the past several years have returned California to a deficit situation in 2016-17. Additionally, although the 2017-18 budget shows a modest surplus, the following year would see a slight operating deficit, and annual operating deficits in excess of $1 billion would return by 2019-20, as shown in the chart below.



Solutions Package Offers Temporary Savings. The budget includes $2.8 billion in spending solutions to address the deficit, most of which are one-time in nature and do not address spending growth going forward. However, the Governor's "official" list of solutions excludes major savings actions such as a "bait and switch" on voters to redirect over $711 million in Proposition 56 tobacco tax revenues to plug the budget hole rather than increase access to care through Medi-Cal and Denti-Cal. On a positive note, the budget does reject the Governor's ill-advised January proposals to freeze the child care expansion and to reduce middle-class scholarships.

Rainy Day Reserve Improved Though Likely Not Enough. The Rainy Day Fund (Proposition 2 of 2014) would grow to reach $8.5 billion by the end of 2017-18, or 6.6 percent of General Fund revenue. When combined with the discretionary reserve of $1.4 billion, the total reserve would reach $9.9 billion, or 8 percent of General Fund revenue. However, this is insufficient compared to the potential $20 billion shortfall a recession could bring.

Reversing Questionable Changes to State Spending Limit. In January the Governor proposed a significant technical change to a constitutional spending limit known as the "Gann limit" that would have provided California's budget with more room to increase spending. After Senate Republicans raised significant concerns about the legality of this proposed change, the Governor reversed course and agreed to continue using the previously accepted method for the 2017 Budget Act.

Democrats Abuse the Budget Process to Protect Their Own. The 2017-18 budget package continues to demonstrate Senate Democrats' willingness to abuse the special budget rules to force through non-budget policies. Most notably, this includes changes that lengthen the state's recall process by five months, apply those changes retroactively, and make it more difficult to qualify a recall, all to benefit a current senator now facing a potential recall. Also, the budget imposes changes that seek to expand the influence of public employee unions throughout the state, such as forcing public employees' private emails to be shared with public employee unions.

Proposition 98 Education Spending Sets New Record. Proposition 98 funding for K-14 education grows by over $5.4 billion over three years, reaching a record $74.5 billion in 2017-18. Senate Republicans applaud the increase in local control provided through progress on the Local Control Funding Formula. Unfortunately, the budget does nothing to forestall the previously planned reductions to career technical education funding, and anticipated sales of K-12 school facilities bonds (which are off-budget) remain insufficient to meet facility needs.

Higher Education: Tuition Hikes, Audits, and Budget Choices. In response to recent State Auditor criticism, the budget plan holds $50 million in University of California (UC) funding back until UC acts on the audit's recommendations and various other issues. It accepts UC and the California State University's recent actions to raise tuition by 2.5 percent and 5 percent respectively. The UC certainly could improve transparency and cut waste prior to raising tuition, but Sacramento Democrats have created substantial pressure on UC finances over the past decade by providing only $286 million more General Fund compared to 2007-08, a mere 9 percent increase, while dramatically raising spending by billions of dollars in other areas of the budget.

Revised Shift of In-Home Supportive Services (IHSS) Costs. The 2017-18 budget reduces the shift of IHSS costs to counties substantially compared to the Governor's January proposal, and would leave counties with a net cost of $141 million in 2017-18. However, it remains a cynical strategy for the state to ramp up costs in the program following the beginning of the Coordinated Care Initiative in 2012, and then seek to hand the higher-cost program back to counties.

Costs of "Resisting" the Federal Government Mount. The budget includes over $50 million General Fund for the Attorney General and for community grants to continue efforts to "resist" recent federal policy changes. The funding will pay for state legal staff to challenge the constitutionality of executive actions and will provide grants to private agencies to defend people in the country illegally, including some who commit violent crimes. This amounts to little more than political grandstanding, and using taxpayer dollars in such a manner shows disdain for the hard-working Californians who are forced to pay the bills.

Significant Transportation Spending Skips Roads. The budget includes increased spending of $2.8 billion generated from the new gas, diesel, and vehicle taxes. Of this $2.8 billion, $873 million would be spent on programs that do not fix or maintain California's roads and highways. The extra tax dollars are being spent on other projects such as public transit, walking and biking paths, local planning, state and local park operations and maintenance, and university research programs. Additionally, only about 5 percent of the taxes will expand road capacity, despite the clogged roads and highways that force Californians to waste countless hours stuck in traffic.

Missed Opportunities for Infrastructure and Environmental Projects. The budget recognizes that California's drought is over and removes funds that had been slated in January for drought response. Unfortunately, the budget largely overlooks opportunities to redirect resources to major needs such as widespread tree mortality and critical flood infrastructure repair needs. (The budget also does not specify how to spend Cap and Trade revenues, instead deferring that issue to policy legislation.)

Taxpayer Rights Reduced Under Late Tax Agency Changes. Under the guise of reform, Sacramento Democrats introduced unprecedented changes to the Board of Equalization at the end of the budget process. While some reforms were needed, the last-minute actions ignore more extensive discussions of thoughtful improvements and instead increase bureaucracy while minimizing taxpayers' rights to appeal to elected tax representatives.

Underfunding of Trial Courts Compounded by Change in Court Collections Authority. The enacted budget provides $37 million in new funding for the trial courts, which still leaves them with more than $400 million in unmet operational needs. This chronic underfunding, which has continued for the past decade, has resulted in court closures, decreased services to the public, and for many Californians, difficulty accessing justice. Additionally, the budget eliminates longstanding authority for a judge to suspend a person's driver's license for failure to pay court-ordered debt, further compounding budget problems.

Expansion of Tax Credit to Self-Employed. The 2017 budget expands the state Earned Income Tax Credit (EITC) to workers with self-employment income. Previously, only workers who earned wages from an employer were eligible to participate. This important change levels the playing field for workers who are self-employed.

Too Many Unknowns for Supplemental Pension Payment. The budget provides a loan of $6 billion as a supplemental payment to the California Public Employment Retirement System (CalPERS) to pay down unfunded liabilities. By providing this additional payment now, the state may be able to lower the future estimated employer contributions and potentially save $11 billion over the next 20 years. While additional payments to CalPERS are necessary, the proposal included in this budget was rushed and left too many crucial questions unanswered.

Pension and Retiree Health Costs Continue to Climb. State spending on retiree health and pension obligations continues to outpace almost any other area of the budget. The budget provides $10.7 billion in spending for pension and retiree health in the 2017-18 budget, an increase of 11 percent over spending in last year's budget. By the 2020-21 budget, costs for pension and retiree health are on pace to exceed $12.7 billion.

Revenues, Expenditures, and Deficits

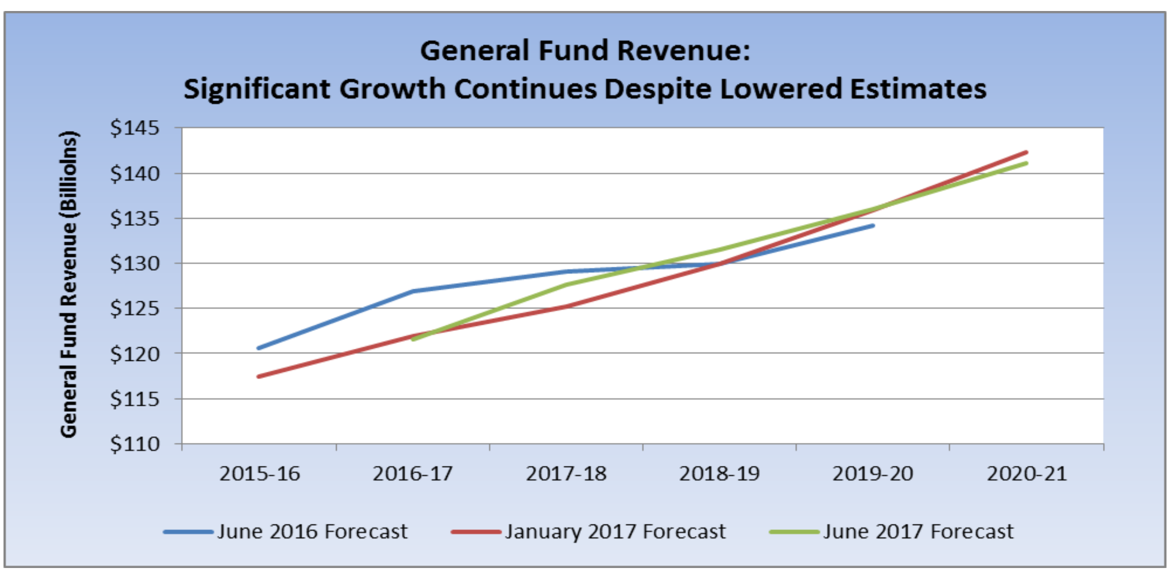
Key Points

- **Record Revenues Can't Keep Up With Rising Spending.** California continues to set new records for tax revenues, but spending is growing just as fast due to budget decisions.
- **Annual Deficits Set to Return.** Despite record-high revenue, California's unrelenting spending growth means that the state has an operating deficit in 2016-17 and will see annual deficits each year from 2018-19 through 2020-21.
- **Spending Reductions Mostly One-Time.** The budget reflects spending adjustments of $2.8 billion over two years to help avoid an operating deficit in 2017-18. Most of these adjustments consist of pulling back one-time allocations for housing or offices. One positive note is that the budget avoids any reduction to middle class scholarships.

Revenues Continue to Set Record Highs

The budget reflects total General Fund revenues and transfers of $127.7 billion for 2017-18, an increase of $6.1 billion (5 percent) from the previous year, to set another record high. The most significant growth factor is an increase of $5.7 billion or 6.8 percent in personal income taxes, largely attributed to capital gains associated with the strong stock market performance since January. The Administration projects this gain to be mostly one-time in nature and that personal income taxes will grow more slowly after this year.

The chart below shows the shifts in estimates since the 2016 Budget Act forecast. The final budget revenue estimates represent a cumulative decrease of more than $6.7 billion over 2016-17 and 2017-18 compared to expectations just one year ago, which highlights how much revenue projections can shift in a short time. Despite this softening outlook, significant annual increases ranging from 3.1 percent to 3.7 percent are still projected through 2020-21. These revenues include over $7 billion annually from Proposition 30 (2012) tax increases, which will continue past 2018 as a result of Proposition 55 (2016). The steady revenue growth makes it clear the state budget does not have a revenue problem.



Fast-Growing Expenditures Gobble Up Record Revenue

Recent Decisions Drive Spending Growth. General Fund spending in the Budget Act would reach a record $125 billion in 2017-18, an increase of $3.7 billion (3.0 percent) compared to the updated current year amount, even with the enacted savings actions. A significant portion of spending growth results from long-established laws that require spending to increase along with revenue growth, such as Proposition 98 for education spending. In 2012, Governor Brown promoted Proposition 30 tax increases as a way to avoid spending cuts to education, and voters approved the tax increases that now contribute about $7 billion annually in tax revenue. Since then, however, Sacramento Democrats have made major new spending commitments that now cost billions per year, thus enacting a bait-and-switch on voters.

The table below highlights several recent examples of major new spending commitments that together cost $3.9 billion in 2017-18, which will reach $9.2 billion when fully implemented. In essence, Proposition 30 tax increases have enabled these new spending commitments. All told, General Fund spending is budgeted to be $28.5 billion higher (29.5 percent) in 2017-18 than five years ago when the state began recovering from the recession and voters passed Proposition 30.

Major Recent General Fund Spending Decisions

Dollars in Millions

Program	Year Enacted	2017-18 Cost	Annual Cost Upon Full Implementation
Optional Adult Medi-Cal Expansion (1)	2013	$937	$2,466
State Employee Pay Increases Since 2012-13	Multi	$1,700	$2,385
In-Home Supportive Services Program Expansion	2012	$400	$150
Statewide Minimum Wage to $15	2016	$287	$3,600
Full Medi-Cal Benefits for Undocumented Children	2015	$331	$331
CalWORKs Expansion (Maximum Family Grant Repeal)	2016	$223	$223
Total		**$3,878**	**$9,155**

(1) 2017-18 amount is net of nearly $1.5 billion in costs less $546 million offset from counties.

The table on the next page summarizes General Fund spending by area.

General Fund Expenditures by Agency (Dollars in Millions)				
Agency	Budget Act 2016-17	Revised 2016-17	Enacted Budget 2017-18	Change from 2016-17 Budget Act
Legislative, Judicial, & Executive	$3,513	$3,508	$3,487	-$26
Business, Consumer Srvcs, & Housing	$877	$494	$410	-$467
Transportation	$237	$225	$241	$4
Natural Resources	$2,819	$3,078	$2,857	$38
Environmental Protection	$88	$90	$95	$7
Health and Human Services	$33,240	$34,685	$34,824	$1,584
Corrections and Rehabilitation	$10,571	$10,944	$11,228	$657
K-12 Education	$51,277	$50,714	$53,455	$2,178
Higher Education	$14,531	$14,591	$14,892	$361
Labor and Workforce Development	$176	$179	$129	-$47
Government Operations	$1,756	$938	$747	-$1,009
General Government & Other	$3,383	$1,975	$2,731	-$652
Total, General Fund Expenditures	**$122,468**	**$121,421**	**$125,096**	**$2,628**

Overall Spending Rises Significantly. While the General Fund typically dominates budget discussions, federal and other funds play a much more significant role today than in past decades. As shown in the table below, the General Fund now accounts for only about 43 percent of total spending. Each category of funds would grow in the final budget, including a nearly 10 percent increase for Special & Bond funds. Total spending from all sources would increase to $291 billion in 2017-18, a jump of $24 billion (nearly 9 percent), relative to the 2016 Budget Act.

Expenditures by Fund Type
Dollars in Billions

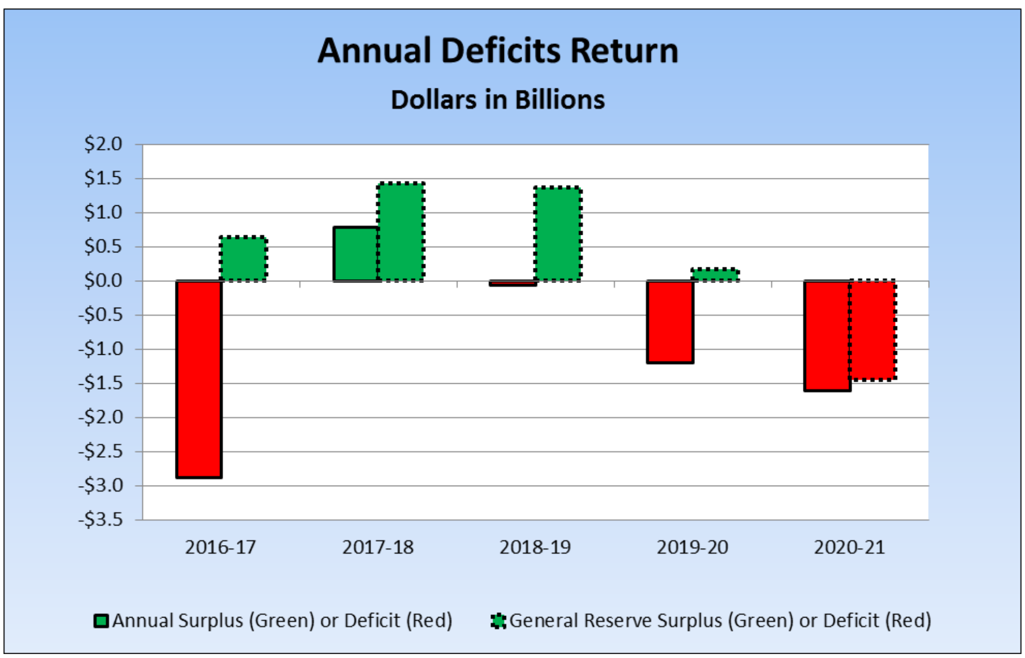
	Budget Act 2016-17	% of Total	May Rev. 2016-17	% of Total	Final Budget 2017-18	% of Total
General Fund	$122.5	46%	$122.3	45%	$125.1	43%
Special & Bond Funds	48.4	18%	53.0	20%	58.2	20%
Federal Funds	95.9	36%	96.2	35%	107.5	37%
Total	**$266.8**	**100%**	**$271.5**	**100%**	**$290.8**	**100%**
Total Increase from 2016-17 Budget Act			**2%**		**9%**	

Significant increases in special funds are the result of ballot measures or tax increases. The recently enacted gas and car tax (SB 1, Beall, 2017) will add $2.8 billion in special fund spending in 2017-18, and Proposition 56 tobacco taxes will increase special fund spending by about $1.7 billion.

Federal Fund Risk Remains. Federal funds account for 37 percent of California's budget, or nearly $108 billion, as shown in the table above. This reliance on federal funds creates risks of severe budget problems should any major changes emerge from the federal government. The most significant potential change could come through revisions to federal Medicaid spending, given that California's federal funds include nearly $70 billion for Medi-Cal and related health programs. It is unclear what the eventual terms of federal health reform could be, but the Administration estimates that the General Fund impact would be $3 billion in 2020 and up to $30 billion by 2027. This uncertainty highlights the need for more spending restraint and a more robust reserve in order to avoid significant cuts to needed state programs.

Deficits Return Despite Record Revenue

Annual Deficits Return. The budgetary balance in 2017-18 appears short-lived: annual operating deficits in excess of $1 billion are set to return within a couple years under the Governor's forecast. Annual deficits show an ongoing, built-in budget problem since each year's revenues do not pay for that year's expenses—the state must use general reserves to cover the extra costs. As shown by the solid bars in the chart below, a brief annual surplus in 2017-18 would be replaced by a narrow deficit in 2018-19 and by annual deficits exceeding $1 billion by 2019-20. The deficits force the state to spend down its general reserves, as shown by the dashed bars in the chart. By 2020-21, the state would have exhausted its general reserve and would need to cut spending or potentially dip into the Rainy Day Fund. **It is alarming that the state is already projecting deficits even though revenues are at all-time highs. This indicates that California has returned to a position of structural imbalance, in which even good years of revenue are not sufficient to pay for the state's excessive spending. Such imbalance could prevent the state from honoring commitments made to Californians who must rely on the state government for essential programs like education.**



Spending Reductions Mostly One Time. The fnal budget reduces the Governor's package of General Fund budget solutions from $3.2 billion in January to roughly $2.8 billion in the final budget. The table below summarizes these solutions, which include nearly $1.7 billion in 2016-17 and $1.1 billion in 2017-18. The solutions include $1.8 billion in actions that are one-time in nature, which is nearly two-thirds of the two-year total. The largest policy change is the reduction of $851 million in 2016-17 and $300 million in 2017-18 that had been authorized to build or remodel several Sacramento office buildings. This action is discussed in more detail on page 44. An additional $400 million will not be provided in 2016-17 because the budget made this amount contingent on the Legislature enacting some form of the Governor's "By Right" housing reforms in 2016, which did not happen. Notably, the Legislature rejected the Governor's previous proposal to phase out the middle class scholarship program. Senate Republicans argued against making that cut, since middle class scholarships are one of the few ways that state government helps regular Californians deal with our high cost of living.

General Fund Solutions in 2017-18 Governor's Budget
(Dollars in Millions)

Department	Spending Adjustment	2016-	2017-	2018-	2019-	2020-
Department of Education	Adjust Proposition 98 to Minimum Guarantee	$405	$420	$874	$1,201	$1,350
General Services	Cancel funds for Sacramento office buildings	$851	$300	$0	$0	$0
Housing and Community Development	Recognize affordable housing funding not authorized due to lack of "By Right" reform	$400	$0	$0	$0	$0
Various	Avoidance of various new proposals*	$0	$329	$127	$276	$286
Health Care Services	Major Risk Medical Insurance Fund Abolishment and Balance Transfer	$0	$47	-$10	-$9	-$8
California Health Facilities Financing Authority	Reduction of Children's Mental Health Crisis Services Grants	$17	$0	$0	$0	$0
Social Services	Delay Adoption of CalWORKs Welfare-to-Work 25/25A Report	$0	$6	$0	$0	$0
Total Solutions		**$1,673**	**$1,101**	**$991**	**$1,468**	**$1,628**
Includes One-Time Solutions		***$1,268***	***$549***			

* Details not provided by Department of Finance at time of publication.

Tobacco Tax Bait-and Switch Continues. The "official" list of budget solutions included in the final budget as noted above excludes a cost shift of $711 million from Medi-Cal General Fund to Proposition 56 tobacco taxes, even though this shift helps to plug the budget hole. (This shift is discussed in more detail on page 9.) This fund shift continues the bait-and-switch on California voters, who supported Proposition 56 with the expectation that the funds would help increase access to health and dental benefits through Medi-Cal. In keeping with voter intent, Republicans proposed to use the tobacco taxes to improve the Denti-Cal program through legislation (Assembly Bill 15, Maienschein), but Democrats refused to pass the bill.

Proposition 2 Rainy Day Fund

The 2017 Budget demonstrates that the Rainy Day Fund (RDF) approved by California voters in 2014 is taking positive steps toward fiscal stability. As shown in the table below, the budget would transfer nearly $1.8 billion to the RDF and allocate nearly $1.8 billion for debt reduction in 2017-18, as required by Proposition 2. In addition, the up-front 1.5 percent set-aside that Republicans negotiated as part of Proposition 2 will contribute $8 billion of the RDF amounts over four years. This is a far more stable contribution than the capital gains portion, which the Governor projects would begin to decline significantly by 2020-21.

Rainy Day Fund Forecast

Dollars in Millions

	2017-18	Forecast			
	Enacted	2018-19	2019-20	2020-21	Total
Annual 1.5% of General Fund Revenues	$1,915	$1,973	$2,040	$2,116	**$8,044**
Capital Gains Taxes in Excess of 8% of General Fund Revenues	$1,630	$833	$521	$312	**$3,296**
Rainy Day Amounts Available	**$3,545**	**$2,806**	**$2,561**	**$2,428**	**$11,340**
Required Debt Repayment (50%)	$1,773	$1,403	$1,281	$1,214	**$5,671**
Required Deposit to Rainy Day Fund (50%)	$1,773	$1,403	$1,281	$1,214	**$5,671**
Total Rainy Day Fund Deposit	**$1,773**	**$1,403**	**$1,281**	**$1,214**	
Rainy Day Fund Balance at End of Year[1]	**$8,486**	**$9,889**	**$11,170**	**$12,384**	
Balance as % of General Fund Revenue	**6.6%**	**7.5%**	**8.2%**	**8.8%**	

1. Includes beginning balance of $6.7 billion from previous years' deposits.

Note: Capital gains amounts are net of revenues attributable to Proposition 98. All estimates assume there are no budget shortfalls that would allow other uses of Rainy Day amounts to maintain spending.

Source: Department of Finance, June 2017

Rainy Day Fund (RDF) Would Grow, Though Still Inadequate to Offset Recession. Even with strong revenue growth, the balance of the Rainy Day Fund as a percent of General Fund revenues is projected to reach only 6.6 percent in 2017-18, significantly lower than the constitutional limit of 10 percent. When combined with the discretionary reserve of $1.4 billion, the total reserve would reach $9.9 billion, or 7.9 percent of General Fund revenue.

While this is a substantial improvement over the past, it remains insufficient given that California's economic expansion may be nearing its end. The risk of low reserves is that when the good times end, the state will have to reach out and take back services that it may have just begun or expanded. The large swings in tax revenues that are typical in California mean that healthy reserves are all the more important to avoid major reductions to important programs. The Department of Finance estimates the General Fund shortfall could reach $20 billion, or 15.7 percent of revenue, in one year of a moderate recession. However, even with strong revenue growth, the 2017 budget estimates that the RDF would reach 8.8 percent of revenue by 2020-21.

Additionally, in order to prohibit the state from using its entire reserve in one year, Proposition 2 limits the amount available for withdrawal to half the balance in the first year of a budget problem. This means only about $4.2 billion of the RDF would be available in the first year to offset the effects of a moderate recession. This magnifies the importance of building the overall reserve to a higher level. The current record revenue provides the state with a perfect opportunity to build adequate reserves in the Rainy Day Fund while continuing to preserve education and public safety programs. Senate Republicans will continue to advocate for strong reserves to protect against economic downturns.

Protecting the State Spending Limit

<u>**Key Point**</u>

- **Protecting the Constitutional Spending Limit.** In January 2017 the Governor quietly changed the method for calculating how much California can spend under its constitutional spending limit. Republicans raised concerns about the legality of this change, and the Governor agreed to return to the accepted method.

Background. The recent rapid growth in state spending has brought a decades-old constitutional spending cap known as the State Appropriations Limit, or "Gann limit," back into relevance. Voters first enacted the Gann limit in 1979, and as a result of excess revenues over the limit in 1986-87, the state gave taxpayers mandatory rebates in 1987. Voters later loosened the limit in 1990, and it grew much faster than state spending during the 1990s, leaving substantial "room" under the cap. Following the 1990 changes, the Gann limit requires that any "excess" revenues over a two-year period would be split between tax rebates and certain education spending.

Governor's Changes Raised Concerns. In the Governor's January budget, the Department of Finance quietly but dramatically revised the methods it uses to calculate the Gann limit, and estimated that the state had $25 billion in spending room under the limit. The Department of Finance claimed informally that these changes were the result of correcting past misinterpretations of how the calculation should be done, not any intentional attempt to free up more spending for Democrat priorities.

However, the nonpartisan Legislative Analyst's Office (LAO) issued a report in March 2017 criticizing the Governor's changes. The LAO estimated that the state had only $2.8 billion in room under the Gann limit in 2017-18, not the $25 billion estimated by the Governor's revised methods. This meant that the Governor could only spend $2.8 billion in tax revenue above his estimated 2017-18 January budget projection before potentially crossing the Gann threshold. The LAO further highlighted that the Governor maneuvering $22 billion away from being counted under the Gann Limit "contradicts long-standing policies," "violates [the] spirit" of the spending limit, and would be "highly vulnerable to legal challenges."

Republicans Successfully Oppose Changes. To further explore the issue, Senate and Assembly Republicans jointly requested additional information from the Department of Finance, and subsequently obtained a legal opinion from Legislative Counsel (available here). This opinion effectively corroborated the LAO's conclusion that the Governor's changes were likely not legal. Following the release of this opinion, the Department of Finance withdrew its proposed changes and agreed to calculate the Gann limit for the 2017 Budget Act according to the legally required methods, which had been in use through the 2016 Budget Act. Finance further indicated an intention to have additional discussions regarding appropriate Gann expenditure calculations in the fall.

Senate Republicans applaud the Governor for recognizing the validity of the concerns raised regarding its Gann limit changes, and will remain vigilant to ensure that this reasonable spending restraint enacted by voters will be observed. Any changes to it must be submitted to voters, not enacted unilaterally by the Administration.

Abusing the Budget Process

Key Point

- **Budget Process Abused to Enact Unrelated Policies.** The 2017-18 budget package demonstrates the majority party's willingness to abuse California's special budget rules to slip unrelated policy changes into law without the normal transparency and public review.

Background. In 2010, following years of late budgets, California voters enacted Proposition 25 to lower the vote requirement needed to enact the state budget bill from the previous two-thirds majority to a simple majority. Under the terms of the proposition, this simple majority standard also applied to "other bills providing for appropriations related to the budget bill," which are frequently referred to as budget "trailer bills." As a penalty to help prevent future late budgets, Proposition 25 also prohibited legislators from receiving their pay for each day past the June 15 annual deadline that the Legislature did not pass the budget.

The budget bill had long been enacted on an "urgency" basis, meaning it takes effect immediately, rather than on a delayed basis, in order to begin paying for the next fiscal year. Policy bills other than the budget bill typically take effect on January 1 in the year following their enactment, unless they pass the Legislature with a two-thirds majority vote, which allows them to take effect immediately as "urgency" bills. A critical part of Proposition 25 is that it allowed budget trailer bills to also take effect immediately, like the budget bill, with only a simple majority vote.

Bait-and-Switch to Enact Non-Budget Policies. Groups supporting Proposition 25 focused on the need for an on-time budget to relieve pressure on schools and small businesses that work with the state government. Unfortunately, Sacramento Democrats have pulled a bait-and-switch on voters by taking advantage of Proposition 25's rules to enact policies that are not necessary for the budget. In some cases, Sacramento Democrats have also used the special trailer bill rules to force through policies that may actually have fiscal effects but that previously failed to pass on their own merits when going through the standard policy bill process.

Non-budget policies jammed into trailer bills this year include changes to election laws, employment requirements favorable to public employee unions, and an extension of special treatment for one selected county (Marin) on building affordable housing. The table on the next page lists several of these. None of these policies have anything to do with the budget or with funds provided through the budget, and they certainly fall outside the reasons that voters were given for Proposition 25. Nonetheless, ***Sacramento Democrats use the special budget rules to bypass the transparency and accountability that should occur through a regular policy bill process***, which would include publishing the contents of bills and holding hearings over a period of weeks or months, not just a few days.

Policies with No Budget Effect Enacted Through Budget Process		
Trailer Bill	**Subject**	**Comments**
SB 96	Changes recall election rules to enable delays in timing of recall elections	Statements by Senate Democrats during the debate clearly indicate their intent is to protect one current senator facing a potential recall election.
SB 106	Extends exemption from certain affordable housing requirements for Marin County	Marin County previously obtained an exemption that was not due to expire until 2023, meaning use of the budget process for this policy is all the more unnecessary.
AB 103	Prohibits counties from leasing out additional county jail beds to federal law enforcement agencies	This policy interferes with local county decisions in order to enact Sacramento Democrats' immigration policies.
AB 119	Authorizes the release of public employees' personal email addresses to union officials, even if those employees do not belong to the union. Requires public employees to sit through a union presentation at new employee orientation.	These changes had been proposed in previous non-budget policy bills but had not passed (AB 2843 in 2016; AB 52 in 2017).

Abusing the Budget for Election Purposes. In the case of the recall election policy, which changes the rules for recall petition signatures partway through an ongoing recall process, the specific legislation appeared to the public only three days before the Legislature enacted it. (Without voters' enactment in 2016 of Proposition 54, which requires bills to be publicly available in their final form for 72 hours prior to enactment, it is likely that the legislation would not even have been available that long.) Abuse of the Proposition 25 rules allowed the majority party to enact these changes immediately with only a simple majority vote, thus applying them to an ongoing recall process.

If trailer bills were truly only used to enact policies necessary for the budget, as intended, Sacramento Democrats would have needed a two-thirds majority vote to approve the election changes in time to affect the ongoing recall. In fact, the bill that enacted the recall changes (SB 96) did not reach the two-thirds level. Senate Republicans believe that to keep faith with voters, Proposition 25's rules should be applied for the stated purpose of enacting the budget on time, not to jam unrelated policies through at the eleventh hour to serve special interests.

Health

Key Points

- **Tobacco Tax Bait-and-Switch Continues.** The 2017-18 budget continues to transgress voter intent by using more than half of the tobacco taxes to plug budget holes instead of expanding access to dental and health care.
- **Skilled Nursing Facility Union Handout.** The budget imposes new minimum staff ratios at skilled nursing facilities that will create costly and arbitrary staffing patterns unrelated to the needs of the patients.
- **Full Adult Dental and Optical Benefits Restored.** The 2017-18 budget restores full adult dental benefits (in 2018) and optical benefits (in 2020) that were cut from the Medi-Cal program since 2009.

Tobacco Tax Bait-and-Switch Enacted. Despite extensive negotiations with stakeholders, the 2017-18 budget plans to use $711 million in Proposition 56 tobacco taxes to backfill General Fund expenditures in Medi-Cal, thus plugging a budget hole instead of increasing access to care. Fortunately, $465 million of the tobacco tax revenues can be used to attract and retain Medi-Cal and Denti-Cal providers through supplemental provider payments for physician and dental services. This is an improvement over the Governor's January proposal, which would have redirected all discretionary tobacco tax revenue to replace General Fund, but the budget continues to undermine what voters were told, namely that *all* of the revenue earmarked for Medi-Cal would be used to improve access to needed services.

Costly New Nursing Home Staffing Ratios. The 2017-18 budget includes a requirement that skilled nursing facilities institute a 2.4 hours per patient per day certified nursing assistant (CNA) staffing ratio, plus a higher minimum total staffing ratio of 3.5 hours per patient per day. This was a last-minute request by public employee unions that the nursing facility representatives stated will be financially "devastating" as it will mandate the hiring of more than 2,000 CNAs by July 1, 2018 regardless of facility need, and despite the fact that there is already a shortage of CNAs. This policy was rejected in past legislation AB 2079 (Calderon, 2016) and SB 779 (Hall, 2015).

Restoration of Full Adult-Dental and Optical Benefits. The 2017-18 budget includes $34.8 million for the restoration of full adult dental benefits in the Denti-Cal program beginning January 1, 2018. It also restores Medi-Cal optical services beginning on January 1, 2020. During the recession, the state eliminated several optional Medi-Cal benefits, including adult dental services, acupuncture, audiology, speech therapy, chiropractic services, optician and optical lab services, podiatric services, psychology services, and incontinence creams and washes. Senate Republicans previously sought to restore optical benefits in 2016 (SB 1361, Nielsen), but our efforts were blocked by Democrats at the time. Senate Republicans would restore these benefits sooner than 2020, but nonetheless applaud the action to schedule their restoration.

Federal Medicaid Funds Assumed to Continue. The 2017-18 budget does not include any adjustments to plan for possible reductions in federal Medicaid funding to California in future years, despite a recent California Department of Health Care Services analysis that claims federal reforms could equate to $3 billion in new annual costs in 2020 and up to $30 billion annually by 2027. While President Trump has yet to sign a healthcare reform bill, both the measure passed by the U.S. House of Representatives and proposals discussed by the U.S. Senate would result in a shift of funding responsibility from the federal government to California. Predicting that a federal correction was inevitable, California's Senate Republicans warned of Obamacare's financial risks, namely the addition of 5 million new individuals to Medi-Cal in just three years at a cost of more than $20 billion annually. Senate Republicans believe that California should engage constructively with its federal partners to ensure our residents' needs are met, but should also begin prioritizing its spending to account for new healthcare responsibilities.

Continuation of the Coordinated Care Initiative (CCI). The 2017-18 budget continues the non-In Home Supportive Services (IHSS) portions of CCI in seven counties (Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Mateo, and Santa Clara). Specifically, it continues Cal MediConnect, the duals demonstration project where individuals that are dually eligible for Medicare and Medi-Cal can enroll in one Medi-Cal managed care plan. It also continues the integration of long-term services and supports into Medi-Cal managed care for dual eligibles.

Medi-Cal Benefits for Undocumented Minors, Not Young Adults. The budget reflects full-year costs of $331 million General Fund for this policy created by SB 75 (Lara, 2015) to provide full-scope Medi-Cal coverage to undocumented minors under age 19. A proposal urged by advocates to extend this coverage up through age 25 was not included in the budget package.

Funds for Primary Care Workforce Training. The budget includes $33.3 million for new primary care residency slots and student loan repayments. This is a restoration of the Governor's proposed January cut to the Song Brown program within the Office of Statewide Health Planning and Development. $66 million will also be provided over the following two fiscal years.

Healthcare Facilities Construction Financing Funds Shifted to Clinic Operations. The 2017-18 budget permits the existing funding within the "HELP II" program under the State Treasurer's Office to be used for a new Lifeline Grant Program, which would fund the operations costs of non-profit small or rural health centers in critical service areas, or those centers at risk of losing federal funding. Current law states that HELP II funding can only be allocated to the expansion of facilities, not operations. The budget transfers $20 million for these operations grants. Although not stated specifically in the budget package, State Treasurer John Chiang has signaled in a press release that he intends for this funding to assist Planned Parenthood clinics.

Children's Mental Health Crisis Service Grants. The 2017-18 budget includes $28 million in funding for grants to local governments to increase the number of facilities, crisis services, and triage personnel to assist youth under the age of 21.

Community Infrastructure Grants. The budget includes $67.5 million General Fund for grants to cities or counties to promote public safety diversion by increasing the number of mental health, substance abuse, and trauma-related service facilities.

New Federal Funds for Opioid Epidemic. The 2017-18 budget includes an increase of $44.7 million in federal funding to reflect the receipt of a federal Opioid State Targeted Response grant. This funding will be directed to participating physicians for increased medication assisted treatment for individuals with substance use disorders.

Creation of Three New Health Programs. The 2017-18 budget created three new health-related programs: (1) the Richard Paul Hemann Parkinson's Disease Program, which would require the Department of Public Health to collect data on Parkinson's disease in California, and beginning on July 1, 2018, would require certain health care providers to report each case of Parkinson's disease; (2) the Diabetes Prevention Program within Medi-Cal designed to prevent or delay the onset of type 2 diabetes through lifestyle changes; and (3) a medically-tailored, home delivered meal program available to 2,500 Medi-Cal beneficiaries with traditionally high-cost health conditions.

Human Services

Key Points

- **In Home Supportive Services (IHSS) County Costs Reduced.** The 2017-18 budget reduces the impact of the state-to-counties cost shift of the IHSS program, but it remains a shameless strategy for the state to ramp up IHSS program costs through wage hikes and then pass the buck back to counties.
- **Deportation Defense Funding for the Anti-Trump "Resistance".** The 2017-18 budget spends $45 million to provide deportation legal defense services to undocumented individuals residing in or formerly residing in California.
- **Creates CalWORKs Education Incentive Grants.** The 2017-18 budget includes $4 million to award education achievement grants to CalWORKs recipients.

IHSS Cost Shift to Counties Continues, Though at Lower Level. In January, the Governor proposed shifting $623 million in IHSS program costs to the counties. The 2017-18 budget made several substantial changes that lower the cost to counties to $141 million initially with annual costs ranging from $129 million to $251 million thereafter. While this partial mitigation is an improvement from January, the dramatic cost increases to IHSS over the past five years were predictable effects of state and federal wage and overtime policy changes. It remains a cynical and brazen strategy for the state to ramp up IHSS program costs and then pass the buck to counties. In fact, the budget requires that the state and the counties revisit this new funding structure as part of the development of the 2019-20 Governor's budget.

Specifically, the 2017-18 budget:

- Contributes General Fund at declining levels to offset counties' additional IHSS costs: $400 million in 2017-18, $330 million in 2018-19, $200 million in 2019-20, and $150 million in subsequent years.
- Reprioritizes local Vehicle License Fee (VLF) funds given to the counties through realignment. Specifically, the plan redirects the VLF growth from the county health and mental health subaccounts to fund the IHSS program costs. This change reduces local control and will divert county funds from mental health services.
- Modifies the county maintenance-of-effort (MOE) to make counties responsible for a sliding share of non-federal IHSS costs. Specifically, the proposal sets a new baseline obligation on the counties but caps the counties' growth of this obligation based on realignment revenue collections each year. Better revenue years would mean greater county share of IHSS program costs, while bad revenue years would result in the state covering all of the IHSS program growth costs.
- Authorizes counties to access a new low-interest loan program to help hardship counties pay for their share.
- Continues the January proposal to return IHSS collective bargaining to counties, but proposes that the state participation in wage increases ends at $1.10 above the hourly minimum wage. This state participation cap would continue to rise with inflation once the minimum wage reaches $15 per hour. For counties currently at or exceeding the current state cap of $12.10, the state would agree to participate at its 65 percent share of costs up to a 10 percent increase in wages and benefits over three years. This means that the state must pay for the impact of the

state-imposed minimum wage increases but stops its cost participation if union bargaining agreements go beyond the 10 percent.

- Revises county/IHSS worker union mediation procedures if an impasse arises.

Deportation Defense Services. The budget includes $45 million for the Department of Social Service to award legal services grants to non-profit entities engaged in deportation defense proceedings on behalf undocumented individuals *residing in, or formerly residing in* California. Although the funding for legal services supposedly is not to be used for undocumented individuals convicted of or appealing a conviction of "violent" or "serious" felonies, loopholes in the law will allow undocumented individuals convicted of some dangerous crimes to obtain the state-funded legal services. Some of these crimes include human trafficking, child abuse, stalking, solicitation to commit murder or a designated sexual assault, taking a hostage to prevent arrest or to use as a shield, felony elder abuse, and possession/distribution of child pornography. Democrats could have ensured that individuals convicted of these crimes are not eligible for assistance, but they chose not to provide that protection.

CalWORKs Education Incentive Grants. The 2017-18 budget includes $4 million for one-time grants of $500 for each CalWORKs recipient that earns a high school diploma and a one-time $1,000 stipend for CalWORKs recipients that enroll in an associate's degree, bachelor's degree, or career technical education program. Given that a barrier to mobility exists for the majority of CalWORKs recipients who do not have a high school education, this policy will provide a tangible reward for accomplishing a goal that will help these recipients after they exit the CalWORKs program. This proposal originated as a Republican policy bill (AB 227, Mayes) prior to its eventual inclusion in the budget.

Additional County Funding for CalWORKs Administration. The budget adds $109 million in additional General Fund to the $1.6 billion county "Single Allocation," which funds CalWORKs administration and employment services. The administration and the counties plan on working out a new funding methodology in 2018.

Emergency Foster Youth Child Care. The 2017-18 budget appropriates $15.5 million to create a program that would allocate an immediate child care voucher for families who would need child care in order to take in foster children. It would also create child care navigators to provide these families with support in navigating the state's child care system. Senate Republicans support efforts like this to help families better care for foster children.

Housing and Disability Income Advocacy Program. The budget includes $45 million General Fund for the Housing and Disability Income Advocacy program, which incentivizes local governments to boost outreach efforts and advocacy to get more people enrolled in the Supplemental Security Income/State Supplementary Payment (SSI/SSP) program.

Food Bank Assistance Program. The budget includes $8 million General Fund in 2017-18 and $6 million ongoing for the CalFood program which provides funding assistance to food banks.

CalFresh Drinking Water Pilot Program. The budget creates a three-year pilot program to permit individuals in areas with low-standard drinking water to obtain additional CalFresh (food stamp) benefits for the purchase of bottled water. The budget appropriates $5 million over the three year period.

Restores Funding for Three Central Valley Independent Living Centers. The budget adds back $705,000 General Fund to restore three budget cuts to the Independent Living Center of Kern County, the Disability Resource Agency for Independent Living (Amador, Calaveras, Tuolumne, Mariposa, Stanislaus, and San Joaquin Counties), and Placer Independent Living Resources. These facilities provide a variety of services to individuals with disabilities of all ages.

Funding for Long-Term Care Ombudsman. The budget includes one-time funding of $1 million for the state's Long-Term Care Ombudsman Program, which oversees long-term care facilities and resolves complaints made by care facility residents.

Developmental Services

Overall Enrollment Grows. The Department of Developmental Services (DDS) estimates it will serve over 318,000 developmentally disabled Californians in 2017-18 in community settings and institutional developmental centers (DCs). While the vast majority of these individuals receive community-based services, the final budget estimates that DCs will serve 493 residents at the end of 2017-18, a decline of 298 residents (38 percent). In contrast, the number of individuals served in community settings is projected to grow to nearly 318,000 in 2017-18, an increase of 4.7 percent over the 2016-17 caseload.

Some Improvements for Community Services. The enacted budget includes $6.4 billion total funds ($3.8 billion General Fund) for Community Services in 2017-18, an increase of $335 million total funds (5.5 percent) over the revised 2016-17 budget. The majority of the increase is due to growing program enrollment. Significant policy changes include:

- ***"Safety Net Plan" Implementation.*** $19 million to expand community-based acute crisis services as part of the Administration's Safety Net Plan, including by establishing two state-operated mobile crisis teams and relocating or renovating four crisis services homes (two each in Northern and Southern California).
- ***Respite Benefit Restoration.*** $5.6 million to repeal limits placed on respite services in 2009 as part of budget-balancing reductions. This is an important policy restoration to help families continue to care for disabled members. Senate Republicans believe this should have been corrected several years ago when the budget began recovering.

In 2016 the state provided a package of sorely overdue funds intended to shore up the community services system. However, service providers in some areas of the system continue to struggle, particularly in counties that have enacted local minimum wages higher than the state requirement. The budget establishes a working group of providers and consumers to explore ways to expedite provider payment adjustments in some circumstances. ***Senate Republicans continue to call for California to fully honor its commitment to the original vision of the Lanterman Act and ensure that developmentally disabled people can thrive in a sustainable community environment.***

Developmental Center (DC) Closure Plans Continue as Costs Per Resident Rise. The enacted budget includes DC funding of $466 million ($348 million General Fund) for 2017-18, which is lower than the revised 2016-17 budget by $74 million ($28 million General Fund) or 16 percent. The proposed funding declines by less than the population on a percentage basis, so the ***average cost per DC resident would increase from $615,000 (total funds) for 2016-17 to $724,000 in 2017-18, an increase of 17.7 percent.*** This is far higher than the cost to serve similar individuals in community settings.

The enacted budget continues the process begun in 2015-16 of closing the three remaining DCs (with the exception of the secured area at Porterville DC). The target dates for closure have not been changed: December 31, 2018, for Sonoma and December 31, 2021, for Fairview and Porterville DCs. In light of the skyrocketing costs per DC resident noted above, Senate Republicans will monitor the closure process to ensure that spending is truly focused on disabled residents' needs, and not on paying for unnecessary staff or administration costs.

Education

Key Points

- **Proposition 98 Spending Reaches New High.** The Proposition 98 guarantee of funding for K-14 education grows in 2017-18 by over $3.1 billion, from $71.4 billion to $74.5 billion.
- **Career Technical Education Phase-Out Continues**. Dedicated funding for K-12 career technical education falls by $100 million, potentially leaving high school graduates less prepared to join the workforce.
- **Child Care Expansion Proceeds.** Last year's multi-year child care expansion continues with an augmentation of almost $300 million to increase payment rates and available slots.

Proposition 98 education funding sets new record. The chart below displays 2017-18 Proposition 98 funding for K-14 education, which reaches an all-time high of $74.5 billion in 2017-18, over $3.1 billion above the revised 2016-17 level. Average per pupil K-12 spending is expected to be $11,051,[1] and the Proposition 98 maintenance factor obligation is expected to fall from about $1.4 billion at the end of 2016-17 to $900 million by the end of 2017-18.[2]

Proposition 98 Funding at 2017-18 Budget Act

Source: Legislative Analyst's Office

($ in millions)	2015-16	2016-17	2017-18
K-12 education [1/]			
General Fund	$43,958	$44,930	$46,886
Local property tax revenue	$17,047	$18,133	$18,981
K-12 subtotal	$61,005	$63,063	$65,867
California Community Colleges [2/]			
General Fund	$5,384	$5,473	$5,654
Local property tax revenue	$2,631	$2,768	$2,911
CCC subtotal	$8,016	$8,241	$8,565
Other Agencies	$82	$85	$91
Total Proposition 98 [3/]	$69,103	$71,389	$74,523
General Fund	$49,425	$50,488	$52,631
Local property tax revenue	$19,678	$20,901	$21,892

[1/] K-12 education totals include state preschool and related 'wraparound care'

[2/] CCC display includes $500m for adult ed which can flow to any K-14 provider (not restricted to CCCs)

[3/] Any discrepancies are due to rounding

[1] Per-pupil spending varies widely across the state under the Local Control Funding Formula, which provides substantially more funding to districts with high proportions of low-income students; $11,051 is an estimate of *average* per-pupil spending.

[2] 2017-18 is expected to be a Test 2 year, meaning that the operative funding formula grows the previous year's funding level by the same rate that the state's per-capita personal income and student attendance are expected to grow. The maintenance factor obligation is the amount by which Proposition 98 funding must eventually be increased to bring it to the long-term Test 2 level.

Local Control Funding Formula (LCFF) grows to 97% of target level. The state's local control funding formula for K-12 schools will enter its fifth year of implementation in 2017-18. The 2017 Budget Act increases locally-controlled funding by $1.4 billion, to about $57.3 billion, or 97% of the statewide target level of $59 billion.[3] The Department of Finance continues to expect that full funding will be reached by 2020-21. Senate Republicans have supported full funding of the LCFF because it provides greater flexibility for local school districts to control their own budgets.

One-time discretionary funds reduce mandate debt. In addition to its ongoing LCFF augmentation, the 2017-18 budget includes about $877 million in one-time funding, to be allocated on a per-student basis for any local educational priority. To the extent that schools have unpaid mandate claims, the funds will be scored in satisfaction of those claims, which is consistent with Senate Republicans' support for the extinguishment of the state's debt as a budgetary priority.

Career technical education (CTE) funding continues to fall. In an effort to ensure that K-12 CTE programs continued after a two-year maintenance-of-effort requirement ended in June 2015, the 2015-16 budget included a new transitional CTE incentive grant program funded at $900 million over three years ($400 million in year one, $300 million in year two, $200 million in year three, and nothing thereafter). Unfortunately, the 2017-18 budget allows the current-law $100 million reduction (from $300 million to $200 million) to proceed. Senate Republicans have opposed these reductions and argued for restoration of ongoing funding for CTE, which is essential to ensure that high school graduates who wish to join the workforce leave school with the skills to do so. While local educational agencies are free to use their flexible funding to support CTE, the unfortunate reality is that without dedicated funding, CTE will continue to shrivel as influential labor unions force the bulk of new resources onto the bargaining table.

Child care funding grows. The 2017-18 budget plan continues the multi-year child care expansion negotiated as part of the 2016 Budget Act with General Fund augmentations of almost $300 million to increase reimbursement rates and slots for child care, state preschool, and after school programs. Total funding from all sources for these programs will approach $4 billion. Child care is a necessary service for low-income parents who want to work, but the bulk of any funding augmentation should be used to create new slots to get families off waiting lists rather than to increase the state's cost per slot.

California Community Colleges (CCCs). As the chart above shows, the 2017 Budget Act increases the colleges' share of 2017-18 Proposition 98 funding by $324 million from the revised 2016-17 level, to almost $8.6 billion.[4] The additional funds, along with existing funds freed up by lower-than-anticipated enrollment growth, will support a variety of augmentations, most notably including:

- $184 million for an unallocated base funding increase
- $150 million for a Guided Pathways program to reorganize colleges' student services, instruction, and administrative practices to streamline students' paths to degrees and certificates
- $102 million for a 1.58 percent cost-of-living adjustment to apportionments and selected categorical programs
- $77 million for deferred maintenance and instructional equipment.[5]
- $58 million for one percent enrollment growth
- $25 million to increase Full Time Student Success Grants from $650 to $1,000 per year

[3] LCFF targets grow annually by a cost-of-living adjustment (1.56% in 2017-18).
[4] CCC funding includes $500 million for adult education, which can flow to any K-14 education agency.
[5] In addition, to balance one-time and ongoing fund sources, the budget shifts $86 million in one-time funds from this program to the Guided Pathways Program, and the same amount of ongoing funds from Guided Pathways into this program.

- $25 million for Completion Grants of $2,000 for needy students on track to graduate in two years
- $20 million in one-time funding for Innovation Awards
- $17 million in Proposition 51 bond funds to begin 15 capital facilities projects
- $10 million for system-wide access to the Online Education Initiative's learning management system
- $12 million, including $7 million in one-time funding, for veterans' resource centers
- $5 million for part-time faculty office hours
- $4.5 million in one-time funding for mental health services

Senate Republicans have been strong supporters of the state's community colleges, as they are efficient providers of early college coursework and career technical education that prepares students for jobs.

UC, CSU, and Student Financial Aid

Key Points

- **Tuition Rises at the University of California (UC) and the California State University (CSU).** The 2017-18 budget plan acknowledges new revenue generated by the UC Regents' decision to raise tuition by 2.5 percent and the CSU Trustees' decision to raise it by five percent. A decade of weak General Fund support has contributed to these decisions.
- **Middle Class Scholarships Continue.** The budget plan rejects the Governor's proposal to phase out middle class scholarships, instead continuing them as envisioned under current law.
- **Bait and Switch for Medical Education Approved**. The budget plan uses $50 million in Proposition 56 tobacco tax funding to replace existing funding for UC medical education, rather than expand it as the voters intended.

Tuition Hikes Follow Years of Stagnant State Support. The chart below displays expected core instructional funding for UC and CSU and compares the enacted budget to 2007-08, the last year prior to the recession.

UC & CSU Funding at 2017-18 Budget Act

$ in millions

University of California	2007-08	2016-17	2017-18	Δ from 07-08 to 17-18
General Fund	$3,257	$3,541	$3,543	9%
Resident tuition & fees	$1,622	$3,417	$3,573	120%
Non-resident tuition & fees	248	976	1,050	323%
Lottery & other misc instructional funds	355	345	396	12%
Total core instructional funds	$5,482	$8,279	$8,562	56%
General Fund as % of total instructional funds	59%	43%	41%	
Tuition & fees as % of total instructional funds	34%	53%	54%	
Enrollment (full-time equivalent)	221,313	264,633	268,633	21%

California State University	2007-08	2016-17	2017-18	Δ from 07-08 to 17-18
General Fund	$2,971	$3,589	$3,743	26%
Resident tuition & fees	$1,329	$2,767	$2,902	118%
Non-resident tuition & fees	129	196	213	65%
Lottery	58	55	55	-5%
Total core instructional funds	$4,487	$6,607	$6,913	54%
General Fund as % of total instructional funds	66%	54%	54%	
Tuition & fees as % of total instructional funds	32%	45%	45%	
Enrollment (full-time equivalent)	368,621	400,055	402,542	9%

Notes: Amounts not adjusted for inflation. Any discrepancies due to rounding.

Source: Legislative Analyst's Office

Notably, over the past decade of largely Democrat management of the state budget, General Fund support for UC has increased by only about $286 million (nine percent) beyond the amount provided in 2007-08. In contrast, the state has provided over $2 billion in pay increases to state workers over the same period, and overall General Fund spending has increased by over $21 billion. UC's *total* instructional funding has increased by almost $3.1 billion since 2007-08, largely due to tuition hikes in

2008-09 through 2011-12, but **if Democrats made UC a higher budgetary priority, there would be substantially less pressure for the tuition increases that make it harder for middle class students to afford college.**

UC Raises Tuition While Hiding Money; Legislature Responds With Reforms. In January 2017, the UC Regents voted to increase tuition by 2.5 percent, from $11,220 to $11,502 per year, beginning in the fall 2017 term. The fee hike will generate $74 million in new revenue, of which $26 million will be diverted to student financial aid and $48 million used for other purposes. Shortly thereafter, in April 2017, the State Auditor released a scathing audit of the UC Office of the President (UCOP).[6] Senate Republicans and others expressed serious concerns with its findings that UCOP maintained a $175 million fund out of sight of the Regents and the public, overcompensated staff, and spent lavishly on parties, dinners, and travel. In response to the Auditor's findings, the enacted budget establishes a separate line item for the UCOP to enhance transparency and withholds $50 million in General Fund support until UC completes several reforms, including:

- disclosing all revenues and expenditures
- addressing the audit's recommendations
- stopping its policy of providing supplemental retirement payments to new senior management employees, and
- complying with the terms of its 2015 budget agreement with the Governor to increase admission of transfer students and complete two activity-based costing pilot programs.

Other UC Budget Adjustments. In addition to its recognition of the new tuition revenue, the budget plan makes several other adjustments to UC's funding, most notably:

- $169 million to pay down unfunded pension liability[7]
- $131 million for an unrestricted base funding increase
- $5 million to enroll 500 additional graduate students
- $2.5 million in one-time funding to encourage "hunger free" campuses
- $2 million in one-time funding for equal employment opportunity programs to enhance faculty diversity
- $2 million for UC Davis' marine mammal stranding networks and $100,000 for whale disentanglement activities

Bait and Switch for UC Medical Education. The 2017 Budget Act continues to include a fund swap that replaces $50 million in existing General Fund support for medical education with a like amount of new Proposition 56 tobacco tax revenue. Senate Republicans view this fund swap as an affront to the voters who were led to believe that this tax hike would increase funding for medical education in California. Instead, Sacramento Democrats have decided to use the funds to plug budget holes and make room for their other priorities.

CSU Tuition Also Rises. For CSU, the 2017-18 budget plan provides General Fund support of about $3.7 billion, or about $732 million above the amount provided in 2007-08. CSU's *total* funding has increased by about $2.4 billion since then, largely due to tuition hikes in 2008-09 through 2011-12. Like

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[6] *The University of California Office of the President: It Failed to Disclose Millions in Surplus Funds, and its Budget Practices are Misleading.* https://www.bsa.ca.gov/pdfs/reports/2016-130.pdf

[7] This payment is made from Proposition 2 Rainy Day funds and is the final installment of a total of $436 million in one-time funds provided over a three-year period.

UC, CSU is increasing its system-wide undergraduate tuition, which will rise by five percent in fall 2017 (from $5,472 to $5,742), generating about $119 million in new revenue. CSU plans to divert about $40 million to student financial aid, leaving about $79 million available for other uses. These additional funds, along with $154 million in new General Fund support and $109 million in existing funds freed up for new uses, will support a variety of adjustments to CSU's budget, most notably:

- $157 million for an unrestricted base funding increase
- $60 million for rising pension and retiree health costs
- $20 million to increase enrollment by 2,487 full time equivalent students
- $12.5 million for CSU's graduation initiative, which seeks to increase graduation rates while narrowing achievement gaps
- $3 million in one-time funding for expansion of CSU San Bernardino's Palm Desert campus
- $2.5 million in one-time funding to encourage "hunger free" campuses
- $2 million in one-time funding to create or expand equal employment opportunity programs

Student Financial Aid Hits Record High. The 2017 Budget Act increases General Fund support for student financial aid to over $2.2 billion, which includes:

- $153 million for Cal Grant growth, with $49 million offsetting the higher cost of UC and CSU tuition.
- $8 million to maintain the maximum Cal Grant for students attending private, non-profit universities (such as Stanford, USC, or Pepperdine) at $9,084 for one year rather than letting it fall to $8,056 as existing law would have required. Senate Republicans have supported a *permanent* repeal of the statutory reduction to these awards, as the recession that prompted the reduction has ended, and private non-profit universities provide excellent value to the taxpayer by relieving pressure on UC and CSU campuses that have no room to grow.
- $1.7 million to double the Cal Grant C books and supplies award to $1,094 per year.

Middle Class Scholarships Continue. The final 2017-18 budget plan rejects the Governor's January proposal to phase out the Middle Class Scholarship Program. The program will continue as authorized in statute, with expected costs of $96 million. Senate Republicans opposed the phase-out, as this is one of the few state programs established to benefit the middle class.

Public Safety and Judiciary

Key Points

- **Underfunding Courts Limits Access to Justice.** The budget continues to underfund the trial courts by more than $400 million, making it difficult for many Californians to find justice.
- **Governor, Legislative Democrats Complicit in Attorney General's Misuse of Funds.** The Attorney General will use taxpayer funds and revenues from fees paid by lawful gun owners to advance the ruling party's political agenda with respect to gun control, immigration, healthcare, and the environment.
- **Proposition 57 Perils Loom.** A legal challenge to the Department of Corrections and Rehabilitation's (CDCR's) regulations implementing Proposition 57 of 2016 could put unrehabilitated sex offenders back on the streets. With no resources for data collection and analysis, the potentially negative impacts on public safety may never be fully understood.

Judicial Branch

The budget provides $3.6 billion ($1.7 billion General Fund) to support the Judicial Branch, including approximately $2.8 billion ($1.3 billion General Fund) for the trial courts. These spending levels remain virtually unchanged from 2016-17 budget levels.

Underfunding of Trial Courts Continues. The Judicial Council conducts regular assessments of judicial needs and trial court workload. These assessments have shown a consistent underfunding of the trial courts for the last decade. Although modest progress has been made in recent years toward closing the gap, the trial courts remain underfunded by more than $400 million. In a statement released after the Budget Act was signed, the Chief Justice said, "…I remain disappointed that our underfunded court system did not receive more help. Chronic underfunding of the courts unfairly affects members of the public seeking their day in court. Trial courts receive a little more than a penny for every General Fund tax dollar, and in the past the judicial branch has had funds swept to support the state budget during times of crisis. Now the courts have an ongoing funding crisis, new laws are added annually, there are more complex cases, but there is no stable funding solution for the judicial branch and the people we all serve."

The enacted budget reflects the priorities of the Governor and legislative Democrats. Clearly, they place a higher value on public employee union raises, services for undocumented immigrants, and resistance to federal administrative policy changes than ensuring access to justice for all Californians. Senate Republicans believe additional funds should be provided to enable the trial courts to fulfill their role in keeping our communities safe.

Elimination of Driver's License Suspension Compounds Funding Problem. The budget deletes the authority of the court to suspend a person's driving privileges for failing to pay court-ordered debt. Proponents of this change have argued that suspension for failure to pay is often counterproductive because it can inhibit a person's ability to work, which in turn can cause the person's financial situation to further deteriorate, decreasing the likelihood that he or she will ever be able to pay the debt. While there may be merit to this argument in some cases, the budget fails to backfill revenues that will be lost due to reduced effectiveness of collections efforts. The loss of revenue compounds the trial court funding shortfall discussed above. Moreover, this policy change, which was enacted in a budget trailer bill, was not necessary to implement the budget (the purported standard for inclusion of policy changes in a trailer bill). To the contrary, it actually makes the budget situation worse.

Department of Justice (DOJ)

Funding "the Resistance" is Counterproductive. The budget includes $13 million General Fund over the next two years for the Attorney General to continue his efforts to derail recent federal policy changes. The proposed funding will pay for 19 attorneys and supporting staff who will look for ways to challenge the constitutionality of executive actions related to immigration, healthcare, and the environment. As the ruling party misappropriates state tax dollars to meddle in federal policymaking, Senate Republicans will continue to look for ways to work with the federal government to maximize value for Californians.

Legally Questionable Gun Control Moves Ahead Full Steam. The budget includes $2.6 million in special funds for the DOJ to implement 2016 legislation that expanded the state's assault weapons ban to include so-called "bullet-button" firearms. Legal challenges to the DOJ's implementing regulations made it clear that the Department would not be ready to accept registration applications in time for legal assault weapon owners to comply with the January 1, 2018 registration deadline. This fact did not deter the DOJ or legislative Democrats. They simply passed a trailer bill (AB 103) extending the registration deadline by six months and included a provision in the Budget Act making the $2.6 million 2017-18 appropriation available through June 30, 2019. Senate Republicans believe the focus should be on understanding and mitigating the circumstances that lead people to commit violent acts, rather than restricting the constitutional rights of law-abiding citizens.

Department of Corrections and Rehabilitation (CDCR)

The enacted budget sets 2017-18 General Fund spending for CDCR at $11.1 billion, which is approximately $807 million above Budget Act of 2016 spending levels. The spending increase is comprised mostly of the following:

- Employee compensation and benefit cost increases ($389 million)
- A permanent transfer of responsibility for in-prison psychiatric programs from the Department of State Hospitals (DSH) to CDCR ($254 million, with a corresponding decrease to the DSH budget)
- Roof replacement projects at facilities impacted by the unseasonably wet winter ($35 million)
- Increased debt service costs associated with recent prison construction projects ($26 million)
- Increased pharmaceutical costs ($20 million)

Proposition 57 – Lawsuit Could Increase Prison Savings, Public Safety Threat. Proposition 57 (2016) accelerated parole eligibility, authorized CDCR to increase sentence credits for nonviolent felons, and eliminated direct filing of juvenile cases in adult court. As a result, the enacted budget reflects estimated savings in 2017-18 of $38.8 million from a projected decrease of 2,675 in the average daily population (ADP) of prison inmates. The decrease in ADP is expected to grow to 11,500 and the resulting annual savings to $186 million by 2020-21.

The emergency regulations CDCR developed to implement Proposition 57 define "nonviolent offender". The definition excludes offenders who are condemned, serving a life term, serving a term for a violent felony as enumerated in Section 667.5 of the Penal Code, or required to register as a sex offender. Unfortunately, on April 27, 2017, the Alliance for Constitutional Sex Offense Laws (a group advocating for the rights of registered sex offenders) filed suit against CDCR over the Proposition 57 regulations.

The lawsuit alleges that the exclusion of sex offenders contradicts the intent of the voters and asks the court to declare CDCR's definition of "nonviolent offender" invalid and void.

If the plaintiffs were to prevail, more convicted felons would be eligible for enhanced credits and early parole consideration, which would ultimately result in further ADP reductions and thus, greater savings. More significantly, it would pose a threat to public safety because sex offenders and possibly anyone else serving a primary term for an offense that is not on the list of violent felonies could become eligible for early release, regardless of whether they have been rehabilitated and without respect to their risk of reoffending. Senate Republicans believe these factors should be of primary importance when determining whether an offender is ready for release back into the community.

Proposition 57 – Analysis Component Still Missing. As CDCR implements Proposition 57, it will be critical to carefully monitor the public safety impacts and make adjustments as needed. Unfortunately, as was the case with the Governor's January budget and May Revision, the enacted budget fails to provide resources for the kind of robust data collection and analysis necessary to accurately assess Proposition 57 outcomes. This will mean that many questions about the initiative's effects will go unanswered and the state's ability to take corrective action will be limited.

Measuring the effects of policy changes is essential to creating a responsible government that respects the voters. Regrettably, Proposition 57, like other recent public safety reforms (such as the 2011 public safety realignment, Proposition 36, and Proposition 47), was not designed with the goal of assessment in mind, and the Administration and legislative Democrats missed an opportunity to correct that omission during the early stages of implementation. Senate Republicans will continue to call for responsible data collection and assessment for Proposition 57, as well as for other major policy changes.

Transfer of Psychiatric Treatment Programs Moves Forward. The enacted budget transfers $254 million General Fund and 1,978 positions from DSH's budget to CDCR's to reflect the shift of responsibility for all prison-based psychiatric care to CDCR. The shift is expected to improve efficiency and decrease the amount of time that inmate-patients who are part of the *Coleman v. Brown* class action spend waiting for referral to in-patient mental health treatment programs. Excessive wait times have been an ongoing concern to the *Coleman* court. The move highlights the progress CDCR has made in its ability to provide constitutionally adequate mental health care and could hasten the end of federal court oversight of prison mental health care if successful.

Transportation

Key Points

- **Gas Tax Bait-and-Switch.** The budget allocates $2.8 billion from the new gas and car taxes (SB 1), including a bait-and-switch by using hundreds of millions for non-road purposes such as park maintenance and operations.
- **High-Speed Rail Still Searching for Funds.** The budget includes $1.1 billion to continue to build the high-speed rail system, despite a $42.3 billion funding gap.
- **New Costs to Californians for State's ID Card Neglect.** Following years of delays, the budget contains new costs to implement the federal "Real ID" licenses and identification cards.

Transportation Tax Bait-and-Switch Funds Parks, Other Non-Road Projects. With the increased gas, diesel, and vehicle taxes approved in SB1 expected to add $2.8 billion to state coffers in the budget year, the budget spends the amounts shown in the chart below.

2017-18 New Gas and Car Tax Spending
(Dollars in Millions)

	Program	*Amount*
Local Allocations	Local Streets and Roads	$445.4
	Transit and Intercity Rail Capital Program	$330.0
	State Transit Assistance	$305.1
	Local Partnership Program	$200.0
	Active Transportation Program	$100.0
	Local Planning Grants	$25.0
	Total:	**$1,405.5**
State Allocations	SHOPP/Maintenance	$445.4
	Bridges and Culverts	$400.0
	Congested Corridors	$250.0
	Trade Corridor Enhancement	$199.8
	Department of Parks and Recreation	$54.3
	Freeway Service Patrol	$25.0
	Department of Food and Agriculture	$17.3
	CSU and UC Research	$7.0
	Workforce Development Board	$5.0
	Total:	**$1,403.8**
Administration	State Controller's Office	$0.1
	California Transportation Commission	$0.2
	Department of Motor Vehicles	$3.8
	Total:	**$4.1**
Revenue	Transportation Improvement Fee	$727.0
	Gasoline Excise Tax	$1,251.5
	Diesel Excise Tax	$399.7
	Diesel Sales Tax	$200.1
	General Fund Loan Repayment	$235.0
	Total:	**$2,813.3**

Source: Department of Finance

Unfortunately, Democrats have once again misled the public by advertising that the increased taxes and fees were needed to fix California's crumbling roads and highways, while failing to **explain that only about 5 percent of the taxes would expand road capacity, despite the clogged roads and highways that force Californians to waste countless hours stuck in traffic.** Additionally, Democrats failed to mention that the taxes would also pay for other Democrat priorities that have nothing to do with roads.

Not a penny of new tax revenue has been collected, and $873 million is already allocated to non-road uses like public transit, walking and biking paths, local planning grant programs, state and local parks, and university research programs. As reported by the media, transit ridership in California has seen serious declines. Los Angeles Metropolitan Transportation Authority has seen a decrease of more than 10 percent in boardings over that last decade, including a 6 percent drop in 2016. Bay Area Rapid Transit (BART) reported ridership for the first half of the 2016-17 fiscal year at 5.2 percent below projections. Still, the budget invests $635 million in local transit programs, reflecting the advancement of the Democrats' ideological agenda rather than providing the critical infrastructure Californians need on a daily basis. Arguably, the most egregious non-transportation use is $54 million for the Department of Parks and Recreation for park maintenance and to train park staff. Additionally, $18 million will go to fund a ***local*** park district in Jurupa, Riverside County, a hand-out for that city, even though the normal expectation is that local park districts use local taxes to pay for their own parks (see page 36 for more detail). All of this will now happen while Democrats continue to divert $1 billion in existing transportation dollars to free up money for other state program expansions that have nothing to do with transportation.

Caltrans Bureaucracy Continues to Grow. SB 1 increases workload for Caltrans, but it's likely the department could absorb the workload with existing positions. As a continued follow-up to a 2014 LAO report that found Caltrans' Capital Outlay Support (COS) program to be overstaffed by about 3,500 positions, last May the LAO indicated the COS program remained overstaffed by at least 1,000 positions but could be overstaffed by more than 2,000 positions. For SB 1 workload, the budget retains 243 positions at a cost of $21.8 million that would have otherwise been eliminated, and allows Caltrans to reinstate 88 positions that were previously eliminated, should it be determined the positions are needed. ***Furthermore, the budget provides that Caltrans, with approval of the Department of Finance, may add more positions to this program, without limitation, by simply notifying the Joint Legislative Budget Committee and the chair of the budget committees of each house.*** Senate Republicans remain concerned about the lack of oversight of this overstaffed, growing program.

Caltrans to Audit and Investigate Itself. The budget includes the redirection of 48 existing audit positions and the addition of 10 new positions costing $9.4 million for the Caltrans' Independent Audit and Investigation Office tasked with ensuring taxpayer dollars are spent responsibly. But a closer look at the "Independent" Audit and Investigation Office within Caltrans reveals this is nothing more than a name change of the existing Division of Audits and Investigations. The only thing making this office "independent" is the declaration of said independence. The head of this office, the Inspector General, will report to the Director of Caltrans and the Transportation Agency. Given the continued conflicts of interest, Senate Republicans are concerned the newly renamed Caltrans audit office is mere window dressing. The budget also requires the Inspector General to audit Caltrans contracts to ensure contractors receiving awards are diverse. While perhaps a worthy social goal, this office should be focused on making sure transportation funds are spent efficiently and effectively.

High-Speed Rail

High-Speed Rail Continues Despite Lack of Funding. The budget includes $1.1 billion (Proposition 1A bond funds and Cap & Trade funds) to continue to build the high-speed rail system.

Specifically, $500 million is for the local/regional components of the system, $552 million is for capital outlay, and the remaining $44 million is for administration and contracts. This includes an initial baseline appropriation of $750,000 from the Property Fund to pay costs of owning various properties acquired through right-of-way activities.

This project continues to move along despite the near impossibility of ever completing the high-speed rail system that was promised. To cut costs, the system being built today varies greatly from the system envisioned and approved by voters. Despite these significant cost-cutting modifications, the 2016 Business Plan reflects a funding gap of $42.3 billion to complete the rail line from San Francisco to Los Angeles. The shortfall could be greater if the state's Cap and Trade program is not extended. The business plan assumes $10.5 billion in Cap and Trade revenues through 2050 for the train. The California High-Speed Rail Authority will have to find a way to fund the remainder of the project if the train, in some form, will ever be completed. To date, no private investment has materialized and no additional federal funding is anticipated.

Department of Motor Vehicles

State Neglect on Federal Real ID Will Cost Californians. The willingness of Sacramento Democrats to put politics before the interests of residents is now going to result, once again, in higher costs and hurdles for Californians. California has had ample time to comply with the 2005 federal Real ID law but has failed to do so, resulting in the need to rush to meet the deadline and costing taxpayers hundreds of millions of dollars. The budget includes $221 million and 2,750 positions over the next six years for the DMV to offer Saturday and extended weekday office hours, and to extend the operation of temporary offices to issue driver's licenses (DL) and identification (ID) cards that would be accepted by the federal Transportation Security Administration to board an airplane starting October 1, 2020. Under the new budget policy, beginning January 2, 2018, Californians can apply for federally compliant DL and ID cards. Had the state begun issuing compliant cards sooner, instead of repeatedly asking the federal government for delays, residents could have upgraded to the compliant card in their normal cycle of renewal, but now they will need to make a special trip to the DMV and incur another $29-$33 fee to obtain the required card.

New Motor Voter Program Increased Automation. The budget includes $7 million ($1.8 million General Fund, $5.2 million Motor Vehicle Account) and 10 positions to continue the development of a fully automated voter registration process that is integrated with DMV's driver's license application and renewal process. The New Motor Voter Program was authorized by Chapter 729, Statutes of 2015 (AB 1461) and established a process to automatically register to vote every "eligible" individual that applies for a driver's license, identification card, or change of address unless the individual declines to be registered. Specifically, the proposal will require individuals to submit applications to DMV electronically, either in advance or via a terminal at a DMV office. During the electronic application process, customers would be prompted to complete voter registration information or have an opportunity to opt out. This new process is expected to significantly reduce the number of applicants who only provide partial voter registration information. Senate Republicans remain concerned that this program does not provide sufficient safeguards to ensure only eligible voters are registered.

Permanent Resources for AB 60 Driver's Licenses. The budget includes $8.6 million (Motor Vehicle Account) and 91 permanent positions to process driver's license applications from undocumented immigrants. The DMV began accepting these applications in January of 2015 and as of June 30, 2016 had seen over 900,000 AB 60 customers and issued more than 730,000 AB 60 driver's licenses. Three years of funding was provided for the initial implementation of the program, requiring DMV to request permanent funding once customer flow stabilized and the new workload was better known. The budget reflects this request.

Housing

The lack of affordable housing is one of California's greatest challenges, yet the 2017 budget does nothing to address any of the significant housing issues facing the state. People of all income levels struggle to find housing they can afford. Only 31 percent of households in California can afford to buy the median-priced home, compared to 58 percent for the country.

Excessive regulations and restrictions on building have raised the costs of building and slowed down the production of housing units, thus creating a classic supply-and-demand problem.

- Production of housing units is low in recent years (less than 100,000 units per year) compared to historic levels (an average of 200,000 new homes from 1955-1989), despite California's substantially larger population today.
- Estimates of total new housing units needed by 2025 range from 1.8 million (Dept. of Housing and Community Development) to 3.5 million (McKinsey). This suggests annual production should be 180,000 to 350,000 per year.

Broader policy changes will be needed to deal with the underlying causes of unaffordable housing, including incentivizing compliance with state laws, minimizing barriers of land-use planning, minimizing regulation barriers, and improved inter-regional, state, and local coordination. A significant challenge is how to address these issues while maintaining appropriate local control over development decisions that affect residents.

No Policy Reform Yet Pet Projects Funded. The 2017 budget includes $28.2 million in one-time General Fund expenditures for three pet projects; (1) provides $20 million to create additional navigation centers (supportive housing homeless shelters, (2) provides $8 million for homeless housing rehabilitation and property purchase for the Weingart Center for the Homeless (a comprehensive center for homeless in Los Angeles county, and (3) provides $250,000 for Napa County migrant farmworker housing. These augmentations are classic examples of budget "pork" and will not address the state's severe housing crisis in any way.

State Cannot Subsidize Itself Out of Housing Crisis. According to the study *California's High Housing Costs: Causes and Consequences*, released by the Legislative Analyst's Office (LAO) last year, California needs to increase its supply of housing dramatically to make a dent in the need for homes and to reduce the cost of housing. The state plans to spend $3.5 billion in 2017-18 on affordable housing and homelessness as summarized in the chart below. However, even with the No Place Like Home Initiative, government will not be able to subsidize itself out of the housing affordability problem. According to a supplemental report from the LAO, *Perspectives on Helping Low-Income Californians Afford Housing* released last year, expanding housing assistance to low-income Californians who do not currently receive it would require an annual funding commitment in the low tens of billions of dollars, which the state simply cannot afford.

Figure SLA-04

2017-18 Affordable Housing and Homelessness Funding

(Dollars in Millions)

Department	*Program*	*Amount*
Department of Housing and Community Development	No Place Like Home Program	$262
	Federal Funds	$122
	Housing for Veterans Funds	$75
	Legislative Housing and Homelessness Priorities	$28
	Office of Migrant Services	$6
	Various	$15
California Housing Finance Agency[1/]	Single Family 1st Mortgage Lending	$1,500
	Multifamily Conduit Lending	$300
	Multifamily Lending	$200
	Mortgage Credit Certificates	$165
	Single Family Down Payment Assistance	$108
	Special Needs Housing Program	$30 [2/]
Strategic Growth Council[3/]	Affordable Housing and Sustainable Communities	TBD
	Transformative Climate Communities	TBD
Tax Credit Allocation Committee	Low Income Housing Tax Credits (Federal)	$241 [4/]
	Low Income Housing Tax Credits (State)	$95
	Farmworker Housing Assistance Tax Credits	$6
Department of Veterans Affairs	CalVet Farm and Home Loan Program	$230
Department of Social Services	CalWORKS Housing Support Program	$47
	CalWORKS Homeless Assistance Program	$21 [5/]
	CalWORKS Family Stabilization, Housing Component	$15 [5/]
Office of Emergency Services	Transitional Housing Program, Victim of Crimes Act	$18
	Homeless Youth and Exploitation Program	$12
	Domestic Violence Housing First Program	$11
	Homeless Youth Emergency Services	$10
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 [6/]
California Department of Corrections and Rehabilitation	Integrated Services for Mentally-Ill Parolees	$2
	Specialized Treatment of Optimized Programming, Parole Service Center, Day Reporting Center, Female Offender Treatment and Employment Program	N/A [6/]
Total		**$3,519**

[1/] Amounts are based on the lending activities from 2016-17 trends.

[2/] This amount represents a voluntary allocation of Proposition 63 funds from 16 participating counties.

[3/] 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.

[4/] 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.

[5/] This amount represents an estimate of the portion of the program associated with housing and homelessness activities.

[6/] 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.

Resources, Environmental Protection, and Energy

Key Points

- **Inadequate Response to Crucial Flood Infrastructure Needs.** While the budget provides some funds, it also ignores calls for millions more that are needed for critical flood control infrastructure projects.

- **Gas Tax Bait-and-Switch.** The Budget Act directs $54 million from the new gas and car taxes to state parks, despite Democrats selling the tax increase as a way to fix roads.

- **Tree Mortality.** The budget includes a modest $8 million to begin addressing this significant public safety risk.

- **Commercial Fishing Fees Increase.** The budget includes a questionable fee increase on commercial fishermen.

- **Cap and Trade Approved After Budget.** Although the budget did not include an extension of the Cap and Trade program, the Governor continued to seek a two-thirds approval for the program after the budget process, and AB 398 (E. Garcia) was approved on July 17, 2017.

Democrats Reject Needed Additional Flood Control Investments. Through a bipartisan effort, Senator Nielsen (R-Tehama) requested $100 million General Fund annually to DWR for critical infrastructure repairs and reimbursements to local agencies for flood control infrastructure work. A consistent source of funding is necessary to address the backlog of operation and maintenance needs across the state, as shown by the severe damage to the Oroville Dam spillways earlier this year. Critical repairs are needed to the Sacramento, Feather, and Yuba River levees along with the Sutter and Yolo Bypasses and to urban and rural flood protection facilities in high flood risk areas across the state. This year alone, local agencies have spent millions of dollars on emergency response activities which need to be reimbursed in order to help them recover from these unexpected financial burdens.

The Central Valley Flood Protection Plan estimates up to $21 billion is needed over 30 years for upkeep of the State Plan of Flood Control system of levees and bypasses, while DWR and the U.S. Army Corps of Engineers identified needs of more than $50 billion in a 2013 report. Senator Nielsen's request of $100 million represented the amount of work that can be achieved each year to incrementally reduce this backlog of deferred maintenance needs.

This requested funding investment in our water infrastructure will save lives, protect property, and save the state billions in avoided emergency repairs. ***Unfortunately, the Governor did not make funding for these critical repairs a priority in the 2017-18 Budget Act and provided no additional funding for these flood protection projects.***

Some Dam Safety and Flood Control Investments. SB 92 (Resources Trailer Bill) of 2017 includes new requirements on dam owners to prepare inundation maps and emergency action plans while providing the Department of Water Resources (DWR) with more enforcement authority through the use of fines and dam operational restrictions for failure to comply. In addition, the budget bill provides funding for DWR to conduct more extensive evaluations of appurtenance structures, such as spillways, gates, and outlets. The new activities will be funded from $6.5 million in additional annual fees on dam owners. Although large entities with significant resources, such as the state water project contractors or utility companies could fund these new costs, midsized or small local governments, businesses, or private property owners may not have the financial resources.

In addition, $1.9 million of General Fund is included for the Office of Emergency Services (OES) to review and approve dam related emergency response plans and to coordinate with local emergency management agencies on incorporation into all-hazard emergency plans.

The budget also includes $111 million of Proposition 1 Bond funds for flood protection and habitat restoration projects for the Delta, Central Valley, and coastal areas of the state. The funding is appropriated as follows:

- Delta Levee Subventions ($20 million)
- Delta Special Projects ($10 million)
- Delta System-wide Flood Risk Reduction ($20 million)
- Delta Emergency Response ($5 million)
- Coastal Watershed Flood Risk Reduction ($9 million)
- Central Valley Tributary Program ($40 million)
- Central Valley System-wide Flood Risk Reduction ($7 million)

It should be noted that this one-time funding is mostly for Delta-centric projects specified in Proposition 1 and will not help the levees damaged as a result of the Oroville Dam Spillway failure. Furthermore, billions of dollars of ongoing funding is needed for deferred levee maintenance and current funding is inadequate.

Bait and Switch: Gas Taxes for Parks and Pork, Not Roads. The Budget Act gives $54 million of the new gas tax revenue (SB 1) to the Department of Parks and Recreation (DPR) to maintain its properties and to improve access to state parks, establish an employee training program, and fund the ***local*** Jurupa Area Recreation and Park District (Riverside County). This local park district will receive $18 million in gas taxes, yet DPR has provided no justification for using the money for that region of the state. Furthermore, these gas tax revenues are derived from fuel purchases by the Off-Highway Vehicle (OHV) and boating communities. However, the budget only gives the OHV and boating programs $1 million each. California motorists, OHV riders, and boaters are all paying more at the pump but not receiving the road or program benefits that they were promised.

In addition, DPR had to use $12.6 million of the State Parks and Recreation Fund (SPRF) to backfill its ongoing operating deficit instead of providing new recreational opportunities for park visitors or to improve existing parks. Last year, the Administration ripped off $31 million in fuel tax revenues meant for the OHV program to cover its ongoing operating budget problems. The department’s operations were supposed to be more self-sufficient by this time since the Legislature had required the department to develop revenue generating projects and partnerships for the operation and maintenance of its park units. This is the fourth consecutive year of providing additional funding to keep the department solvent. DPR indicates that they are continuing to work towards self-sufficiency; however, no one should be surprised when the department requests gas tax revenues in 2018-19 to keep park units open and operating.

Some Help for Tree Mortality and Forest Health. After the initial budget bill was passed, the Administration finally acknowledged that counties suffering from the tree mortality crisis needed assistance to help secure existing California Disaster Assistance Act (CDAA) funding. AB 123, which amends the budget bill, transferred $6 million General Fund from OES to the Department of Forestry and Fire Protection (CalFire) for grants to local agencies in counties subject to the tree mortality emergency declaration. This $6 million can be used as matching fund assistance for local cost sharing requirements. OES had originally estimated that there would only be a $2 million need for tree mortality funding; however, one of the main reasons for the low spending rate was the local agencies’ inability to provide the required matching funds. With this additional $6 million grant funding, requests are expected to exceed the existing $2 million available for projects. Anything above the $2 million in requests for assistance would have to come out of the $67.5 million available in OES' budget for CDAA and compete with other disaster assistance requests. Although this is a step in the right direction, the state should provide a larger pot of money specifically dedicated to tree mortality projects to improve forest health and reduce the risk of wildfires.

Dubious Increase on Commercial Fish Landing Fees. The budget increased commercial landing fees by $900,000 annually on commercial fishing in order to partially support the Department of Fish and Wildlife's commercial fishing program. Expenditures from the non-dedicated Fish and Game Preservation Fund (FGPF) currently exceed revenues by more than $20 million annually. The fee increase utilizes an eleven-tier system where fisheries that are the highest value per pound pay the highest rate. The fee increases were not consistent across all fisheries: some will receive significant increases and others decreases. At the time of publishing this report, it is unclear whether this proposal is appropriate since no details have been provided on the current revenues and costs associated with each individual commercial fishing program. The budget also provides one-time General Fund ($5.1 million) and special funds ($4 million) to help close the structural deficit in 2017-18.

Budget Rips Off Fishing and Hunting Fees. Furthermore, the budget rips off sportfishing and hunting fees to make up for the department's ongoing operating problems. The budget transfers the entire existing $8.7 million balance in the Lifetime License Trust Account to the non-dedicated FGPF and then redirects most of these revenues annually to the fund beginning in 2017-18. The use of the Lifetime License Trust Account is inappropriate given that its fee revenues are collected to provide funding for sporthunting and sportfishing programs and to protect and preserve the fish and game resources. The fees collected are intended to be spent during the actuarially determined life expectancy of the licensee. A one-time redirection to backfill a hole in the department's budget is not consistent with current law, and therefore, a statutory change was approved in SB 92 (Resources Trailer Bill) of 2017 to enable the rip-off.

California Water Action Plan Expenditures. The budget bill includes the following funding to implement the California Water Action Plan that was released in January 2014:

- $248 million Proposition 1 Bond funds to DWR for integrated regional water management projects.

- $15 million General Fund to DWR for the Sustainable Groundwater Management Act (SGMA) implementation activities related to statewide technical assistance and to provide detailed information on basin scale water use, water supplies, and groundwater conditions.

- $2.3 million Water Rights Fund to the State Water Resources Control Board (SWRCB) to enforce reporting requirements and protect local groundwater resources beginning July 1, 2017, in high- or medium-priority groundwater basins that fail to form local governance structures as required by the SGMA. The funding will ultimately come from the SGMA fee on groundwater users once implemented. The proposed funding will come from a loan from the Underground Storage Tank Cleanup Fund.

- $1.9 million reimbursements from the California Water Commission's (CWC) Proposition 1 Bond Funds allotment (out of a total of $2.7 billion for storage projects) to the Department of Fish and Wildlife to support initial outreach and technical review of the ecosystem benefits of water storage project proposals submitted to the CWC.

- $1 million from the Waste Discharge Permit Fund to the SWRCB to address contamination of groundwater basins from agricultural practices. The Administration indicates that it intends to generate new revenues from agricultural waste dischargers on agricultural lands that are currently not enrolled in the Irrigated Lands Regulatory program. However, in the short term, waste discharge permit fees will likely increase until more dischargers are enrolled.

To date, no funding has been allocated from the $2.7 billion of continuous appropriation Proposition 1 bond funds by the CWC for surface water storage projects; however, project applications are due by August 14, 2017, with funding decision expected in May/June of 2018. These projects are crucial in order to capture and store water for future use. Recent storms have provided substantial new water supplies, but unfortunately no major state water storage facility has been built in the past 40 years to capture the runoff. The CWC needs to move forward expeditiously to fund these much needed surface water storage projects.

The Drought is Over. The Governor finally acknowledged that 2016-17 has been the wettest on record in the northern Sierra Nevada Mountains and reduced the drought funding to $62.9 million General Fund/special fund in the 2017-18 budget. These funds support drought response activities within various departments for the protection of water supplies, water conservation, water curtailment and enforcement actions, enhanced fire protection, and fish and wildlife protection, as summarized in the chart below. In addition to the funding identified in the chart for CalFire, an additional $42 million General Fund is included for ongoing enhanced fire protection activities.

Drought Response Funding
(Dollars in Millions)

Investment Category	*Department*	*Program*	*Budget Act*
Protecting Water Supplies and Water	Department of Water Resources/Water Board	Emergency Drinking Water Projects	$17.0
	Water Board	Water Rights Management	$0.6
	Department of Water Resources	Save Our Water Campaign	$1.0
Emergency Response	Department of Forestry and Fire Protection	Enhanced Fire Protection	$41.7
	Department of Forestry and Fire Protection	fire Prevention Grants	$10.0
	Office of Emergency Services	Emergency Water Tank Program/Tree Mortality	$8.5
Protecting Fish and Wildlife	Department of Fish and Wildlife	At-Risk Fish Monitoring	$2.6
	Department of Water Resources	Delta Smelt	$3.5
Total			**$84.9**

Source: Department of Finance

The Drought Is Over – Why Aren't the Regulations? The Budget Act includes two new positions for SWRCB to continue to evaluate ongoing reporting of local water conservation data meant to support the Administration's ultimate goal of "Making Water Conservation a Way of Life." The Governor had proposed trailer bill language that directed the SWRCB to enact permanent water conservation requirements on both urban and agricultural water users. However, the trailer bill was rejected by both the Assembly and Senate; therefore, the Governor has committed to working with the Legislature through the policy process to enact legislation this year. ***Senate Republicans remain concerned that the goal of the Administration's conservation efforts is to gain complete command of all water***

resources by eliminating local control without regard for the harm to local water agencies, irrigation districts, and communities statewide.

Separate Bill Extends Cap and Trade Program, But Still No Spending Plan. During the regular budget process, the Legislature rejected the Governor's January proposal to spend Cap and Trade funds and to obtain a two-thirds vote to extend the Cap and Trade program beyond 2020. The Governor sought a two-thirds vote to make certain that the Cap and Trade auction revenues would be taxes that could be spent on any program, not merely fees that would have more limited use. The two-thirds vote, therefore, shields Cap and Trade revenue from future legal challenges under Proposition 26 (2010).

However, the Governor continued to seek a two-thirds approval for an extension after the budget process, and AB 398 (E. Garcia) was approved on July 17, 2017. AB 398 extends Cap and Trade by 10 years after 2020, and it also retroactively approves AB 32 (Nunez) of 2006, the Global Warming Solution Act, by that same two-thirds vote, ensuring that the current Cap and Trade program are in fact taxes as well. However, AB 398 passed without a spending plan to determine which future programs and projects will receive money, and it is unclear when that plan will be made public or approved through legislation. Furthermore, the 2017 -18 Budget Act did not include Cap and Trade revenues from the existing program, meaning that a budget bill adjustment would be needed before the end of legislative session to spend the current money.

The revenues from the Cap and Trade program have experienced significant volatility over the past year, partly due to the legal concerns raised by Senate Republicans (as confirmed by the Legislature's nonpartisan attorneys in a written opinion) that the current program was not authorized to continue past 2020 without legislative approval.

In a case regarding the current program, the California Chamber of Commerce and the Morning Star Packing Company both sued, arguing that the Air Resources Board (ARB) was never delegated the authority to impose an auction-based Cap and Trade system and that such an auction-based system constituted an illegal tax under Proposition 13 because AB 32 was enacted with a simple majority vote. However, the California Third District Court of Appeal upheld ARB's auction-based Cap and Trade program in a decision on April 6th, 2017, and the California Supreme Court recently decided not to take up an appeal by the California Chamber of Commerce. Therefore, the lower court ruling stands.

On the first issue, the court found that even if ARB wasn't authorized under AB 32 to adopt an auction-based cap and trade system, subsequent legislatures effectively ratified that system when they determined how to spend its revenues. On the second issue, the court argued that the auction-based system wasn't a tax because participation was purely voluntary and included the purchase of a valuable commodity (an allowance that could be traded or sold to other entities).

It is important to note that the case only impacted the existing Cap and Trade program, which falls under the Proposition 13 definition of "tax," whereas the extension of the Cap and Trade program would have been evaluated under the much more restrictive Proposition 26 definition. Now that AB 398 received a two-thirds vote, all revenues will be viewed as taxes, thus eliminating the potential for a Proposition 26 legal challenge.

No Beverage Container Recycling Program Reform, Only Talks of Another Interim Fix. The Governor's 2017-18 plan to modernize the Beverage Container Recycling Program contained no specific budget proposal to review, only a concept paper that proposed to align the state's climate change goals, the state's 75 percent solid waste reduction, recycling, and composting goal, and fiscal sustainability. This program has needed comprehensive reform for several years, yet few policy bills have been proposed with the exception of SB 168 (Wieckowski) of 2017, which failed passage on the

Senate Floor. At the time this report was published, there are ongoing discussions between the Administration and Legislative Democrats on an interim fix to address the state's recycling infrastructure and consumer redemption opportunities.

Increased Costs to Fund the California LifeLine Program. The budget includes an increase of $146.9 million to support subscriber growth and expanded subsidies for wireless service plans provided through the California LifeLine program. For 2017-18, the program is projecting 3.2 million subscribers, a 25 percent increase. Additionally, subsidies have been increased by extending a $39 reimbursement for wireless activation fees, previously set to expire, and increasing the monthly subsidy by 4 percent as of January 1, 2017, with another 4 percent increase expected next January.

The LifeLine program allows eligible households to subscribe to discounted wireless service plans that include voice, text, and internet access. Unlike the landline portion of the program, which provides one phone line per residence, it is possible for a single residence to have more than one cell phone. **The cost of this program has grown by 123 percent since wireless service plans were added in 2013-14.**

The LifeLine program was meant to provide essential phone service, not texting and internet access. Families who pay for their own cell phone plans are really funding two plans: their own and one for LifeLine participants. Pursuant to Proposition 26, these ratepayer fees are really a tax because the ratepayer is receiving no direct benefit.

Employee Compensation & Retirement

Key Points

- **State Employee Pay Keeps Rising.** Employee compensation increases by $1.2 billion.
- **Pension Costs Continue to Rise.** Pension payments will exceed $8.9 billion in this budget and will rise to $10 billion by 2020, crowding out resources from critical state programs.
- **Too Many Unknowns for Supplemental Pension Payment**. While additional payments to CalPERS are necessary, the proposal included in this budget was rushed and left too many crucial questions unanswered.

Employee Compensation

Employee Compensation Increases. The budget includes an additional $1.2 billion ($602.3 million General Fund) for employee pay raises and benefits. Over the past five budgets the state has spent over $8 billion ($3.9 billion General Fund) cumulatively for increased employee compensation and benefits. An additional $5.6 billion has been provided to state employees since 2006 for "merit salary adjustments," which, despite the misleading title, are automatic pay raises awarded on an employee's work anniversary.

Everybody Gets a Raise! Earlier this year the Governor negotiated with a number of employee bargaining units whose contracts expired at the end of the 2015-16 fiscal year. Unfortunately, during the negotiation process the unions consistently leveraged new retiree health contributions for significant pay raises. Salary increases under these contracts range from 8 percent to 26.5 percent over the life of the contracts. Combined, salary increases alone will cost taxpayer $4.3 billion ($2 billion General Fund) over the life of these contracts, and result in a $1.3 billion ($620 million General Fund) ongoing cost to the state after the contracts expire.

California Public Employees Retirement System (CalPERS)

Public Employee Pension Costs Continue to Rise. The budget provides $5.9 billion ($3.4 billion General Fund) for employer contributions to CalPERS for retirement costs for state employees, including California State University employees. This is 11 percent higher than the amount budgeted in Fiscal Year 2016-17. Current estimates show that state contributions to CalPERS will increase by $3 billion ($1.8 billion General Fund) by the 2023-24 budget, accounting for a combined state contribution of nearly $8.5 billion ($4 billion General Fund).

Paying Down Pension Debt. The budget approved a $6 billion supplemental payment to CalPERS. This payment is in addition to the $8.9 billion already provided in the budget for CalPERS and CalSTRS contributions.

This additional payment will allow the state to lower its employer contribution over the next 20 years. While this reduced rate will fluctuate from year to year, it is estimated to be about 2.1 percent lower and save the state $11 billion over 20 years. The $6 billion would be a long-term loan from the state's cash accounts, which would be paid back over time with the General Fund's share credited toward Proposition 2's debt repayment requirements. While steps must be taken to address unfunded pension liabilities that are spiraling out of control, counting this supplemental payment towards Proposition 2's requirement to pay down debt could result in other debt repayments being delayed.

Over the years Senate Republicans have continued their call for paying down unfunded pension liabilities. While the proposal included in this budget has merits, the Administration and majority party leaders failed to address many of the concerns raised by both Senate Democrats and Republicans. Questions were brought up numerous times about the timing of the payment, number of payments, constitutional issues, and the overall risk of the payment to generate state savings. Many of these concerns could have been alleviated if more time was provided for all parties to discuss these issues, but unfortunately the majority party decided to jam this proposal through without even a formal vote in the Senate Budget and Fiscal Review Committee. Had appropriate time been afforded, a better payment plan could have been crafted, but since that important consideration was not provided, taxpayers are stuck with a payment scheme that is unnecessarily risky and does not maximize value.

California State Teachers' Retirement System (CalSTRS)

Plan to Address Liabilities Having Large Effect on State Costs. The budget provides $2.8 billion General Fund to pay for the state's share of CalSTRS costs. This is a 13 percent increase above 2016-17 spending. By 2020-21 state contributions to CalSTRS will be $3.6 billion, 29 percent higher than the amount the state is projected to pay in this budget.

Taking Money Out of the Classroom. A contribution made to CalSTRS by a school district is money taken out of the classroom. The LAO estimated that **by the 2020-21 fiscal year, school districts will be sending somewhere between 25 percent and 33 percent of new cumulative Proposition 98 dollars to CalSTRS**.

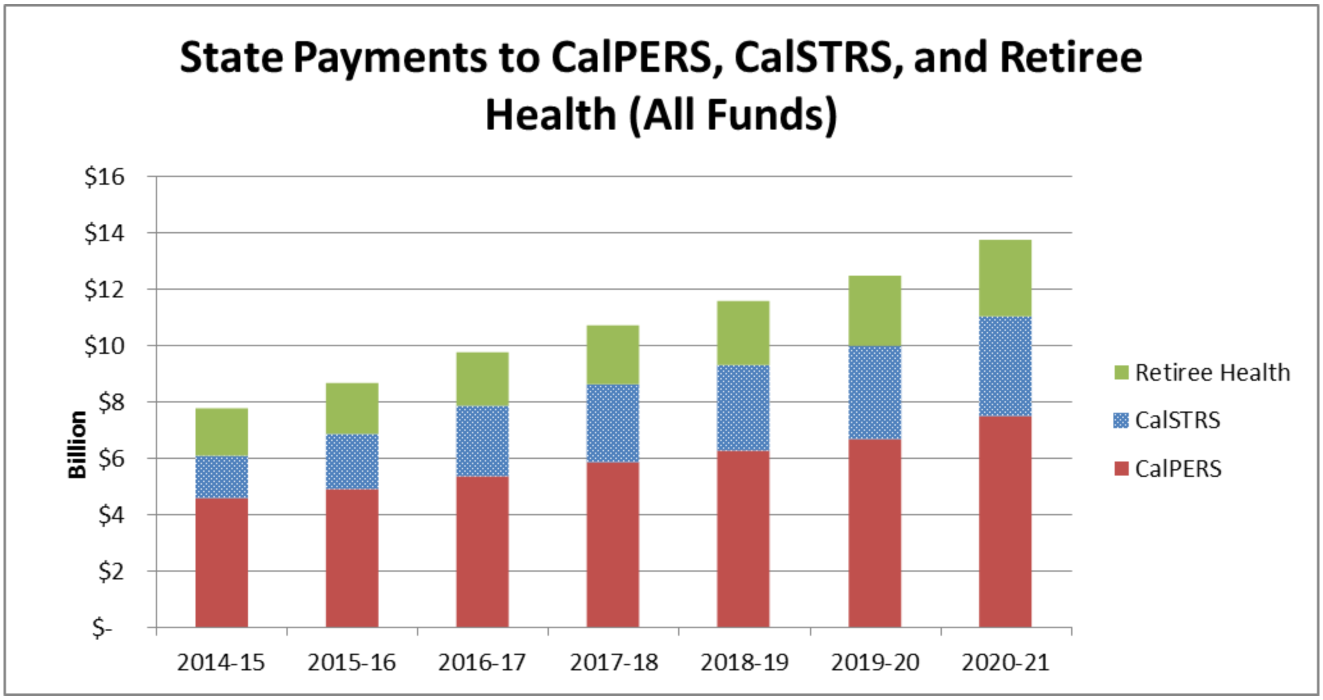
Retiree Health Care Benefits

The budget includes $1.8 billion General Fund for health care benefits for more than 300,000 state retirees and eligible dependents. The state General Fund also pays for health benefits for retired employees of the California State University (CSU), which cost $295 million in this budget.

Retiree health care benefits continue to be paid out on a "pay-as-you-go" approach, which has led to the creation of a $76.7 billion unfunded liability for the state. Without action to address these rising costs, this unfunded liability could grow to $100 billion by 2020-21, and potentially exceed $300 billion by 2047-48. Pre-funding contributions from the state and employees will provide almost $400 million in the budget year.

Total State Cost for Retirement Programs

To evaluate the combined effects of the budget actions described above, the graph below illustrates combined budgetary costs for employer contributions to CalPERS and CalSTRS, along with retiree health costs through the 2020-21 budget year.



State retirement costs are projected to grow by more than 15 percent between now and the 2020-21 budget, which is faster than the overall projected state revenue growth of only 10 percent. Thus, retirement costs' share of the budget is only going to grow as time goes on. Absent structural reform, discretionary programs will see larger portions of their General Fund resources siphoned off to pay for pension and retiree health costs. However, Democrats have taken only modest steps to address this problem while at the same time dedicating state resources to new programs or expansions in other areas.

General Government

Key Points

- **Budget continues to use non-competitive process.** State project uses no-bid process for project management work.
- **Infrastructure funding redirected.** Even as the state collects record levels of revenue, one-time infrastructure project funding will be redirected to pay for ongoing program spending.
- **No funding for deferred maintenance.** While the budget includes additional funding for unions and their members, it does too little to address tens of billions in deferred maintenance needs.

Non-Competitive Bid Process Reduces Transparency. The 2017 budget includes $1.7 million and authorizes the future expenditure of an additional $30 million for the construction of a new state parking structure. The project was not reflected in the Administration's recent infrastructure planning documents, which provide the Legislature with information on future projects, facilitating Legislative review and planning. The budget also designates one local agency as the project manager through a non-competitive process. Without a competitive process to award this significant contract, accountability and transparency are reduced, and there is no way to determine whether the approved approach is the best alternative to fund and manage the project.

Infrastructure Funds Shifted for Ongoing Democrat Priorities. The 2016 Budget Act included $1.3 billion for state-owned building projects in Sacramento. While work has begun on two of the projects, the 2017 budget redirects nearly all of the previously approved General Fund, leaving only about $150 million out of the $1.3 billion. Rescinding the General Fund for the bulk of the projects leaves the Administration with the need to seek another source of funding, likely increasing the state’s overall debt. In 2016, Senate Republicans argued that these funds should go to transportation projects. Now, Democrats want to use the money for other priorities. Utilizing one-time General Fund resources for infrastructure projects is a smart way to spend the state's record level revenues without committing the state to unsustainable ongoing spending and additional debt, but Sacramento Democrats have chosen to do the opposite.

Administration Fails to Prioritize Deferred Maintenance. The 2017 budget includes a number of spending increases for unions, such as state employees’ wage increases, but does not include any funding to address the state’s deferred maintenance liabilities. The Governor’s 2017 California Five-Year Infrastructure Plan identifies more than $75 billion in deferred maintenance needs across the state. Of this amount, 73 percent is in transportation, nearly 17 percent in water resources, 4 percent in higher education, and nearly 2 percent in parks and recreation. The 2015 and 2016 budgets included nearly $1 billion to address the maintenance backlog, but the 2017 budget only provides $421 million for transportation maintenance projects and provides nothing to address the state’s water maintenance issues. This minimal amount of funding fails to address the very serious backlog of critical deferred maintenance issues, leaving about $54 billion in outstanding transportation needs and about $13 billion in water and flood infrastructure. It is unclear exactly how much of the SB 1 gas tax monies will go to the deferred maintenance transportation needs of the state as opposed to bolstering alternative facilities like bike paths and pedestrian facilities.

Taxpayer Risk Increases for State-Run Private Retirement Scheme. The 2017 budget approves a $15 million loan from the General Fund to help start the California Secure Choice Program, a state-run retirement plan for private residents that was authorized by SB 1234 (De Leon, 2016). The budget allows the Department of Finance to unilaterally increase this loan to $35 million without proper legislative oversight. Additionally, budget trailer bill language increases the risk that taxpayers could eventually be on the hook for possible liabilities incurred by Secure Choice by deleting current law that protects taxpayers from such liabilities. Instead, the majority party changed the law to state that the program would "self-certify," without the need to produce any legal opinion, that they met federal requirements to protect taxpayers. Removing this taxpayer protection has nothing to do with the budget this year, thus providing another example of Democrats misusing budget approval rules enacted in Proposition 25. The employer community would also be on the hook for these liabilities and they are currently seeking their own legal opinion to understand their potential legal exposure.

Budget Benefits Veterans, but More Could be Done. The budget includes The 2017 budget provides $5 million to the Southern California Veterans Cemetery, which will be built near Irvine. Additionally, the budget appropriates $1.5 million to the Central Coast Veterans Cemetery near Monterey. Additionally, the 2017 budget provides $670,000 to continue the successful Work for Warriors program, which has successfully placed 6,000 service members and veterans in well-paying jobs. Senate Republicans applaud these steps but believe that the state could do more to assist veterans, such as by expanding services to assist returning veterans in transitioning from military to civilian life.

Democrats Abuse Budget Rules to Benefit Special Interests. The budget enacts numerous new policies that have nothing to do with the actual budget. The majority party continues to abuse Proposition 25 budget law to slip through a number of proposals that are not actually related to the budget but happen to benefit public employee unions. For example, one so-called "trailer bill" requires public employers to allow unions to make a presentation during new employee orientation sessions. This exact proposal had previously failed when attempted through the more transparent policy process in the form of AB 2835 (Cooper, 2016) and AB 52 (Cooper, 2017), but Democrats quietly slipped it into the budget as part of a bill that addresses various government issues. Additionally, the trailer bill <u>requires</u> public employers to share employees' private e-mail addresses with the union, even if the employees are not members of the union and do not want their emails shared.

Arts Funding Helps Underserved Communities. The 2017 budget includes $6.8 million General Fund for the California Arts Council to support arts grant programs in underserved communities in 2016-17 and to establish a reentry/bridging grant program to facilitate inmate transition from prison back to their communities. Senate Republicans support positive and creative transition programs that can increase self-confidence and skills for former inmates seeking to improve life for themselves and their families.

Precision Medicine Funding Continues. The 2017 budget provides $10 million General Fund for continued investment in the California Initiative to Advance Precision Medicine. The initiative was implemented with $3 million General Fund in 2014-15 and supported two precision medicine demonstration projects. In 2016-17, an additional $10 million was provided and resulted in six new projected receiving awards through a competitive process.

Statewide Issues

Key Points

- **Taxpayer Rights Reduced Under Tax Agency Changes.** Under the guise of fairness and transparency, Sacramento Democrats minimize taxpayer rights while increasing bureaucracy as they "reform" the Board of Equalization.
- **Democrats Change Rules to Help Themselves.** Democrats abuse the budget process to change recall election rules in their favor.
- **Earned Income Tax Credit.** The budget improves the EITC by increasing the income limit and allowing self-employed workers to participate.

Board of Equalization

Taxpayer Rights Minimized Through Overreaching Reforms. Recently, the State Controller and Department of Finance conducted independent audits on the Board of Equalization (BOE). Both audits found serious issues within the administrative process functions and the financial data systems, and both audits identified weaknesses that could lead to waste and abuse of funds.

In response to the extensive number of concerns brought to light with recent audits, the 2017 budget includes sweeping legislation that establishes a new and costly tax bureaucracy by reassigning most of the Board of Equalization's current function to the new California Department of Tax and Fee Administration, which will fall under the direct authority of the Governor. Additionally, the budget establishes the Office of Tax Appeals, an independent appeals panel.

While there is no doubt that significant BOE reforms were needed, Sacramento Democrats waited until very late in the budget process to propose vast and overreaching changes that had never been specifically discussed in a public hearing. These specific changes should have been given at least several hearings in order to fully evaluate the effects on taxpayers. Instead, Democrats abused the budget rules to slam changes through in only a few days.

Moving the tax appeal functions of the BOE into the state's bureaucracy under the direction of government appointees effectively eliminates the direct accountability between elected officials and their constituents. This new structure will not preserve core BOE functions that protect taxpayers' rights; on the contrary, it eliminates the existing checks and balances between taxpayers and tax collectors. Instead of having one behemoth bureaucracy, the state will now have two, a sure sign that government "efficiency" is alive and well.

Elections

Sacramento Democrats Change Election Laws to Help One of Their Own. The 2017 budget lengthens the state's recall process by five months and applies those changes retroactively. By significantly lengthening the time it takes to qualify a recall election and changing other procedural rules, these changes will drag out the recall process in order to make it more difficult to qualify a recall, and make those recalls that do qualify less likely to succeed. The action by Sacramento Democrats undermines direct democracy, which is intended to give the people a say in their government. Democrats made no effort to disguise the fact that this action is specifically intended to benefit one sitting senator who is now facing a recall election.

In order to provide a token connection to the budget and pass these changes on an urgency basis, Democrats provided $5 million to pay for a manual recount of ballots. These funds are a sharp contrast to recent special elections, in which no funds were provided for recounts, and this action is also inconsistent with Democrats' failure to pay local elections officials $75 million for suspended election mandates. In spite of the funding fig leaf, this is a clear abuse of Proposition 25, which voters passed in order to provide an on-time budget, not to open the door to blatant political power plays.

Census Address Outreach Program. The 2017 budget includes up to $10 million ($7 million initially, with up to $3 million in additional funding) in grant authority to local governments for use in the Census Bureau's Local Update of Census Addresses program. The funding can be used for outreach and additional activities, such as hiring a census outreach coordinator, in order to review and update the master address lists that are used to conduct the decennial census.

California Earned Income Tax Credit

The budget makes two changes that will expand the effect of the Earned Income Tax Credit (EITC). As described below, it both expands the EITC to self-employed workers and raises the income threshold. Overall, these changes are expected to increase the number of low-income Californians eligible to claim the tax credit by 1 million additional households, bringing the total to 1.5 million households. The amount of tax credits provided to low-income working families is expected to grow from $200 million in 2016 to $340 million in 2017. Senate Republicans believe that the EITC is a better way to help lower-income Californians move toward prosperity, compared to programs that simply provide hand-outs to people who may or may not be working or seeking employment.

Expansion of Tax Credit to Self-Employed. The 2017 budget expands the state Earned Income Tax Credit (EITC) to workers with self-employment income. Previously, only workers who earned wages from an employer were eligible to participate. This important change levels the playing field for workers who are self-employed. The budget also recognizes that there are higher fraud risks for self-employed workers, though, and it adds $10 million for administration at the Franchise Tax Board to combat potentially false claims. This funding level may or may not be adequate to address fraud within the program, but until the expansion is rolled out, the FTB is unsure of the total amount of resources necessary.

Income Allowed for Eligibility Significantly Raised. The budget raises the income level allowed for people to receive the EITC up to $22,300 annually. This does not change the actual tax credit that an individual taxpayer would receive, which is a maximum of $2,765 for families with three or more children; rather, it expands the income level at which people may receive that credit, allowing Californians to earn higher wages and still be eligible for the tax credit.

Statewide Debts and Liabilities

The 2017 Budget Act includes $8 billion to pay the state's current debts and liabilities, including the following components:

- About $6.2 billion to pay debt service costs for the state's outstanding and planned General Obligation (GO) and Lease Revenue (LR) bonds in 2017-18, as required by the California Constitution and respective debt issuance documents. According to the State Treasurer, the state currently has outstanding bonds totaling some $73.7 billion and has authorization to issue $35.6 billion more.
- Nearly $1.8 billion to pay a variety of debts and liabilities as mandated by Proposition 2, which was passed by the voters in November 2014. The 2017 Budget Act differs from previous budgets in that $398 million of truck weight fee repayments is counted within the $1.8 billion of Proposition 2 debt repayments for the first time. While such debts are eligible to be counted against Proposition 2 requirements, these repayments were previously made in addition to Proposition 2 repayments. Thus, the effect of this shift is to decrease debt repayment for other critical areas such as Proposition 98 settle-up and to free up room for more spending on Democrat priorities.

Missed Opportunity to Pay Down More Debt. Though this budget does meet constitutional requirements for debt payments, it only pays off a small portion of the state's debts and liabilities. With its current windfall revenues, the budget misses an opportunity to pay down additional debts and avoid future costs. For instance, the Democrats continued to suspend dozens of local mandates in the 2017 Budget Act. These annual suspensions have resulted in more than $1 billion in accumulated mandate reimbursement debt owed to the counties. Paying down state debt while revenues are reaching record levels will provide the state with a cushion for softening the fiscal effect of the economic recession that is likely on the horizon.

Overall Debt and Liabilities Over $300 Billion. The 2017-18 budget identifies nearly $302 billion of debts and liabilities facing the state at the start of 2017-18, including outstanding budgetary borrowing and state retirement liabilities. The following table identifies Proposition 2 outstanding liabilities as well as other debts and obligations, including GO and LR bonds. In addition to the amounts shown, the budget authorizes a new $6 billion loan from the state's cash reserves for a prepayment to CalPERS. This loan is described in more detail on page 41 of the Employee Compensation and Retirement section.

Statewide Debts and Liabilities *(Dollars in Millions)*	**At Start of 2017-18**	**Estimated Payments**				**Remaining Liabilities***
		2017-18	**2018-19**	**2019-20**	**2020-21**	
Eligible for Proposition 2 Payments						
Budgetary Borrowing						
Loans from Special Funds	$1,381	$133	$204	$39	$290	$0
Weight Fee Payments	$1,395	$398	$469	$445	$83	
Underfunding of Proposition 98 - Settle-Up	1,043	603	100	100	190	$0
Pre-Proposition 42 Transportation Loans	706	235	235	236	*0*	$0
State Retirement Liabilities						
State Retiree Health	76,533	89	200	250	300	N/A
State Employee Pensions***	59,578	146	195	211	351	N/A
Teachers' Pensions (state portion)	29,332	0	0	0	0	N/A
Judges' Pensions	3,489	0	0	0	0	N/A
Deferred payments to CalPERS	627	0	0	0	0	N/A
University of California Retirement Liabilities**						
UC Employee Pensions	15,141	169	0	0	0	N/A
UC Retiree Health	21,860	0	0	0		N/A
Subtotal, Eligible for Proposition 2	**$211,085**	$1,773	$1,403	$1,281	$1,214	
Other State Debts						
Long-Term Infrastructure (General Obligation & Lease-Revenue Bonds)	$83,887	$6,222	$0	$0	$0	$77,665
Unemployment Insurance	3,900	50	0	0	0	$3,850
Suspended Mandate	1,016	0	0	0	0	$1,016
Education Mandate	2,025	0	0	0	0	$2,025
Subtotal, Other State Debts	**$90,828**	$6,272	$0	$0	$0	
Total	**$301,913**	$8,045	$1,403	$1,281	$1,214	

* Assumes no additional debts incurred.

** UC liabilities technically belong to the UC system alone, not the State of California, due to UC's constitutional autonomy, but these liabilites are nonetheless included as eligible for repayment under Proposition 2.

*** Includes cost to pay off the $6 billion supplmental payment loan which came from the Surplus Money Investment Fund. However, the $6 billion loan is not reflected in the beginning balance because the loan will be during the year.

Cannabis Regulation

Key Points

- **Cannabis Regulation Resources Ramp-up.** The budget roughly doubles resources for regulation of the cannabis industry as licensing and enforcement begins January 1, 2018.

Cannabis Regulatory Resources. The budget includes $100.5 million and 381.7 new staff positions to continue preparations to regulate both the medical and recreational segments of the cannabis industry and begin licensing and enforcement on January 1, 2018. The table below shows the funding by department, including funding provided through 2016-17 to reflect program growth:

State Spending on Cannabis Regulation			
Department	**Funding Through 2016-17 (millions)**	**2017-18 Budget (millions)**	**Responsibilities**
Department of Consumer Affairs	$11.3	$26.3	Regulate the transportation, storage, distribution, testing, and sale of cannabis within the state; licensing, investigation, enforcement, and coordination with local governments.
Department of Fish and Wildlife	$13.7	$17.2	Support regulatory programs implemented by CDFA and Water Board, provide law enforcement for compliance efforts, and issue Lake and Streambed Alteration Permits.
State Water Resources Control Board	$7.2	$9.8	Develop a statewide water quality permit and expanded water rights registration process for cannabis cultivators.
Department of Food and Agriculture	$8.6	$28.6	License and regulate cannabis cultivation, perform an Environmental Impact Report, and establish a track and trace program.
Department of Public Health	$4.6	$10.3	License and regulate of cannabis product manufacturers.
Department of Pesticide Regulation	$0.7	$1.3	Develop guidelines for the use of pesticides in the cultivation of cannabis, prepare training programs and outreach materials.
Board of Equalization	$1.1	$2.7	Administer an excise tax on cannabis sales and a cultivation tax on all harvested cannabis that enters the commercial market.
Department of Health Care Services	$5.0	$0.3	Establish and implement a public information program relative to cannabis health-related topics and products.
Cannabis Appeals Panel	-	$1.0	Review all appeals related to cannabis licensing decisions.
California Highway Patrol	-	$3.0	Train Drug Recognition Experts.
Total	$53.2	$100.5	

Cannabis Regulatory Structure. The budget includes legislation (SB 94) to implement a single regulatory structure for both the medicinal and recreational cannabis industries. SB 94 takes many positive steps, including:

- Establishing a working group to find a safe and viable way to accept cash payments of taxes and fees.
- Opening a "one-stop-shop" office in the Emerald Triangle.
- Applying existing state transport laws to cannabis.
- Providing $3 million to the California Highway Patrol to begin training additional officers as drug recognition experts.

However, there are also less favorable provisions, including:

- Continued special treatment of cannabis cultivators when compared to cultivators of other agricultural products.
- Creation of a complicated process for coordination with local governments.
- Permitting retail sales of cannabis from non-store fronts.
- Allowing for consumption or sale at a county fair or agricultural event with certain restrictions.

These policies could compromise public safety, and it is clear there is still more work to be done regulating this industry. In this new world of legal cannabis consumption, Senate Republicans will continue to advocate for laws that both enhance the health and safety of Californians and treat cannabis products similar to other agriculture producers.

Appendix: List of Budget-Related Bills

Budget and Related Bills	
Bill Number	**Subject**
AB 97	**Primary Budget Bill**
	Authorizes most of the $291 billion to be spent for the year from all fund sources.
AB 98	**Medi-Cal Deficiency Bill**
	Appropriates $1.16 billion for 2016-17 Medi-Cal deficiency.
AB 99	**Omnibus Education Bill**
	Appropriates $2.8 billion for a variety of K-12 education programs, extends the District of Choice program for five years, and repeals the prohibition on school bond funding for career technical education, among other things.
AB 102	**Board of Equalization Reform**
	Strips the Board of Equalization of all tax adjudication authority except what is included in the Constitution. Creates two new state agencies, the Office of Tax Appeals, which will be an independent agency, and the California Department of Tax and Fee Administration within the Government Operations Agency, under the authority of the Governor.
AB 103	**Public Safety**
	Expands state prohibitions on firearms possession. Authorizes certain state hospital patients who have been charged with crimes and found not guilty by reason of insanity to petition the court for early release. Prohibits local agencies from expanding contracts with the federal government to house civil immigration detainees. Requires local jails to provide in-person visitation and prohibits them from charging for on-site video visitation. Reallocates four vacant judgeships to counties with severe judicial shortages.
AB 107	**Developmental Services**
	Enacts various actions including expanding funds to develop crisis facilities in the community, reversing a recession-era limit on family respite services, and improving transparency.
AB 111	**General Government I**
	Increases fees for school construction, provides Military Department with design-build authority, increases flexibility within the Community-Based Transitional Housing program, requires BReEze business process review changes.
AB 114	**Miscellaneous Health**
	Reforms Proposition 63 Mental Health Services Act administration. Extends sunsets of umbilical cord blood collection and health legislation analysis programs.

AB 115	**Transportation Trailer Bill I**
	Includes SB 1 clean-up, Riverside County project accelerations, property tax restrictions on specified California Department of Transportation surplus properties, and other non-controversial changes to existing law.
AB 119	**General Government II**
	Eliminates all General Fund for the State Project Infrastructure Fund, removes language which protected the state and employers from accruing any liability for Secure Choice, streamlines process for Public Works Board expense accounting, provides Governor authority to appoint Arts Council director, requires personal emails shared with unions.
AB 120	**Proposition 56 Allocations Bill**
	Appropriates $1.3 billion in Proposition 56 tobacco tax revenues.
AB 126	**Developmental Services Cleanup**
	Corrects an erroneous start date for restoration of respite services
SB 84	**Supplemental Pension Payment**
	Provides a $6 billion supplemental payment payment to the Califorina Public Employees' Retirement Fund. Payment comes from a $6 billion loan from the Surplus Money Investment Fund.
SB 85	**Higher Education**
	Postpones decrease in private CalGrants, forces UC to use union labor for capital projects, and funds veterans' centers and mental health, hunger prevention, & sexual harassment prevention activities, among other things.
SB 88	**General Government III**
	Provides authority for Administration to begin process for construction of new state garage, requires personal email addresses of In Home Supportive Service providers be shared with unions.
SB 89	**Human Services Trailer Bill**
	Provides deportation defense services to undocumented immigrants and CalWORKs incentives to recipients.
SB 90	**In-Home Supportive Services Trailer Bill**
	Enacts new state/local cost-sharing agreement for IHSS program.
SB 92	**Resources Trailer Bill**
	Creates several new fees, imposes stricter requirements on dairy digester technology, imposes new dam safety inspection standards and evacuation/inundation plan requirements, clarifies the Milk Quota Program, among numerous other issues.

SB 94	**Cannabis Trailer Bill**
	Repeals and recasts provisions related to the regulation of medicinal cannabis and adds provisions related to the regulation of recreational cannabis.
SB 96	**Recall & General Government IV (Public Works)**
	Recall election timeframe changes, veteran home prioritization, Orange County veteran cemetary, new misdeanor for contractors.
SB 97	**Health Trailer Bill**
	Restores dental and optical Medi-Cal benefits and imposes new nursing staff ratios.
SB 103	**Transportation Trailer Bill II**
	Provides contracting requirements and outreach for transportation projects and further develops the Advance Mitigation and Trade Corridor Freight Programs as created by SB 1 (the recently enacted car and gas taxes).
SB 106	**General Government V**
	Expands the state Earned Income Tax Credit to self-employed and increases allowable income, revises the Community Development Block Grant program structure, extends until 2028 Marin County's distinction as a "rural" county for purposes of restricting the construction of density housing within the county.
SB 107	**Riverside County Transportation Projects and Education**
	Allows Riverside County to bypass the bureaucratic California Department of Tranportation's funding agreement process (part of Gas Tax agreement) and makes technical corrections to capture Proposition 98 education savings assumed in the 2017-18 budget package.
SB 108	**"Clean Up" Budget Bill**
	Tree mortality programs, cannibus regulation, deportation legal assistance, and earned income tax credit administration.
SB 110	**Clean Energy Job Creation Program**
	Authorizes the California Energy Commission to allocate revenues to schools, universities, and community colleges for energy efficiency improvement projects, effectively extending Proposition 39 (2012) projects indefinitely.
SB 130	**Local Govt - Property Taxes - Vehicle License Fees**
	Changes the formulas for calculating annual vehicle license fee adjustment amounts for four cities in Riverside County that incorporated after 2004 but before 2012. Part of the Gas Tax agreement.
SB 131	**State Employment: Physicians, Dentists, & Podiatrists**
	Ratifies contract with the Union of American Physicians and Dentists.
SB 132	**Transportation and Employee Compensation Funding**
	Allocates $927 million to specific local transportation projects, $50 million for a warehouse emission reduction program, and $5.5 million for increased employee compensation costs. Part of the Gas Tax agreement.

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