Overview of the 2017-18 Budget Bill

Senate Bill 72
As Introduced January 10, 2017

Senate Committee on Budget and Fiscal Review
Senator Holly J. Mitchell, Chair

February 2017

1602-S

OVERVIEW OF THE 2017-18 BUDGET BILL

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Dear Colleague:

I am pleased to provide you with a copy of the *Overview of the 2017-18 Budget Bill*, which has been prepared by the staff of the Senate Committee on Budget and Fiscal Review. The document is intended to highlight the Governor's major proposals and provide additional information and framework to support the review of these proposals. This document, together with other materials, will provide the basis for budget hearings throughout the spring.

The first section presents an overview of the state's fiscal condition and the Governor's fiscal proposals. The next section, entitled "Major Issues," is organized by budget subcommittee. For each major issue, this report provides relevant background material, an explanation of the budget proposal, and a discussion of important matters to consider.

In the Appendix, we include supplementary fiscal documents prepared by the Department of Finance. The Appendix also includes a working timeline for completing the 2017-18 budget, a historical listing of adopted state budgets, and a schedule of budget committee consultants and their respective areas of responsibility.

If you have questions, please do not hesitate to contact me or the committee staff.

Sincerely,

HOLLY J. MITCHELL
Chair

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Budget Overview

INTRODUCTION

The Governor has proposed a budget for the 2017-18 fiscal year that includes resources – carry forward balance, revenues and transfers – of $125.1 billion and expenditures of $122.5 billion. Based on the budget proposal, the General Fund would end the 2017-18 fiscal year with an unencumbered reserve of over $1.5 billion and include a deposit of $1.2 billion to the Budget Stabilization Account (BSA), resulting in an expected balance in this account of over $7.9 billion at the end of the budget year. In the Governor's budget, the Administration has identified an on-going annual budget problem of between $1 and $2 billion, largely stemming from slightly softening revenues. The budget proposes a variety of solutions to address this shortfall, which include pulling back on specified one-time spending commitments and reducing or delaying anticipated spending increases. For the budget year, the expected shortfall of $1.6 billion is minor by historical standards, accounting for less than 1.3 percent of General Fund resources.

Despite the minor budget shortfall that has developed since the adoption of the 2016 Budget Act, the General Fund continues to be in a strong position, as a result of the combined efforts of the Administration and the Legislature over the last few years. In the budget, the state will continue its ongoing commitments to eliminate the overhang of budgetary borrowing as well as make efforts to reduce longer term pension and retirement debt. Additionally, the budget proposes that, based on the slight revenue deterioration, specific expenditure adjustments be adopted. In total, compared to the 2016-17 adopted budget, revenues are down by about $5.8 billion over the three year period (past year, current year and budget year). The proposed 2017-18 budget uses this adjusted base, incorporating a general reserve and BSA of approximately $9.4 billion (with another almost $1 billion reserved for encumbrances). Overall, General Fund spending in 2017-18 is expected to decline by $241 million (or 0.2 percent) from the 2016-17 fiscal year; however, the budget notes that spending requirements in core areas will continue to be addressed.

OVERVIEW OF GOVERNOR'S BUDGET PROPOSAL

Overall Structure

The Governor's budget includes $125.1 billion in General Fund revenues and other resources and $122.5 billion in total General Fund expenditures ($71.2 billion in non-Proposition 98 and $51.4 billion in Proposition 98), providing for a $1.6 billion unencumbered reserve as well as setting aside an additional $1.2 billion for the BSA. Expenditures in 2017-18 are proposed to be about $241 million lower than revised 2016-17 expenditures. Nevertheless, as a result of budget shifts and adjustments to the current year, additional funding is proposed for K-14 education and corrections and rehabilitation, with generally level funding for most other areas of the budget. Budget resources have allowed for measured expansions and workload growth based on relatively stable revenues and one-time current year reductions. The General Fund budget details are summarized below.

2016-17 and 2017-18
General Fund Summary
(Dollars in Millions)

	Revised 2016-17	**Proposed 2017-18**
PRIOR YEAR BALANCE	$5,023	$1,027
Revenues and transfers	$118,765	$124,027
TOTAL RESOURCES AVAILABLE	**$123,788**	**$125,054**
Non-Proposition 98 Expenditures	$72,431	$71,169
Proposition 98 Expenditures	$50,330	$51,351
TOTAL EXPENDITURES	**$122,761**	**$122,520**
FUND BALANCE		
Encumbrances	$980	$980
Special Fund for Economic Uncertainties	$47	$1,554
BUDGET STABILIZATION ACCOUNT	**$6,713**	**$7,869**

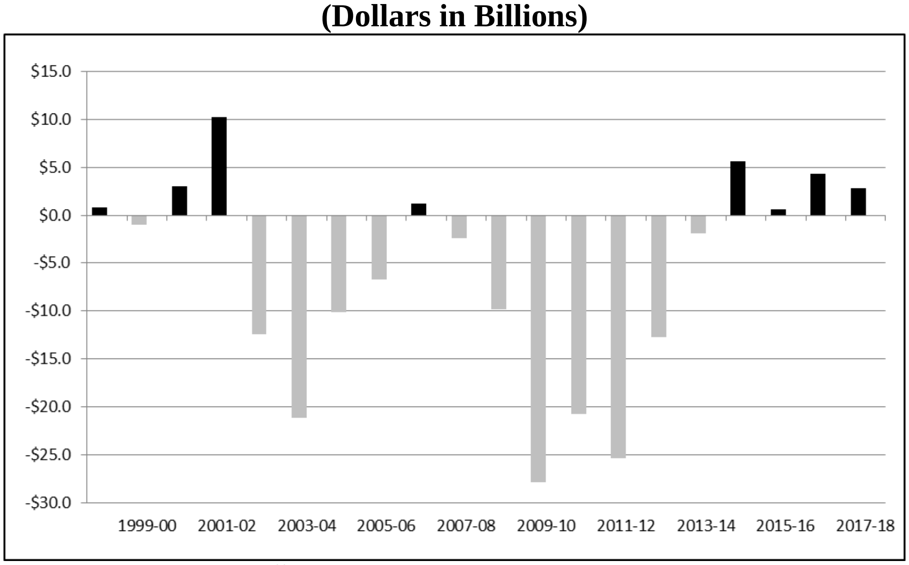
Budget Shortfall

The budget shortfall identified by the Administration for 2017-18 is $1.6 billion, representing less than 1.3 percent of overall resources. This shortfall is relatively small, especially compared to recent previous deficits, and well within the range of reasonable revenue estimation error that occurs with any statewide budget. In contrast, according to the Department of Finance (DOF), the deficit in 2009-10 approached $40 billion, and the deficits addressed from 2008-09 through 2011-12 were all in excess of $10 billion. Nevertheless, despite the relatively small expected deficit, DOF strikes several notes of caution, and in particular observes in the budget documents that "balanced budgets have been quickly followed by huge deficits."

According to the Administration, compared to the 2016 Budget Act, the two main factors causing this budget deficit are a revenue forecast that is $5.8 billion lower than expected and a current-year shortfall in the Medi-Cal program. The Administration notes that the deficit would be billions worse if not for the passage of a number of ballot measures at the November election, including Proposition 52 (hospital fee), Proposition 56 (tobacco tax), and Proposition 57 (prison reform). Proposition 55's extension of temporary income tax rates on the wealthiest Californians will begin to help balance the budget in 2018-19.

As shown in the figure below, the Legislative Analyst's Office (LAO) has a slightly different version of historic deficits and surpluses, although the overall profile largely mirrors the DOF version. For the budget year, however, based on its November 2016 fiscal analysis, the LAO expects the General Fund to have a surplus of $2.7 billion in 2017-18 rather than the slight deficit forecasted by the Administration. Using the LAO forecast, and accounting for the net impact of expenditure adjustments noted in the Governor's budget, the state would still be in a positive position. In addition, it should be noted that after 2014-15, negative transfers to the BSA (and an equivalent amount used for debt retirement) reduce revenues and transfers substantially, leading to smaller surpluses (or larger deficits) than would otherwise occur. For example, the deposits in 2016-17 are budgeted at $3.2 billion and in 2017-18 are expected to be $1.2 billion.

General Fund Deficits and Surpluses
1998-99 through 2017-18
(Dollars in Billions)



Source: Legislative Analyst's Office

Despite the somewhat different interpretations regarding the financial position of the General Fund for the current year and budget year, both DOF and LAO urge budgetary caution. As we discuss elsewhere in this report, estimates of General Fund revenues, are reliant on numerous assumptions and are likely subject to significant revision as additional quarterly income tax payments and the April personal income tax returns are taken into account. In addition, the change in the Administration at the national level imposes additional uncertainty with respect to both expenditure levels and support from federal funds.

Addressing the Shortfall

To address the DOF forecasted shortfall, the Administration proposes expenditure solutions, largely focused on one-time savings and delays in implementation. The budget proposes $3.2 billion in budget solutions to address the shortfall and rebuild the general reserve. The Administration asserts that these proposed actions are designed to minimize any negative effects on California residents and, rather than cut existing program levels, "temper spending growth" based on the lower revenue projections. However, the measures proposed by the Administration also result in delaying or cancelling components of the budget agreement reached with the Legislature last year. A summary and detailed listing of the budget delays, reductions and eliminations are presented in the appendix to this report. In broad terms, the budget solutions are:

- **Adjust Proposition 98 ($1.7 billion).** Appropriations made in 2015-16 and 2016-17 would over-appropriate the Proposition 98 minimum guarantee. The budget proposes adjustments designed to fund K-14 education at the guarantee for 2015-16 through 2017-18. With these adjustments overall K-14 funding still grows by $2.1 billion for 2017-18.

- **Reduce or Eliminate 2016 Appropriations ($0.9 billion**). The 2016-17 budget contained a large package of one-time spending. Much of that spending remains uncommitted and the budget proposes to eliminate the authority to spend the dollars. The two largest components of this proposal are eliminating the $400 million set-aside for affordable housing that was never allocated and a $300 million transfer to modernize state office buildings planned for 2017-18.

- **Constrain Spending Growth ($0.6 billion)**. The budget limits spending proposals to keep spending flat in 2017-18 compared to 2016-17, at about $123 billion. This involves pausing rate increases for child care, not providing Middle Class Scholarships to any new students, and not submitting a variety of spending proposals (including those to implement new legislation) from state departments that were otherwise justified.

CURRENT-YEAR BUDGET HIGHLIGHTS AND UPDATE

Adopted Budget

As adopted, the current year budget continues the restoration of essential educational, human services, and health programs, while maintaining the state's solid fiscal position. Specifically, the budget provides resources for many of the Legislature's priorities – especially in the areas of child care, human services, health, and education – within the established fiscal framework. The foundation for the plan largely begins with the Governor's base level funding, but incorporates distinctive and important changes in program spending reflecting the Legislature's priorities. The current year budget as adopted included funding for the following initiatives and programs:

Homelessness Initiative. The Senate's "No Place Like Home" initiative is a multifaceted plan to address homelessness and related issues. The initiative includes a grant program for supportive housing funded through Proposition 63 revenue bonds (which are currently going through the validation process). As part of this initiative, the budget includes more outreach to individuals with disabilities who may qualify for Supplemental Security Income (SSI), as well as additional resources for programs to reduce homelessness for CalWORKs families and for families that participate in the child welfare system. The plan also continues to fulfill the promise to rebuild the state's social safety net by reinvesting in CalWORKs through the elimination of the maximum family grant and by increasing the grant levels for maximum aid payment.

K-12 Education. In K-12 education, the budget continues to provide ongoing resources for the Local Control Funding Formula and one-time discretionary resources. To address the teacher shortage facing the state, there is additional funding for teacher recruitment, preparation, and retention. The plan funds a college readiness block grant, to ensure all students have the access and support needed to graduate and then attend college.

Early Childhood Education. For child care and preschool programs, the budget includes a major investment in childcare rate increases and preschool slots, together totaling over $500 million when fully phased-in over four years. These substantial increases are implemented as minimum wage increases in future years.

Higher Education. In higher education, the budget provides additional funds to enroll more resident undergraduate students at the University of California (UC) and the California State University (CSU) systems, and incorporates the Senate's "College Readiness" program to assist low-income students attend and complete college. In addition, $200 million more in Proposition 98 funding is provided to community colleges to expand access to career technical education.

Housing Programs. In housing, the budget includes a tax credit program that is intended to increase the effectiveness of affordable housing programs, adds enforcement staff to investigate housing discrimination complaints and facilitate compliance, adds a local government grant program that will facilitate the development of transitional housing for ex-offenders, and designates $400 million for affordable housing, if subsequent legislation is agreed upon.

Health and Developmental Services. In health and developmental services, the budget augments programs for healthcare workforce development, limits estate recovery in the Medi-Cal program, restores acupuncture services as a benefit in the Medi-Cal program, provides funding for health programs such as drug overdose and hepatitis prevention, and creates a grant program for children's crisis services. The plan also improves the closure plans for the state developmental centers and improves oversight of the transition of developmental center residents into the community.

Human Services. In human services, the budget eliminates the CalWORKs maximum family grant, increases the SSI/SSP grant, provides augmentations for the Immigration Services Program and the Commercially Sexually Exploited Children Program, provides additional resources for the monitoring of psychotropic medications for foster youth, makes one-time investments in senior nutrition programs and the State Emergency Food Assistance Program, and makes clarifications regarding the legal protections for immigrant youth.

Resources and the Environment. In resources and the environment, the budget continues oversight of the drought and statewide efforts to reduce water consumption. In addition, the budget provides oversight of the energy and utility ratepayer funds, expedites Aliso Canyon mitigation efforts, and provides funding for pest prevention studies in the Department of Pesticide Regulation.

Public Safety and Justice. In public safety and justice, the budget adheres to the Legislature's emphasis on positive programs to help individuals avoid the criminal justice system, rehabilitate incarcerated individuals, and facilitate the transition of ex-offenders to society through longer term and more effective programs. Among the priorities is to increase the availability of transitional housing, mental health and substance abuse treatment, and services for victims of domestic violence.

Recent Developments

Since the adoption of the 2016 Budget Act, there have been various expenditure adjustments and several significant proposed changes. These changes occur in K-12 education, health and human services and one-time statewide expenditures. For example, as more fully described in the next section, the Governor's budget affects funding for some current year augmentations approved by the Legislature, including eliminating the augmentations for healthcare workforce development, eliminating the grant program for children's crisis services, cutting the community infrastructure grants for public safety diversion programs, delaying increases to child care and early education, and eliminating the outreach to individuals with disabilities component of the Homelessness Initiative. In addition, other modest adjustments – and proposed adjustments – are scattered throughout the budget. The resulting differences between the adopted and revised current year budget are presented below:

General Fund Expenditures
Current Year Adopted and Revised
(Dollars in Millions)

Program Area	Adopted 2016-17	Revised 2016-17	Change	Percent Change
K-12 Education	$51,277	$50,589	-$688	-1.34%
Higher Education	14,531	14,527	-4	-0.03%
Health and Human Services	33,240	35,263	2,023	6.09%
Corrections and Rehabilitation	10,571	10,889	328	3.10%
Business, Consumer Services, Housing	877	493	-384	-43.79%
Transportation	237	225	-12	-5.06%
Natural Resources	2,819	3,110	291	10.32%
Environmental Protection	88	90	2	2.27%
Labor and Workforce Development	176	177	1	0.57%
Government Operations	1,756	1,772	16	0.91%
General Government				
Non-Agency Departments	752	787	35	4.65%
Tax Relief / Local Government	474	459	-15	-3.16%
Statewide Expenditures	2,157	880	-1,277	-59.20%
Legislative, Judicial and Executive	3,513	3,500	-13	-0.37%
Total	**$122,468**	**$122,761**	**$293**	**0.24%**

BUDGET YEAR PROPOSED EXPENDITURES

As noted, the proposed budget incorporates additional required programmatic increases and limited new spending. The table below summarizes the Governor's proposed expenditures by program area. The largest dollar changes in expenditures by program are in health and human services and K-12 education.

General Fund Expenditures
Current and Budget Year
(Dollars in Millions)

Program Area	Revised 2016-17	Proposed 2017-18	Change	Percent Change
K-12 Education	$50,589	$52,169	$1,580	3.12%
Higher Education	14,527	14,627	100	0.69%
Health and Human Services	35,263	33,994	-1,269	-3.60%
Corrections and Rehabilitation	10,899	11,088	189	1.73%
Business, Consumer Services, Housing	493	388	-105	-21.30%
Transportation	225	243	18	8.00%
Natural Resources	3,110	2,811	-299	-9.61%
Environmental Protection	90	89	-1	-1.11%
Labor and Workforce Development	177	122	-55	-31.07%
Government Operations	1,772	741	-1,031	-58.18%
General Government				
Non-Agency Departments	787	691	-96	-12.20%
Tax Relief / Local Government	459	435	-24	-5.23%
Statewide Expenditures	880	1,800	920	104.55%
Legislative, Judicial and Executive	3,500	3,322	-178	-5.09%
Total	**$122,761**	**$122,520**	-$241	-0.20%

The Governor's budget proposes some specific policy and budgetary changes. Some of the more important aspects of the budget proposal are outlined below:

Education

Education Funding. Estimated reductions in General Fund revenues reduce the Proposition 98 guarantee in the 2015-16 and 2016-17 fiscal years, but there is still significant growth in Proposition 98 in 2017-18 over the 2016-17 year, resulting in a net increase in investments in K-14 education over the three-year period. The key changes in the education area include:

- **Early Education.** As a result of dampened General Fund revenues, the budget proposes to delay increases to child care and early education that were scheduled for 2017-18 as a result of the 2016 budget agreement. Specifically, the budget includes the full year costs of the increases in provider reimbursement rates and additional state preschool slots provided in 2016-17, but delays additional planned rate increases, cost-of-living increases, and state preschool slots from 2017-18 until 2018-19.

- **K-12 Schools.** Per student funding levels (from all fund sources) will increase to $15,216 in 2017-18 from $14,822 in 2016-17 (and from $14,135 in 2015-16). Proposition 98 funding, although increasing by $2.1 billion from 2016-17 (revised) to 2017-18 for a total of $73.5 billion, was reduced in 2015-16 and 2016-17 from the 2016 Budget Act levels. These reduced guarantee levels means the state must reduce expenditures in these years to avoid over-appropriating the Proposition 98 guarantee. The budget proposes to accomplish this by deferring one-time and ongoing expenditures until the 2016-17 and 2017-18 years. In 2017-18, the bulk of new funding, in additional to paying off deferrals, is invested in transition funding for the Local Control Funding Formula ($744 million in new funding in 2017-18) – funding approximately 96 percent of the formula.

- **Higher Education.** Despite lower than expected revenue growth, the budget continues to provide additional funding to the state's higher education system. Specifically, the budget creates a grant program to increase student success in community colleges, as well as continue the Administration's multi-year funding plan at UC and CSU. However, in order to support long-term stable growth in funding for higher education and benefit the General Fund, the Administration proposes to phase out the Middle Class Scholarship Program.

Health

Coordinated Care Initiative (CCI). The budget estimates that CCI will no longer be cost-effective and does not meet the statutory savings requirements. Therefore, the budget discontinues many components of CCI in 2017-18. As a result, the budget would: (1) remove IHSS benefits from plan capitation rates, (2) eliminate the statewide authority responsible for bargaining IHSS workers' wages and benefits in the seven CCI counties; and (3) re-establish the state-county share of cost arrangement for the IHSS program that existed prior to the implementation of CCI. The net result of these three changes is a General Fund savings of $626.6 million in 2017-18.

The budget notes that Cal MediConnect (the duals demonstration project and a component of CCI) has the potential to reduce the health care costs for individuals and improve health outcomes and, consequently, proposes to extend the Cal MediConnect program. The budget reflects approximately $20 million in General Fund savings from the continuation of Cal MediConnect, as allowed under federal law through December 31, 2019.

Affordable Care Act (ACA). Although the incoming federal administration and leaders in Congress have suggested major changes to the ACA and Medi-Cal, the budget continues to reflect existing state and federal law. The budget notes that the Administration stands ready to play a constructive role to protect and enhance the lives and health of Californians.

Human Services and Housing

Housing and Disability Advocacy Program. The budget includes one-time savings of $45 million General Fund in the current year by halting implementation of the Housing and Disability Advocacy Program, which was included in the 2016 Budget Act to incentivize local governments to boost outreach and advocacy efforts to increase enrollment in the SSI/SSP program.

Housing Programs. The budget eliminates the $400 million set aside in the current year for affordable housing that was never allocated. In addition, the budget provides $3.2 billion in various state and federal funding for housing affordability and homelessness programs. The budget also includes $355 million in General Fund for debt service on previously-passed affordable housing bonds.

Transportation and Infrastructure

Transportation Funding Package. The budget proposes $1.9 billion in 2017-18, and $4.3 billion on an annual ongoing basis, for transportation funding and reform. The annual funding package provides $2.1 billion from a new $65 fee on all vehicles: $1.1 billion by setting the gasoline excise tax at 21.5 cents (includes future adjustments for inflation); $425 million from an 11-cent increase in the diesel excise tax; $500 million in additional cap-and-trade proceeds; and $100 million from cost-saving reforms to be implemented by Caltrans. The $1.9 billion in additional funding in 2017-18 includes $235 million from the acceleration of General Fund loan repayments over the next three years ($706 million total), rather than repaying these loans over the next 20 years. The additional funding will be used for local streets and roads, transit and intercity rail capital projects, highway maintenance, the Active Transportation Program, and trade corridors.

Statewide Infrastructure Investments. The budget proposes to reduce by $300 million the General Fund transfer to a new State Office Infrastructure Fund to be used for deferred renovation, or replacement of, state office buildings in the Sacramento region.

Resources, Environment and Energy

Cap-and-Trade Revenues. The budget proposes legislation, requiring a 2/3rds urgency vote, to confirm the Air Resources Board’s authority to administer Cap-and-Trade auctions beyond 2020. Additionally, the budget proposes the following $2.2 billion expenditure plan: (1) $900 million continuously appropriated for state transit assistance ($75 million), transit and intercity rail ($150 million), the Sustainable Communities Strategy ($300 million), and the state’s high-speed rail project ($375 million), and; (2) $1.3 billion in discretionary funding for a variety of projects. This includes $500 million for the Governor’s transportation package and $363 million for the Air Resources Board’s Low Carbon Transportation Program, as well as $392 million for a variety of other greenhouse gas reducing programs.

Continued Drought Response. The budget proposes to build on previous years efforts to respond to drought impacts including: (1) $5 million General Fund for the Department of Water Resources (DWR) to provide emergency drinking water support for small communities; (2) $88 million General Fund and $3 million from the State Responsibility Area Fund for CalFIRE to expand fire protection in the 2017 fire season ($90 million General Fund in the current year to initiate these enhancements); (3) $52.7 million General Fund for the Office of Emergency Services to provide assistance to counties through the California Disaster Assistance Act, and; (4) $2.6 million General Fund and $900,000 from the Harbors and Watercraft Fund for the DWR to continue implementation of the state's Delta Smelt Resiliency Strategy.

Energy Programs. The budget includes $953,000 from various special funds to implement a variety of transparency reforms, and $549,000 from various special funds to improve governance and to collaborate with other agencies working on climate and energy issues.

Public Safety and Judicial

Proposition 57. The budget includes significant changes for the California Department of Corrections and Rehabilitation (CDCR) related to the passage of Proposition 57, which changed the calculation for parole, authorized an increase in credits for good behavior and participating in programming, and changed the way the determination is made regarding juveniles being tried as adults for certain crimes. The budget proposes $5.7 million General Fund for the workload associated with the implementation of Proposition 57. In addition, the budget estimates a net savings of $22.4 million General Fund in 2017-18, growing to a net savings of approximately $140 million by 2020-21.

Inpatient Psychiatric Programs. The Department of State Hospitals (DSH) currently operates 1,156 inpatient mental health treatment beds at three CDCR prisons. The budget proposes transferring these programs to CDCR, effective July 2017. In addition, the budget redirects $250.4 million and 1,977.6 positions from DSH to CDCR.

Fiscal Management

Budget Reserve Deposits. As an integral part of the proposal, the budget includes measures that would result in additional reserves for fiscal emergencies. The deposit to the BSA, redefined by Proposition 2, will total $1.2 billion. This will result in a $7.9 billion balance in that account at the conclusion of 2016-17, when combined with prior deposits to the fund. This would represent a funding level equivalent to 63 percent of the constitutional target amount.

Debt Repayments. The budget continues to pay down the debt overhang as required under Proposition 2. Under the proposal, $1.2 billion in Proposition 2 funds will pay off loans from special funds and past Proposition 98 liabilities. $252 million will pay off budgetary borrowing from special funds, $400 million for Proposition 98 settle-up costs, $235 for pre-Proposition 42 transportation loans, and $100 million for state retiree health. In addition, the Administration proposes a payment of $169 million for UC pension obligations.

STATE ECONOMY AND REVENUES

Economic Outlook

Economic forecasts play an integral role in the state's revenue forecast and fiscal outlook. The state's revenue structure is very 'elastic', meaning it is highly sensitive to economic changes. This is particularly true for personal income tax receipts, which tend to grow (or decline) proportionally more than increases (or decreases) in the underlying income base. The sales and use tax, the second largest state revenue source, is sensitive to consumer confidence and consumption patterns. The property tax – which benefits the General Fund through additional resources for K-12 education – reacts to changes in the underlying property asset values and home sale prices.

The Governor and the LAO both forecast continued growth in the economy, and accompanying increases in state revenues. The state's recovery continued in 2016, but at a somewhat slower pace than in the previous two years. In California, personal income should display relatively strong growth in 2017 and 2018. For 2017, the pace of income growth in California is expected to be roughly four percent, or about the same as in 2016. Nationally, while significant concerns remain regarding income distribution, job gains have continued, labor participation has improved, and widespread wage gains are finally occurring. The Administration's economic forecast assumes that the current moderate economic recovery will rebound somewhat in 2017, leading to broad-based improvements in both the U.S. and California economies over the next two years.

The assumed growth rates for the U.S. and California are equivalent to rates of improvement in a mature economic expansion, reflecting the consensus outlook that U.S. economic growth is returning to more normal levels. While there are no obvious signs of an economic slowdown, the Administration nevertheless notes three major risks to the economic forecast – the state's housing supply, changes in international trade, and the stock market. Specifically:

- California housing supply has expanded slowly and unevenly across the state, and caused statewide housing stress, particularly in areas of high employment growth. The lack of supply and higher prices could constrain the ability of business to relocate or expand in California.

- International trade is a vital component of the U.S. and California economies, equivalent to about 30 percent of the national GDP. Changes to existing trade agreements upon which this central component of the economy is based could have a negative impact on economic growth and employment in the state.

- The stock market continues to show robust performance, with the S&P 500 Index growing by almost 10 percent in 2016. A stock market correction that causes firms to slow or reverse growth could significantly alter California's economic performance and state revenues.

General Fund Revenues

California relies on a broad range of taxes and other revenues to support the activities of the General Fund; however, the personal income tax, sales and use tax, and corporation taxes account for over 97 percent of General Fund revenues. For the budget year, the personal income tax is expected to generate $85.9 billion (68.5 percent), the sales and use tax $25.2 billion (20.1 percent), and the corporation tax $10.9 billion (8.7 percent). As discussed, the Administration's revenue estimates for the major taxes are somewhat reduced from the 2016 Budget Act. California's economy and revenues are expected to continue to grow, although somewhat more slowly than assumed in the 2016 Budget Act. The Governor's General Fund revenue forecast has been reduced, reflecting lower growth in wages, proprietorship income, consumption, and investment. As a result, before accounting for transfers, such as to the BSA, General Fund revenue is lower than the 2016 Budget Act projections for the period 2015-16 through 2017-18.

Over the three year period, the Administration's estimated General Fund revenues are down by approximately $5.8 billion from the 2016 Budget Act, or a modest 1.6 percent decline. From the current year to budget year, the major revenue sources are expected to grow by 3.3 percent for the personal income tax, 0.7 percent for the sales and use tax, and 4.7 percent for the corporation tax. Overall year-to-year revenue growth is estimated to be 2.7 percent. The table below presents the state's General Fund revenues for the current and budget year:

General Fund Revenues
Current Year Revised and Budget Year Forecast
(Dollars in Millions)

Revenue Source	2016-17	2017-18	Change	Percent Change
Personal Income Tax	$83,136	$85,866	$2,730	3.28%
Sales and Use Tax	24,994	25,179	185	0.74%
Corporation Tax	10,389	10,878	489	4.71%
Insurance Tax	2,309	2,368	59	2.56%
Alcohol Beverage Tax	370	372	2	0.54%
Cigarette Tax	79	65	-14	-17.72%
Motor Vehicle Fees	24`	24	0	0.00%
Other Taxes and Fees	648	431	-217	-33.49%
Subtotal	$121,949	$125,183	3,234	2.65%
Transfer to BSA	-3,184	-1,156	2,028	-63.69%
Total	**$118,765**	**$124,027**	**$5,262**	**4.43%**

SUBCOMMITTEE NO. 1

EDUCATION

K-14 Education

Higher Education

Proposed Expenditures of Proposition 98 Resources

BACKGROUND

California provides academic instruction and support services to over six million public school students in kindergarten through twelfth grade (K-12) and 2.3 million students in community colleges. There are 58 county offices of education, approximately 1,000 local K-12 school districts, more than 10,000 K-12 schools, and more than 1,200 charter schools throughout the state, as well as 72 community college districts, 113 community college campuses, and 70 educational centers. Proposition 98, which was passed by voters as an amendment to the state Constitution in 1988, and revised in 1990 by Proposition 111, was designed to guarantee a minimum level of funding for public schools and community colleges.

The proposed 2017-18 budget includes funding at the Proposition 98 minimum guarantee level of $73.5 billion. The budget proposal also revises the 2016-17 Proposition 98 minimum guarantee downward to $71.4 billion, a decrease of $506 million from the 2016 Budget Act, and revises the 2015-16 Proposition 98 minimum guarantee down to $68.7 billion, a decrease of $379 million from the 2016 Budget Act as a result of a decline in revenues. The Governor also proposes to pay $400 million in Proposition 98 settle-up towards meeting the 2009-10 Proposition 98 minimum guarantee. Together, the revised guarantee levels and settle-up payments net out to a total of almost $1.6 billion in increased funding for education over the three years, as compared to the 2016 Budget Act.

The Governor proposes to eliminate the over-appropriation of funding for the guarantee in 2015-16 and 2017-18 by shifting or deferring expenditures to the 2016-17 and 2017-18 years, as discussed later in this section. The remaining Proposition 98 funds in 2017-18, after the changes for over-appropriations and funding workload growth and cost-of-living adjustments, are proposed to be used primarily towards implementing the Local Control Funding Formula (LCFF). These proposals are more fully described later in this section and in separate sections of this report.

Proposition 98 Funding. State funding for K-14 education—primarily K-12 local educational agencies and community colleges—is governed largely by Proposition 98. The measure, as modified by Proposition 111, establishes minimum funding requirements (referred to as the “minimum guarantee”) for K-14 education. General Fund resources, consisting largely of personal income taxes, sales and use taxes, and corporation taxes, are combined with the schools’ share of local property tax revenues to fund the Proposition 98 minimum guarantee. These funds typically represent about 80 percent of statewide funds that K-12 schools receive. Non-Proposition 98 education funds largely consist of revenues from local parcel taxes, other local taxes and fees, federal funds and proceeds from the state lottery. In recent years, there have been 2 statewide initiatives that increased General Fund Revenues and therefore, Proposition 98. Proposition 30, passed by the voters in 2012, raised sales and income taxes, but phases out over seven years. Recently, anticipating the expiration of the Proposition 30 taxes, Proposition 55 was passed by voters in 2016, extending the income tax portion of Proposition 30 for another 12 years.

The table below summarizes overall Proposition 98 funding for K-12 schools and community colleges since 2007-08, or just prior to the beginning of the steep recent recession. 2011-12 marks the low point for the guarantee with steady increases since then. The economic recession impacted both General Fund resources and property taxes. The amount of property taxes has also been impacted by a large policy change in the past few years—the elimination of redevelopment agencies (RDAs) and the shift of property taxes formerly captured by the RDAs back to school districts. The guarantee was adjusted to account for these additional property taxes, so although Local Educational Agencies (LEAs) received significantly increased property taxes starting in 2012-13, they received a roughly corresponding reduction in General Fund.

Proposition 98 Funding
Sources and Distributions
(Dollars in Millions)

	Pre-Recession **2007-08**	Low Point **2011-12**	Revised **2015-16**	Revised **2016-17**	Proposed **2017-18**
Sources					
General Fund	42,015	33,136	48,989	50,330	51,351
Property taxes	14,563	14,132	19,681	21,038	22,160
Total	**56,577**	**47,268**	**68,670**	**71,368**	**73,511**
Distribution					
K-12	50,344	41,901	60,655	63,039	65,007
CCC	6,112	5,285	7,933	8,246	8,424
Other	121	83	82	83	80

Source: Legislative Analysts' Office and Department of Finance

Calculating the Minimum Guarantee. The Proposition 98 minimum guarantee is determined by comparing the results of three "tests", or formulas, that are based on specific economic and fiscal data. The factors considered in these tests include growth in personal income of state residents, growth in General Fund revenues, changes in student average daily attendance, and a calculated share of the General Fund. When Proposition 98 was first enacted by the voters in 1988, there were two "tests", or formulas, to determine the required funding level. Test 1 calculates a percentage of General Fund revenues based on the pre-Proposition 98 level of General Fund that was provided to education, plus local property taxes. Test 2 calculates the prior year funding level adjusted for growth in student average daily attendance and per capita personal income. K-14 education was guaranteed funding at the higher of these two tests. In 1990, Proposition 111 added a third test, Test 3 which takes the prior year funding level and adjusts it for growth in student average daily attendance and per capita General Fund revenues. The Proposition 98 formula was adjusted to compare Test 2 and Test 3, the lower of which is applicable. This applicable test is then compared to Test 1 and the higher of the tests determines the Proposition 98 guarantee level.

Proposition 98 Tests
Calculating the Level of Education Funding

Test	Calculated Level	Operative Year	Times Used
Test 1	Based on a calculated percent of General Fund revenues (currently around 38.1%).	If it would provide more funding than Test 2 or 3 (whichever is applicable).	4
Test 2	Based on prior year funding, adjusted for changes in per capita personal income and attendance.	If growth in personal income is ≤ growth in General Fund revenues plus 0.5%.	13
Test 3	Based on prior year funding, adjusted for changes in General Fund revenues plus 0.5% and attendance.	If statewide personal income growth > growth in General Fund revenues plus 0.5%.	11

Generally, Test 2 is operative during years when the General Fund is growing quickly and Test 3 is operative when General Fund revenues fall or grow slowly. The Test 1 percentage is historically-based, but is adjusted, or "rebenched", to account for large policy changes that impact local property taxes for education or changes to the mix of programs funded within Proposition 98. In the past few years, rebenching was done to account for property tax changes, such as the dissolution of the RDAs, and program changes, such as removing childcare from the Proposition 98 minimum guarantee and adding mental health services. In the budget year, the Test 1 calculation is adjusted to reflect RDA changes. Proposition 98 tests are based on estimated factors during budget planning; however, the factors are updated over time and can change past guarantee amounts and even which test is applicable in a previous year. Statute specifies that at a certain point the Proposition 98 minimum guarantee for a given year shall be certified and no further changes shall be made. The guarantee was last fully certified for 2007-08.

The Governor's proposal assumes that in all three years; 2015-16, 2016-17, and 2017-18, the Proposition 98 guarantee is calculated under Test 3. A Test 3 is reflective of strong per capita personal income growth in comparison to relatively lower General Fund growth. Generally, the Proposition 98 minimum guarantee calculation was designed in order to provide growth in education funding equivalent to growth in the overall economy, as reflected by changes in personal income (incorporated in Test 2). In a Test 3 year, the Proposition 98 minimum guarantee does not grow as fast as in a Test 2 year, in recognition that the state's General Fund is not reflecting the same strong growth as personal income and the state may not have the resources to fund at a Test 2 level; however, a maintenance factor is created as discussed in more detail later. As noted in the table above, in most years the Proposition 98 minimum guarantee has been determined by the application of Test 2; however, this latest budget proposal which includes reductions in General Fund Revenues, is pushing the guarantee back into an era of Test 3.

Suspension of Minimum Guarantee. Proposition 98 includes a provision that allows the Legislature and Governor to suspend the minimum funding requirements and instead provide an alternative level of funding. Such a suspension requires a two-thirds vote of the Legislature and the concurrence of the Governor. To date, the Legislature and Governor have suspended the Proposition 98 minimum guarantee twice - in 2004-05 and 2010-11. While the suspension of Proposition 98 can create General Fund savings during the year in which it is invoked, it also creates obligations in the out-years, as explained below.

Maintenance Factor. When the state suspends the Proposition 98 minimum guarantee or Test 3 is operative (that is, when the Proposition 98 guarantee grows more slowly due to declining or low General Fund growth), the state creates an out-year obligation referred to as the "maintenance factor." When growth in per capita General Fund revenues is higher than growth in per capita personal income (as determined by a specific formula also set forth in the state Constitution), the state is required to make maintenance factor payments, which accelerate growth in K-14 funding, until the determined maintenance factor obligation is fully restored. Outstanding maintenance factor balances are adjusted each year by growth in student average daily attendance and per capita personal income.

The maintenance factor payment is added on to the minimum guarantee calculation using either Test 1 or Test 2.

- In a Test 2 year, the rule of thumb is that roughly 55 percent of additional revenues would be devoted to Proposition 98 to pay off the maintenance factor.

- In a Test 1 year, the amount of additional revenues going to Proposition 98 could approach 100 percent or more. This can occur because the required payment would be a combination of the 55 percent (or more) of new revenues plus the established percentage of the General Fund—roughly 38.1 percent—that is used to determine the minimum guarantee.

Prior to 2012-13, the payment of maintenance factor was made only on top of Test 2; however, in 2012-13, the Proposition 98 guarantee was in an unusual situation as the state recovered from the recession. It was a Test 1 year and per capita General Fund revenues were growing significantly faster than per capita personal income. Based on a strict reading of the Constitution, the payment of maintenance factor is not linked to a specific test, but instead is required whenever growth in per capita General Fund revenues is higher than growth in per capita personal income. As a result the state funded a maintenance factor payment on top of Test 1 and this interpretation continues today and results in the potential for up to 100 percent or more of new revenues going to Proposition 98 in a Test 1 year with high per capita General Fund growth. This was the case in 2014-15, when the maintenance factor payment was more than $5.6 billion.

The Governor's proposal assumes a Test 3 calculation of the guarantee in all three years (2015-16, 2016-17, and 2017-18) and therefore a maintenance factor is created in each of the three years resulting in a total outstanding maintenance factor balance of $1.6 billion at the end of 2017-18. In 2017-18, a relatively small amount of new revenues – approximately $1.5 billion - could move the guarantee into a Test 2 calculation and require a maintenance factor payment, therefore increasing funding for schools in the budget year.

Settle-Up. Every year, the Legislature and Governor estimate the Proposition 98 minimum guarantee before the final economic, fiscal, and attendance factors for the budget year are known. If the estimate included in the budget for a given year is ultimately lower than the final calculation of the minimum guarantee, Proposition 98 requires the state to make a "settle-up" payment, or series of payments, in order to meet the final guarantee for that year. The Governor's budget proposes General Fund settle-up payments of $400 million in 2017-18 counting towards the 2009-10 minimum guarantee. After this payment, the state would owe $626 million in settle-up for years prior to 2014-15. In the recent past, the state was not required to make settle-up payments on schedule; however, Proposition 2, passed in 2014, requires the state to spend a minimum amount each year to buy down eligible state debt. Proposition 98 settle-up debt is one area that meets Proposition 2 requirements, and in compliance with this requirement, the state has made settle-up payments in the past few years.

Spike Protection. Proposition 98 also has a built-in formula to prevent large increases in the guarantee, referred to as "spike protection". This constitutional formula specifies that in years when a Test 1 is operative and is greater than the Test 2 amount by 1.5 percent of General Fund revenues, then when calculating the guarantee level in the subsequent year, the excess amount over the 1.5 percent of General Fund revenues is not included in the calculation. This part of the formula has only been in play twice, and reduced the impact of revenue gains on the 2013-14 and 2015-16 minimum guarantee calculations.

Proposition 98 Rainy Day Fund and District Reserve Caps. Proposition 2 also requires a deposit in a Proposition 98 Rainy Day Fund under certain circumstances. These required conditions are that maintenance factor (accumulated prior to 2014-15) is paid off, Test 1 is in effect, the Proposition 98 guarantee is not suspended, and no maintenance factor is created. Related statute requires that in the year following a deposit into this fund, a cap on local school district reserves would be implemented. Both the Governor and the Legislative Analyst's Office (LAO) continue to project that a Test 1 will not be in effect in their forecast period over the next few years. The conditions needed to trigger Test 1 include significant year-over-year revenue gains that are unlikely, given the modest growth projections and potential for a slowing economy in the near future.

Outstanding Obligations. The state currently has paid most of the outstanding obligations to school districts and community colleges that built up over the last recession. However, as of the 2016 Budget Act, the state still has more than $1.8 billion in unpaid mandate claims. The Governor's proposal for 2017-18 would retire approximately $287 million of these mandate obligations.

GOVERNOR'S PROPOSAL

The budget includes a proposed Proposition 98 funding level of $64 billion for K-12 programs. This includes a year-to-year increase of almost $2 billion in Proposition 98 funding for K-12 education, as compared to the revised Proposition 98 K-12 funding level for 2016-17. Under the Governor's proposal, ongoing K-12 Proposition 98 per pupil expenditures increase from $10,579 provided in 2016-17 (revised) to $10,910 in 2017-18. This 2017-18 proposed Proposition 98 funding level for K-12 reflects a per-pupil increase of 3.1 percent, as compared to the revised per-pupil funding level provided for in 2016-17. The Governor's major K-12 spending proposals are identified below.

K-12 Local Control Funding Formula. The 2013 Budget Act changed how the state provides funding to school districts and county offices of education by creating the Local Control Funding Formula (LCFF). Since its inception, the state has dedicated a large portion of the new Proposition 98 revenues in each year towards full implementation of the LCFF. The 2016 Budget Act included $2.9 billion in new Proposition 98 funds for LCFF implementation. However, the Governor's budget includes Proposition 98 estimates for 2015-16 and 2016-17 that are below the levels assumed in the 2016 Budget Act and, as a result, proposes to defer $859.1 million of the funding scheduled to be provided for LCFF implementation from 2016-17 to 2017-18 (payments to LEAs would shift from June 2017 to July 2017). This would result in a one-time deferral, fully paid off in the 2017-18 fiscal year. In addition to the one-year deferral, the Governor's budget proposes an increase of approximately $744 million in 2017-18 to implement the LCFF. Overall, this investment results in the formula funded at 96 percent of full implementation in 2017-18, maintaining the same implementation percentage assumed as of the 2016 Budget Act. County offices of education reached full implementation with the LCFF allocation in the 2014 Budget Act. The accountability system for LCFF is also not yet fully implemented. Implementation of LCFF is more fully discussed in *Local Control Funding Formula and Accountability* in this report.

Discretionary Funds / Mandate Backlog Reduction. The budget proposes an increase of $287 million in discretionary one-time Proposition 98 funding provided to school districts, charter schools, and county offices of education. The Administration indicates that this funding will allow school districts, charter schools, and county offices of education to continue to invest in implementing state adopted academic content standards, upgrade technology, provide professional development, support beginning teacher induction and address deferred maintenance projects. These funds would also serve to offset outstanding mandate reimbursement claims. In addition, as part of the actions taken to reduce the Proposition 98 appropriation levels, $310 million in discretionary, one-time Proposition 98 expenditures for school districts, charter schools, and county offices of education for these same purposes in 2015-16, would be shifted to the 2016-17 year.

K-12 Special Education. The budget proposes to begin a series of stakeholder meetings during the spring budget process on the funding model for special education. In 2017-18, the budget proposes expenditures of $3.2 billion in Proposition 98 funding and $1.2 billion in federal funds for special education. Unlike other categorical programs, funding for special education was not rolled into the funding for local educational agencies under the LCFF. LEAs are required to operate as, or be a member of, a Special Education Local Plan Area (SELPA). The majority of funding for special education is provided to the SELPAs which distribute funds to member LEAs agencies based on a locally-determined formula. The Governor's budget notes that stakeholder conversations would be centered on principles aligned with the LCFF, including equity, transparency, flexibility, local control and focus on the needs of students.

K-12 School Facilities. In November, 2016, the voters passed the Kindergarten through Community College Facilities Bond Act of 2016 (Proposition 51), which authorizes the state to sell $9 billion in general obligation bonds with the proceeds to be used for K-12 and community college facilities. The K-12 share of the proceeds, $7 billion, would be subject to the rules of the state's existing school facilities program and could be used for new construction, modernization, career technical education facilities, and charter school facilities. The Administration notes concerns with the proper expenditure of funding from prior facilities bonds and proposes to strengthen program oversight and accountability prior to expenditure of the Proposition 51 bond funds. The Administration plans to accomplish this in two ways: (a) supporting the State Allocation Board and the Office of Public School Construction on revising and creating policies and regulations; and, (b) introducing legislation requiring that the annual K-12 Audit Guide include facility bond expenditures.

Enrollment and Cost-of-Living Adjustments. The proposed budget reflects an estimated decrease in student enrollment in the K-12 system. Specifically, it reflects a decrease of $168.9 million in 2016-17, as a result of a decrease in the projected average daily attendance (ADA), compared to the 2016 Budget Act. For 2017-18, the Governor's proposed budget reflects a decrease of $63.1 million to reflect a projected further decline in ADA for the budget year. (For charter schools, the Governor's proposed budget funds an estimated increase in charter school ADA , as discussed below.) The proposed budget also provides $58.1 million to support a 1.48 percent cost-of-living adjustment for categorical programs that are not included in the new LCFF. These programs include special education and child nutrition, among others. The proposed funding level for the LCFF includes cost-of-living adjustments for school districts and county offices of education.

Other K-12 Education Budget Proposals. Additional proposals contained within the budget related to K-12 education include the following**:**

- **Career Technical Education Incentive Grant.** The budget includes $200 million in Proposition 98 funding for career technical education grants to local educational agencies. This is the final installment of funding for a three-year grant program adopted in the 2015 Budget Act.

- **Proposition 39 Energy Efficiency Investments**. The budget proposes to allocate $422.9 million in Proposition 39 energy funds available in 2017-18 to K-12 school districts and charter schools for energy efficiency project grants. Funds for Proposition 39 flow from a change made to the corporate income tax code in 2013-14. Under the Proposition, half of the General Fund revenue gained as a result of the tax changes are to be used for clean energy projects in schools for the first five years. 2017-18 is the fifth and final year that funds must be used for this purpose.

- **Charter Schools**. The budget proposes an increase of $93 million in Proposition 98 funds to reflect a projected increase in charter school ADA.

- **Special Education**. The budget proposes a decrease of $4.9 million in Proposition 98 funds to reflect a projected decrease in special education ADA.

- **Proposition 56.** The budget proposes $29.9 million to support tobacco and nicotine prevention and reduction programs at K-12 schools. This funding is the result of an increase in taxes on tobacco products as a result of the passage of Proposition 56 in

November 2016, which requires a percentage of the revenues to be available for school-based tobacco prevention programs.

- **Proposition 47.** The budget proposes $10.1 million in Proposition 98 funding to support improved outcomes for students who are truant, at risk of dropping out of school, or are victims of crimes. Proposition 47 reduced penalties for some crimes and required that 25 percent of the resulting savings be invested in K-12 truancy, dropout prevention, victim services, and drug and mental health treatments. SB 527 (Liu), Chapter 533, Statutes of 2016 and AB 1014 (Thurmond), Chapter 397, Statues of 2016 created a program for the expenditure of K-12 Proposition 47 funds. Pursuant to this legislation, the Department of Education will award grants to LEAs and provide training and technical assistance to grantees on pupil engagement, school climate, truancy reduction, and supporting pupils who are at risk of dropping out of school or are victims of crime. This is a slight increase from the $9.9 million estimate from this funding source included in the 2016 Budget Act.

- **Mandate Block Grant.** The budget provides $8.5 million in Proposition 98 for the mandate block grant to reflect the addition of the Training for School Employee Mandated Reporters program.

- **Child Care and Development**. The budget provides nearly $3.8 billion total funds ($1 billion federal funds; $1.7 billion Proposition 98 General Fund; and $1 billion non-Proposition 98 General Fund) for child care and early education programs. However, the Governor does not include scheduled increases in rates and state preschool slots that were scheduled to be included for the 2017-18 year as part of the 2016-17 budget agreement. This saves $226.8 million in 2017-18 ($121.4 million in non-Proposition 98 General Fund and $105.4 million in Proposition 98.)

ISSUES TO CONSIDER

Legislative Education Priorities.
Reflecting the cautious approach of the Governor's overall budget picture, the budget does not include significant new programs in the area of K-12 education. Most new ongoing funds are committed to further implementation of the LCFF; however, because the cost of full funding increases each year for growth and COLA, the new funding in 2017-18 essentially maintains the same level of progress towards full implementation as the current year (96 percent of full funding.) The Legislature should continue to monitor progress towards full implementation of the LCFF and understand that continued investment over the next few years will be needed to reach funding targets. Since the inception of LCFF, this continued investment eats up the bulk of new ongoing Proposition 98 resources. To the extent large state revenue gains and corresponding Proposition 98 growth we have seen in the past few years slow, it will be critical to understand both how new revenue growth and expenditure changes within the guarantee can continue to be tapped for the LCFF over the next few years. The accountability part of this funding formula is also key for the Legislature to ensure that education resources are directed where they are needed most. (See *Local Control Funding Formula and Accountability* for a detailed discussion of the LCFF and accountability.)

Ultimately, while new ongoing resources under Proposition 98 are limited, the Legislature should prioritize expenditure funds to align with and support its priorities in the areas of early education and K-12 education. This may include continuing to move towards greater access to high-quality child care and early education by directing resources towards implementing the timelines for rate and slot increases in the 2016-17 budget agreement. This may also include continued support of full implementation of LCFF, while at the same time building capacity for a robust accountability system. The Legislature's role as an oversight body is particularly important as California continues to break new ground with a multiple-measures accountability system that allows for and encourages local decision-making. The Legislature should also direct funds for strategic smaller investments in program areas outside of the LCFF, such as support for our special education students, pathways for teachers in areas of greatest need, and other targeted investments in improving student outcomes. Lastly, funding for education is more closely tied to changes in state revenue than many other areas of the budget. The impact of new revenue estimates at the May Revision, particularly in this potentially first year of slowed growth, will determine the ability of the Governor and the Legislature to implement any new or major budget changes.

Local Control Funding Formula and Accountability

BACKGROUND

As part of the 2013 Budget Act, the state adopted a new funding formula for education and the framework of a new accountability system. While the K-12 education funding allocation is still transitioning to this new formula, the Local Control Funding Formula (LCFF) and accountability systems are still in development, however significant progress has been made on both fronts.

Local Control Funding Formula

Commencing in the 2013-14 fiscal year, the state significantly reformed the system for allocating funding to school districts, charter schools, and county offices of education. The LCFF replaced the state's prior system of distributing funds to local education agencies (LEAs) through revenue limit apportionments (based on per student average daily attendance) and approximately 50 state categorical education programs. Under the previous system, revenue limits provided LEAs with discretionary (unrestricted) funding for general education purposes, and categorical program (restricted) funding was provided for specialized purposes, with each program having a unique allocation methodology, spending restrictions, and reporting requirements. Revenue limits made up about two-thirds of state funding for schools, while categorical program funding made up the remaining one-third portion. That system became increasingly cumbersome to LEAs as they tried to meet student needs through various fund sources that were layered with individual requirements.

The LCFF combines the prior funding from revenue limits and more than 30 categorical programs that were eliminated, and uses new methods to allocate these resources, additional amounts of new Proposition 98 funding since 2013-14, and future allocations to school districts, charter schools, and county offices of education. The LCFF allows LEAs much greater flexibility in how they spend the funds. There is a single funding formula for school districts and charter schools, and a separate funding formula for county offices of education that has some similarities to the district formula, but also some key differences.

School Districts and Charter Schools Formula. The LCFF is designed to provide districts and charter schools with the bulk of their resources in unrestricted funding to support the basic educational program for all students. It also includes additional funding based on the enrollment of low-income students, English learners, and foster youth for increasing or improving services to these high-needs students. Low-income students, English learners, and foster youth students are referred to as "unduplicated" students in reference to the LCFF because, for the purpose of providing supplemental and concentration grant funding, these students are counted once, regardless of if they fit into more than one of the three identified high-need categories. Major components of the formula are briefly described below.

- **Base Grants** are calculated on a per-student basis (measured by student average daily attendance) according to grade span (K-3, 4-6, 7-8, and 9-12) with adjustments that increase the base rates for grades K-3 (10.4 percent of base rate) and grades 9-12 (2.6 percent of base rate). The adjustment for grades K-3 is associated with a requirement to reduce class sizes in those grades to no more than 24 students by 2020-21, unless other agreements are collectively bargained at the local level. The adjustment for grades 9-12 recognizes the additional cost of providing career technical education in high schools.

- **Supplemental Grants** provide an additional 20 percent in base grant funding for the percentage of enrollment that is made up of unduplicated students.

- **Concentration Grants** provide an additional 50 percent above base grant funding for the percentage of unduplicated students that exceed 55 percent of total enrollment.

- **Categorical Program** add-ons for Targeted Instructional Improvement Block Grant and Home-to-School Transportation provide districts the same amount of funding they received for these two programs in 2012-13. The transportation funds must be used for transportation purposes. Charter schools are not eligible for these add-ons.

- **LCFF Economic Recovery Target** add-on ensures that districts receive, by 2020-21, at least the amount of funding they would have received under the old finance system to restore funding to their 2007-08 level adjusted for inflation. Districts are not eligible for this add-on if their LCFF funding exceeds the 90th percentile of per-pupil funding rates estimated under the old system.

- **Hold Harmless Provision** ensures that no school district or charter school will receive less funding under the LCFF than its 2012-13 funding level under the old system.

County Offices of Education Formula. The County Offices of Education (COE) formula is very similar to the school district formula, in terms of providing base grants, plus supplemental and concentration grants for the students that COEs serve directly, typically in an alternative school setting. However, COEs also receive an operational grant that is calculated based on the number of districts within the COE and the number of students county-wide. This operational grant reflects the additional responsibilities COEs have for support and oversight of the districts and students in their county.

Budget Appropriations. The LCFF establishes new “target” LCFF funding amounts for each LEA, and these amounts are adjusted annually for COLAs and pupil counts. When the formula was initially introduced, funding all school districts and charter schools at their target levels was expected to take eight years and cost an additional $18 billion, with completion by 2020-21. The Department of Finance (DOF) still estimates a completion date of 2020-21. County offices of education reached their target funding levels in 2014-15, which adjusts each year for COLAs and ADA growth.

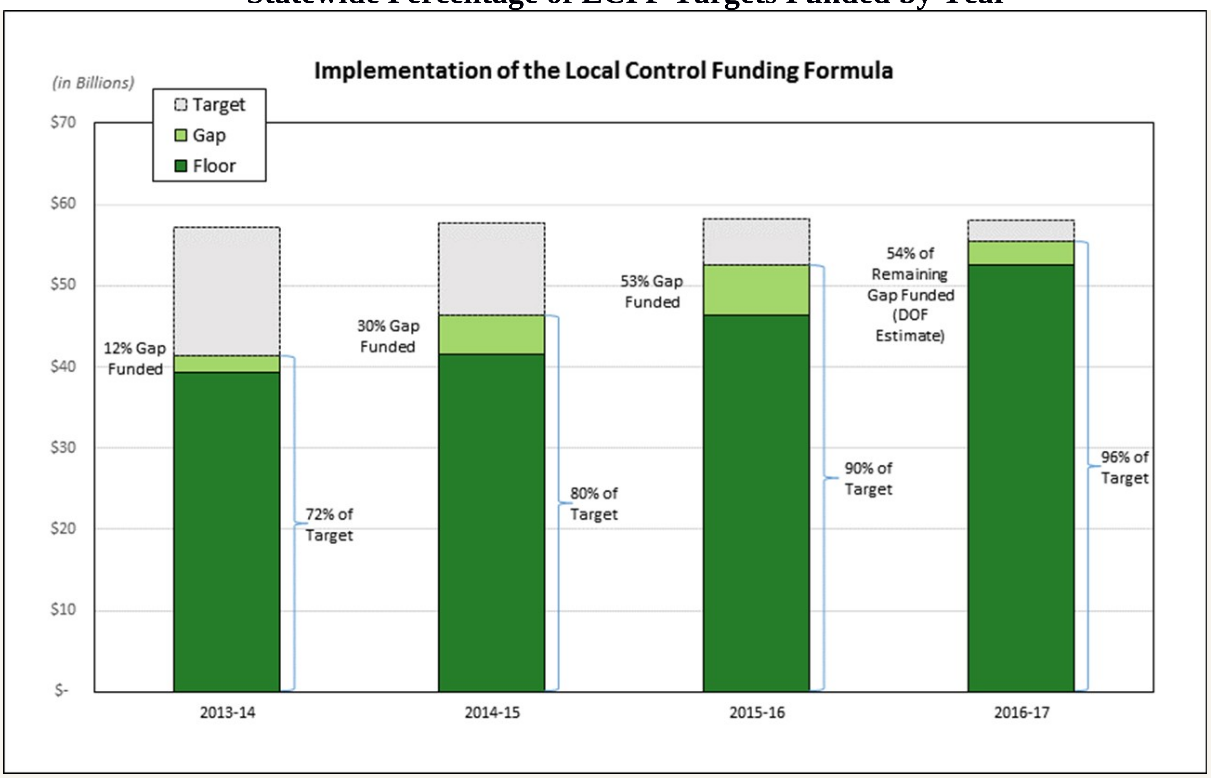
Since 2013-14, the state has made considerable investments towards implementing the LCFF, as shown in the table and graph below. The 2016-17 funding brought the formula to 96 percent of full funding of the LCFF target levels for school districts and charter schools and reduced by 56 percent the remaining gap to full implementation.

Amounts Provided in the Annual Budget to fund increased costs for LCFF (Dollars in Billions)

Fiscal Year	Original Estimated Need to Fully Fund LCFF	Gap Appropriation	Remaining Need to Fully Fund LCFF
2013-14	$18.0	$2.1	$15.8
2014-15	N/A	$4.7	$11.3
2015-16	N/A	$6.0	$5.6
2016-17	N/A	$2.9	$2.7 (estimated)

Figures may not sum due to changes between years for growth and cost of living adjustments.
Source: California Department of Education

Statewide Percentage of LCFF Targets Funded by Year



Source: California Department of Education

Each individual LEA was differently situated relative to its LCFF target when the formula was implemented in 2013-14. Each LEA receives the same percentage of its remaining need in new implementation funding, although the actual dollar amounts may vary. The intent is that all LEAs reach full implementation at approximately the same time. There are some exceptions as an LEA may have already been at its target at initial implementation or reached its target faster or slower based on other changes in its individual LCFF calculation. As of 2015-16, of all the school districts and charter schools in the state, 71 were at full implementation, 1,362 were funded between 90 and 100 percent of their target and 716 were between 82 and 90 percent of target.

The significant ongoing allocations of funding for the LCFF was made possible by considerable growth in the Proposition 98 guarantee over the past few years. A strong economic recovery has accelerated growth in the Proposition 98 guarantee, including funding to make up for years of low growth beginning in 2008-09. However, DOF projections for 2017-18 suggest a slowing in state revenues, as reflected in available Proposition 98 resources for LCFF. For more information on changes within the Proposition 98 guarantee, see *Proposed Expenditures of Proposition 98 Resource*s.

Restrictions on Supplemental Funding. Statute requires LEAs to increase or improve services for unduplicated students in proportion to the supplemental funding LEAs receive for the enrollment of these students. The law also allows this funding to be used for school-wide and district-wide purposes. The State Board of Education (SBE) adopted regulations governing LEAs expenditures of this supplemental funding that require an LEA to increase or improve services for unduplicated students, compared to the services provided for all students, in proportion to the supplemental funding LEAs receive for the enrollment of these students. The regulations allow an LEA to meet this requirement in a qualitative or quantitative manner and detail these expenditures in their local control and accountability plan (LCAP).

Accountability

Prior to 2013-14, LEAs were held accountable in different ways for variety of programs. Each individual categorical program had its own accountability requirements, although often this was limited to accountability for the expenditure of funds in accordance with allowable uses, rather than the impact on actual student outcomes. State and federal accountability systems provided an aggregate measure of school and district performance. The state and federal accountability systems relied primarily on student assessment data. The state used the Academic Performance Index (API)-constructed data from previous statewide assessments, aligned to the former academic standards, to create a performance target. School districts, schools, and student subgroups that did not meet the performance target were required to meet growth targets. The federal accountability system used a measure called Adequate Yearly Progress (AYP) that relies on student assessment scores, student participation in assessments, graduation rates and the API. Schools and districts that failed to meet benchmarks and make progress could be subject to interventions.

In 2013-14, the state began to transition to new assessments, aligned to new statewide academic content standards. Most student assessment scores were not available for assessments given in the spring of 2014, since the state was piloting a new assessment system. Accordingly, based on statutory authority, the SBE approved a recommendation by the state superintendent to not calculate the API for the 2013-14, 2014-15, and 2015-16 years In addition, California initially applied for and received a waiver of federal law exempting the state from the calculation of the AYP for some schools and districts. In December 2015, the federal No Child Left Behind Act was reauthorized as the Every Student Succeeds Act (ESSA). Most federal accountability requirements are frozen based on 2016-17 during the transition, with most new ESSA accountability requirements effective in 2017-18.

This transition in test scores and, therefore, aggregate accountability scores, aligns with an evolution in what the state expects from LEAs with respect to accountability. The LCFF statute included new requirements for local planning and accountability that focus on improving student outcomes in state educational priorities and ensuring engagement of parents, students, teachers, school employees, and the public in the local process. In addition, the LCFF features a new system of continuous support for underperforming school districts that do not meet their goals for improving student outcomes.

Local Control and Accountability Plans (LCAP). To ensure accountability for LCFF funds, the state requires that all school districts, charter schools, and county offices of education annually adopt and update a LCAP. The LCAP must include locally-determined goals, actions, services, and expenditures of LCFF funds for each school year in support of the state educational priorities that are specified in statute, as well as any additional local priorities. In adopting the LCAP, LEAs must consult with parents, students, teachers, and other school employees.

The eight state priorities that must be addressed in the LCAP, for all students and significant student subgroups in a school district and at each school, are:

- *Williams* settlement issues (adequacy of credentialed teachers, instructional materials, and school facilities).
- Implementation of academic content standards.
- Parental involvement.
- Pupil achievement (measured in part by statewide assessments, Academic Performance Index, and progress of English-language learners toward English proficiency).
- Pupil engagement (measured by attendance, graduation, and dropout data).
- School climate (measured in part by suspension and expulsion rates).
- The extent to which students have access to a broad course of study.
- Pupil outcomes for non-state-assessed courses of study.

County offices of education must address the following two priorities, in addition:

- Coordination of services for foster youth.
- Coordination of education for expelled students.

School district LCAPs are subject to review and approval by county offices of education, while county office of education LCAPs are subject to review and approval by the State Superintendent of Public Instruction (SPI). Statute also established a process for districts to receive technical assistance related to their LCAPs. The SPI is authorized to intervene in a district that is failing to improve outcomes for students after receiving technical assistance.

At the November 2016 SBE meeting, the board took action to adopt an updated version of the LCAP. As part of the updating process, the CDE and SBE staff involved stakeholders and reviewed input. Along with formatting changes to make the LCAP easier to complete and review, the new version includes an executive summary section including prompts designed to highlight how LEAs are addressing the needs of their students. In addition, the new LCAP, for use in the 2017-18 fiscal year, is a three year static plan that is updated annually, rather than a rolling three-year plan as in the previous versions of the LCAP. Initial reactions from the field on the new template have been very positive.

Evaluation Rubrics. As required by LCFF statute, the SBE adopted tools that evaluate performance based on specified criteria, known as evaluation rubrics, in September 2016. Specifically, the evaluation rubrics developed by the SBE will: (1) assist LEAs in evaluating their strengths, weaknesses, and areas that require improvement; (2) assist county superintendents of schools in identifying and providing resources for LEAs in need of technical assistance; and, (3) assist the SPI in identifying LEAs for which technical support and/or intervention is warranted. Statute further requires that the evaluation rubrics provide for a multidimensional assessment of district and school site performance, including adopting standards for performance and improvement in each of the state priority areas.

The SBE is continuing work to refine the rubrics and is developing them as an easy-to-use online tool called the California School Dashboard, which is anticipated to be online in spring of 2017. This new tool includes the following components, some of which are still in progress:

1) State and local performance indicators that reflect performance on the LCFF priorities:

- State level indicators are available through the CDE data system, CALPADS, are comparable statewide, and include the following:
    - Academic indicator based on student test scores on English Language Arts (ELA) and Math for grades 3–8, including a measure of individual student growth, when feasible, and results on the Next Generation Science Standards assessment, when available.
    - College/career indicator, which combines Grade 11 test scores on ELA and Math and other measures of college and career readiness.

  - English learner indicator that measures progress of English learners toward English language proficiency and incorporates data on reclassification rates.
  - High school graduation rate.
  - Chronic absence rates, when available.
  - Suspension rates by grade span.

- Local indicators rely on local data and are not reported at the state level. These include:
  - Appropriately assigned teachers, access to curriculum-aligned instructional materials, and safe, clean and functional school facilities.
  - Implementation of state academic standards.
  - Parent engagement.
  - School climate – local climate surveys.
  - Coordination of services for expelled students (county offices of education).
  - Coordination of services for foster youth (county offices of education).

2) Performance standards for each indicator allowing LEAs and schools to identify both progress and needed improvements. For each state indicator, the SBE has determined a measurement based on an LEAs current performance and improvement over time (over a three-year period if available). This combined measure then falls into a color-coded range, with each LEA, school, and student group measured annually. This method will allow for a easily accessible display as part of the dashboard for district and school administrators, teachers, students, parents, and other stakeholders. Currently the SBE has approved performance standards for the college/career indicator, English learner indicator, graduation rate indicator, and suspension rate indicator. The SBE is working on performance standards for the Academic indicator and the Chronic Absence indicator, both of which will be completed in 2017. For local indicators, the SBE has approved some self-reflection tools and a method for LEAs to self-assess as “met”, “not met”, or “not met for more than two years.” The SBE and CDE have several working groups in special subject areas that will continue to inform and help refine the indicators over the next few years.

3) Criteria for determining when an LEA is eligible for technical assistance or intervention. Based on the performance standards for each of the indicators, the SBE has adopted a plan that details for each state priority area, the levels for each indicator at which technical assistance and intervention are needed.

4) Statements of model practice that describe research and evidence-based practices related to each indicator, as well as links to vetted external resources. The development of these statements

of model practice is still underway through working groups and have not yet been approved by the SBE.

California Collaborative for Educational Excellence (CCEE). The CCEE was created as part of the new LCFF accountability framework, with its goal to advise and assist school districts charter schools, and county offices of education to achieve goals in their LCAPs under the LCFF. The CCEE is required to advise and assist school districts, county offices of education, and charter schools in meeting the goals in their LCAPs. Statue allows the SPI to assign the CCEE to LEAs in need of assistance. The CCEE may contract with individuals, LEAs, or organizations with expertise in the LCAP state priority areas and experience in improving the quality of teaching, improving school and district leadership, and addressing the needs of student populations (such as unduplicated students or students with exceptional needs.) The 2013 budget provided $10 million in Proposition 98 funding for the CCEE, and subsequent legislation, SB 858 (Committee on Budget and Fiscal Review), Chapter 32, Statutes of 2014, extended the encumbrance date for these funds through the 2014-15 fiscal year. Of the total, $4.4 million was encumbered. The remaining $5.6 million was reallocated through the 2016 Budget Act in addition to a new appropriation of $24 million in one-time Proposition 98 funds for the CCEE to conduct statewide training for all LEAs and education stakeholders on the evaluation rubrics and their use to inform development of local control and accountability plans, with a focus on improving student outcomes and closing the achievement gap. At least $20 million of the total is to be used for the statewide training activities. Up to $9.6 million of the remaining funds may be used to support a pilot program for the CCEE to assist LEAs in improving pupil outcomes.

Since the initial allocation of funds, the CCEE has hired an executive director and key staff, who have conducted outreach and visited the 58 county offices of education, involving study sessions with a select, diverse group of LEAs. The CCEE has also developed an expenditure plan for the statewide training activities and pilot program. Some components are already underway, as summarized below:

Professional Development Plan:

- Annual workshops in the fall of 2016 (completed) and the spring of 2017. These are held across the state and open to all levels of interested parties from school boards and district personnel to the general public.

- A content library that houses the information from the workshops as well as other vetted materials that are available as an ongoing resource for LEAs and others in conducting local trainings and supporting local efforts. Content for the library will be developed and added over the next few years.

- Professional Learning Networks (PLNs) made up of county offices of education, statewide organizations, and non-profits led by facilitators to support collaborative efforts to build capacity. Professional learning exchanges will provide the ability for PLN facilitators to collaborate and work together to ensure consistency in training and sharing of information.

- A learning lab to provide a resource for LEAs and other stakeholders to reach out for guidance. The advice line should be available in early 2017 to coincide with the launch of the California School Dashboard.

Pilot Program

The pilot program is designed to assist the CCEE in developing and designing their work in providing technical assistance and intervention to LEAs. The CCEE has approved an initial plan for up to 10 pilot LEAs that reflect urban, suburban, and rural areas with different needs for technical assistance. An LEA may volunteer for the pilot program and the CCEE is currently selecting LEAs to participate. In selecting a pilot, the CCEE considers whether the LEA has: 1) persistent academic/achievement challenges as evidenced by achievement gaps between student demographic groups, test scores, or other metrics; 2) a leadership team, including the Board of Trustees overseeing the LEA, that fully commits to participating in pilot process; and 3) the support of their county office of education. The CCEE anticipates up to 11 pilots in the first year; as of January 2017, the CCEE has selected 8 LEAs and one county office of education.

GOVERNOR'S PROPOSAL

The 2017-18 Governor's budget includes Proposition 98 estimates for 2015-16 and 2016-17 that are below the levels assumed in the 2016 Budget Act. In order to avoid over-appropriating the Proposition 98 minimum guarantee, the Governor proposes to defer $859.1 million of the funding scheduled to be provided for LCFF implementation from 2016-17 to 2017-18. Thus payments to LEAs would shift from June 2017 to July 2017. This would be a one-time deferral, fully paid off in the 2017-18 fiscal year. Changes to the Proposition 98 guarantee are more fully discussed in: *Proposed Expenditures of Proposition 98 Resources* in this report.

In addition to the one-year deferral, the Governor's budget proposes an increase of approximately $744 million in 2017-18 to implement the LCFF. Overall, this investment results in the formula funding at 96 percent of full implementation in 2017-18, maintaining the same implementation percentage assumed as of the 2016 Budget Act. The implementation percentage remains unchanged as the new funding is essentially covering the cost of full implementation as adjusted in 2017-18 for changes in average daily attendance growth and cost of living adjustments.

ISSUES TO CONSIDER

The Governor's proposed budget for 2017-18 reflects slower growth for the budget year and revises revenues downward for the previous two years. In the area of education, this essentially results in a workload budget with few new programs funded and the LCFF maintained at 96 percent fully funded. The Legislature may wish to consider whether to prioritize any additional Proposition 98 funding, if available at the May Revision, for LCFF implementation. Although the formula is almost fully funded, it still will take more than $5 billion in additional ongoing resources to meet the target. Additional funding would support LEAs as they work on improving in the state priority areas identified under the new accountability system.

The Legislature should also continue to monitor the ongoing accountability work of the SBE and partners. Over the past few years, LEAs have been uneven in the ability to complete comprehensive LCAPs. The new LCAP template is designed to address many of these concerns and the Legislature may wish to review progress as LEAs continue work with the new template in the spring. The LCAP is intended to be the dynamic planning tool that helps to focus resources and drive improvements. The new California Schools Dashboard is intended to help make a new more complex, multi-measure, accountability system easily understandable to the school community and broader public. The Legislature should monitor the roll=out of this new system.

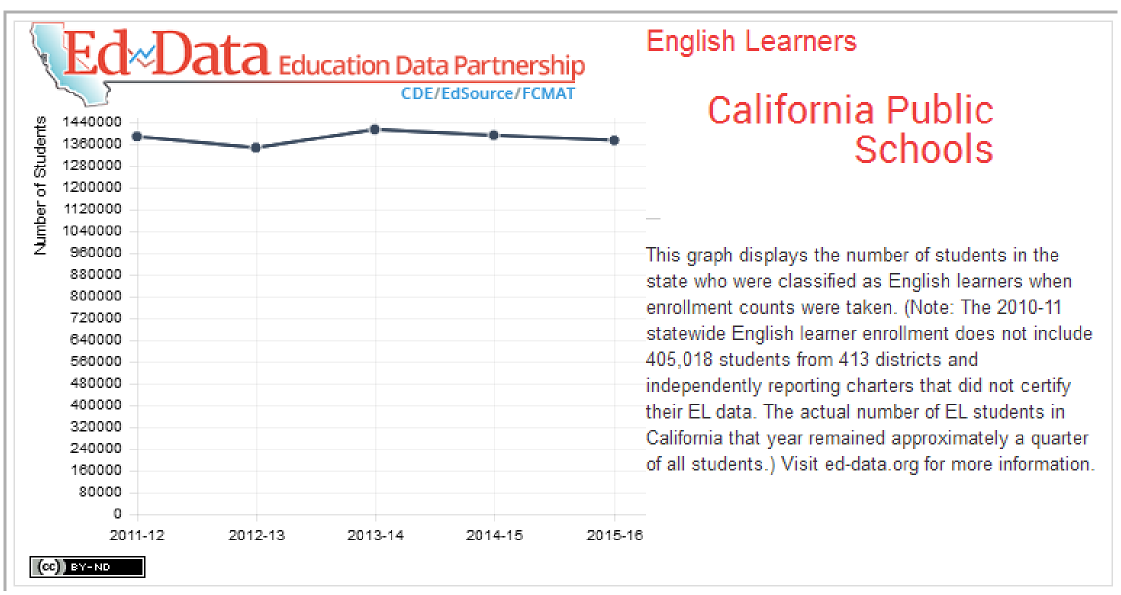
Finally, the accountability system is intended to be a catalyst for improvement. LEAs and their stakeholders can use the information to drive change in practices at the local level to support outcomes for students and to make progress towards closing the achievement gap. However, for our schools and districts facing the most challenges, the tools provided through the SBE and the work of the CDE, county offices of education, and the CCEE will be critical in providing the guidance to ensure these schools and districts are providing the education the students deserve. There have been multiple intervention, turnaround, and support programs through federal and state law in past years, this new approach is designed to create a continuous improvement culture and build local capacity. The Legislature and Governor have worked over multiple years on this new approach. As with any new system, there will be the need for adjustments along the way and the Legislature should continue to be engaged in oversight of the system and keep the focus on outcomes for all students, including unduplicated and subgroups of students.

English Learners in K-12 Education

BACKGROUND

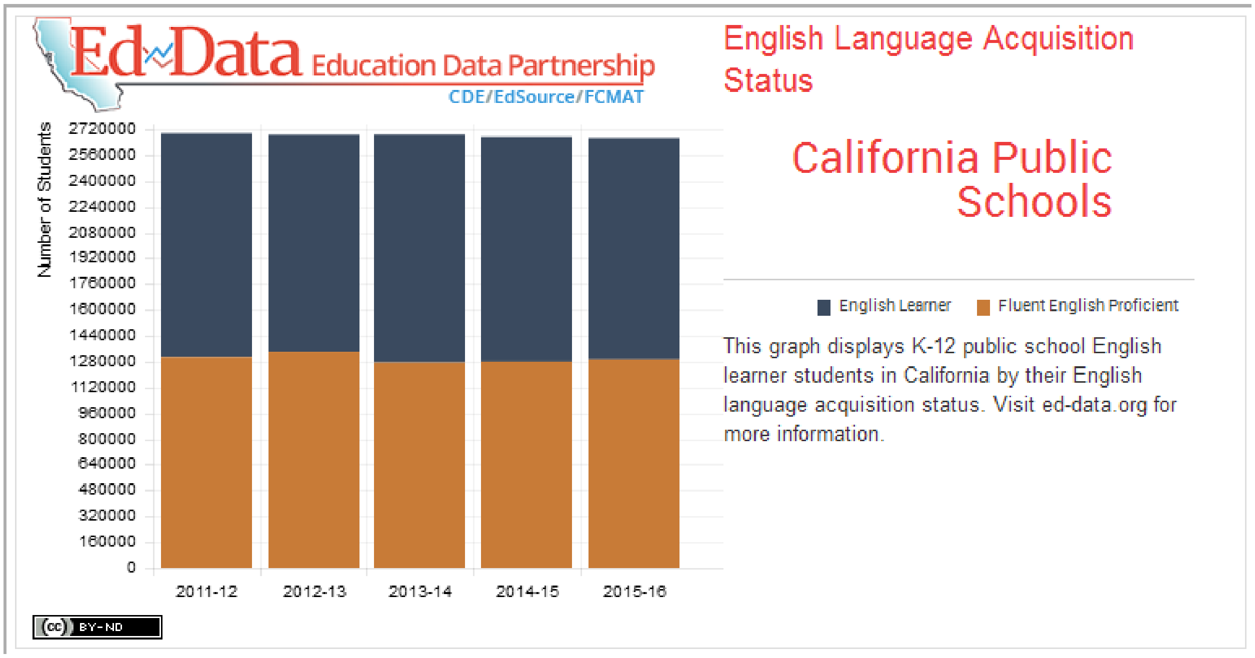
California's public schools serve a population that is both demographically diverse and has diverse challenges. One of the largest groups of students who face a unique educational challenge is English learners. As defined by the California Department of Education (CDE), an English learner is "A student in kindergarten through grade twelve who, based on objective assessment, has not developed listening, speaking, reading, and writing proficiencies in English sufficient for participation in the regular school program."

In California, the most recent complete year of data is from 2015-16 which indicates that there were 1,373,724 English learners enrolled in K-12 education, or about 22.1 percent of total K-12 enrollment. This is a just below the high point of 1.6 million for English learner enrollment, which was set in 2003. Spanish is, by far, the most common language, with 18.4 percent of enrollment made up of Spanish-speaking, English learners. Data on English learners is collected by the CDE through the California Longitudinal Pupil Achievement Data System (CALPADS). Nationally, California has the highest number and percentage of English learner students compared to other states, according to the U.S. Department of Education, National Center for Education Statistics. National data is available for the 2013-14 and shows that California far surpasses other states (over 22 percent of students in English language learner programs in 2013-14.) New Mexico and Texas have the next highest percentage of English learner enrollment, with slightly more than 15 percent of students in English language learner programs. Nationally, in 2013-14, there were almost 4.5 million English learner students, with California serving over 31 percent.



Source: Ed-Data (A partnership of the California Department of Education, the Fiscal Crisis and Management Assistance Team, and EdSource). www.ed-data.org

Identification of English Learners. Students who are new to a California public school must complete a home language survey, and those students who report a primary language other than English take a state assessment (within 30 days of enrollment or within 60 days prior to instruction) to determine if they are to be classified as an English learner or as an initially fluent English proficient student. Approximately 42.8 percent of California public school students (or 2,664,921 students) speak a language other than English in their home, over half are identified as English learners, while the remainder have become proficient in the English language, or were determined to be fluent upon enrollment.



Source: www.ed-data.org

Serving English Learners. Local Educational Agencies (LEAs) serving English learner students are required by state and federal law to provide those students with both instruction to become proficient in English and instruction in the core curriculum. State regulations also require LEAs to ensure that all students meet grade-level core curriculum within a reasonable amount of time. LEAs have some discretion to define "a reasonable amount of time", but this requirement applies to English learners, along with any other student, with respect to the core curriculum.

Since 1998, when Proposition 227 was passed (and until the recent passage of Proposition 58 in 2016), English learners have been served in programs where instruction was primarily given in English, unless a parent requested and received a waiver for the student to participate in an alternative program. English learners who were less fluent were placed in Structured English Immersion (SEI) programs (intended to be for one-year only, although a student could be re-enrolled if needed), and those with a higher level of fluency were placed in classrooms with native English speakers, a program known as English Language Mainstream (ELM). Alternative programs include dual-immersion and bilingual programs where native and non-native English speakers are in the same classroom and instruction can be given in more than one language with the intent of bi-literacy for students. Proposition 58, recently passed in November, 2016 repeals most of the requirements of Proposition 227, effectively allowing bilingual education in public schools and removing English learner parental waiver requirements for non-English only classes.

The state also provides curricular guidance for serving English learners. Following the adoption of the California Common Core State Standards in 2010, the State Board of Education adopted new California English Language Development (ELD) Standards in 2012. Curriculum standards describe the knowledge, skills, and abilities that an English learner needs to demonstrate mastery of English. These new ELD standards have been widely viewed by the field as an improvement from the previous version and are aligned to the California Common Core State Standards (CCSS) for English Language Arts (ELA), Mathematics, and Literacy. The state also adopted an ELA/ELD framework that provides further guidance to teachers in providing sequenced instruction designed to ensure mastery of the standards.

Teachers of English learners, whether in SEI, ELM, or alternative type programs are required to have specific training and authorization to teach English learners. With the passage of Proposition 58, the demand for teachers with a bilingual certification is likely to increase. Bilingual teachers are already identified as one of the areas in which the state is experiencing a teacher shortage. The 2016 budget included funding for a variety of programs to begin addressing the teacher shortage, including grants to create opportunities for classified employees to become teachers, grants to make create or expand four-year integrated teacher preparation programs, and funds to recruit additional teachers, particularly in shortage areas including bilingual education, into the profession.

Reclassifying English Learners. Students who are identified as English learners are served by the LEA in a variety of different ways, as discussed above, with the intention of moving students to proficiency in English with an ability to perform academically similar to other non-English learner students in the same cohort. English learners who are reclassified are known as Reclassified Fluent English Proficient (RFEP).

Current state law requires the CDE to establish, and the State Board of Education to approve, procedures for the reclassification of a pupil from English learner to English proficient. The criteria adopted through regulations require a local procedure to assess reclassification that includes the following criteria:

(1) Assessment of language proficiency using an objective assessment instrument, including, but not limited to, the state test of English language development. Regulations further define this as the state-adopted ELD assessment.

(2) Teacher evaluation, including, but not limited to, a review of the pupil’s curriculum mastery. Regulations also include the involvement of other certificated staff as appropriate.

(3) Parental opinion and consultation. Regulations further speak to providing notice to parents, and encouraging parental participation.

(4) Comparison of the performance of the pupil in basic skills against an empirically established range of performance in basic skills based upon the performance of English proficient pupils of the same age.

Although state law and regulation guide the reclassification process, LEAs have a lot of discretion in applying the criteria. For example, although all English learner students currently take the California English Language Development Test (CELDT), the LEA has some discretion to determine the scores on each of the test domains (speaking, listening, reading, and writing) that are required to be eligible for reclassification. Also there is little guidance about teacher evaluation and parent input, meaning these criteria are very locally driven. The statewide average rate of annual reclassification is around 11 percent, this is the number of RFEPS that were reclassified since the last annual census date as a percentage of the total number of English learners in the prior year.

Reclassification Rates for Counties with English Learner Enrollment > 50,000				
County	**Enrollment**	**English Learners (# and percentage of enrollment)**	**Fluent English Proficient Students (# and percentage of enrollment)**	**RFEPs reclassified (# and percentage of English learner enrollment since the last census date)**
Los Angeles	1,523,212	346,469 (22.7%)	422,660 (27.7%)	38,949 (11.1%)
Orange	493,030	123,001 (24.9%)	112,524 (22.8%)	15,949 (12.3%)
Riverside	427,537	88,697 (20.7%)	74,216 (17.4%)	9,149 (10.3%)
San Bernardino	408,948	77,324 (18.9%)	67,452 (16.5%)	8,750 (11.1%)
San Diego	504,561	111,284 (22.1%)	96,306 (19.1%)	13,840 (12.3%)
Santa Clara	274,948	64,143 (23.3%)	78,155 (28.4%)	8,705 (13.0%)

Source: California Department of Education, Data Quest.

Finally, a student who is reclassified as RFEP may continue to need additional support to be successful in the core curriculum. LEAs who receive federal Title I or III funds must monitor RFEPs for four years after they are reclassified. In addition, current state regulations specify that RFEP students are monitored for correct placement. In practice, monitoring and successfully supporting RFEPs appropriately is up to the individual LEA.

Although the intent of state and federal laws is clearly to move English learner students to proficiency in English and the ability to participate in core curriculum similar to non-English learners as quickly as possible, this does not always happen in practice. Some English learners fail to be reclassified and are considered Long-Term English Learners (LTELs). An LTEL is defined by the CDE as an English learner who: 1) is in grade 6-12; 2) has been enrolled in a school in the U.S. for six or more years; 3) has either failed to make progress towards English language proficiency for two or more consecutive prior years, or has regressed to a lower level; and 4) for students in grades 6 through 9, has received a score in the range of “standard not met” on the CAASPP ELA portion. Once English learner students reach middle and high school, they have a higher chance of becoming LTELs. In 2015-16, there were 238,576 LTELs in California public schools grades 6 through 12 inclusive, which represents just over 51 percent of English learners in that grade range.

Assessment of English learners. The current statewide assessment is the CELDT, as required by federal and state laws. The test is designed to measure listening, speaking, reading, and writing proficiencies in English. Results from the test are used to identify new students who are

English learners, measure progress towards English proficiency on an annual basis, and help determine when a student is eligible for reclassification and can sufficiently participate in the regular school program.

In 2015, the state began the development of a new English Language Development Test, called the English Language Proficiency Assessment for California (ELPAC). The new ELPAC is aligned to the new ELD standards, includes two different tests; an initial screener and an annual summative assessment. Field testing of the ELPAC is scheduled to begin in March 2017, and results from the field testing will be used for initial standards setting. One important difference from the previous test is the timing of the assessment; while the CELDT was given in the fall and served as both a screener and summative assessment, the summative ELPAC will be given in the spring, allowing for more days of instruction, and possible reclassification before the start of the next school year. The state's ELD assessment is one of the main drivers of reclassification of students and, consequently, moving from the CELDT to the ELPAC may impact reclassification rates.

English learners are also subject to the same state assessments in academic content areas as other non-English learner students. For example, students must take California Assessment of Student Performance and Progress (CAASPP) assessments in ELA and mathematics. English learners do have some access to supports, including translation of test instructions. English learners can be exempted from the ELA portion of the CAASPP if they have been enrolled in school in the United States for less than 12 months. California has also historically provided for a primary language assessment for English learners to demonstrate mastery of reading/language arts standards. Currently, the state allows LEAs the option of continuing to administer the existing Standards-based Test in Spanish (STS) until the successor assessment is operational. LEAs may also administer the STS to students enrolled in dual-immersion programs at their own expense. The new primary language assessment in Spanish is under development and has an anticipated operational date of 2019. The assessment would be available for English learners who have been enrolled for less than twelve months, students who receive instruction in Spanish, and students who wish to meet the requirements of the State Seal of Biliteracy.

Special Education and English Learners. An area of concern for English learner students and parents is the correct identification of special education needs. English learners already have difficulty accessing the standard curriculum because of language barriers, therefore it may be more difficult to identify other learning disabilities. According to the CDE, in 2014-15 while 10 percent of all California students qualify for special education services, 9.1 percent of non-English learner students and 14.4 percent of English learners qualified for these services. The data generally shows that English learners begin to be identified for special education services in greater percentages than non-English learners in third grade through middle school, and particularly in high school. In order to promote a careful consideration of the different needs of a student, guidance from the CDE specifies that for English learners who also have an Individualized Education Plan (IEP), the IEP team must include a professional with training and expertise in second language acquisition and knowledge specific to the differentiation of a specific disability and limited English proficiency. When a student is referred for an assessment to determine if the student has a disability, the IEP team is charged with determining that the suspected disability is not a result of a language or cultural difference. English learners with an

IEP must also receive appropriate ELD instruction in addition to disability-related services. Teachers, or the team of teachers, that provide instruction to English learners with disabilities must have the appropriate special education and English learner authorizations. Related legislation, AB 2785 (O'Donnell) Chapter 579, Statutes of 2016, requires the CDE to develop a manual providing guidance to LEAs on identifying and supporting English learners with disabilities.

Funding for English Learners. State funding for English learners is provided through the Local Control Funding Formula (LCFF). The LCFF provides a per student grant with a base amount, then a supplemental amount is added for students who are low-income, English learners, or foster youth. If the LEA has a concentration of low-income, English learner, or foster youth students, then the district also receives a per student concentration grant for the number of students who are above 55 percent of enrollment and identified as one or more of those three groups. While these supplemental and concentration grants are not required to spend dollar for dollar on the students who generate the additional funding, the LEA must increase or improve services for these students in comparison to services provided for all students. (For more information, please see *Local Control Funding Formula and Accountability* in this report).

According to CDE, in 2015-16, LEAs received $52.6 billion in LCFF funding. If LCFF has reached full implementation in 2015-16, LEAs would have received $58.2 billion, of which $9.3 billion would have been distributed as supplemental and concentration grants. The total LCFF amount at full implementation is adjusted each year for growth and cost-of-living and, until full implementation, LEAs must use a formula defined in regulation to estimate the proportion of transition funding that is attributed to supplemental and concentration grants.

Prior to LCFF, LEAs received a total of approximately $1 billion for English learner students through the Economic Impact Aid (EIA) categorical program. Funds received under this program were required to be expended to help English learners reach proficiency and to support other educationally-disadvantaged students. After LCFF was implemented in 2013-14, LEAs who had EIA carryover were able to retain and expend those funds for the original purpose of the funding.

Federal Title III funds are also provided for English learners. Previously, under the No Child Left Behind (NCLB) Act, and now under the reauthorization of this statute known as the Every Student Succeeds Act (ESSA), the federal government has provided funding for English learners under Title III. Similar to NCLB, ESSA Title III funds are to be used as supplemental funding to the state's support of English learners with a purpose of ensuring that English learners attain English proficiency and meet the state's academic standards. Funds are awarded to states based on the enrollment of English learner and immigrant children and are provided to LEAs serving these students. In 2016-17, California is anticipated to receive approximately $144 million in Title III Language Acquisition funds.

Accountability. In concert with changes under LCFF, the state has been working on a new, multiple measures accountability system. Under the new system, each LEA must annually create a Local Control and Accountability Plan (LCAP), that details the goals the LEA has set for each of eight state priorities and the actions, services, and expenditures to achieve that goal. (See *Local Control Funding Formula and Accountability* for more information about state accountability under LCFF). The eight state priorities broadly cover conditions of learning, student outcomes, and engagement of school personnel, students, parents, and the community. English learners are identified in state law as a specific subgroup, and an LEA must determine how it is meeting the priorities in the LCAP for English learners as well as all subgroups and all students as a whole. In addition, English learners are specifically referenced in two of the eight state priorities. First, English learners are part of the implementation of state academic standards, which includes how the programs and services will enable English learners to access academic content standards and ELD standards to reach English proficiency and gain academic content knowledge. A second priority related to student achievement, includes measuring: 1) the percentage of English learners making progress towards proficiency, as determined by the state's ELD assessment and 2) the English learner reclassification rate.

As required by state law, the State Board of Education (SBE) has adopted evaluation rubrics as a multi-dimensional tool for LEAs to self-assess performance and other entities to identify LEAs in need of support and assistance. As a part of the evaluation rubrics, the board was also required to adopt standards for performance on the state priorities. As of January 2017, the SBE has adopted some state indicators for LEA performance, including an English learner indicator that measures progress toward proficiency and includes data on reclassification. Also at the January SBE meeting, the board adopted a definition of the subgroup English learner for purposes of the academic indicator (based on ELA and mathematics assessment scores) that includes current English learners and RFEPs for four or less years after reclassification. Information on subgroup performance, including English learners, will be used to determine if an LEA requires additional support or intervention.

Under federal law, there are also accountability requirements related to receiving Title III funds. Under NCLB Title III, LEAs were required to meet and report on Annual Measurable Achievement Objectives (AMAOs) in areas including reading and writing, as measured by the state's English language development assessment, currently the CELDT. Under ESSA, federal accountability for English learners is now under Title I, which maintains these accountability requirements for measuring progress of English learners with some changes. ESSA legislation requires statewide standardized criteria for entering and exiting English learner status, a more detailed state plan on tracking student progress, and prohibits criteria from including a score on an academic content assessment. As part of the transition to ESSA, accountability for English learners is suspended in 2016-17, with new rules taking effect in 2017-18. The SBE will adopt a new state plan for implementing ESSA in September of 2017, but must sign assurances of compliance with the law by April of 2017. Accountability measures under ESSA will be in effect in 2017-18.

English Language Learner Roadmap. The State Superintendent of Public Instruction has recently begun an effort to provide more support for English learners by convening a working group to produce a guide called *The California English Learner Roadmap: Strengthening Comprehensive Educational Policies, Programs, and Practices for English Learners*. The first meeting was held in November of 2016, with additional meetings scheduled through September of 2017. The working group, composed of practitioners with extensive experience in implementing English learner programs, will use a variety of survey data, review related statute, and seek public input to produce a guide that includes evidence-based practices, models, and services.

Summary of Research: There have been several research projects over the past few years that inform the conversation on English learners.

In October of 2015, Policy Analysis for California Education (PACE), an independent, non-partisan research center based at Stanford University, the University of Southern California, and the University of California Davis, published a Policy Brief that summarizes research efforts related to English learner education. The report reminds state policymakers of a few important points. The report finds that English learners vary widely, the population includes: many types including: LTELs, newcomers, first and second generation, those who are also special education students, those who received prior schooling in their home language and those who have not been exposed to formal education. In addition, each district may predominately serve one or more types of English learners. The report finds that this information about English learners can be predictive and informative of the likely success of, and needed intervention for, a specific type of English learner. The report also looks at many of the potential challenges to being an English learner, including less access to core curriculum and advanced or elective courses, and less access to English-speaking or higher achieving peer groups. These limiting factors likely impact academic success and preparation for, and entry into, post-secondary education and/or careers.

The PACE report finds that reclassification rates vary across districts, which may be due to differences in reclassification criteria or processes, differences in the characteristics of the English learners the district generally serves, and the quality of the instructional program and services provided to English learners. In the subset of districts reviewed in the report, the most significant barrier to reclassification in elementary school is passage of the CELDT; while in middle and high-school, the most significant barrier is passage of ELA content criteria. The research also suggests that setting reclassification standards too low can negatively impact academic outcomes as students lose English learner supports just when they need them the most. On the other hand, reclassifying students earlier can increase access to academic core in middle and high school. Of course, services provided to RFEPs after they are reclassified may also be critical. The research also suggests that there can be academic and linguistic benefits to English learner students, now supported under Proposition 58; and that teachers may need additional support to meet the needs of English learner and non-English learner students.

The PACE report includes major recommendations in the following areas:

- Reclassification:
  1) Require a statewide standard reclassification criteria.
  2) Use only English proficiency and not academic performance criteria for reclassification.
  3) Set the ELPAC reclassification score in the range that is similar to non-English learner performance on the CAASPP ELA assessment.

- Data Collection:
  1) Use longitudinal data and include all students who were ever identified as EL when doing analyses on effectiveness.
  2) Support LEAs in setting and monitoring progress toward goals for English learners.

3) Incentivize new research-practice partnerships with LEAs to continue to learn and disseminate best practices.

- Opportunities for English learners:
  1) Support LEAs in ensuring English learners full access to core curriculum.
  2) Require, monitor, and enforce LEA policies to provide full curricular access.
  3) Remove legal barriers to bilingual programs (Prop 58 effectively accomplishes this.
  4) Support access for high quality teachers of English learners.
  5) Support LEA's ability to correctly identify and serve English learners with disabilities.

In 2014, the Public Policy Institute of California completed a longitudinal study of the transition from English learner status to RFEP for all LEAs in California, entitled: *Reclassification of English Learner Students in California.* The report utilized CALPADS data from CDE to track students from 2007-08 through 2012-13. This study also surveyed districts and found that many use additional or more stringent reclassification criteria than what is required under state law. Those districts with more stringent requirements also reported lower reclassification rates, but had slightly better outcomes for their RFEP students. Overall RFEP students statewide are performing better than English learner students, but are also generally on-par with non- English learners on academic measures; and this positive trend also holds for districts with less stringent reclassification criteria. A small change in the reclassification criteria can have a large impact on the number of English learners reclassified. The study also highlights that RFEPs are not a uniform group, those students who are reclassified as RFEP in elementary school show more academic success than those reclassified in high school when compared with non-English learners. The study also notes that the data is most applicable for considering English learners who enrolled in Kindergarten in a California public school. The study asks policymakers to consider the trade-offs between lower reclassification criteria and more RFEPs, compared to higher criteria and slightly better outcomes for RFEPs. Finally, the study recommends one statewide standard for English learner reclassification based on existing law, with continued monitoring as LCFF and new academic content standards are implemented.

GOVERNOR'S PROPOSAL

The Governor has no proposals that are specific to English learners in the 2017-18 budget, beyond continued implementation of the LCFF.

The SBE and CCEE are continuing to implement accountability requirements passed as a part of LCFF which, among other priorities, are intended to hold LEAs accountable for English learner education and identify and support those LEAs who are struggling to meet the needs of English learners.

ISSUES TO CONSIDER

As discussed above, English learners are a large proportion of the student population in California, but finding the most effective ways to support English learners and move them to

English language proficiency and academic success is still very much a work in progress. However, it is promising that based on recent changes in education finance and policy, English learner-related issues are receiving significant attention. Under LCFF, English learners, as one of three identified student groups, are an important driver of the calculation of supplemental and concentration grants. Under the new state accountability system, English learner progress and reclassification are important indicators of the success of an LEA. In addition, the way English learners are being taught is changing with new ELD standards, a new ELPAC, and the passage of Proposition 58.

The Legislature should consider the following as they provide oversight and direction related to these changes:

The new ELPAC, which is aligned with the new ELA/ELD standards, is anticipated to provide better information about an English learner's progress towards proficiency and some information about progress on the core ELA curriculum. The ELPAC is also anticipated to be more rigorous, reflecting the new standards, but may impact the reclassification rate of English learner students. The point in time when a student is reclassified may have a significant effect on that student's academic success. However reclassification criteria, and therefore rates, vary from LEA to LEA.

- What is the state's role in standardizing English learner reclassification statewide?
- What is the appropriate level of local discretion to ensure English learner students are being fully supported and have the most access to core curriculum and advanced classes?

English learner data does not reflect a homogenous population; it encompasses students with very different challenges, and includes newly-identified English learners as well as students for four years after reclassification as an RFEP and all those in between. In addition, while many English learners achieve proficiency and move on, statewide there are a significant number of LTELs. While the SBE fleshes out the details of the statewide accountability system, the California Collaborative for Educational Excellence, an entity created to support LCFF accountability, is beginning to determine how to support LEAs in need of improvement.

- How will English learner data be used to determine the need for intervention? What will intervention look like and how will success be measured for an LEA currently failing its English learner students?
- How will the state improve its ability to identify and execute promising practices for English learner success that move towards closing the achievement gap with non-English learner students?
- How can the state provide guidance and support to the LEAs in serving LTELs, where the typical English learner curriculum has failed?

Finally, both state and federal law require equal education for all students including both English learners and students with disabilities. It is important to accurately determine when a student has a language or a cultural barrier and when a student needs special education services.

- How can the state or LEAs improve accurate diagnoses for all students, including English learner students?

Higher Education Affordability

BACKGROUND

During the recent recession, the state was limited in its ability to invest in public higher education, and significantly cut state support to the universities. The universities responded by shifting more of the financial burden to the students through increased tuition. Most notably, between 2004 and 2013, tuition at the University of California (UC) and California State University (CSU) more than doubled. This rapid tuition increase led to growing concerns about the affordability of higher education. The December 2012 Public Policy Institute of California (PPIC) Statewide Survey found that 65 percent of Californians were concerned about the cost of college. However, as the economy recovered, this trend of divestment started to reverse. The passage of Proposition 30 and recent budget acts facilitated a renewed investment in public higher education. Since the passage of Proposition 30 in 2012, the state has funded a multiyear investment plan at UC and CSU.

Despite the state's investment in higher education, in November 2015 the UC Regents' authorized the UC President to increase student tuition by up to 28 percent over five years. This action led to large public outcry regarding the affordability of higher education. After negotiations, the Administration and the UC developed another multi-year budget framework to hold tuition flat for an additional two years, and to continue to provide four percent increases in direct General Fund support. By 2017-18, tuition will have remained flat for six consecutive years, and the Administration notes that it is reasonable to expect that tuition will begin to increase modestly and predictably at around the rate of inflation. In the intervening years, the Administration suggested that UC must aggressively implement reforms and continue its efforts to obtain administrative efficiencies. The CSU did not have such an agreement.

In January 2017, the UC Regents again voted for a tuition increase of 2.5 percent, or $282, for a total annual tuition of $11,502. Additionally, the UC Regents voted to increase the student services fee by five percent, a $54 increase for a total of $1,128 annually. In March, the CSU Board of Trustees is also scheduled to vote on an up-to five percent tuition increase, or $270, for a total annual tuition price of $5,742. These tuition increases would grow Cal Grant costs for UC students by $17.7 million and for CSU students by $24.9 million in 2017-18 beyond the costs reflected in the Governor's budget.

University of California

The 1960 Master Plan for Higher Education designates the UC as the primary state-supported academic agency for research. In addition, the UC is designated to serve students at all levels of higher education and is the public segment primarily responsible for awarding the doctorate and several professional degrees, including in medicine and law.

There are ten UC campuses: Berkeley, Davis, Irvine, Los Angeles, Merced, Riverside, San Diego, San Francisco, Santa Barbara, and Santa Cruz. Nine of these are general campuses and offer undergraduate, graduate, and professional education. The San Francisco campus is devoted exclusively to the health sciences. The UC operates five teaching hospitals in Los Angeles, San Francisco, Sacramento, San Diego, and Orange counties. The UC has more than 800 research centers, institutes, laboratories, and programs in all parts of the state. The UC also provides oversight of one United States Department of Energy laboratory and is in partnerships with private industry to manage two additional Department of Energy laboratories.

The UC is governed by the Board of Regents which, under Article IX, Section 9 of the California Constitution, has "full powers of organization and governance," subject only to very specific areas of legislative control. The article states that "the university shall be entirely independent of all political and sectarian influence and kept free therefrom in the appointment of its Regents and in the administration of its affairs." The Board of Regents consists of 26 members, as defined in Article IX, Section 9, each of whom has a vote (in addition, two faculty members — the chair and vice chair of the Academic Council — sit on the board as non-voting members):

- 18 regents are appointed by the Governor for 12-year terms.
- One is a student appointed by the regents to a one-year term.
- Seven are ex officio members — the Governor, Lieutenant Governor, Speaker of the Assembly, Superintendent of Public Instruction, president and vice president of the Alumni Associations of UC and the UC president.

The Governor is officially the president of the Board of Regents; however, in practice the presiding officer of the regents is the chairman of the board, elected by the board from among its members for a one-year term, beginning each July 1. The regents also appoint its officers of general counsel; chief investment officer; secretary and chief of staff; and the chief compliance and audit officer.

The following table displays the budgeted expenditures and positions for the UC, as proposed in the Governor's budget. Of the amounts displayed in the table, $3.26 billion in 2015-16, $3.54 billion in 2016-17, and $3.53 billion in 2017-18 are contributed by the General Fund. The remainder of funding comes from tuition and fee revenue and various special and federal fund sources.

University of California
Budgeted Expenditures and Positions
(Dollars in Millions)

	2015-16	2016-17	2017-18
Personal Services	$12,314	$13,332	$13,330
Operating Expenses and Equipment	$18,258	$18,588	$19,429
Total Expenditures	**$30,573**	**$31,920**	**$32,759**
Positions	**100,312**	**103,322**	**103,322**

California State University

The CSU system is comprised of 23 campuses, consisting of 22 university campuses and the California Maritime Academy. The California State Colleges were brought together as a system by the Donahoe Higher Education Act of 1960. In 1972, the system became the California State University and Colleges; the name of the system was changed to the California State University in January 1982. The oldest campus, San Jose State University, was founded in 1857 and became the first institution of public higher education in California. Joint doctoral degrees may also be awarded with the UC. The program goals of the CSU are to:

- Provide instruction in the liberal arts and sciences, the professions, applied fields that require more than two years of college education, and teacher education to undergraduate students and graduate students through the master's degree.

- Provide public services to the people of the state of California.

- Support the primary functions of instruction, public services, and student services in the University.

- Prepare administrative leaders for California public elementary and secondary schools and community colleges with the knowledge and skills needed to be effective leaders by awarding the doctorate degree in education.

- Prepare physical therapists to provide health care services by awarding the doctorate degree in physical therapy.

- Prepare faculty to teach in postsecondary nursing programs and, in so doing, help address California's nursing shortage by awarding the doctorate degree in nursing practice.

The CSU Board of Trustees is responsible for the oversight of the system. The board adopts rules, regulations, and policies governing the CSU. The board has authority over curricular development, use of property, development of facilities, and fiscal and human resources management. The 25-member Board of Trustees meets six times per year. Board meetings allow for communication among the trustees, chancellor, campus presidents, executive committee members of the statewide Academic Senate, representatives of the California State Student Association, and officers of the statewide Alumni Council. The trustees appoint the chancellor, who is the chief executive officer of the system, and the presidents, who are the chief executive officers of the respective campuses.

The following table displays the budgeted expenditures and positions for the CSU, as proposed in the budget. Of the amounts displayed in the table, $3.01 billion in 2015-16, $3.32 billion in 2016-17, and $3.37 billion in 2017-18 are contributed by the General Fund. The remainder of funding comes from tuition and fee revenue and various special and federal fund sources.

California State University
Budgeted Expenditures and Positions
(Dollars in Millions)

	2015-16	2016-17	2017-18
Personal Services	$4,357	$4,598	$4,598
Operating Expenses and Equipment	$5,091	$4,964	$5,017
Total Expenditures	**$9,449**	**9,562**	**9,616**
Positions	**46,014**	**48,093**	**48,093**

GOVERNOR'S PROPOSAL

University of California

- **Unrestricted Base Increase.** Provides an $82.1 million unrestricted base increase, plus $50 million in funds from Proposition 56 (Cigarette and Tobacco Products Surtax Fund) for graduate medical education.

- **Enrollment.** The budget does not provide additional funds for enrollment growth, however it does assumes UC meets enrollment expectation set forth in last year's budget. Specifically, the Administration assumes UC will (1) enroll 2,500 more resident undergraduates in 2017-18 and (2) receive an $18.5 million ongoing augmentation in 2016-17.

- **One-Time Funding.** The budget provides $169 million, funded from a one-time Proposition 2 payment, for the third and final installment to help pay down the UC Retirement Plan's unfunded liability.

- **Assumes No Increase in Resident Undergraduate Tuition**. The budget's only assumed increases in systemwide charges for resident undergraduate students is a $54 (five percent) increase in the Student Services Fee, and a five percent increase in nonresident supplemental tuition. However, the Regents voted in its January board meeting to increase tuition.

- **Eliminates Academic Sustainability Plan Requirement.** As with CSU, the Governor proposes to eliminate budget language that directs UC to develop an annual Academic Sustainability Plan.

- **Eliminates Sunset Dates for Two Programs.** Forthcoming trailer legislation will propose eliminating sunset dates for the California Health Benefits Review program (sunsets July 1, 2017) and Umbilical Cord Blood Collection program (sunsets January 1, 2018). Both programs are funded from special funds.

California State University

- **Unrestricted Base Increases.** The Governor's budget proposes a $157.2 million increase as follows: (1) a $131.2 million unallocated augmentation and (2) an additional unallocated $26 million increase associated with savings from changes to the Middle Class Scholarship program made in 2015-16.

- **Other Allocations.** The proposed budget provides (1) a $5.1 million increase to CSU's support budget for lease-revenue bond debt service and (2) an additional $22.6 million above revised current-year levels for CSU retiree health benefit costs, which is budgeted separately from CSU's support budget.

- **Assumes No Increases in Tuition.** While the budget does not assume any increases in tuition levels, the Chancellor's Office has proposed increasing resident and nonresident tuition charges for 2017-18. The trustees are expected to vote on this proposal during their March meeting, after concluding a statutorily required consultation process with students.

- **Eliminates Sustainability Plan Requirement.** The Governor proposes eliminating budget language pertaining to academic sustainability plans, which requires CSU to develop an expenditure plan and set performance targets under revenue assumptions developed by the Department of Finance.

California Student Aid Commission

- **Middle Class Scholarship.** The Governor proposes to phase out the Middle Class Scholarship program. The budget proposes to only fund Middle Class Scholarships in 2017-18 for students already receiving an award in 2016-17. The budget assumes General Fund spending on Middle Class Scholarships remains flat at $74 million from 2016-17 to 2017-18, whereas current law appropriates $117 million for the program in 2017-18.

ISSUES TO CONSIDER

According to the Public Policy Institute of California, college costs are at their highest point ever at California's public universities. However, over the last five years, with an improving economy and state investment in higher education, tuition at UC and CSU has remained flat. The Administration's budget proposes to increase funding for UC and CSU, yet the UC Regents have voted to increase tuition, and CSU is expected to vote for a tuition increase in March. Though these increases are modest compared to the large increases from 2006 to 2011, this raises questions regarding the affordability of higher education.

According to the Legislative Analyst's Office (LAO), UC and CSU's tuition and fee levels vary compared to public colleges in other states. UC tends to have higher tuition and fees compared to other public universities with a similar level of research activity. Specifically, UC's tuition and fees are higher than all but ten of the 65 largest public research universities in other states. By contrast, tuition and fees at CSU are lower than all but 42 universities among a group of 244 masters–level public universities in other states.

Moreover, tuition and fees at UC and CSU tend to be volatile, with periods of flat tuition followed by sharp increases. The periods of flat tuition generally correspond to years in which the state experienced economic growth, whereas the periods of steep tuition increases generally correspond to periods when the state experienced a recession. During recessions, the state has often balanced its budget in part by reducing state funding for the segments. UC and CSU, in turn, increased tuition and fees to make up for the loss of state support.

In addition to tuition and fees, other expenses such as housing and food, personal expenses, books and supplies, and transportation make up the total cost of attendance for higher education. The cost of attendance varies across campuses within each system because some expenses, such as housing, vary by location. The cost also varies depending on whether a student lives on campus, off campus not with family, or off campus with family. For each system, students living at home with family have the lowest cost of attendance. The cost of attendance for students living on campus and off campus not with family tend to be similar.

Financial Aid. California has one of the country's most generous state financial aid programs, which helps many low-income students attend UC and CSU. The state's Cal Grant program guarantees aid to California high school graduates and community college transfer students who meet financial need criteria and academic criteria. In addition, students who do not qualify for high school or community college entitlement awards but meet other eligibility criteria may apply for a limited number of competitive grants. Awards cover full systemwide tuition and fees at the UC and CSU, and up to a fixed dollar amount toward costs at private colleges. The Cal Grant program also offers stipends, known as access awards, for some students to help cover some living expenses, such as the cost of books, supplies, and transportation. A student generally may receive a Cal Grant for a maximum four years of full–time college enrollment or the equivalent. Cal Grant spending is driven by increased tuition and participation. The Administration estimates that should the proposed tuition increases be adopted, Cal Grant spending will increase by $17.7 million for UC students and $24.9 million for CSU students in 2017-18 beyond the costs reflected in the budget. The Legislature may wish to consider exploring ways to constrain the anticipated growth in associated Cal Grant program costs.

Student Loans and Debt. According to the Legislative Analyst's Office, by the time UC and CSU students graduate, 55 percent of UC students and 49 percent of CSU students have taken out student loans. Among those borrowing, the average student loan debt at graduation is $19,100 for UC students and $14,388 for CSU students. Student borrowing at UC and CSU is lower than the national average, with 60 percent of students at other four–year public universities graduating with loans, with an average debt load of $25,900.

UC Cost Structure. The Administration's budget assumes no tuition increase; however, the Governor's budget summary notes that any tuition increase at UC must be viewed in the context of reducing the overall cost structure. In 2015, the Governor and the UC President agreed on several initiatives to reduce the cost structure of the UC. Their framework, which was ultimately adopted by the Board of Regents, requires UC to reevaluate how students' prior academic experiences are recognized as part of UC degree programs, how academic programs are structured, and how instruction is delivered. The Administration's budget does not specify what indicators or metrics to use to evaluate whether UC has reduced the overall cost structure, and instead stated that it will continue to monitor how UC implements its budget framework. UC has noted that it has completed eight of the 13 elements:

1. *Implementation of the Public Employee Pension Reforms Act (PEPRA) Pensionable Salary Cap:* In March 2016, the UC Board of Regents approved changes to retirement benefits, including the introduction of the PEPRA-level cap to pensionable income. The implementation process for the cap was completed and all eligible new employees were subject to the cap as of July 1, 2016.

2. *Systemwide Major Preparation Transfer Pathways:* UC adopted systemwide agreements on the major preparation transfer pathways for the top 22 majors. Additional majors that also use one of these pathways are being incorporated as they are identified by the campuses.

3. *State's Common Identification Numbering (C-ID) system*: President Napolitano sent a letter to Academic Senate Chair Hare strongly encouraging the Senate to "examine adoption of the C-ID system to further simplify identification of similar courses across the University's undergraduate campuses and transferable courses at California Community Colleges."

4. *Online Courses for Undergraduates:* Led by the Innovative Learning Technology Initiative and in coordination with UC campuses, UCOP representatives developed a report that demonstrates the prioritized funding for bottleneck courses.

5. *Alternative Credits:* President Napolitano sent a letter to Academic Senate Chair Hare strongly encouraging the Senate to "reexamine current policies regarding Advanced Placement and the College Board's College-Level Examination Program tests."

6. *Time-to-Degree Advising:* President Napolitano transmitted a report on time-to-degree advising to the nine undergraduate campuses' leadership and staff, who are sharing it with those responsible for student advising on each of these campuses. This guidance included practices that support timely graduation of students and help reduce the achievement gap among different socioeconomic cohorts of UC students.

7. *Data to Identify At-risk Students:* UC expanded the use of data systems, such as predictive analytics, to identify undergraduate students at risk of academic difficulty. A summary report, "Data to Identify At-Risk Undergraduate Students: UC Campus Efforts," was shared with UC campus Undergraduate Education Deans and Institutional Research Directors.

8. *Stakeholder Convening for Online Programs:* UCOP convened industry and academic leaders to further identify online programs that may be developed to enhance delivery of UC's instructional programs to better meet industry workforce needs.

In addition to completing the elements above, UC notes that the following are framework elements in progress:

1. *Adaptive Learning:* Pilot “adaptive learning technology” at UC Davis and two other campuses focused on improving instruction and increasing the number of students who master content in particularly difficult courses and persist to completion. Data collection and analysis are largely complete.

2. *Transfer Ratio:* Increase the proportion of students entering as community college transfers, so that by the 2017-18 academic year, one third of all incoming California resident students will enter as transfers, systemwide and at every campus except Merced.

3. *Activity-based Costing:* Pilot “activity-based costing” at UC Riverside and engage two other campuses in a scoping study to potentially expand the piloting of activity-based costing to either or both of these two other campuses.

4. *Major Requirements:* Review upper-division course requirements for the top 75 percent of undergraduate majors. The goal of this review is to reduce the number of units required to complete a major by a full year of academic work where possible by July 1, 2017.

5. *Summer Session:* Pilot alternative pricing models in summer sessions at three campuses by summer 2016 to determine effective strategies for increasing summer enrollment.

The Administration is silent on whether or not UC has met these latter elements of the framework; however, they do note in the budget summary that they are focused on monitoring activities-based costing, and increasing the transfer ratio.

In order to avoid a tuition increase, the 2015-16 budget framework was developed by the “Committee of Two,” between the Governor and President Napolitano. This framework was developed without consultation with the Legislature. As the Legislature deliberates the 2017-18 budget, it may wish to consider whether the existing framework is an appropriate measure of how UC should reduce its cost structure, or if there are other elements the Legislature should evaluate. Moreover, the Legislature may wish to consider whether the UC adopted tuition increase is appropriate given the significant state investment over the last several years.

CSU Graduation Rates. The Governor’s budget summary states that CSU’s proposed tuition increase must be viewed in the context of improving the graduation rates. CSU’s four-year graduation rate is about 19 percent, and its six-year graduation rate is about 57 percent. The 2016 budget called on the CSU to increase four-year graduation rates and two-year transfer graduation rates, with specific emphasis on closing achievement gaps for low-income students, first-generation students, and students from underrepresented minority groups.

The CSU Graduation Initiative 2025 adopted by the Board of Trustees in September 2016 commits the CSU to increasing the four-year graduation rate to at least 40 percent, increasing the two-year transfer graduation rate to at least 45 percent, and closing gaps in outcomes between the targeted students and their peers. The CSU’s plan focuses on increasing the average number of courses students take each term, including during summer and winter terms, and reducing the number of courses taken unnecessarily or repeated. To jumpstart this effort, the 2016 budget included $35 million in one-time funding, which is now assisting campuses in making immediate changes. According to CSU, $20.5 million was allocated to campuses based on the number of students receiving Pell Grant awards, and number of students with remedial education needs; $12.5 million was allocated to campuses to help students and transfer graduate in 4.5 and 2.5 years, respectively; and $2.5 million was allocated to campuses with less than 11,000 full-time-equivalent students.

According to the Administration, the CSU Graduation Initiative 2025 can only be successful if education leaders across the system are clear about what a CSU education entails. For example, more than 40 percent of CSU freshmen are still identified as unprepared for college-level courses based on their performance on a sequence of tests. Evidence from other contexts, including California community colleges, suggests that many of these students are actually prepared for those college courses and that other measures - like high school grades - are better indicators of such preparation. In preliminary conversations with the segment, CSU leadership has indicated that funding the Graduation Initiative is its main priority. The Administration notes that it will continue to monitor CSU's commitment to the initiative, and whether the CSU will submit annual campus reporting on their progress.

Given the recent significant investments in CSU, the Legislature may wish to continue monitoring the CSU's implementation of the 2025 Graduation Initiative. As noted in the previous section, student success is a priority of the Legislature. In recent budgets, the Senate has championed various proposals to increase graduation rates at the CSU, including the Completion Incentive Grant (CIG), which provided grants to students who were on-track to graduating in four-years. As the Legislature evaluates the 2017-18 budget, it may wish to consider if the CSU's proposed tuition is reasonable in addressing the system's needs, without compromising affordability for students. Similar to UC, the Legislature may wish to consider CSU's cost structure, and what initiatives or reforms CSU should undertake in order to become more cost efficient.

Investing in Community College Student Success

BACKGROUND

The California Community Colleges (CCC) is the largest system of community college education in the United States, serving approximately 2.1 million students annually, with 1.2 million of these full-time equivalent students. The CCC system is made up of 113 colleges operated by 72 community college districts throughout the state. California's two-year institutions provide programs of study and courses, in both credit and noncredit categories, which address its three primary areas of mission: education leading to associates degrees and university transfer; career technical education; and basic skills. The community colleges also offer a wide range of programs and courses to support economic development and specialized populations.

As outlined in the Master Plan for Higher Education in 1960, the community colleges were designated to have an open admission policy and bear the most extensive responsibility for lower-division, undergraduate instruction. The community college mission was further revised with the passage of Assembly Bill 1725 (Vasconcellos), Chapter 973, Statutes of 1988, which called for comprehensive reforms in every aspect of community college education and organization.

The Board of Governors (BOG) of the CCCs was established in 1967 to provide statewide leadership to California's community colleges. The board has 17 members appointed by the Governor, subject to Senate confirmation. Twelve members are appointed to six-year terms and two student members, two faculty members, and one classified member are appointed to two-year terms. The objectives of the board are:

- Provide direction, and coordination to California's community colleges.
- Apportion state funds to districts and ensure prudent use of public resources.
- Improve district and campus programs through informational and technical services on a statewide basis.

The following table displays proposed 2017-18 expenditures and positions for the CCCs, as compared to the previous and current budget years. Of the amounts displayed in the table, $5.3 billion in 2015-16, $5.4 billion in 2016-17, and $5.5 billion in 2017-18 is from Proposition 98 General Fund, and $10.7 million in 2015-16, $21.2 million in 2016-17, and $12.76 million in 2017-18 is from non-Proposition 98 General Fund. The remainder of funding comes from local property tax revenue, fee revenue and various special and federal fund sources.

California Community Colleges Budgeted Expenditures and Positions
Dollars in Millions

(Dollars in Millions)	**2015-16**	**2016-17**	**2017-18**
Personal Services	$16.1	$17.3	$17.7
Operating Expenses and Equipment	$5.5	$10.3	$7.8
Local Assistance	$8,650.1	$9,016.9	$9,164.2
Total Expenditures	**$7,954**	**$8,728**	**$9,022**
Positions	**141.7**	**142.5**	**144.5**

Student Success at the Community Colleges. Pursuant to Senate Bill 1143 (Liu), Chapter 409, Statutes of 2010, the Board of Governors (BOG) of the California Community Colleges created the Student Success Task Force (SSTF). The SSTF was comprised of 20 individuals (community college chief executive officers, faculty, students, researchers, staff and external stake holders) who spent a year researching, studying and debating the best methods to improve student outcomes at the community colleges.

According to the SSTF report, which was unanimously adopted by the BOG in January 2012, it was their goal to identify best practices for promoting student success and to develop statewide strategies to take these approaches to scale while ensuring that educational opportunity for historically underrepresented students would not just be maintained, but bolstered.

The SSTF efforts resulted in 22 specific recommendations focused on the following eight areas:

1. Increasing college and career readiness.
2. Strengthening support for entering students.
3. Incentivizing successful student behaviors.
4. Aligning course offerings to meet student needs.
5. Improving education of basic skills students.
6. Revitalizing and re-envisioning professional development.
7. Enabling efficient statewide leadership and increase coordination among colleges.
8. Aligning resources with student success recommendations.

Implementation of these recommendations is being accomplished by the Chancellor's Office via the "Student Success Initiative" through regulatory changes, system-wide administrative policies, local best practices and legislation. These implementation efforts include the following:

SB 1456 (Lowenthal), Chapter 624, Statutes of 2012, recast the Seymour-Campbell Matriculation Act of 1986 in order to target funding to services such as orientation, assessment, and counseling and advising to assist students with the development of education plans. It also required that students define goals, required that students declare a course of study and mandated student participation in assessment, orientation and education planning.

At a regulatory level, the Board of Governors approved regulations that provide enrollment priority to students who have participated in assessment, orientation, and who have developed an education plan. In addition, districts are now required to notify students that accumulating 100 degree applicable units or being on academic or progress probation for two consecutive terms will result in the loss of enrollment priority.

Additionally, budget trailer bill language, SB 860 (Committee on Budget and Fiscal Review), Chapter 34, Statutes of 2014, codified the regulatory requirement that each CCC district maintain a student equity plan to help ensure that historically underrepresented students have equal opportunity for access, success and transfer at colleges. Colleges are required to develop plans to examine specific student populations, determine if they are achieving access, success and transfer rates at the same level as other students, and develop strategies for improving these results, as needed. These plans must include the following:

- Campus-based research on student equity issues related to the following: gender, foster youth status, low-income, veteran, disabled, and specific ethnic and racial categories.

- Goals for access to, and completion of basic skills, career technical education and workforce training, and transfer courses (overall student population and population subgroups). Determination of types of activities most likely to effectively achieve these goals.

- Measures for addressing disparities, including: a means of coordinating with, at a minimum, the following student equity-related categorical programs or campus-based programs.

    - Student Success for Basic Skills Students
    - Student Financial Aid Administration
    - Disabled Students
    - Special Services for CalWORKs Recipients
    - Extended Opportunity Programs and Services and Special Services (EOPS)
    - Fund for Student Success
    - Student Success and Support Program
    - Programs for foster youth
    - Programs for veterans

- Sources of funds for activities in the plan.

- A schedule and process for evaluation.

- An executive summary.

While student equity plans have been established in regulation since 1996, the Budget Act of 2014 is the first time that dedicated state resources have been provided for those plans. In order to implement activities and goals outlined in student equity plans, the Chancellor of the CCCs allocates the funds to ensure that districts serving a greater population of students who are high-need, receive greater resources.

The 2015-16 budget included trailer bill language to allow up to $15 million of the student equity appropriation be used for the purpose of SB 1023 (Liu), Chapter 771, Statutes of 2014, which authorized the Chancellor's Office to fund specialized foster youth services in some community college districts. The new program, the Cooperating Agencies Foster Youth Educational Support Program (CAFYES), is meant to encourage enrollment and academic success of current and former foster youth. Through a competitive grant process, the Chancellor's Office awarded CAFYES funds in January 2016, to ten districts operating 26 colleges.

Additionally, there are many well-established categorical programs and campus-based programs, mentioned above, that address specific student populations on areas such as retention and completion. The descriptions below provide a short summary of the various programs:

- **Extended Opportunity Programs and Services (EOPS):** EOPS provides academic and financial support to community college students whose educational and socioeconomic backgrounds may deter them from successfully attending college and completing their educational goals. Services are specifically designed to offer educational support services to address the specific needs of at-risk students, including but not limited to individualized counseling and support, academic progress monitoring, and tutoring services.

- **Disabled Student Program and Services (DSPS):** The DSPS program provides support services and educational accommodations to students with disabilities. Many colleges also provide specialized instruction as part of their DSPS program. DSPS services may include test-proctoring, assessment for learning disabilities, specialized counseling, and interpreter or captioning services for students who are deaf or hard of hearing.

- **Basic Skills Initiative (BSI):** The 2016-17 budget included trailer bill language that refines this longstanding categorical program. To date, funding has been provided for various activities intended to improve the outcomes of students needing basic skills help. Allowable activities have included curriculum planning and development, advising and counseling, and supplemental instruction and tutoring. The 2016-17 budget continues to allow these activities while specifying four new allowable activities: (1) implementing or expanding the use of evidence–based practices and principles; (2) accelerating the adoption and use of open educational resources in basic skills English, math, and English as a second language (ESL) courses; (3) collaborating with high schools and the California State University (CSU) campuses to better align remedial instruction among LEAs, community colleges, and CSU campuses; and (4) implementing assessment and placement practices that increase the likelihood students will be appropriately placed in college–level, rather than remedial, courses.

The 2016-17 budget provided $30 million for additional Basic Skills and Student Outcomes Transformation Program grants. Established in 2015-16 as a one–time initiative, this program initially had more eligible applicants than available funding and the Chancellor's Office awarded $60 million to 43 eligible colleges. The 2016–17 funding will provide grants to another 21 eligible colleges that did not receive an award from 2015-16 funds due to limited funding. The grants are for colleges to adopt or expand the use of evidence–based models for basic skills assessment, placement, instruction, and student support. Beginning in 2017–18, the $30 million is to be repurposed on an ongoing basis for the Basic Skills Initiative.

The 2015-16 budget also included $10 million one-time Proposition 98 General Funds for the Basic Skills Partnership Pilot Program, which provides incentive grants for colleges to collaborate with high schools and CSU campuses in the delivery of basic skills instruction.

- **CalWORKs Student Services:** CalWORKs funds are used for the purpose of assisting welfare recipient students and those in transition off of welfare, to achieve long-term self-sufficiency through coordinated student services offered at community colleges including: work study; job placement; child care; coordination; curriculum development and redesign; and under certain conditions, post-employment skills training and instructional services.

- **Institutional Effectiveness Partnership Initiative (IEPI):** IEPI is a statewide collaborative effort to help advance the effective practices of the community colleges and, in the process, significantly reduce the number of accreditation sanctions and state and federal audit issues. The 2016-17 budget augments statewide professional development activities by $8 million, bringing the total for this component of the program to $20 million. The 2016-17 budget also augments technical assistance funding by $2 million, bringing the total for this component of the program to $7.5 million.

- **Fund for Student Success:** This fund supports the Mathematics, Engineering, and Science Achievement (MESA); Puente Project; and Middle College High School (MCHS) programs. Established over 40 years ago, MESA programs serve students who are financially and educationally disadvantaged and who are seeking majors in math and science based fields. Middle College High School (MCHS) is a unique collaborative program that enables high-potential, "at-risk" students to obtain a high school education while concurrently receiving direct access to college courses and services. High school students attend classes at a community college and earn credit toward a high school diploma while having the opportunity to concurrently take college courses and to receive more intensive counseling and administrative attention. The Puente Project was established over 25 years ago and is co-sponsored by community colleges and the University of California (UC). The Puente Project is an academic, counseling and mentoring program for students to build the skills necessary for success in both academic and career goals in community college. Students enrolled in the program work closely with their counselor, English instructor and mentor to prepare for transfer to four-year colleges and universities.

Below is a chart from the Legislative Analyst's Office that displays state funding for the various student success programs at the state's community colleges.

State Funding for California Community Colleges' Student Success Programs

(Dollars in millions)

	2012–13 Actual	2013–14 Actual	2014–15 Actual	2015–16 Revised	2016–17 Enacted	Increase From 2012–13
Student Success and Support Program	$49	$85	$185	$285	$285	$236
Student Equity Plans	—	—	70	155	155	155
Extended Opportunity Programs and Services	74	89	89	123	123	49
Disabled Student Program and Services	69	84	114	115	115	46
Basic Skills Initiative	20	20	20	20[a]	50	30
CalWORKs Student Services	27	35	35	35	44	17
Institutional Effectiveness	—	—	3	18	28	28
Technology Projects[b]	—	14	14	14	14	14
Fund for Student Success[c]	4	4	4	4	6	2
Totals	**$243**	**$331**	**$604**	**$769**	**$820**	**$577**

[a]In addition to the ongoing funding shown, the state provided $70 million in one–time funding—$60 million for the Community Colleges Basic Skills and Outcomes Transformation Program and $10 million for the Basic Skills Partnership Pilot Program.

[b]Consists of the Common Assessment Initiative, Education Planning Initiative, and electronic transcripts.

[c]Supports the Mathematics, Engineering, and Science Achievement program; Middle College High School program; and Puente Project.

On July 5, 2016, the Chancellor's Office announced the suspension of Student Success and Support Program (SSSP), Equity, and Basic Skills plans for 2016-17. The Chancellor's Office notes that while the initiatives of SSSP, Student Equity, and Basic Skills have provided colleges with much needed financial support, colleges have been required to submit annual action and expenditure plans to the Chancellor's Office. As these three areas were developed independently, the Chancellor's Office notes that the planning processes have proved to be laborious and redundant. In response, the Chancellor's Office is suspending the requirement for colleges to submit plans in these areas for 2016-17. The requirement to submit a plan will resume in 2017-18. During this one-year hiatus, Academic Affairs and Student Services—the two divisions that oversee these three areas—will investigate how to merge the three plans into one plan that covers all three areas.

GOVERNOR'S PROPOSAL

Guided Pathways Program – The budget includes $150 million one-time Proposition 98 General Fund for grants to support community colleges to develop an integrated, institution-wide approach to student success.

Apportionments – The budget assumes a decrease of $27.1 million Proposition 98 General Fund, which reflects: (1) an increase of $94.1 million for a 1.48 percent cost-of-living adjustment, (2) an increase of $79.3 million for enrollment growth (1.34 percent), (3) an increase of $3.8 million as a result of decreased offsetting student enrollment fee revenues, (4) a decrease of $56.6 million to reflect unused growth funding provided in 2015-16, and (5) a decrease of $147.7 million as a result of increased offsetting local property tax revenues.

Operating Expenses – The budget provides an increase of $23.6 million Proposition 98 General Fund to support community college operating expenses, such as employee benefits, facilities, professional development, and other general expenses.

Online Education Initiative – The budget provides an increase of $10 million Proposition 98 General Fund to provide systemwide access to the initiative's learning management system.

Integrated Library System – The budget provides an increase of $6 million one-time Proposition 98 General Fund to develop an integrated library system that would allow for students to access a cloud-based library system.

Deferred Maintenance – The budget proposes a $43.7 million one-time Proposition 98 General Fund increase for deferred maintenance, instructional equipment, and specified water conservation projects. Community colleges will not need to provide matching funds for deferred maintenance.

Proposition 39 – The budget proposes an increase of $3 million Clean Energy Job Creation Fund for community college energy efficiency projects, consistent with Proposition 39.

Innovation Awards – The budget proposes $20 million one-time Proposition 98 General Fund for innovation awards for the development and implementation of innovative practices as determined by the Chancellor's Office.

Strong Workforce Program – The budget proposes to move $48 million from the Career Technical Education Pathways program, which is scheduled to sunset on July 1, 2017, into the Strong Workforce Program.

ISSUES TO CONSIDER

Oversight. For years, the Legislature has expressed concern about the low completion rates of CCC students. In an effort to promote better results, the Legislature passed legislation and made significant investments in student support services and programs. In September 2016, the Legislative Analyst's Office (LAO) released its second report on the overall implementation of the Student Success Act of 2012. The report found that colleges are spending half of SSSP funding for counseling and education planning services. When broken down by operating expenses, staff salaries and benefits comprised about 81 percent of SSSP allocations. Colleges report hiring 1,800 new full-time equivalent employees with SSSP funding in 2014-15 and 2015-16 combined. The new hires include 800 FTE counselors, roughly 44 percent of the total, and nearly all the remaining new hires were assistants and student workers. However, a majority of colleges continued to hire primarily or exclusively part-time counselors, and the LAO notes that colleges expressed a reluctance using SSSP and equity funds to hire more full-time staff due to a fear of possible cuts to categorical programs during a future recession.

The BOG adopted policies requiring colleges to offer students assessment and placement, orientation, and education planning, as prescribed in SSSP. Certain "exempt" students, such as those with an associate degree or higher, are not required to complete these services. However, the LAO notes that in fall 2015, only 54 percent of nonexempt students enrolled received assessment and placement services, and 49 percent received orientation. Given the large investments in SSSP and its goal for all students to complete these core services, the Legislature may wish to consider directing the BOG to strengthen the requirement that students complete these services, while requiring colleges to mitigate any disproportionate impact on groups of students.

The student success scorecard was implemented under SSSP to show performance outcomes for a cohort of students six years after initial enrollment. The current scorecard is based on first-time students in 2009-10, and it notes that only 47.1 percent of degree, certificate and/or transfer-seeking students achieved their goal. This data does not reflect students who enrolled after SSSP and student equity was implemented. Information regarding students post-SSSP and student equity will not be available until 2020-21. In order to provide a better oversight on the implementation and outcomes of SSSP and student equity, the Legislature may wish to consider requesting the Chancellor's Office to produce an interim three-year scorecard.

Regulations also specify that student equity plans must be based on campus-level data in the areas of access, retention, degree and certification completion, English as a second language, basic skills competition, and transfer, and must identify any disparities in these outcomes among various student groups. The Chancellor's Office provided three equity gap methodologies colleges to use to disaggregate enrollment and outcomes data. The LAO notes that these methodologies are very sensitive to the methodology a college chooses and the reference group the college selects. As a result, one college may consider a certain gap in outcomes a disparity that needs to be addressed, while another college would consider the same gap acceptable. Additionally, a group's underrepresentation for an outcome does not necessarily indicate an equity gap for a group. Lastly, since colleges may choose between three different methodologies, it may be difficult to compare and evaluate the disparities between colleges, and whether services provided are the most effective in reducing disparities. The Legislature may wish to direct the Chancellor's Office to identify a consistent way of measuring disparities for each of the specified student outcomes.

Pathways Model. According to the Administration, a guided pathway program is an integrated, institution-wide approach focused on improving student success. The Administration's proposal allows participating community colleges to use these grants for activities including the design of academic roadmaps and transfer pathways that explicitly detail the courses students must take to complete a credential or degree on time. According to the Administration, colleges can also use these grants to provide targeted advising and support services; redesign assessment, placement, and remedial education policies and courses; and redesign or refresh courses and programs to better align learning outcomes with the requirements for successful employment. The expectation is to improve completion rates, reduce time-to-degree, increase California students' employment opportunities, and reduce student debt.

The Board of Governors describes the Pathways Model as a whole-college redesign of the student experience, with changes to the way programs instruction and support services are structured and integrated to help students complete their degrees more efficiently. The January board agenda noted that there are numerous existing community college initiatives that already incorporate elements of the pathways model. These initiatives include:

- **Associate Degree for Transfer.** Senate Bill 1440 (Padilla), Chapter 428 Statutes of 2009 established the associate degree for transfer, which guarantees an Associate of Arts or Associate of Science degree upon completion of 60 transferable units at a CCC that meet IGETC or CSU breadth general education requirements, with 18 units in a major determined by the college, and have a 2.0 grade point average. Statute requires CSU to accept all students who earn the degree and grant them junior status, and prohibits CSU from requiring students to repeat courses or take more than 60 additional units and will earn a Bachelor of Arts or Bachelor of Science degree upon fulfillment of their major requirements. These transfer students will not be required to take any lower division courses for their majors.

- **The Common Assessment Initiative**. The initiative includes the Multiple Measures Assessment Project, which determines a high school student's college preparedness by using multiple measures, such as a placement exam score in conjunction with their grade point average. Typically, a multiple measures assessment places a student at a higher level than a placement exam alone does, so less remediation is required at the community college level.

- **The California Acceleration Project.** This project focuses on moving students through remediation quickly so that they are prepared to take college level classes and/or classes of greater interest to them sooner. Acceleration through remedial classes is meant to lessen the risk of student discouragement and dropout. Many of the best practices that are adopted by the project are also incorporated in the basic skills transformation grants, as well as the latest reforms to the basic skills initiative.

- **The California Guided Pathways Project.** This project was inspired by the American Association of Community Colleges (AACC) Pathways Project. Three California community colleges were selected for the national project—Bakersfield College, Irvine Valley College, and Mt. San Antonio College. The AACC project is funded by the Bill and Melinda Gates Foundation. Participating colleges receive no direct funding, but participate in a series of institutes that will be entirely paid for by the project and receive technical assistance from AACC and project partners.

  Additionally, the Foundation for CCC recently received $2 million from the Teagle Foundation and College Futures Foundation to launch the California Guided Pathways Project, which will be similar to the AACC project. Over the next three years, total expected funding is about $4.2 million. Similar to the AACC, this project will provide professional development and technical assistance to 15 to 20 colleges. Participating colleges receive no direct funding.

While not noted in the BOG's agenda item, there are also various categorical programs noted earlier that seek to support student completion. Additionally, there are various initiatives and programs that colleges are participating in. These include:

- **California Community College Promise Innovation Grant Program.** AB 1741 (Rodriguez), Chapter 434 Statutes of 2016, established this program. This program establishes or expands regional programs to address college preparedness, attendance, and graduation in partnership with school districts and public postsecondary universities in California. The 2016-17 budget provided $15 million one-time Proposition 98 General Fund for this purpose. There are numerous existing college promise programs, including the Long Beach Promise, which until recently, did not receive dedicated funding for this purpose.

- **UC Transfer Pathways.** As a part of the 2015-16 budget agreement between the Administration and UC, the UC implemented the UC Transfer Pathways. Similar to SB 1440, each pathway outlines the set of courses students should take to be competitive in one of 21 of the most popular majors found at every UC campus. Whereas an associate degree for transfer guarantees admission to a CSU campus, completing transfer pathway courses for UC does not.

While there are various initiatives and programs that the community college system is implementing, the Administration's proposal for guided pathways seeks to help colleges identify gaps in service and support and to fill those gaps. However, the effectiveness of existing initiatives, such as the SSSP, equity plans and basic skills transformation, are still unclear since data regarding the student cohort since implementation of the program is not yet available. While improving student success and outcomes have been a priority of the Legislature, it is unclear how the Administration's proposal will coordinate and integrate all the various initiatives. The

Legislature may wish to consider whether it should prioritize existing programs, or if it should invest in a new program. Additionally, the Legislature may wish to consider whether colleges will be able to step back and take a holistic approach in revamping and reforming its courses, academic programs, and services. Moreover, the California Guided Pathways project does not provide direct funding to colleges, instead foundations provided about $2 million for the institute to provide seminars and technical assistance to 15-20 colleges. Staff notes that the IEPI receives about $28 million to provide technical support, assistance and professional development to colleges. The Legislature may wish to consider if colleges should receive direct funding for the purpose of guided pathways, and if so, if $150 million Proposition 98 General Funds is the appropriate amount.

SUBCOMMITTEE NO. 2

RESOURCES, ENVIRONMENTAL PROTECTION, ENERGY and TRANSPORTATION

Resources

Energy

Transportation

Managing the State's Beverage Container Recycling Programs

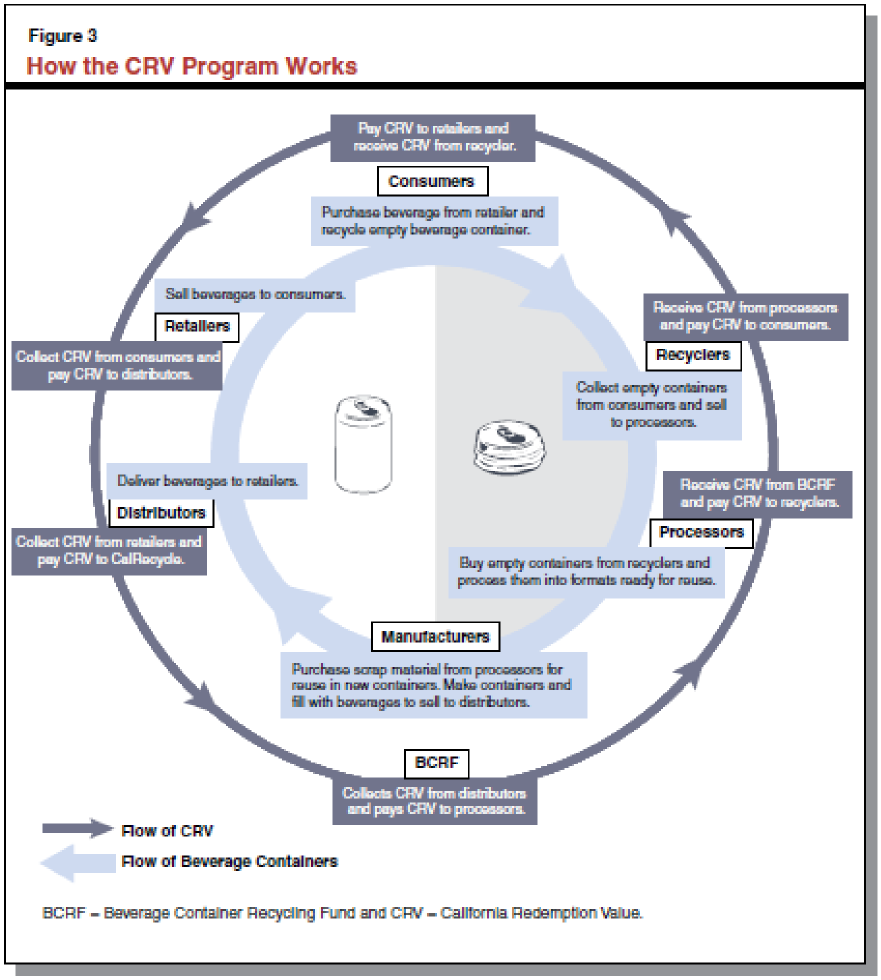
BACKGROUND

The Department of Resources, Recycling and Recovery (CalRecycle) oversees and provides guidelines for most household and commercial waste, including the garbage picked up outside homes and businesses, recycling and compost. CalRecycle's mission is to restore, protect, and manage the state's natural, historical, and cultural resources for current and future generations using creative approaches and solutions based on science, collaboration, and respect for all the communities and interests involved. The largest single program at CalRecycle is the Beverage Container Recycling Program (BCRP).

The BCRP was established almost 30 years ago with the enactment of AB 2020 (Margolin), Chapter 624, Statutes of 1986. The purpose of the program is to be a self-funded program that encourages consumers to recycle certain beverage containers. The program accomplishes this goal by first requiring consumers to pay a deposit for each eligible container purchased. Then the program guarantees consumers repayment of that deposit—the California Redemption Value, or "CRV"—for each eligible container returned to a certified recycler. Statute includes two main goals for the program: (1) reducing litter and (2) achieving a recycling rate of 80 percent for eligible containers.

Despite paying the CRV deposit, not all consumers recycle their CRV-eligible containers. In 2015–16, for example, CalRecycle reports that the Beverage Container Recycling Fund (BCRF) received roughly $1.3 billion in deposits, but only about $1.1 billion was spent on redemption payments. The BCRF retains unredeemed deposits, and state law requires that much of the unredeemed CRV be spent on specified recycling–related programs. These supplemental programs are not directly involved in the exchange of CRV, but they are intended to help achieve the programmatic goals of increased recycling and reduced litter. There are currently ten supplemental programs funded from the BCRF (including program administration). Such programs include subsidizing glass and plastic recycling, encouraging supermarket recycling collection sites, and providing grants for market development and other recycling–related activities. CalRecycle estimates that a total of $257.4 million will be spent on supplemental programs in 2016–17. The figure below describes how the CRV works.

How the California Redemption Value (CRV) Recycling Program Works



Source: Legislative Analyst's Office, 2015

Quarterly Report on the BCRP. CalRecycle is required to report quarterly on the status of the BCRP in order to review the adequacy of resources in the BCRF for purposes of making payments specified in Public Resources Code (PRC) Section 14581 and the processing fee offsets specified in PRC Section 14575. This statutorily-required report provides updates on the status of all five funds (Beverage Container Recycling, Glass Processing Fee Account, Plastic Processing Fee Account, Bimetal Processing Fee Account, and Penalty Account) in the BCRP. This report also provides projections for sales, recycling volumes (returns), processing payments, processing fees, and processing fee offsets, by material type, and handling fees.

Update from the Most Recent Quarterly Report. According to CalRecycle, the BCRP is currently operating with a projected $50 million structural deficit for 2016-17. The structural deficit means that program expenditures exceed program revenues under the current mandated expenditure and revenue structure. Based on this structural deficit and current fund balances, the department estimates that there may be insufficient funds to fully support program payments and maintain minimal reserve requirements in 2017-18. The structural deficit can fluctuate as much as tens of millions of dollars from quarter to quarter as a result of economic shifts and other factors (including scrap value rates). Previously, the gap between expenditures and revenues has been temporarily bridged through repayments of loans, particularly to the General Fund, made from the fund when it was operating at a surplus. The final loan repayment, amounting to $82.3 million, was paid in full at the end of 2014-15.

In order to address the structural deficit, CalRecycle has implemented several program reforms, including reduced daily load limits for redemption at recycling centers, increased monitoring of the importation of out-of-state beverage containers, and elimination of the commingled rate at buyback centers. This last reform allowed for slightly lower per-pound refund rate for loads containing a combination of CRV and non-CRV material. However, actions taken thus far have secured only partial success; while the gap is smaller, the amount of money coming into the BCRF is still insufficient to cover the amount being paid out. In order to eliminate the structural deficit and achieve a secure financial future for the fund and the programs it supports, further measures will be necessary. The following table displays the projected operating shortfall for 2016-17:

Operating Revenues and Expenditures - Beverage Container Recycling Fund (Dollars in Millions)

Revenues and Expenditures	2016-17 Projection
Revenues from Redemption Fees	$1,280
California Redemption Payments	1,073
Supplemental Program Expenditures	
Processing fee offsets	102.6
Handling fees	47.8
CalRecycle administration	50.7
Curbside supplemental payments	15.0
Payments to local governments	10.5
Plastic Market Development Payments	10.0
Quality Incentive Payments	10.0
Local Conservation Corps grants	6.8
Public Education	2.5
Beverage Container Recycling Competitive Grants	1.5
Subtotal Supplemental Programs	***$257.4***
Total Expenditures	**$1,330.4**
Balance	**($50.4)**

Source: CalRecylce Quarterly Report, November 2016

2014 State Auditor Report and Recommendations. An audit by the Bureau of State Audits (BSA), released in November 2014, confirmed both the positive impact of the first round of reforms and the need for more. The audit confirmed the BCRF structural deficit, then approximately $100 million, and recognized that changes could improve the program’s financial condition. These changes include reducing or eliminating administrative fees for beverage distributors; enacting changes to mandatory payments, such as those for curbside programs or quality incentives to beverage program participants; and reducing or eliminating processing fee offsets.

The report made a series of recommendations, most of which the department has embraced. To ensure that it can demonstrate that its fraud prevention efforts are maximizing financial recoveries for the beverage program, BSA recommended CalRecycle modify and annually update its fraud management plan to include the following:

- Finalize a process to analyze the data the Department of Food and Agriculture provided on out-of-state containers and act on the results to identify and prosecute those committing fraud.
- Develop fraud estimates—by type of fraudulent activity—that quantify the potential financial losses to the beverage program and the methodology CalRecycle used to develop these estimates.
- Identify the amount of actual fraud in the prior year by type of fraudulent activity, such as the financial losses resulting from the redemption of out-of-state beverage containers or the falsification of reports used to substantiate program payments.
- Identify the amount actually recovered for the beverage program in the form of cash for restitution and penalties resulting from fraud.
- Contract with the Board of Equalization (BOE) to determine the feasibility and cost of transferring its revenue collection duties and audit reviews to them.
- Pursue feasible and cost-effective legislative changes that enable the BOE to collect revenues for the beverage program at the point of sale and remit the money to the beverage fund.

Legislative Analyst's Office Review. In 2015, the Legislative Analyst's Office (LAO) conducted a thorough review of the BCRP and determined that not only is the shortfall accurate, but that certain offsets place additional costs on the program and the effectiveness of some of the supplemental programs are unclear. The LAO review found the following:

- **High Recycling Rates and Spending on Supplemental Programs Create BCRF Shortfall.** The BCRF has operated under an annual structural deficit averaging about $90 million since 2008-09. According to CalRecycle estimates, the fund is currently forecast to run an average deficit of $56 million from 2014-15 to 2017-18, absent any changes made to reduce expenditures or increase revenues. This deficit is largely due to increased recycling rates in recent years, which have resulted in a greater share of BCRF revenue being paid out for CRV. Moreover, some supplemental programs are paid on a per container basis, and therefore these expenditures increase as the number of containers redeemed increases. The combined effects of higher recycling rates—more spending on CRV payments and certain supplemental program expenditures—make it much more difficult for the BCRF to operate with a structural balance.

For the last several years, the fund balance that accumulated when recycling rates were lower was able to support this expenditure level. However, the balance is being steadily depleted each year, and programmatic changes will need to be made in the next few years in order to keep the fund solvent and avoid statutorily required automatic funding cuts (referred to as "proportional reductions"). Acting sooner would provide the Legislature a greater number of options to address the deficit and allow for more flexibility when implementing any changes.

- **Offsets Are Major Cost to BCRF and Do Not Clearly Support Goals.** The state subsidizes recycling by making "processing payments" from the BCRF to recyclers and processors. Processing payments are intended to cover the difference between a container's scrap value and the cost of recycling it (including a reasonable rate of return). These payments are funded from two sources: (1) "processing fees" paid by beverage manufacturers and (2) the BCRF supplemental program, referred to as "processing fee offsets," which reduces the amount of processing fees that manufacturers must pay.

  The LAO found that it is unclear how current processing fee offsets provided to manufacturers incentivize increased recycling. Additionally, providing offsets does not require manufacturers to consider the lifecycle costs of the materials that they use in their products. By reducing the amount of processing fees, the offsets effectively subsidize materials that are relatively more expensive to recycle.

- **Effectiveness of Some Supplemental Programs Unclear.** While supplemental programs might have merit, the LAO found that many of the programs have not been evaluated for their effectiveness at improving recycling. This lack of evaluation makes it difficult to compare the relative cost–effectiveness of supplemental programs and to determine how they help to achieve program goals of increasing recycling and reducing litter. This information is critical in determining the best use of limited program dollars. In addition, the existing structure of "handling fee" payments currently made to certain recyclers does not maximize convenience for many consumers, and may raise convenience–zone recycler costs, resulting in higher handling fee payments from the BCRF. Finally, the department has not evaluated whether administrative fees—funds that beverage container distributors, processors, and recyclers receive to cover their administrative costs to participate in the BCRP—accurately reflect costs for these program participants.

2014 Proposal—Phase 2 Reform. In January 2014, the budget proposed programmatic changes that were expected to result in a net increase to the BCRF annual fund balance of $72.3 million in 2014-15, growing to $127 million when fully implemented in 2016-17. The changes would have both raised revenue and decreased overall program expenditures, while at the same time modestly increased specific expenditures for fraud prevention, data collection, and expanded grant programs. The Administration projected that these changes would eliminate the program's structural deficit once fully implemented, and avoid the need to implement proportional reductions.

2014 Budget and Trailer Bill Actions. The budget subcommittees did not approve trailer bill language and the budget proposals that would have provided the second phase of the BCRF reform. Instead, the Legislature approved trailer bill language to remove the Local Conservation Corps (LCC) from the statutory provisions of the program funding and diversified the LCC funding in a manner similar to that proposed by the Governor under the program reform proposal.

The budget also included several positions to increase audit coverage of beverage manufacturers and distributors to better protect the integrity of the BCRF. The emphasis was on collecting revenues owed to CalRecycle and mitigating risk to the fund.

2015 Legislative Oversight and Actions. The Legislature took action in the 2015 budget to make additional changes to the BCRP, specifically to address issues raised by the Legislature and BSA related to audits and compliance. These actions included:

- **Targeted Activities to Improve Program Integrity.** $357,000 (BCRF) and three positions, and $717,000 (BCRF penalty account) and seven two-year, limited-term positions, to implement targeted activities to enhance program integrity, reduce expenditures, and mitigate potential program funding shortfalls. The budget converted eight existing limited-term positions to permanent for ongoing program certification workload.

- **Processor Oversight Activities.** $933,000 and 10 two-year limited-term positions to establish a pilot program with dedicated on-site investigation resources at certified processor facilities. These positions were to create a new pilot program to expand current fraud investigation activities on recyclers to processing facilities.

- **Rigid Plastic Packaging Container Program.** $296,000 (BCRF) and three positions, to conduct annual rigid plastic packaging container compliance certification reviews, pursuant to recently adopted regulations, and provide additional compliance assistance tools.

Interim Reform Package. The Administration, the LAO, and members of the public testified in 2016 hearings that a reform package would stabilize funding within the BCRF. Concerns were raised regarding the closure of multiple recycling centers due to the scrap value of recycled materials, thus challenging the ability of retailers to provide recycling opportunities to consumers. After multiple stakeholder meetings, the following interim proposal was discussed among stakeholders and the Administration, although, no proposal was adopted in 2016.

1. **Reduce Processing Fee Offsets First Under Proportional Reductions.** Currently, CalRecycle has no discretion to target expenditure reductions once the BCRF falls below a five percent prudent reserve. Under mandated proportional reductions, CalRecycle must make across the board cuts to expenditures. This proposal would give the department the ability to cut processing fee offsets first before reducing other program expenditures.

2. **Convenience Pilot Programs.** Allow up to three jurisdictions (one urban northern, one urban southern, and one rural) to create a convenience pilot program that would waive convenience requirements.

3. **Enforcement Relief.** Suspend enforcement for dealers impacted by closures that occurred from January 1 to March 31, 2016; grant exemptions to dealers impacted by closures due to enforcement activities July 1, 2016 to June 30, 2017; and allow the department the authority to exempt dealers impacted by closures due to local government action July 1, 2016, to June 30, 2017.

4. **Handling Fees.** Freeze handling fees at the 2015 rate and tier payments to sustain recycling centers in low volume areas until June 30, 2020. Provide supplemental payments for low volume sites in rural areas only until June 30, 2017.

5. **Processing Payments.** Revert to a 2015 cost of recycling for processing payments and shift to a three-month scrap value average for processing payments.

GOVERNOR'S PROPOSAL

Although the Governor's budget does not contain a specific proposal, the budget does include a framework for comprehensive reform of the BCRP based on three guiding principles: (1) improving recycling and remanufacturing; (2) sharing responsibility; and (3) enhancing adaptability and sustainability. The Administration is proposing that this framework guide conversations of a stakeholder process that will be used to develop the final reform package.

The Administration's framework is predicated on the belief that to maximize the environmental and economic benefits of recycling beverage containers, the program requires comprehensive reform that aligns with the state's climate change goals, the state's 75 percent solid waste reduction, recycling, and composting goal, and fiscal sustainability based on the following principles:

Improving Recycling and Remanufacturing. The program has been successful in its initial goal of reducing litter by providing recycling collection opportunities for consumers. However, collection does not ensure that a product is recycled into a new commodity. Future investments should be focused on creating clean, recyclable streams of material, which will improve the recycling and remanufacturing segments of the current system.

Improving Recycling and Remanufacturing	

Recycling Center Infrastructure	• Restructure processing payments and handling fees to support lower volume and rural sites through a tiered structure that combines these payments.
	• Maintain grocer and retailer obligation and give the department the authority to expand compliance options.
	• Increase local responsibility to support solutions for consumers to redeem.
	  o Restructure city/county payments and competitive grants to provide competitive grant funding.
	  o Option to link program payments to local opportunities to redeem.

Curbside Operations	• Create a single curbside payment based on recycled feedstock quality and system efficiency. • Convert curbside supplemental payment into a competitive grant program to support modernization of collection and material recovery infrastructure.
Beverages and Beverage Containers	• Include beverages in current materials, and add wine and distilled spirits, on July 1, 2018. • Authority to add additional container material types, including but not limited to aseptics, cartons, and flexible packaging.

Sharing Responsibility. Historically, the consumer has shouldered most of the financial burden to sustain the program. Program responsibilities and financing should be rebalanced among all program participants.

Sharing Responsibility	
Require beverage manufacturers to cover the full cost of recycling.	• Restore this requirement.

Require beverage manufacturers, or an organization representing manufacturers, to create markets for recycled products.	• Accomplished by:
	  o Minimum content requirements.
	  o Material buy-back requirements.
	  o Refillable container options.
	  o Designs for recyclability.

Reform resin identification codes to enhance recyclability.	• Require that beverage container labels reflect their recyclability.

Enhancing Adaptability and Sustainability. Increases in the recycling rate have resulted in a structural deficit in the Beverage Container Recycling Fund. In addition, the program does not respond quickly to fluctuations in the global commodities market. The program must be both nimble and fiscally sustainable.

Enhancing Adaptability and Sustainability	
Cleanup antiquated program provisions.	• Clarify definitions and reporting requirements.
Evaluate and improve program efficiency.	• Optimize program payments and implement other program improvements.
Provide authority to respond to changes in the global commodities market.	• Modify existing payment mechanisms to reduce lag in responding to market changes.
Limit adverse impacts such as the need to proportionally reduce payments.	• Incrementally implement reforms.

ISSUES TO CONSIDER

LAO Recommendations. The LAO has made several recommendations, some of which are consistent with the Administrations framework, which could help "right-size" the BCRP. Specifically, the LAO recommendations include:

- **Shifting Processing Costs to Manufacturers.** The LAO recommends shifting processing costs to manufacturers. This would reduce BCRF expenditures significantly, probably eliminating the structural deficit. It would also require producers to cover the recycling costs of their products, which means that these costs are incorporated or "internalized" into the total cost of the product when it is sold. Therefore, the price that consumers pay reflects the entire cost of the product—its production and disposal. Shifting costs to manufacturers could be done in two ways, either by eliminating processing fee offsets or by moving to a market–based system where manufacturers are responsible for the recycling of materials. While either approach could work, the LAO states that the market–based approach would have several potential advantages.

- **Improving the Cost–Effectiveness of BCRP.** The LAO makes several recommendations designed to improve the cost–effectiveness of the BCRP, including: (1) evaluating supplemental programs to determine how cost effective they are at achieving recycling and litter reduction goals; (2) giving recyclers more flexibility in where they locate and piloting a new payment structure in order to improve convenience for consumers; and, (3) adjusting the administrative fee to reflect the actual costs of program participation. In combination, the LAO believes these recommendations would improve the program's financial sustainability at current and potentially higher future recycling rates.

How does the BRCP impact the state's broader recycling goals? In 2011, AB 341 (Chesbro), Chapter 476, Statutes of 2011, established a new statewide goal of 75 percent recycling, including source reduction, recycling, and composting, by 2020. Under this program, a base generation level is calculated using the average per resident generation from 1990 to 2010 (10.7 pounds per person per day). According to a 2016 CalRecycle State of Recycling report, in order for California to reach a statewide recycling rate of 75 percent, at least half of the solid waste that is currently disposed would need to be recycled through source reduction, recycling, or composting. In the report, CalRecycle identified five priorities critical for achieving the 75 percent recycling goal: (1) moving organics out of the landfill; (2) expanding recycling and manufacturing infrastructure; (3) exploring new models for state and local funding of sustainable waste management programs; (4) promoting state procurement of post-consumer recycled content projects, and; (5) promoting extended producer responsibility.

Absent ability for comprehensive reform, should we revisit pilot proposal? In May 2016, the Senate Committee on Budget and Fiscal Review Subcommittee No. 2 voted to adopt a convenience pilot program; however, the proposal was not included in the final budget. Certain jurisdictions feel they can achieve the goals of the recycling program in a more efficient and effective manner than the state. Given the likelihood that program reform will take multiple years, the Legislature could consider allowing temporary pilot programs to move forward to better inform the department as it reforms its overall recycling programs. This could be done in a manner so as not to harm the overall program, and with proper reporting and accountability. It could also help to mitigate some of the issues that have resulted in the closing of recycling centers. According to the LAO, as of May 2016, 330 (or about 15 percent) convenience zone recycling centers had closed since the beginning of the year. The closure of so many recycling centers is problematic because it reduces consumers' ability to easily redeem containers and places a burden on supermarkets that either must pay a fee or take back containers themselves.

Department of Fish and Wildlife—Fish and Game Preservation Fund

BACKGROUND

The Fish and Game Preservation Fund (FGPF) was established in 1909 as a repository for all funds collected under the Fish and Game Code and any other law relating to the protection and preservation of birds, mammals, fish, reptiles and amphibia in California. These revenues are generated from the sale of licenses for hunting, recreational and commercial fishing, and numerous special permits. Over time, the Legislature has created various subaccounts within the FGPF, which have specified permit fees generating revenue for projects benefitting those species. For example, the taking of migratory waterfowl in California requires a state duck stamp validation in addition to a general hunting license. Revenues from the duck stamps are deposited into the Duck Stamp Account within the FGPF to be used for waterfowl protection and habitat restoration. There are currently 28 dedicated subaccounts within the FGPF.

Revenue from licenses, fees and permits that are not directed by statute to a dedicated account are accounted for in what is known as the non-dedicated FGPF. This is the largest repository for department revenues, including sales of general fishing and hunting licenses. Approximately 75 percent to 80 percent of total FGPF revenues are deposited into the non-dedicated account, with the remainder going to the various 28 dedicated subaccounts. There is a running deficit in the non-dedicated FGPF.

Program Activities Supported by the FGPF. The FGPF is the Department of Fish and Wildlife's (DFW) largest single fund source and supports a multitude of program activities. Some of the main functions supported by the FGPF are displayed in the following table:

Main Functions Supported by the Fish and Game Preservation Fund	
Law Enforcement	Support for more than 400 wildlife officers positioned throughout the state to promote compliance with laws and regulations protecting fish and wildlife resources. Wildlife officers also investigate habitat destruction, pollution incidents and illegal commercialization of wildlife, and serve the public through general law enforcement, mutual aid and homeland security.
Lands Management	Management of department-owned lands including wildlife areas, ecological reserves, and public access areas to contribute to the conservation, protection, and management of fish and wildlife. Among other things, these activities support hunting opportunities and

	serve as required match for federal wildlife restoration grant funds.
Wildlife Conservation	Activities conducted by regional and field staff related to resource assessment and monitoring, conservation and management activities for game and nongame species, and public outreach related to those species. Funding for these activities also serves as required match for federal wildlife restoration grant funds.
Fisheries Management	Development and implementation of policies to address management, protection, and restoration of fish species and their habitats. Also promotes commercial and public recreational angling opportunities. These funds serve as required match for federal sport fish restoration grant funds.
Fish and Game Commission	The commission establishes regulations for hunting, sport and commercial fishing, aquaculture, exotic pets, falconry, depredation control, listing of threatened or endangered animals, marine protected areas, public use of department lands, kelp harvest, and acts as a quasi-judicial appeal body.

FGPF Structural Imbalance. According to the Governor's budget, in 2016-17, FGPF expenditure authority exceeds projected revenues by approximately $24.1 million. In the past, the department has been able to sustain FGPF program activities by utilizing the balance in the reserve and lowering actual expenditures, thereby creating savings. However, the current situation is not sustainable. Expenditures have continued to increase and the fund balance continues to decrease, which, without action, will lead to a projected deficit in 2018-19. The following tables provide a summary of the FGPF's condition, both with and without the Governor's budget proposal:

Fish and Game Preservation Fund (with Governor's Proposal) (Dollars in Millions)			
	2015-16	**2016-17**	**2017-18**
Total Revenue	$94.7	$101.1	$124.1
Total Expenditures	124.4	125.2	130.3
	-29.7	-24.1	-6.2
Fund Balance	**$61.0**	**$36.9**	**$30.7**

Fish and Game Preservation Fund (without Governor's Proposal) (Dollars in Millions)			
	2015-16	**2016-17**	**2017-18**
Total Revenue	$94.7	$101.1	$101.1
Total Expenditures	124.4	125.2	130.3
	-29.7	-24.1	-29.2
Fund Balance	**$61.0**	**$36.9**	**$7.7**

Some of the causes of the FGPF's structural imbalance that the department has identified include; fund shifts (particularly to the General Fund), lifting of prior spending restrictions (e.g. vehicles, furloughs), increased need for federal funds, and cost of business increases (e.g. employee compensation).

Landing Fees. Commercial landing fees are established in statute as a fixed rate per pound. The rate was last amended in 1992 and currently generates revenue that is approximately 0.5 percent of the three-year historical average value of the fishery. An evaluation by the DFW in 2007 calculated that the total revenue from commercial fisheries (landing fee revenue and permit fees) covered approximately 22 percent of the total costs to manage, license, and enforce the fisheries. Since that evaluation was conducted, a number of proposed mechanisms to generate additional revenue from commercial fisheries have been evaluated over the years. The development of an ad valorem approach (value based), which is used by other west coast states, routinely rises to the top as a preferred approach. An ad valorem approach is advantageous as it is based on a set rate and reflects current market conditions. In addition, fishermen only pay the fee based on the landings and income they make.

However, DGW reports that implementation of an ad valorem approach can be extremely costly and difficult to track. Amending the statute to use an ad valorem collection approach would require establishing (and regularly amending) state regulations defining average market prices for each commercial fish species. It would also require new audits and collection processes, and law enforcement staff at the field level would need to develop new methods of investigating for compliance using business records in addition to commercial fish tickets. Costs of developing and implementing these new regulatory programs, internal business practices, and enforcement costs would offset a significant portion of the additional revenue generated.

Lifetime License Trust Account. Fish and Game Code Section 13005 established the Lifetime License Trust Account (LLTA) as a repository for revenues generated from the sale of lifetime fishing and hunting licenses. These licenses range from $700 to $1,200, depending on the age of the buyer. The LLTA was established to hold these revenues, with a specified amount made available for expenditure by an annual transfer to the FGPF, effectively amortizing the revenues from lifetime licenses over the buyers' lifetimes.

GOVERNOR'S PROPOSAL

Restructuring the FGPF. The budget proposes $12.4 million in additional revenue from an increase in commercial fish landing fees to support DFW's commercial fishing program, and a one-time redirection of $10.6 million from the LLTA ($8.7 million of which would go to the non-dedicated account). This proposal is intended to address the approximately $20 million deficit in the FGPF.

Landing Fees. The department proposes trailer bill language to increase commercial landing fees established in Fish and Game Code Section 8051, which will more closely align revenues from commercial fishing with department activities related to management and oversight of commercial fishing programs. This proposal is estimated to increase commercial landing fee revenue by approximately $12.4 million per year.

The proposed approach uses an "Eleven-Tier System," with fees based on the ad valorem concept. While generating many of the same benefits of an ad valorem system, the proposed approach would take advantage of the current structure to set, implement, and enforce landing fees, eliminating the need to establish new mechanisms to set and collect landing fees. According to the department, the proposal would not require new regulations to implement and there are minimal and absorbable anticipated new costs associated with notification to payees of the new fee rates. This proposal would utilize an eleven-tier system such that fisheries that are the highest value per pound pay the highest rate. All fisheries would pay a higher rate than status quo under the proposal, resulting in an average overall rate of five percent based on the three-year historical average value of all California fisheries.

Lifetime License Trust Account. The department proposes trailer bill language to eliminate the LLTA. The balance of the account, currently approximately $12.5 million, would be transferred to the non-dedicated FGPF, to various dedicated accounts within the FGPF, and to the Hatchery and Inland Fisheries Fund. Beginning in 2017-18, annual revenues of approximately $910,000 would instead be deposited into the FGPF. Of this amount, approximately $750,000 would be deposited into the non-dedicated FGPF and approximately $160,000 would go to the appropriate dedicated accounts. In addition, approximately $198,000 would go to the Hatchery and Inland Fisheries Fund.

According to the department, funds currently in the account are derived from fishing and hunting licenses so it is appropriate to shift these funds to the FGPF and this proposal would make these funds available for expenditure for their intended purposes.

Additional Budget Proposals. In addition to the proposal to address the FGPF's deficit, the Governor's budget includes the following proposals that would increase FGPF expenditures:

- $1.7 million to develop and implement a sampling program, in coordination with the Department of Public Health, to protect public health and prevent unnecessary fishery closures associated with harmful microalgae blooms (aka "red tides").

- $1.8 million to improve efficiency in the conservation of natural resources through compliance with the State Water Resources Control Board's emergency regulation for measuring and reporting on the diversion of water related to management and operations of department lands and facilities.

ISSUES TO CONSIDER

Impact on Commercial Fisheries. Although the Governor's proposal is intended to align revenue with the costs of supporting the program's activities and takes product value into account, the increased landing fees would nonetheless impact commercial fisheries' cost of doing business in California. Just last year, the Legislature heard about the devastating effect the drought and warmer river temperatures have had on salmon and the fishing industry and how the high domoic acid levels impacted the crab industry.

What are options for a comprehensive solution? The Governor's budget proposal amounts to a partial, ongoing solution to addressing the FGPF's structural imbalance. As such, the Administration acknowledges in their proposal that further permanent solutions will be necessary. Some of the solutions that have been brought up include; statewide fees/taxes, water rights fee (assessed by State Water Resources Control Board), or a non-consumption user fee (boat rentals, diving, whale watching). In addition the following table displays some the revenue generating options that other states use, as noted by the department.

Other States Fish and Wildlife Revenue Generation	
General Sales Tax	Missouri, Arkansas
Sales Tax on Outdoor Gear	Texas, Virginia
Real Estate Transfer Tax	Florida, South Carolina
General Obligation Bonds	Nevada
Lottery Funds	Arizona, Maine

Alternatively, the Legislature may wish to scrutinize program expenditures by requiring the department to produce more detailed program information, including, which activities are being supported without associate generation of funds, update definitions of game, nongame and commercial programs, or expand the use of dedicated accounts. Currently, almost all of the FGPF's revenue is derived from fees from recreational hunters and anglers, with some funding coming from California Environmental Quality Act filers and commercial fishers. However, some have raised the argument that the department's work serves a statewide purpose and the public good, which should merit the consideration of some of these alternative proposals.

Department of Toxic Substances Control—Reform Progress

BACKGROUND

The Department of Toxic Substances Control (DTSC) is charged with protecting the people of California and the environment from the harmful effects of toxic substances by restoring contaminated resources, enforcing hazardous waste laws, reducing hazardous waste generation, and encouraging the manufacture of chemically-safer products. In addition to administration, the budget includes the following five programs for DTSC:

1. **Site Mitigation and Brownfields Reuse –** The program implements the state's laws regarding site cleanup and the federal Superfund program. The program currently oversees approximately 1,170 hazardous substance release site investigations and cleanups, and monitors long-term operations and maintenance activities at more than 470 sites where the cleanup process is complete. Additionally, the program is responsible for ensuring compliance with the terms of approximately 820 land-use restrictions in place on properties throughout the state.

2. **Hazardous Waste Management –** The program regulates the generation, storage, transportation, treatment, and disposal of hazardous waste to minimize risks to public health and the environment. The program oversees permitting and compliance at approximately 120 facilities that manage hazardous waste, approximately 900 registered businesses that transport hazardous waste, and approximately 300 facilities/generators that are subject to corrective actions.

3. **Safer Consumer Products –** The Safe Consumer Products (SCP) program strives to get manufacturers to reduce human and environmental exposure to toxic chemicals. SCP calls for industry to develop safer consumer products and use pollution prevention best practices. The program implements the SCP regulations. SCP also collects information on the presence of toxic chemicals in products in order to identify priority products for possible regulation; provides support and guidance to priority product manufacturers for the analysis of safer alternatives; and issues regulatory responses to proposed alternatives. Lastly, the program encourages the adoption of "green chemistry" practices.

4. **State as Certified Unified Program Agency –** The California Environmental Protection Agency designated the Department of Toxic Substances Control as the Certified Unified Program Agency (CUPA) in Trinity and Imperial Counties. As the CUPA, the department is responsible for implementing the six elements of the unified program: hazardous waste generator and onsite treatment activities; spill prevention control and countermeasure plans for owners of above-ground petroleum storage tanks; underground storage tank program; hazardous material release response plans and inventories; California Accidental Release Prevention program; and certain Uniform Fire Code.

5. **Exide Technologies Facility Contamination Clean Up Program** – The program oversees the removal and remedial actions in the communities surrounding the Exide Technologies facility in the City of Vernon.

The Governor's budget proposes $285.9 million and 923.3 positions for DTSC in 2017-18. The following table outlines Governor's budget resources by program and fiscal year:

DTSC - 2017-18 Governor's Budget **Dollars in Thousands**						
	Positions			**Expenditures**		
Program	**2015-16**	**2016-17**	**2017-18**	**2015-16**	**2016-17**	**2017-18**
Site Mitigation Brownfield Reuse	286.7	280.2	285.2	$130,007	$135,187	$123,776
Hazardous Waste Management	371.2	389.2	389.7	80,599	83,720	78,659
Safer Consumer Products	61.0	61.8	61.8	14,960	15,611	13,417
Certified Unified Program Agency	9.3	9.7	9.7	2,876	2,781	2,784
Exide Cleanup	-	-	-	4,790	24,393	67,191
Administration	174.9	176.9	176.9	33,964	34,580	34,477
Distributed Administration	-	-	-	-33,964	-34,580	-34,477
Total	**903.1**	**917.8**	**923.3**	**$233,232**	**$261,692**	**$285,827**

DTSC is funded from multiple sources, including; the General Fund, special funds, and federal funds. Following are some of the departments more significant funding sources as outlined in the Governor's budget:

DTSC – Significant Funding Sources **Dollars in Thousands**			
Funding Source	**2015-16**	**2016-17**	**2017-18**
General Fund	$27,379	$44,090	$32,087
Toxic Substances Control Account	70,441	81,970	121,426
Hazardous Waste Control Account	63,512	65,892	62,302
Federal Funds	32,499	33,414	33,144
Reimbursements	13,075	13,525	13,531
Site Remediation Account	11,047	9,626	6,626
Removal and Remedial Action Account	3,346	3,185	3,185

Legislative Oversight. Over the last five years, the Legislature has conducted numerous hearings on DTSC's internal controls, business practices, and statutory obligations. In those hearings, the budget and policy committees have evaluated four main areas: 1) reviewing and monitoring the department's strategic plan and reorganization; 2) auditing cost recovery; 3) providing staffing to improve the ability to address permit backlogs and business operations; and, 4) improving enforcement at the department.

This effort has been spurred by incidents across California that have exposed glaring issues in DTSC's operations. In particular, issues with hazardous waste facility permitting and enforcement at the Exide and Quemetco battery recycling facilities; shortcomings in cost-recovery efforts for cleanups leading to an accumulation of 1,661 projects totaling approximately $194 million in uncollected cleanup costs; a growing backlog of applications to renew hazardous waste permits; delayed site remediation; lack of public participation and transparency activities; and personnel issues, have all contributed to the need for increased scrutiny by the Legislature.

Permitting. DTSC issues hazardous waste facility permits to facilities that manage waste that is toxic, corrosive, reactive, and ignitable. When DTSC issues hazardous waste facility permits it establishes conditions that the facility must meet, in addition to the applicable laws and regulations for the management of public waste. There are 119 facilities permitted to manage hazardous waste in California (91 operating facilities and 28 post closure facilities) with a total of 132 permits. Facility permits are issued for 10-year terms and facilities are required to apply for renewal six months prior to a permit's expiration. If the permit renewal application is submitted on time, the facility may continue to operate under an expired permit, known as a "continued" permit until the final application is approved. As well as permit renewal applications, DTSC makes decisions on applications for new permits and permit modifications. The DTSC's goal is to make decisions on 90 percent of permit applications within an average of two years. Towards achieving this goal, DTSC developed and is implementing the permitting enhancement work plan to create and update processes, guidance, and tools to support consistent processing of permit applications and more-timely permit decisions.

Legislative Analyst's Office (LAO) Analyses of DTSC. In 2016, the LAO concluded that, based on their projections and DTSC's projections, the department will continue to have an ongoing backlog of permit applications. "The department projects it would need to make decisions on an average of 16 permit applications per year—instead of its estimated average of eight per year—in order to make timely decisions on renewals and process new and modified permits. Our own projections confirm that DTSC would need to roughly double the average number of decisions it makes per year, from 8 to 16, to address the existing backlog and move towards attaining its goal of making decisions on 90 percent of permit applications within an average of two years." Subsequent to the LAO's analysis, and, as part of the 2016-17 budget plan, the department was provided resources to accomplish this goal (summarized below in the DTSC – Program Investments table).

Independent Review Panel. The Independent Review Panel (IRP) was established within the DTSC pursuant to SB 83 (Committee on Budget and Fiscal Review), Chapter 24, Statutes of 2015. The IRP is comprised of three members: an appointee of the Assembly Speaker with scientific experience related to toxic materials; an appointee of the Senate Committee on Rules who is a community representative; and an appointee of the Governor who is a local government management expert. The current IRP members are: Dr. Arezoo Campbell (scientist with experience related to toxic materials), Gideon Kracov, JD (community representative), and Mike Vizzier (local government management expert). The panel members are tasked with reviewing and making recommendations regarding improvements to DTSC's permitting, enforcement, public outreach, and fiscal management. The IRP also may make recommendations for other DTSC programs, may advise DTSC on its reporting obligations, and is required to advise DTSC on compliance with the mandate to institute quality government programs to achieve increased levels of environmental protection and public satisfaction.

On January 20, 2017, the IRP issued its fifth quarterly report in compliance with SB 83, which required the panel to report to the Governor and Legislature 90 days after it was appointed and every 90 days thereafter on DTSC's progress in reducing permitting and enforcement backlogs, improving public outreach, and improving fiscal management. The fifth report is devoted to recommendations for improving fiscal management.

In the report, the IRP concludes that DTSC's fiscal resources are more appropriate for its responsibilities than they were in the recent past, although the looming cost of Superfund, national priority list sites, and Orphan, contaminated sites with no responsible party, sites will require evaluation of the Site Remediation Account. The IRP also found that the department has a much better mastery of its cost recovery backlog than it did a few years ago and has put in place a strong foundation for the future. Nevertheless, further work must be done to put in place a suitable billing system and make it more transparent for responsible parties. In addition, the state must remain vigilant to ensure that cost recovery deficiencies do not occur again.

There are two recommendations for the Governor and Legislature in the IRP's report: 1) consider whether to amend Health and Safety Code (HSC) Section 25269.5 to establish deadlines for the meet and confer process, including the preparation of cost estimates for the next phase of the site remediation activity and a procedure for the resolution of cost estimate disputes; and 2) fund the five redirected administrative project manager positions and the redirected staff services manager position that are currently devoted to performing the administrative duties that were tasked to the technical project managers prior to the 2014-15 fiscal year.

The IRP's report noted that in recent years the Legislature had made significant investments in DTSC's programs. These investments were made in response to Legislative oversight hearings and public concerns about the management of the department. The table below displays investments made in the last two budgets:

DTSC – Program Investments		
	Description	**Budget**
Enforcement Division Enhancement	$1.6 million from the Hazardous Waste Control Account (HWCA) and 16 positions to address the increased workloads for the Enforcement Division, Policy and Program Support Division's Financial Responsibility Unit, Office of Planning and Environmental Analysis, Office of Legal Counsel, and Office of Environmental Information Management in support of the Office of Permitting's initiative to reduce DTSC's inventory of backlogged hazardous waste facility permit applications and streamline and enhance protections in the enforcement and permitting processes.	2015
Community Protection and Hazardous Waste Reduction Initiative	$840,000 from the Toxic Substances Control Account and six positions for two years, to develop, implement, and evaluate projects that reduce the generation of hazardous wastes that are treated or disposed in California. This Community Protection and Hazardous Waste Reduction Initiative is intended to reduce hazardous wastes that are generated in significant quantities in California, can pose substantial risks or hazards to human health or the environment, and are treated or disposed in California communities that are disproportionately burdened by multiple sources of pollution.	2015
Hazardous Waste Management Permitting Support	$1.2 million from the HWCA to make permanent eight, limited-term, positions that were set to expire. These positions were previously provided to address a hazardous waste permit renewal backlog, as well as to update cost estimates associated with closing hazardous waste facilities.	2016
Enhanced Permitting Capacity and Support	$2.4 million from the HWCA, and 15 positions within the permitting division, to fully implement process improvements under the permit enhancement work plan. The funding is intended to sustain timely permitting actions, mitigate the incidence of facilities operating for extended periods of time on expired permits, and improve enforcement.	2016

The 2016 budget did not include two additional positions proposed by the Senate, with limited-term funding, to allow for more continuity of staffing for the IRP; and did not include budget bill language requiring the department to provide IRP access to state facilities and workers in order to provide a more robust review of the department.

State Auditor. In August of 2014, the State Auditor released its results of an audit that focused on DTSC's cost recovery efforts. The Auditor's findings included:

- Long-standing shortcomings with the department's recovery of costs have resulted in unbilled, and billed but uncollected, cleanup costs (outstanding costs); as of March 2014 the department had 1,661 projects totaling almost $194 million in outstanding costs.
- Nearly $142 million was unbilled and almost $52 million was billed but uncollected. These outstanding costs were incurred between July 1987 and December 2013.
- The department has made progress in resolving the accuracy of information related to projects with outstanding costs.
- The department may not be able to recover all of its outstanding costs due to several factors—preliminary determinations indicated that the federal and state statutes of limitations have expired for 76 projects with a total of $13.4 million in outstanding costs.
- Despite updating its cost recovery procedures, the auditor found several areas in which the department could better maximize its cost recovery efforts.
- The department has not consistently used some of its methods, such as issuing collection letters or recording liens on the properties of responsible parties to ensure that it maximizes cost recovery.

It's worth noting that the IRP's latest progress report reviews DTSC's cost recovery efforts (the department's record of recovering its cleanup and oversight costs [response costs] from responsible parties), which they cited as, by far, the biggest fiscal management issue during the past few years. DTSC is authorized and required by HSC Section 25360 to recover its response costs.

The IRP believes that DTSC has a much better control of its cost recovery backlog than it did a few years ago and that it has put in place a strong foundation for the future. The IRP found that DTSC's staff members made cost recovery a focus after receiving a "wake-up call" and considerable attention from the Legislature as well as the department's executive leadership. However, it also found that further work must be done to put in place a requisite billing system and make it more transparent for responsible parties. In addition, the state must remain vigilant to ensure this problem does not occur again.

GOVERNOR'S PROPOSAL

The Governor's budget includes the following proposals for DTSC:

Stringfellow Superfund Removal and Remediation Action - $2.5 million General Fund in 2017-18 ($3.0 million in 2018-19 and $2.6 million in 2019-20) to collect environmental data to support the selection of a final remedy for the site.

Lead-Acid Battery Recycling Act Implementation - $610,000 from the Lead-acid Battery Cleanup Fund and five positions to implement AB 2153 (Garcia), Chapter 666, Statues of 2016.

The act requires DTSC to identify, investigate, and clean up areas reasonably suspected to have been contaminated by operation of lead-acid battery recycling facilities.

ISSUES TO CONSIDER

Independent Review Panel Recommendations and Concerns. As noted above, in its fifth progress report, the IRP has two recommendations for the Legislature and Governor related to the budget and fiscal management:

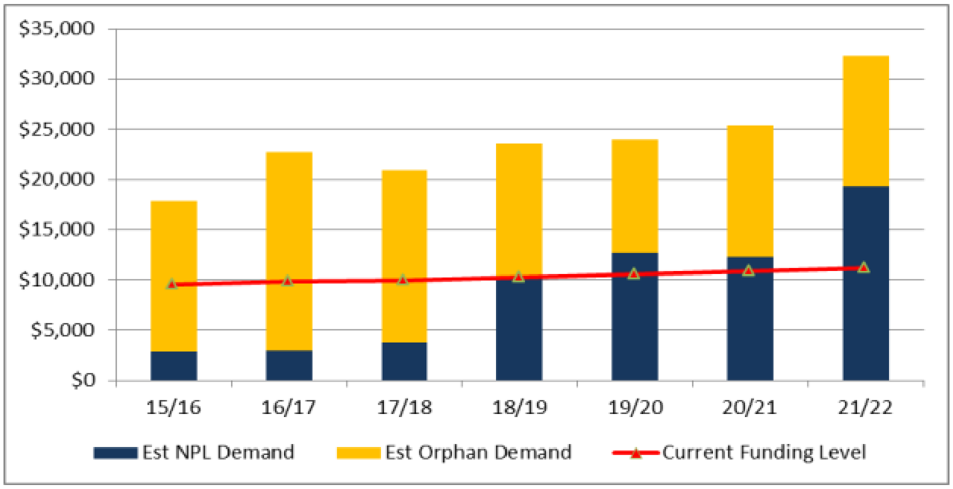
1. Consider whether to amend HSC Section 25269.5 to establish deadlines for the meet and confer process, including the preparation of cost estimates for the next phase of the site remediation activity and a procedure for the resolution of cost estimate disputes.

2. Fund the five redirected administrative project manager positions and the redirected staff services manager position that are currently devoted to performing the administrative duties that were tasked to the technical project managers prior to 2014-15.

The second recommendation is related to positions that were originally created as part of a pilot program, related to enhancing cost recovery efforts, on a limited-term basis to focus on billing and other administrative tasks associated with site cleanup. Because the program was successful, DTSC redirected positions internally to perform these tasks once the limited-term positions expired at the end of the 2015-16 fiscal year.

In addition, the IRP's initial recommendations, submitted on January 28, 2016, expressed a concern about projected shortfalls in the Site Remediation Account (SRA). The SRA is used for remediation on both Superfund and Orphan sites. California must pay 10 percent of the construction-phase cleanup costs on Superfund sites and 100 percent of the costs after the transition from the construction phase to on-going operations and maintenance on those sites. According to the IRPs latest progress report, beginning in 2018-19, the number of Superfund sites transitioning to operations and maintenance is expected to increase substantially (table below). Superfund demand is expected to exceed the 2016-17 SRA appropriation, which is $10.5 million. Unless the SRA is increased, little or no funding would be available for Orphan sites beginning in 2018-19.

National Priority List/Orphan Demand*
($ in thousands)



Department of Toxic Substances Control
*Excludes legacy landfills

The IRP notes that AB 2891 (Committee on Environmental Safety and Toxic Materials), Chapter 704, Statutes of 2016, partially addressed this issue by expressing the intent that funds deposited in the account be appropriated each year to the SRA in an amount that is sufficient to pay for estimated costs for direct site remediation at both Superfund and Orphan sites.

Structural Deficit in the Hazardous Waste Control Account. As noted above, the HWCA is one of DTSC's primary sources of funding and supports the Hazardous Waste Management program, which is responsible for permitting and monitoring hazardous waste facilities. In recent years, the HWCA has had an operating deficit, caused by many factors, including an inadequate fee structure. According to the Governor's Budget, the HWCA is projected to average a structural deficit of $10.4 million from 2015-16 through 2017-18 (excluding a $13 million loan repayment from the General Fund in 2015-16), reducing the fund balance from $29.9 million at the end of 2015-16 to $7.7 million at the end of 2017-18. SB 839 (Committee on Budget and Fiscal Review), Chapter 340, Statutes of 2016, eliminated the option of paying a flat fee for a permit application, which should help address the problem. However, it is likely not a comprehensive solution and additional action may be necessary.

Is there a Role for a Long-Term Advisory Panel or Board? To date, the IRP has released seven reports (five progress and two annual reports) and conducted 16 public meetings. In a short period of time, the IRP has demonstrated value in being an important component in ensuring vital issues are being adequately addressed within DTSC. However, the IRP is only authorized until January 1, 2018. Given that key issues remain to be fully addressed or require further monitoring, the Legislature may wish to consider extending or making permanent the IRP. Establishing a board is another alternative that has been raised in the past; including at last spring's budget subcommittee hearing regarding DTSC. Besides providing additional oversight and accountability functions, both options would provide for greater transparency and public input, which remain ongoing concerns.

California LifeLine Program

BACKGROUND

The Moore Universal Telephone Service Act of 1984 set the goal of providing high quality telephone service at affordable rates to eligible low-income households. The act requires the California Public Utilities Commission (CPUC) to annually designate a class of lifeline service necessary to meet minimum residential communications needs, develop eligibility criteria (currently 150 percent of the federal poverty level or participation in a variety of existing public assistance programs), and set rates for services, which are required to be not more than 50 percent of the rate for basic telephone service. Over the years, the definition of a "basic service," that originally included only traditional wireline (landline) service, has been considered in the broader context of new technologies and trends towards voice, video, and data services.

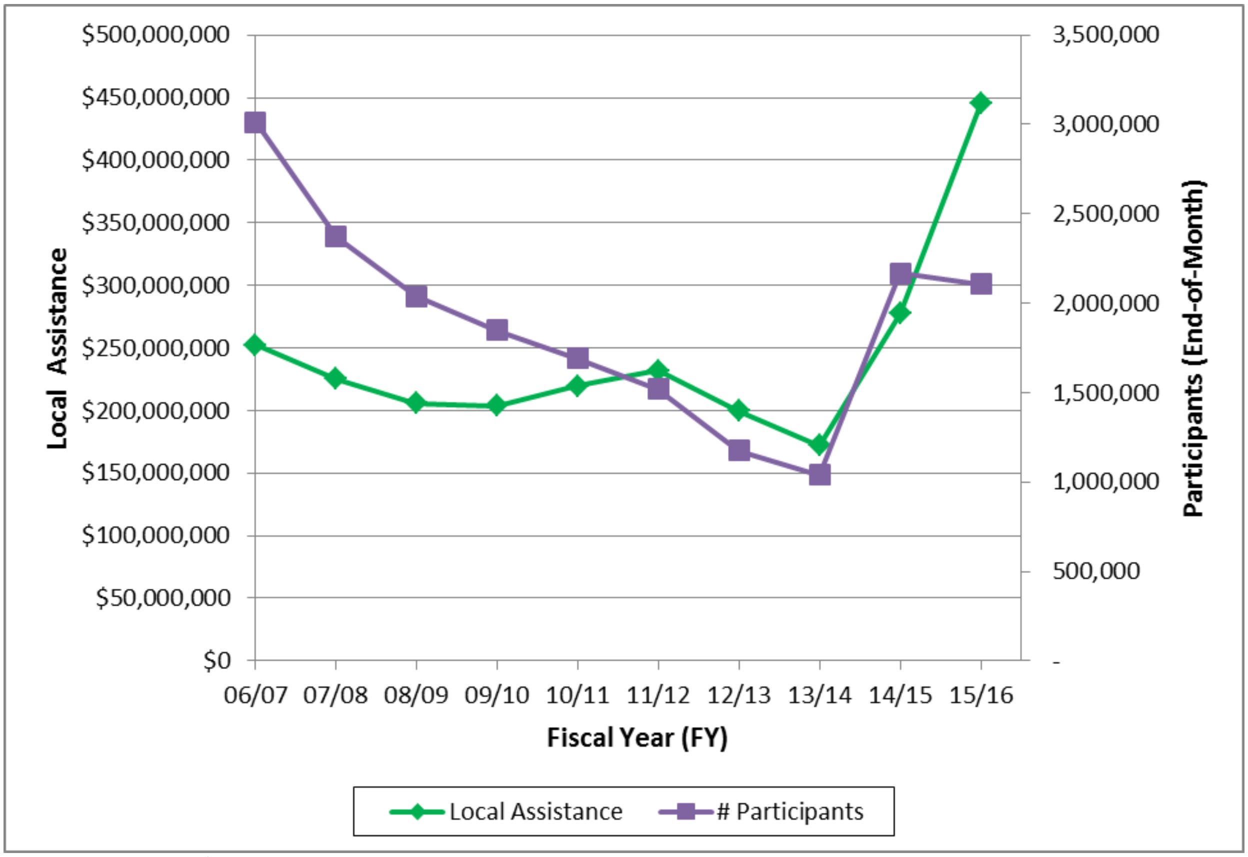
The federal government and the state of California operate separate LifeLine programs. Under federal and state LifeLine program rules, multiple participants are permitted at a single residence if the participants are separate households. A household includes adults and children who are living together at the same address as one economic unit. An economic unit consists of all adults (persons at least 18 years old, unless emancipated) contributing to and sharing the household's income and expenses. Only one LifeLine program discount is provided per household.

For each household enrolled in the program, CPUC provides telephone companies (carriers) a maximum monthly state subsidy that is based on 55 percent of the most expensive basic landline service from the four largest telecommunications carriers. The subsidy is meant to offset the lower rate charged to the consumer. In 2017, the maximum state subsidy is currently about $14 a month. The federal Lifeline program provides an additional monthly discount of about $9. In addition, the state provides: (1) a per enrollee monthly payment to cover carriers' administrative costs; (2) a one-time connection subsidy for new enrollees or enrollees that switch plans; and (3) a subsidy to cover other telephone taxes and surcharges for LifeLine enrollees.

The program is funded by a surcharge assessed against intrastate charges on end-users of all telephone corporations and connected Voice over Internet Protocol (VOIP) service providers in California. These charges provide a revenue base for the program of roughly 11 billion in 2017-18. CPUC periodically reviews the surcharge rate and may change it to balance program cost and cash flow against the financial burden the program imposes on ratepayers. The surcharge rate has increased steadily since 2012-13, and is currently 4.75 percent. This is a decline from the 2015 rate of 5.5 percent, but is significantly higher than the historic rate of 1.15 percent.

Program Participation Dramatically Increased Since Expansion to Wireless Service. In January, 2014, the CPUC issued a decision authorizing voluntary participation in the program by wireless service providers offering discounted wireless service plans to low-income households, if they include wireless voice, text, and data services. Since this change, there has been substantial growth in the program and the number of subscribers doubled from fiscal year 2013-14 to 2014-15, with all of the growth in the number of wireless subscribers (offset by a reduction in the number of wireline subscribers). This increase in program participation has combined with several recent increases in the LifeLine subsidy (which is paid out in Local Assistance expenditures) to increase program costs. The chart below highlights this relationship.

Changes in LifeLine Program Participation and Cost Since 2006-07



Source: California Public Utilities Commission

Wireless Plans Are Diverse, but Many Plans Are Free to Enrollees. A diverse set of wireless plans are available for LifeLine customers. Although all plans currently include at least 1,000 monthly voice minutes, plans offer different monthly rates, additional voice minutes, text messaging, and data. As of January 2017, there were 13 LifeLine wireless providers, offering 49 plans. Of these, 32 are offered at no cost to the consumer, including:

- 27 plans with unlimited voice minutes.
- 26 plans with unlimited text messages.
- One plan with unlimited data.

Ensuring Eligibility and Minimizing Fraud. Prior to 2007, participants self-certified their eligibility and carriers enrolled participants. The very high participation rate in 2006 triggered the CPUC and Federal Communications Commission to require a third-party administrator (TPA) to determine eligibility and manage the consumer participation in the program. Shortly after the introduction of a TPA, participation decreased sharply in 2007 and 2008. Today, participants establish eligibility either through evidence of participation in other federal public assistance programs (for example, CalFresh, Medicare, Section 8 housing, etc.) or by submitting evidence of income. Applications are required to determine both initial eligibility and annual renewals; however program eligibility does not require an annual verification of income eligibility. Applicants provide supporting documentation and information under penalty of perjury.

As a result of the automated anti-fraud mechanisms, applications are identified and rejected if they are determined to be duplicative. These potential participants never receive discounts. Between June 2015 and December 2016, CPUC de-enrolled or denied 4,965 pending or active LifeLine accounts (0.23 percent of the 2.16 million total LifeLine participants) for fraudulent behavior. Very few of these participants have appealed.

In addition to the automated, upfront fraud checks performed by the TPA, periodic detailed queries are conducted to detect and eliminate fraudulent behavior. As an example, the TPA and CPUC collaborate on an annual manual fraud analysis. Participants with duplicative information (some variant of shared social security numbers, date of birth, name, or address) are grouped into four-tiers. A detailed manual comparison of all information submitted by consumers, including qualifying program documentation, is used along with results of identity verification to detect fraud. This process takes about three to four months to complete. The program removes activity determined to be fraudulent immediately. In addition, potential duplicates that are identified are removed. Participants identified either as fraudulent or duplicative are provided with an opportunity to appeal.

GOVERNOR'S PROPOSAL

Caseload Adjustment and Program Participation
The budget requests an augmentation of roughly $151 million ($147 million for Local Assistance, $4 million for State Operations) for the LifeLine program in 2017-18. The Administration has indicated that this is primarily due to increased participation and a projected increase in the LifeLine subsidy level. Specifically, the PUC estimates that LifeLine subscriptions will increase from roughly three million to 3.2 million, with the subsidy projected to increase from $13.75 to $14.30 in the second half of the year. The Administration plans to leave the LifeLine surcharge rate unchanged at 4.75 percent.

ISSUES TO CONSIDER

CPUC Has Broad Authority to Modify the Program. The LifeLine program is intended to help ensure low-income households have access to affordable basic telephone services. To achieve this goal, state law gives CPUC broad authority to establish the major characteristics of the program. The commission's decision to include wireless service appears to be consistent with legislative direction and goals given the rapid pace of technological change in the telecommunications industry. However, there are inherent trade-offs in the way CPUC has developed the program. These decisions affect the overall level of service provided, the discounts available to wireless LifeLine customers, and the overall costs of the program paid by non-LifeLine telephone customers. CPUC continues to evaluate the structure of the program, including developing standards for assessing affordability and analyzing whether current discounts align with program goals. The Legislature may want to consider whether the program, as it currently exists, continues to meet the Legislature's intent, or if CPUC should be given more guidance on future program changes.

Revenue Base for the Program Has Declined. Even as the program has grown, the revenue base used to fund the program has declined significantly, from $17.7 billion in 2010-11 to $11 billion in 2017-18. This decline in the billing base has resulted in increases in the program surcharge to ensure adequate funding for the LifeLine program. This decline in the billing base is related to a number of factors, including a decline in the number of landlines, reductions in the cost of telephone and VOIP service, and a decline in the number of toll calls within the state. CPUC anticipates that the revenue base will be flat or continue to decline slightly in the coming years. This suggests that higher surcharge rates are here to stay.

The program can provide substantial benefits to low-income households enrolled in the program; however, program changes have also contributed to a substantial increase in the surcharges paid by non-LifeLine customers. As such, the Legislature may want to assess the degree to which the current structure of the program correctly balances the benefit provided to subscribers with the financial burden borne by ratepayers.

Enrollment Estimates Subject to Substantial Uncertainty. The relatively recent addition of wireless service to the LifeLine program creates uncertainty about future enrollment and expenditures. For example, the Administration's 2017-18 enrollment projections were based on the following key assumptions: (1) about 4.2 million households are eligible for the program and (2) 77 percent of the eligible households will enroll in the program by the end of 2017-18. There is significant uncertainty about both of these assumptions. Specifically, it's unclear how many eligible households will ultimately enroll in the program by the end of the budget year, or how many will renew their subscriptions on an annual basis. These factors generate considerable uncertainty in LifeLine estimates, and have resulted in frequent updates to program estimates and costs. For example, in 2016-17 the Administration originally requested an increase of $267 million in local assistance for the program, before reducing that request by $142 million in the 2016-17 May Revision following updated enrollment information. The 2017-18 request includes an increase of $22 million in 2016-17 to cover increased enrollment, as well as an additional $147 million increase in local assistance for 2017-18. This underscores the uncertainty in forecasting program costs. As such, the Legislature may want to consider withholding action on the Governor's proposal until updated caseload information is available in May, and formalizing guidance for CPUC to produce LifeLine caseload estimates in future proposals.

Transportation Funding

BACKGROUND

Overview of Transportation Funding in California

The California state highway system includes 50,000 lane-miles of pavement, approximately 13,000 bridges, 205,000 culverts and drainage facilities, 87 roadside rest areas, and 29,183 acres of roadside landscaping. In addition, California's 58 counties and 480 cities are responsible for 304,000 miles of local streets and roads, as well as numerous local bridges. Approximately 180 public agencies provide public transit, such as intercity bus and passenger rail, resulting in about 1.3 billion passenger trips each year. The programs described in this section relate to state highways, local roads, and mass transit, and include the Department of Transportation (Caltrans) and the California Transportation Commission (CTC).

These areas of transportation are funded from local, state, and federal sources as shown in the figure below. In addition, the California Highway Patrol (CHP), the Department of Motor Vehicles (DMV), as well as various programs within the Air Resources Board (ARB), are funded with revenues from vehicle registration and driver licenses' fees. High-speed rail funding is excluded here.

California Transportation Funding
Major Sources

Funding Source	Comments
Local Revenues	Locally-imposed revenues such as add-on sales tax, property tax, developer fees, and transit fares. Some funds used to reimburse Caltrans for locally-supported work on the highway system.
Federal Revenues	Primarily federal gas tax revenue (18.4 cents/gallon). Includes funds for highways and transit.
Motor vehicle fuel taxes	Allocated to the state and local governments. In 2017-18, the state gasoline tax is expected to be 29.7 cents and the diesel excise tax 16.3 cents.
Fees on cars and drivers	Primarily from vehicle registration and driver licenses. Supports the operations of the DMV, CHP, and ARB.
Truck weight fees	Revenue pays for debt service on transportation-related general obligation bonds.
Cap-and-trade	Supports transit operations and capital projects, and active transportation.
Diesel sales tax	Primarily supports local transit operators.
GO bonds	State general obligation bonds, primarily from Proposition 1B.

Special Session on Transportation Funding

The Legislature convened in 2015 a special session on transportation funding to address the funding shortfall for maintaining the current system of state highways, transit, and local streets and roads. For example, the State Highway Operation and Protection Program (SHOPP), which funds highway maintenance and repairs, has an annual funding shortfall of about $6 billion. Various options to increase state funding and achieve efficiencies at Caltrans were proposed during the Special Session by both the Legislature and the Administration. Generally, the total amount of funding the proposed plans would generate each year (for a variety of transportation purposes) varied from the low billions to up to $7 billion. The special session ended without the passage of a funding package.

Options to Increase the Accountability and Efficiency of Caltrans

In addition to increasing funding for transportation infrastructure, many of the options considered during the special session would increase the accountability of Caltrans' work and allow for other efficiencies. Over time, increasing the accountability and efficiency of Caltrans has the potential to decrease the amount of funds that are potentially mismanaged, reduce cost-over runs, and reduce total project costs. The savings from implementing such activities would be less in dollar terms than the funding proposals described earlier. However, improving the department's performance, and better ensuring that the limited funding available for transportation is put to the best use, should also be a priority.

The CTC included several recommendations for improving transparency, accountability, and efficiency in transportation spending in its 2015 and 2016 annual reports. These include:

- Require the State Highway Performance Plan to include measurable targets for improving the state system, and require Caltrans to provide regular reports on its progress to the California State Transportation Agency and the CTC. Give the CTC the responsibility to allocate both project development and delivery costs for Caltrans projects.

- Allow direct contracting between Caltrans and federally-recognized Native American tribes in California for transportation program purposes.

- Provide flexibility for Caltrans to contract for more engineering and right-of-way workload. Permit Caltrans to prequalify consultants by type of work and draw from a list of those consultants as work becomes available. Authorize Caltrans and its partners to use alternative procurement methods permanently and without limits.

- Expand the use of "advance mitigation" and other expedited environmental review processes to streamline the environmental planning and compliance portion of transportation project development.

- Require Caltrans to implement efficiency measures with the goal of generating $100 million per year in savings to invest in maintenance and rehabilitation of the state highway system.

GOVERNOR'S PROPOSAL

Transportation Funding and Reform Package

The budget incorporates a transportation funding package similar to the one the Governor proposed during the transportation special session. The budget proposes to provide new funding of $1.9 billion in 2017-18, and $4.3 billion on an annual ongoing basis. The annual funding package provides $2.1 billion from a new $65 fee on all vehicles; $1.1 billion by setting the gasoline excise tax at 21.5 cents (with future adjustments for inflation); $425 million from an 11-cent increase in the diesel excise tax; $500 million in additional cap-and-trade proceeds; and $100 million from cost-saving reforms to be implemented by Caltrans as shown in the figure below. The $1.9 billion of additional funding in 2016-17 includes $235 million from the acceleration of General Fund loan repayments over the next three years ($706 million in total repayments), rather than repaying these loans over the next 20 years.

Governor's Budget Transportation Funding and Reform Package

Funding Source	Annual Amount	Comments
Road improvement charge	$2.1 billion	A new $65 fee on all vehicles that equally funds state and local transportation priorities.
Gasoline excise tax	$1.1 billion	Sets the gasoline excise tax at the historical average of 21.5 cents beginning in 2018-19 and going forwards adjusts annually for inflation.
Diesel Excise tax increase	$425 million	Increases the diesel excise tax by 11 cents beginning in 2018-19 and going forwards adjusts annually for inflation.
Cap-and-trade	$500 million	Provides additional funding for the Active Transportation Program ($100 million) and transit capital improvements ($400 million).
Caltrans efficiencies	$100 million	Implements cost-savings reforms.

The 2017-18 proposals for spending the increased funding are:

- **Local Streets and Roads.** The increased funding will provide $206 million to cities and counties for local road maintenance.

- **Active Transportation Program.** The budget provides $100 million cap-and-trade revenues for the Active Transportation Program which funds projects encouraging active transportation such as bicycling and walking, with at least 50 percent of the funds going to disadvantaged communities.

- **Transit and Intercity Rail Capital.** The budget provides $400 million from cap-and-trade revenues for transit capital investments that provide greenhouse gas reductions, with at least 50 percent of the funds going to disadvantaged communities.

- **Highway Maintenance and Repair.** The budget provides an increase of $351 million ($42 million from loan repayments) for repairs and maintenance on the state highway system.

- **Trade Corridor Improvements.** The budget provides an increase of $358 million ($108 million from loan repayments) for Caltrans to fund projects along the state's major trade corridors.

- **Corridor Mobility Program.** The budget provides $300 million for the Corridor Mobility Program, including $25 million for local planning grants, to focus on multi-modal investments in key congested commute corridors that demonstrate best practices for public transit and managed highway lanes, such as priced express or high occupancy vehicle lanes.

- **Reforms and Efficiencies.** The budget proposes to improve Caltrans' performance by establishing measurable targets for improvement. It also proposes to streamline project delivery by making various changes that include advancing project environmental mitigation, implementing more innovative procurement, allowing Caltrans to deliver projects funded with new revenues by doubling contract staff over the next five years, and extending the sunset date for public-private partnerships through 2027.

ISSUES TO CONSIDER

The current level of funding is inadequate to maintain the state's transportation system and it is important for the Legislature to address this. The Legislature may want to consider several issues as they review the funding package proposed in the budget:

- **Amount of Funding.** According to the Governor's budget, the cost of deferred maintenance for the state highway system is $59 billion and the annual funding shortfall for maintenance and repair of these roads is $6 billion. The proposed transportation funding package, however, only provides $4.3 billion per year. Given the scale of the problem, and the state's fiscal outlook, the Legislature may want to consider what an appropriate level of funding for transportation projects would be.

- **Use of Funding.** The proposed transportation package provides $4.3 billion per year, spread across highways, public transit, local streets and roads, and active transportation such as biking and walking. However, as stated above, the annual funding shortfall for highways alone is nearly $6 billion. Given this shortfall, the Legislature may want to consider options for prioritizing spending in various transportation categories to ensure that the limited funding available is directed at the highest priority projects.

- **Source of Funding.** The gas tax is the traditional funding source for transportation infrastructure because it follows the "user pays" principle by tying the use of a public good with the cost of maintaining it – the more miles driven, the more gas burned and the more gas tax paid. The gas tax has remained the primary funding source for transportation projects, even as gas mileage has risen and inflation has reduced the value of the collected tax. Any effort to raise additional revenue for transportation will likely include increasing existing taxes and fees or the creation of additional taxes and fees. Obtaining the votes necessary to pass such a package may be challenging. The Legislature may want to consider other options for raising revenues, such as raising fees, though such fees may not follow the “user pays” principle as closely as the existing fuel tax.

SUBCOMMITTEE NO. 3

HEALTH and HUMAN SERVICES

Health[1]

Human Services

[1] Health sections researched and written by Kim Flores, Policy Consultant, Senate Office of Research.

Medi-Cal: Coordinated Care Initiative

BACKGROUND

The Department of Health Care Services (DHCS) administers the Medi-Cal program (California's Medicaid health care program). This program pays for a variety of medical services for children and adults with limited income and resources. Medi-Cal offers free or low-cost health coverage for California residents who meet eligibility requirements. Most applicants who apply to and enroll in Medi-Cal will receive care through managed health plans. Medi-Cal has always covered low-income seniors, persons with disabilities, children, pregnant women and families. In January 2014, California expanded Medi-Cal eligibility to include childless low-income adults.

The Governor proposes total expenditures of $97.8 billion ($18.1 billion General Fund) for 2017-18, not including administrative costs. This is a 2.5 percent decrease in General Fund spending from the prior year. It is projected that Medi-Cal will serve about 14.3 million Medi-Cal eligible individuals (about 5.7 million children), an increase in caseload of about 1.8 percent, primarily due to the implementation of federal health care reform under the Affordable Care Act (ACA). It is estimated that over a third of the state's total population will be enrolled in Medi-Cal.

Coordinated Care Initiative Background. The 2012 budget authorized the Coordinated Care Initiative[1] (CCI), which expanded the number of Medi-Cal enrollees who must enroll in Medi-Cal managed care to receive their benefits. Under the current memorandum of understanding with federal Centers for Medicare and Medicaid Services (CMS), the Cal Medi-Connect (CMC) part of CCI (described below) ends on December 31, 2017; however, based on interest expressed by the director of the Medicare-Medicaid Coordination Office at CMS, CMC may be extended through 2019. This office may be affected by any changes in the Affordable Care Act, as discussed in the section *Health – Affordable Care Act.* The CCI is being implemented in seven counties[2] (Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Mateo, and Santa Clara).

CCI is composed of three major parts related to Medi-Cal:

- **Managed Long-Term Supports and Services (MLTSS) as a Medi-Cal Managed Care Benefit.** CCI was initially proposed to include all of MLTSS into Medi-Cal managed care, including nursing facility care (NF), In-Home Supportive Services (IHSS), Multipurpose Senior Services Program (MSSP), and Community-Based Adult Services (CBAS). This

[1] Enacted in July 2012 through SB 1008 (Committee on Budget and Fiscal Review), Chapter 33, Statutes of 2012, and SB 1036 (Committee on Budget and Fiscal Review), Chapter 45, Statutes of 2012, and amended by SB 94 (Committee on Budget and Fiscal Review), Chapter 37, Statutes of 2013.

[2] Alameda County was initially to be part of CCI but due to fiscal solvency issues with one of its plans, it is not participating in CCI.

approach was estimated to have an impact on about 600,000 Medi-Cal-only enrollees and up to 456,000 persons eligible for both Medicare and Medi-Cal who are eligible for CMC; however, MSSP is still operated under a specific waiver authority that allows only a certain level of slots and has specific payment methods, and thus the planned enrollment level has not been reached.

- **Cal MediConnect Program.** CMC is a three-year demonstration project for persons eligible for both Medicare and Medi-Cal (dual eligibles) to receive coordinated medical, behavioral health, long-term institutional, and home-and community-based services through a single organized delivery system (health plan). As noted above, no more than 456,000 beneficiaries would be eligible for the duals demonstration in the eight counties. CMC is a joint demonstration project with CMS.

- **Mandatory Enrollment of Dual Eligibles and Others into Medi-Cal Managed Care.** Most Medi-Cal beneficiaries, including dual eligibles, partial dual eligibles, and previously excluded seniors and persons with disabilities who are Medi-Cal only, are required to join a Medi-Cal managed care health plan to receive their Medi-Cal benefits.

The purpose and goal of CCI is to promote the coordination of health, behavioral health, and social care for Medi-Cal consumers and to create fiscal incentives for health plans to make decisions that keep their members healthy and out of institutions. The objective is that such incentives will reduce costs, given that hospital and nursing home care are more expensive than home and community-based care. With respect to enrollment, there has been a slight overall decline, coupled with significant increases and decreases across counties. As the table below shows enrollment in CMC dropped between December 2015 and 2016 by 1.4 percent. Most significantly, enrollment in Los Angeles county dropped 19.3 percent and in Santa Clara County by 20.6 percent. Enrollment grew in Orange County by 285 percent, as beneficiaries transitioned into the program over 12 months, beginning in July 2015.

Cal MediConnect
Annual Enrollment

County	December 1, 2015	December 1, 2016	Percent Change
Los Angeles	44,655	36,037	-19.3%
Orange	4,354	16,745	+285%
Riverside	13,813	13,445	-2.7%
San Bernardino	13,718	13,264	-3.3%
San Diego	16,442	14,339	-12.8%
San Mateo	9,684	9,391	-3.0%
Santa Clara	13,077	10,380	-20.6%
Total	**115,743**	**113,601**	**-1.4%**

CCI In-Home Supportive Services (IHSS) Changes. CCI established a county maintenance-of-effort funding formula for the IHSS program. In addition, CCI established a statewide authority for purposes of collective bargaining with respect to the wages and benefits for IHSS providers in the CCI counties. These aspects are discussed in the Human Services section – *"Coordinated Care Initiative and In-Home Supportive Services."*

CCI Universal Assessment. Lastly, another component of CCI was the development of a universal assessment tool (UAT) to be used to streamline the assessment process for connecting consumers to services, such as those defined as part of MLTSS. The Department of Social Services and the Department of Aging are the lead agencies in this effort and have contracted with the University of California - Los Angeles for its development. DHCS advises that a streamlined UAT has yet to be developed.

Requirements on Fiscal Solvency of CCI. SB 94 (Committee on Budget and Fiscal Review), Chapter 37, Statutes of 2013, requires the Department of Finance to annually determine if there are net General Fund savings for CCI. If CCI is not cost-effective, all components of CCI would cease operation.

GOVERNOR'S PROPOSAL

Coordinated Care Initiative. The governor's budget proposes to discontinue CCI in 2017-18. The Administration estimates that CCI will result in net General Fund costs of more than $278 million in 2016-17 and if continued in 2017-18, would result in $42 million net General Fund costs. The table below shows that the net cost calculation was pushed into a net cost by the large IHSS MOE costs. The DOF's calculations for 2015-16 included only $383.1 million General Fund costs from the IHSS MOE, as compared to $622.7 million estimated for 2017-18. The Administration notes that CCI will no longer be cost-effective, even though an allowable managed care tax was recently enacted. DHCS advises that the CCI net cost calculation includes a pro-rated share of the managed care tax that reflects the CCI portion of the Medi-Cal managed care program. The table on the following pages presents the CCI funding summary.

Continuation of Cal MediConnect, Mandatory Enrollment of Duals, and other Long-Term Services and Supports. As a component of the CCI termination process, DHCS is proposing to discontinue IHSS' inclusion in the demonstration program; all of the other pieces of CCI will continue. In addition, DHCS advises that if the beneficiary and IHSS provider agree, the IHSS provider will still be able to be part of the managed care plan's care team. DHCS advises that the hours for the participation in the care team would come from the beneficiaries' overall hours' level. For DHCS, the removal of IHSS from CCI does not appear to be significant. Although the funds for IHSS were calculated as part of the managed care plan's rate, DHCS held back that portion of the rate from the managed care plans and sent the funds to DSS. In essence, DSS continued to administer the IHSS program and the managed care plans did not "manage" that portion of the rate payment under CCI.

Coordinated Care Initiative Funding Summary

January 10, 2017				
	FY 2016-17		**FY 2017-18**	
(In thousands)	Total Fund	General Fund	Total Fund	General Fund
SAVINGS				
Local Assistance Costs (Savings)	**$ 3,348,724**	**$ (7,098)**	**$ 3,413,228**	**$ (114,056)**
Payments to Managed Care Plans	$ 9,609,417	$ 4,804,709	$ 10,239,773	$ 5,119,887
Transfer of IHSS Costs to DHCS	$ -	$ (1,681,460)	$ -	$ (1,820,670)
Savings from Reduced FFS Utilization	$ (6,260,693)	$ (3,130,347)	$ (6,826,545)	$ 3,413,273)
Payment Deferrals	**$ 45,325**	**$ 22,662**	**$ (14,255)**	**$ (7,128)**
Defer Managed Care Payment	$ 48,068	$ 24,034	$ (19,395)	$ (9,698)
Delay 1 Checkwrite	$ (2,743)	$ (1,372)	$ 5,140	$ 2,570
Revenue	**$ (268,244)**	**$ (268,244)**	**$ (432,325)**	**$ (432,325)**
MCO Enrollment Tax from CCI	$ (268,244)	$ (268,244)	$ (432,325)	$ (432,325)
Retro MC Rate Adjustments	**$ (89,203)**	**$ (44,602)**	**$ (89,736)**	**$ (44,868)**
CCI Rates Recasting	$ (89,203)	$ (44,602)	$ (89,736)	$ (44,868)
Savings Sub-Total	**$ 3,036,602**	**$ (297,282)**	**$ 2,876,912**	**$ (598,377)**
COSTS				
Increased DHCS Costs	**$ 25,737**	**$ 12,869**	**$ 26,423**	**$ 13,213**
Administrative Costs	$ 11,213	$ 5,607	$ 11,213	$ 5,607
HCO Contractor Costs	$ 13,514	$ 6,757	$ 14,200	$ 7,101
Actuarial Costs for Rate Dev't.	$ 1,010	$ 505	$ 1,010	$ 505
Increased DSS Costs	**$ 566,030**	**$ 562,096**	**$ 630,571**	**$ 626,637**
Service Costs (increased GF due to IHSS MOE)	$ 558,137	$ 558,137	$ 622,678	$ 622,678
DSS Administrative Costs from CCI	$ 7,893	$ 3,959	$ 7,893	$ 3,959
CalHR Administrative Costs	$ 1,921	$ 961	$ 1,921	$ 961
DMHC Administrative Costs	$ 2,186	$ -	$ 2,186	$ -
CDA Administrative Costs	$ 281	$ -	$ 281	$ -
Costs Sub-Total	**$ 596,155**	**$ 575,926**	**$ 661,382**	**$ 640,811**
Net Impact to CA - Costs	**$ 3,632,757**	**$ 278,644**	**$ 3,538,294**	**$ 42,434**

Source: Department of Health Care Services

ISSUES TO CONSIDER

The Governor's proposal to terminate CCI is a major proposal and represents a significant share of the fiscal solution to the budget problem identified by the Administration. Several issues relating to the Governor's CCI proposal that are likely to warrant legislative scrutiny are outlined briefly below:

How Has MLTSS Affected Health Care Quality or Outcomes? As described above, CCI includes the addition of MLTSS into Medi-Cal managed care; however, the MSSP component has not yet been integrated into CCI. In addition, it's unclear how much IHSS was ever part of the health plan's care team. Data regarding this population is available to DHCS, but the department has not conducted any consumer satisfaction surveys or analyzed data to understand how this component of CCI is changing health outcomes and consumer experiences. For example, DHCS does not know how many IHSS providers have participated in the health plan's care team.

Limited Data Available On Health Care Quality and Outcomes. DHCS advises that it has data on decreased nursing home utilization that it will be reporting soon, along with data on IHSS referrals. Typically, DHCS receives all the encounter data from its managed care health plans. With respect to CCI, the federal CMS has the encounter data, but has not transferred the data to DHCS. CMS withheld a portion of the plans' rates with the promise to release the funds if the plans met the metrics; in the first year, one percent of the plans' payments were withheld. DHCS advises that CMS has reported that California's CCI health plans have met the year one metrics withholds. Given the lack of timely data, the Legislature should consider whether any changes to CCI is premature.

The Future of Cal MediConnect. Based on survey data, a majority of CMC enrollees are satisfied with the choice of doctors they can see and the level of care they receive; however, the data also indicate that in many cases, participants in CMC are not any more satisfied with their care than Medi-Cal beneficiaries who opted out of the program or reside in counties that are not included in the program. In answer to the question, "Do you have a single care manager, such as a nurse or other helper from your health plan who serves as your main point of contact and can arrange all aspects of your care?" CMC enrollees answered yes at about the same percentage as those who had opted out or live in non-CMC counties. This apparent lack of distinction between CMC and non-CMC individuals may be one reason for the slight 1.4 percent enrollment decline noted earlier.

Future of the Affordable Care Act

BACKGROUND

With the new federal Administration, Congress has begun the steps to repeal portions of the Affordable Care Act (ACA), and some Congressional members have spoken of their intent to replace the ACA. In late January, Congressional Republicans held a planning session in Philadelphia and announced that action on the ACA would be one of the main priorities for the year. Repeal of the ACA has major implications for the states, but probably none more than California. California was the first state to establish an exchange, Covered California, and is one of 32 states (including the District of Columbia) that have implemented the optional Medicaid expansion. California has also seen the largest decline in the uninsured rate of any state; its number of uninsured dropped from 6.5 million in 2013 to 3.3 million in 2015.[1] Any changes in the funding and design of the health insurance system and Medicaid program could have major ramifications on health care in California and California's budget.

Affordable Care Act

The comprehensive health care reform act known as the ACA consists of thousands of provisions but the main areas under discussion fall into three broad categories: optional Medicaid expansion, health insurance exchanges, and insurance market reforms.[2]

Optional Medicaid Expansion. The optional Medicaid expansion (Medi-Cal in California) allows states to expand their Medicaid program to adults without children with incomes up to 138 percent of the federal poverty level (FPL). Before the expansion, California provided Medi-Cal benefits to low-income seniors, persons with disabilities, pregnant women, children, and families at various income levels. The ACA provides a generous schedule for federal funding for the Medicaid expansion.[3] The ACA paid for the entire cost of the optional Medicaid expansion from 2014 through 2016. The federal match was reduced to 95 percent in 2017, and is scheduled to decline by 1 percent each year until it reaches 90 percent in 2020. California implemented the expansion on January 1, 2014, the earliest date allowed under the ACA. For 2016-17, DHCS estimates the Medi-Cal ACA optional expansion enrollment at approximately four million at a cost of $19.2 billion ($888 million General Fund).

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[1] Miranda Dietz, Laurel Lucia, Gerald F. Kominski, and Ken Jacobs, "ACA Repeal in California: Who Stands to Lose? UC Berkeley Center for Labor Research and Education and the UCLA Center for Health Policy Research, December, 2016, p. 1.

[2] For a longer discussion of the provisions of the ACA, see Senate Health Committee's Background paper, *Informational Hearing: The Affordable Care Act in California: What's at Stake*? January 19, 2017. http://shea.senate.ca.gov/sites/shea.senate.ca.gov/files/hearing_paper_final.pdf

[3] Federal law provides matching funds to states for the Medicaid program, with poorer states getting higher matching ratios. The federal match is calculated taking into account state per capita income, with no state receiving less than a 50 percent match. California is one of the states that usually receive a 50 percent match.

Health Insurance Exchanges and Covered California. The ACA allowed states to establish their own insurance exchange or participate in the federal exchange to sell health insurance. Exchanges were designed to create a more organized system where small businesses and individuals would be offered a choice of health plans, following common rules. In addition, small businesses and individuals who were not eligible for Medicaid, but had incomes up to 400 percent of the FPL, had to purchase their health coverage through the exchanges in order to be eligible for federal tax credits. The ACA provides the tax credits to offset premium costs and also provides cost-sharing subsidies to reduce copayments and deductibles for those with incomes up to 250 percent FPL.[4]

Covered California was established by SB 900, (Alquist), Chapter 659, Statutes of 2010, and AB 1602, (Perez), Chapter 655, Statutes of 2010, and operates as an independent public entity governed by a five member board. For this reason, Covered California's budget is outside of the state budget. The federal government provided start-up grants to states and state law provides ongoing funding from fees imposed on participating health plans. The current year is the first year that Covered California has operated without federal funds. Enrollment in Covered California health plans was 1.36 million as of June 2016 and its 2016-17 budget totaled $321 million.[5] According to Covered California estimates, in 2016 Californians will receive $4.3 billion in premium tax credits and Covered California health plans will receive $750 million directly from the federal government in cost-sharing reduction payments to reduce copayments and deductibles for lower income enrollees.

Insurance Market Reforms. The ACA also included numerous other provisions intended to reduce the number of the uninsured and to stabilize the health insurance markets. These measures included prohibiting insurers from denying insurance to individuals with pre-existing conditions, allowing children to remain on their parents' health insurance until age 26, requiring large employers to provide insurance to their employees (known as the employer mandate), and requiring individuals to have insurance coverage (known as the individual mandate). The tax credits, subsidies, and individual mandate apply to most U.S. citizens and legal residents. [6]

Federal Actions

U.S. Senate Concurrent Resolution 3. In January 2017 both houses of Congress passed Senate Concurrent Resolution 3 (SCR 3), which authorizes a process for a budget reconciliation bill to be considered. SCR 3 directs the House and Senate finance and health committees to report proposals that would achieve $1 billion in deficit reduction over the next 10 years. The assumption is that the committees will include their proposals to repeal portions of the ACA in their reports. Under budget reconciliation, the Senate needs only a majority vote to approve

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[4] In addition, the ACA established three programs to protect health insurance companies against unpredictable losses or unmanageable risk selection; two were temporary, one is permanent. The risk adjustment program continues and adjusts for differences in the health of plans' enrollees by redistributing funds from companies with healthier-than-average customers to plans with sicker-than-average customers. These funds come from the insurance companies in the market places and are not federal funds.

[5] This enrollment figure is for enrollees who have paid and have "effective" coverage for the month of June, 2016.

[6] The ACA prohibits undocumented persons from purchasing coverage on the exchanges. Medicaid law provides federal funding for emergency, pregnancy, and long-term care services for undocumented persons. SB 75, Committee on Budget and Fiscal Review (Chapter 18, Statutes of 2015), authorized state-funded, full-scope Medi-Cal coverage to all California children, regardless of immigration status.

measures, but the provisions in the bill must substantially impact the budget. Thus, only those provisions in the Affordable Care Act (ACA) that are clearly fiscal in nature, such as the health care taxes, premium tax credits and cost-sharing subsidies, Medicaid expansion funding, or the individual and employer mandate penalties, could be included. House and Senate leadership has said their goal is to have repeal and partial replacement legislation on the House floor by the end of March.

President's Executive Order. On January 20, 2017, the President issued an executive order on the ACA, giving federal agencies broad leeway to "waive, defer, delay or grant exemptions from" requirements of the ACA that impose economic or regulatory burdens on states, families, the health care industry, and others. The ACA, however, was implemented primarily through regulation and guidance. Regulations cannot be rescinded without going through a long process of notice and comment. Guidance can be rewritten but must be consistent with legal and regulatory requirements. Key areas of the ACA are potentially affected by executive action. The current federal Administration could:

- Decline to enforce the individual mandate, or add new "hardship" exemptions.
- Drop the appeal to *House v. Burwell*[7], thus allowing a federal district court's decision to stand that found the ACA lacked legal authority to pay insurers to reduce consumers' deductibles and copayments on the exchanges.[8]
- Rewrite the state guidance for the Section 1332 ACA waiver[9] to give states more flexibility, such as institute work requirements as part of the Medicaid expansion.

GOVERNOR'S PROPOSAL

The budget proposes to continue funding the Medi-Cal optional expansion and assumes no changes will be made to the program. The only change in the Medi-Cal program anticipating a change in federal law, concerns the Children's Health Insurance Program (CHIP). CHIP provides federal funding to states to expand health insurance for pregnant women and children in families with incomes higher than the states' Medicaid program. CHIP's funding expires on September 30, 2017, unless it is reauthorized. The ACA also increased the federal sharing ratio of the CHIP from 65 percent to 88 percent. The budget assumes that CHIP will be reauthorized, but at the 65

[7] *House v. Burwell*, a lawsuit filed by the U.S. House of Representatives against the U.S. Dept. of Health and Human Services, contends that the cost-sharing reduction (CSR) subsidies paid to ACA health plans violated the appropriation authority specified by Congress.

[8] Covered California commissioned a study to estimate the value of the CSR onto the premiums to estimate the effect on the premium tax credits. This study found that eliminating the direct federal funding of CSR would raise premiums by 16.6% for silver plan consumers, which would trigger the premium tax credits in an amount *greater* than the total CSR paid by the federal government. Wesley Yin and Richard Domurat, University of California, Los Angeles, *Evaluating the Potential Consequences of Terminating Direct Federal Cost-Sharing Reduction (CSR) Funding*, January 26, 2017.

[9] Section 1332 of the ACA permits states to apply for State Innovation Waivers to pursue innovative strategies to provide high quality health care to residents, while maintaining the protections and coverage requirements of the ACA.

percent level, at a cost to California of $536 million annually. In addition, under a maintenance-of-effort provision of the ACA, states are required to maintain eligibility and enrollment standards for children in Medicaid and CHIP until 2019. The potential cost to California if CHIP is not reauthorized will depend on the status of this provision.

ISSUES TO CONSIDER

Medicaid Expansion Repeal Would Lead to Uncertainty. Federal repeal of the expansion of Medicaid would result in four million Californians losing health care coverage and the loss of more than $17 billion of federal funds. An increase in California's uninsured population of this magnitude would likely place significant stress on county safety net providers, such as public hospitals and clinics, as their costs for delivery of uncompensated care return to pre-ACA levels. The uncertainty of funding caused by repeal may require the state to reevaluate the funding relationships between state and local health care programs.

The Outcome of the ACA Is Unknown. At this time, it is unknown exactly what actions Congress will take. Congressional members have said they intend to have legislation on the House floor by the end of March. Although members of Congress and the President have repeatedly said they intend to repeal the ACA, recently they have begun to emphasize that they will both repeal and replace it. More recently, Republican Senators Susan Collins and Bill Cassidy introduced the Patient Freedom Act, which gives states the option of continuing their ACA Medicaid and Exchange programs with slightly reduced funding, flexibility to design an alternative program, or reject reform altogether. The bill provides states with 95 percent of the amount available from premium tax credits and cost-sharing subsidies and allows states to continue the ACA or create a market-based health insurance system using Roth Health Savings Accounts (HSA).

With respect to Medicaid, the bill does not reduce Medicaid funds available to states and allows states to use these funds in their market-based system. If a state didn't expand Medicaid under the ACA, the bill provides states the funds they would have received under the Medicaid expansion for the Roth HSA tax credits. Under either scenario, states would be required to maintain the essential consumer protections, including a prohibition on denying coverage for preexisting conditions, annual or lifetime caps, and allowing adult children to remain on their parents' health plan until age 26.

If the Exchange Collapses, Is the General Fund at Risk? Various scenarios have been described that could result in the collapse of health insurance exchanges. For example, if Congress eliminated the tax credit premium subsidies or the individual mandate, the exchanges would see a drop in enrollment that could result in health plans pulling out of the exchanges. If this happened in California, it would result in the loss of health coverage for up to 1.36 million Californians enrolled in Covered California's health plans and a loss of over $5 billion in federal funds to those health plans. DHCS, however, does not anticipate an effect on the Medi-Cal program if this were to occur. Since no General Fund supports Covered California, this would probably have only minor effect on state costs for operation of the exchange.[10] However, as the uninsured population rises, increased reliance on health care services provided by county public health programs would reduce the benefit to the state's General Fund from the redirection of 1991 Health Realignment pursuant to AB 85, (Committee on Budget), Chapter 24, Statutes of 2013.

[10] The ACA included a reduction in disproportionate share hospital funding reflecting the decrease in the number of uninsured. Hospitals would probably see an increase in emergency room visits and uncompensated care, but DHCS anticipates that if Congress reduces payments for insurance coverage, it would increase disproportionate share hospital funding.

Four Propositions Direct Funds to State Health Care Programs

BACKGROUND

The following four propositions, approved by the voters in November 2016 would raise and direct funds to various health care and related programs.

Proposition 52 - Medi-Cal Hospital Fee Program. Proposition 52 continues the current Hospital Quality Assurance Fee, imposed on most private hospitals, which was set to end on January 1, 2018. The fee revenue is used to fund the state share of increased Medi-Cal payments for hospitals and grants for public hospitals, funds the state share of higher rates, and results in significant General Fund savings. Proposition 52 made the hospital fee permanent, but allows the Legislature to end or alter it with a two-thirds vote. The measure continues the current structure of the hospital fee and, as under current practice, excludes these revenues from the annual calculation of school funding.

Proposition 55 - Tax Extension for Education and Healthcare. Proposition 55 extends the current personal income tax rates on high-income taxpayers through 2030. The additional rates, ranging from one percent to three percent depending upon income, were initially imposed by Proposition 30 in 2012 and scheduled to end after tax-year 2018. Proposition 55 also includes a new state budget formula to provide more funding for the Medi-Cal program. The measure requires the Director of Finance to annually determine whether General Fund revenues exceed constitutionally-required education spending and the costs of government programs that were in place as of January 1, 2016. If the revenues exceed these amounts, 50 percent of the excess (up to $2 billion) would be allocated to the Medi-Cal program. The measure specifies that these Medi-Cal funds cannot be used to supplant existing General Fund support for the program.

Proposition 56 - Cigarette Tax. Effective April 1, 2017, the proposition increases the state excise tax on cigarettes by $2 per pack, from 87 cents to $2.87. It also applies an equivalent tax to other tobacco products and extends the tax to electronic cigarettes. Proposition 56 specifies how the revenues would be allocated in a series of four sequential steps, specifically:

- Backfills revenue losses in existing state tobacco funds and sales taxes that occur as a result of the measure and lower consumption of tobacco products.

- Allocates to the Board of Equalization five percent of the remaining funds to pay for the administrative costs of the measure.

- Allocates $40 million to the University of California (UC) for physician training and $30 million to the Department of Public Health (DPH) state dental program for education on preventing and treating dental disease.

- Distributes the remaining funds according to the following schedule: 82 percent for the Medi-Cal program, 11 percent to the California Tobacco Control Program in DPH, five percent to the UC Tobacco-Related Disease Program, and two percent to school prevention programs.

Proposition 64 - Marijuana Legalization. Proposition 64 legalizes adult, nonmedical use of marijuana and creates a system for regulating nonmedical marijuana businesses, imposes taxes on marijuana beginning in January 2018, charges penalties for marijuana-related crimes, and allocates the state revenues for specific purposes. For an additional discussion on Proposition 64, under *State Administration and General Government*. Proposition 64 allocates funds to numerous entities, including the Department of Health Care Services (DHCS), local health departments, and community-based nonprofits. The measure makes the following specific changes and fund allocations:

- Allows for a General Fund loan (to be repaid) to state regulatory bodies to facilitate the establishment of the regulatory framework.

- Provides $5 million to DHCS to establish a public information program by September 1, 2017 regarding the provisions of the proposition, the scientific basis for restricting access to marijuana to persons under 21, and the potential harm of using and overusing marijuana.

- Expands DPH current responsibilities regarding licenses for manufacturers of medical cannabis products (i.e. edibles, lotions, patches), to nonmedical marijuana.

- Directs $10 million annually (increasing to $50 million annually), beginning in 2018-19, to a community reinvestment grant program to address numerous issues including job placement and mental health and substance use disorder treatment.

- Provides 60 percent of the funds remaining after specified disbursements, beginning in 2018-19, to DHCS for youth substance abuse programs, and requires DHCS to enter into interagency agreements with DPH and CDE to implement and administer these programs.

GOVERNOR’S PROPOSAL

Proposition 52 - Medi-Cal Hospital Fee Program. The Governor’s budget continues the Medi-Cal hospital fee program similarly to how it has been administered in the past. The DHCS advises that in order to continue the program, it will need to submit a new model to the federal government to receive approval for the extension of the fee program. These changes will be reflected in the May Revision.

Proposition 55 - Tax Extension for Education and Healthcare. The Department of Finance advises that since it is projecting a deficit for the budget year, absent any corrective actions, it is not proceeding with the calculation required under Proposition 55, described in the section above. Therefore, the Governor's budget does not anticipate that any revenues related to Proposition 55 would be available to direct to the Medi-cal program in 2017-18.

Proposition 56 - Cigarette Tax-Department of Public Health. The Governor's budget includes $223.5 million from the tobacco tax revenues for three main programs in the DPH based on the following:

- $7.5 million in 2017-18 (and $6 million annually thereafter) and 20 permanent positions to the Stop Access to Kids Enforcement (STAKE) Program to increase STAKE Act compliance checks of tobacco retailers by approximately 2800, establish a grant program to local law enforcement agencies, and establish a statewide training and education program for local law enforcement agencies.

- $37.5 million in 2017-18 (and $30 million annually thereafter) to the Oral Health Program (OHP) to support oral health education, prevention, surveillance, and treatment of dental disease. This funding also replaces $3.7 million General Fund that currently funds the dental director and the children's Dental Disease Prevention Program.

- $178.5 million annually (subject to tobacco revenue levels) for tobacco use prevention and reduction efforts including media, competitive grants, local lead agencies, evaluation, and program administration.

Proposition 56 - Cigarette Tax-Department of Health Care Services. The Governor's budget includes $1.2 billion in Proposition 56 funding to support new growth in spending in the Medi-Cal program compared to the 2016 Budget Act. These moneys will not fund any new program or fee-for-service rate increase, but will go to managed care capitation costs from additional beneficiaries, and to higher rates paid as a result of the regular rate determination process. In addition, some of the funds will go towards increased costs from Medi-Cal expenditures for Medicare premiums and Medicare Part D costs.

Proposition 64 – The DHCS budget includes a $5 million increase in reimbursements to reflect the funds that will be provided from the Department of Consumer Affairs (DCA). DOF indicates that the budget includes a $5 million General Fund loan to the Marijuana Control Fund and that the DCA will develop an interagency agreement or a memorandum of understanding with DHCS regarding potential public health concerns.

ISSUES TO CONSIDER

There are a number of issues that are raised by these propositions passage noted above that warrant oversight, analysis and potential action by the Legislature.

Determination by Department of Finance of Excess Revenue under Proposition 55. When the actual revenues are reported for the current year, the Legislature will need to revisit the Director of Finance's determination that General Fund revenues will not exceed constitutionally required education spending and the costs of government programs that were in place as of

January 1, 2016. If the revenues exceed these amounts, 50 percent of the excess (up to $2 billion) is required to be allocated to Medi-Cal.

Cigarette Tax Revenues Will More Than Quadruple the Funding for Three DPH Programs. Passage of Proposition 56 will increase the cigarette tax on April, 1, 2017 and increase the combined funding to three of DPH's branches/programs by 480 percent. The amount of funding for the Oral Health Program is specified in the initiative, as is the total for the Tobacco Control Program at DPH. Because of the magnitude of these increases, the programs may have difficulty or delays hiring the large number of personnel they are requesting. The programs may also have difficulty spending some portion of the increased funds in the budget year. Consideration should be given as to how the DPH will transition to this higher level of staffing and activity.

What is the State's Oral Health Plan? The budget, as directed by Proposition 56, proposes $37.5 million for the Oral Health Program (OHP) to support the recommendations in the state's oral health plan. However, this plan has not been finalized. The budget proposes funding 11 positions (currently, there are five in OHP) and OHP advises that it intends to use the tobacco prevention model in overseeing the use of these funds to educate, prevent, and treat dental disease. At this time, OHP does not have a detailed plan on how they will distribute these funds to the city and county health departments; however, OHP advises that it will be requesting a needs assessment and action plan from the local health departments.

How Should the Funds Be Spent at DPH on Tobacco Control? The budget includes an increase of $7.5 million for the STAKE program and $178.5 million for the Tobacco Control Branch for tobacco use prevention and reduction efforts. This increase for the Tobacco Control Branch is more than four times its total expenditure level in 2015-16 ($44.2 million). Given the size of this increase, the Legislature will want to review the various components of DPH's proposal and available research on these approaches to decide on the appropriate funding levels.

Is the Allocation of Proposition 56 Funds to Medi-Cal Consistent with the Initiative Wording and Intent? The Governor's budget includes $1.2 billion in Prop. 56 funding to support new growth in spending in the Medi-Cal program as compared to the 2016 Budget Act. These funds will not fund any new program or fee-for-service rate increase, but pay for caseload and cost increases. The Legislature should consider whether the Governor's approach is consistent with the proposition's requirement that these funds may not support existing state funds used for this purpose.

Is DHCS the Appropriate Department to Implement a Marijuana Education Campaign? Proposition 64 directs $5 million to DHCS to establish a public information program by September 1, 2017, on the provisions of the proposition, the scientific basis for restricting access to marijuana to persons under 21, and the potential harms of using and overusing marijuana. DHCS does not currently conduct similar public information campaigns, such public health campaigns are typically administered by the DPH. The Health and Human Services Agency indicates that it working with both departments and will have a proposal on this issue.

What Planning and Development Should Begin for the Proposition 64 Funds? The marijuana taxes do not begin until January 1, 2018; and the allocations for social services and substance abuse programs do not go into effect until the 2018-19 budget year. Although DOF has not estimated the level of this funding, with estimated annual tax revenues of about $900 million the funds could be quite significant. The funds for youth substance abuse programs that are directed to DHCS are distributed after the costs for the regulatory bodies and other specified allocations are paid; however, since DHCS receives 60 percent of the remaining funds, the allocation could be in the hundreds of millions. At a minimum, the Legislature could review the level of current funding for these programs through DHCS, CDE, and other state and local departments.

In-Home Supportive Services: Coordinated Care Initiative

BACKGROUND

The passage of the Coordinated Care Initiative (CCI) in 2012 created some major changes in the In-Home Supportive Services (IHSS) program. With the Governor's proposal to repeal the IHSS provisions of CCI this year, the Legislature must address some important questions related to sharing of IHSS costs between the county and the state, whether or not the IHSS portion of the CCI had any merits that may be worth saving, and what long-term implications for programs other than IHSS may be.

The IHSS program provides personal care services to approximately 531,000 qualified low-income individuals who are blind, aged (over 65), or who have disabilities. Services include feeding, bathing, bowel and bladder care, meal preparation and clean-up, laundry, and paramedical care. These services help program recipients avoid or delay more expensive and less desirable institutional care settings. A proposed budget of $10.6 billion ($3.2 billion General Fund) for services and administration includes funding for compliance with federal overtime regulations and state minimum wage increases.

Service Delivery. County social workers determine IHSS eligibility and perform case management after conducting a standardized in-home assessment of an individual's ability to perform activities of daily living. In general, most social workers reassess annually recipients' need for services. Based on authorized hours and services, IHSS recipients are responsible for hiring, firing, and directing their IHSS provider(s). If an IHSS recipient disagrees with the hours authorized by a social worker, the recipient can request a reassessment, or appeal their hour allotment by submitting a request for a state hearing to the Department of Social Services (DSS). According to DSS, around 73 percent of providers are relatives, otherwise known as "kith and kin."

In the current year, IHSS providers' combined hourly wages and health benefits vary by county, and range from approximately $10.00 to $18.00 per hour. Prior to July 1, 2012, county public authorities or nonprofit consortia were designated as "employers of record" for collective bargaining purposes, while the state administered payroll and benefits. Pursuant to 2012-13 trailer bill language, however, collective bargaining responsibilities in seven counties participating in the Coordinated Care Initiative (CCI) – Los Angeles, Orange, Riverside, San Bernardino, San Diego, San Mateo, and Santa Clara, shifted to an IHSS Authority administered by the state. The CCI is further discussed in the Health section of this document.

Program Funding. The average annual cost of services per IHSS client was estimated to be around $15,500 for 2015-16. The program is funded with federal, state, and county resources. Federal funding is provided by Title XIX of the Social Security Act. Before the CCI, the county IHSS share-of-cost (SOC) was determined by 1991 Realignment. When the state transferred various programs from the state to county control, it altered program cost-sharing ratios and provided counties with dedicated tax revenues from the sales tax and vehicle license fee to pay for these changes. Prior to realignment, the state and counties split the non-federal share of IHSS program costs at 65 and 35 percent, respectively.

A 2012-13 budget trailer bill, related to the enactment of the CCI, changed this structure as of July 1, 2012, with county IHSS costs based on a maintenance- of-effort (MOE) requirement. The MOE works differently depending on the county. For a select 15 smaller counties, the MOE levels are based either on the 2011-12 county allocations or county expenditures, whatever is lower. For the other 43 counties, the MOE levels are based on county expenditures in 2011-12. Starting July 1, 2014, a 3.5 percent annual inflation factor was applied to this base along with any adjustments for approved county negotiated wage and health benefit increases. The state assumed responsibility for any additional costs that would have historically been paid under the previous county SOC. However, language embedded in the CCI requires the Department of Finance to annually determine if there are net General Fund savings for CCI. If CCI is not cost-effective, all components of CCI and the county MOE agreement would cease operation.

Coordinated Care Initiative. CCI requires health plans to coordinate medical, behavioral health, long-term institutional, and home and community-based services. Counties continue to administer the program under existing standards and requirements. The intent of CCI is to improve integration of medical and long-term care services through the use of managed health care plans and to realize accompanying fiscal savings by reducing institutional care.

Universal Assessment Tool. In 2012, the Legislature authorized the development and pilot implementation of a universal assessment tool (UAT). The Department of Health Care Services (DHCS), the Department of Aging (CDA), and DSS were tasked with developing a UAT to assess a Medi-Cal beneficiary's need for home and community-based services. The goal was to enhance personalized care planning under CCI, and create a common tool that can be used by all involved in the care of beneficiaries who need home and community-based, long-term care services.

As of last year, DSS, DHCS and CDA continued to work with a design team from the UCLA Boren School of Gerontology to prepare a draft UAT for focus group, pre-pilot and pilot testing. UAT focus group testing was expected to begin in May 2016, and pre-pilot testing was slated for early 2017.

Evaluation of IHSS in the CCI. While there is not robust data available on how the IHSS integration into managed care under the CCI is working, given the short duration of the pilot, a couple of preliminary studies provide some insight into the strengths and weaknesses of the program model. A recent report entitled "Evaluation of CalMediConnect: Results of Focus Groups with Beneficiaries"[1] found that several key stakeholders interviewed found that the program inspired better collaboration and communication between IHSS and plans. Those involved saw the potential for IHSS workers to become more involved and ensure that the number of IHSS hours authorized would be better aligned with the needs of IHSS beneficiaries. However, many IHSS recipients opted out of involvement in the program. Another recent report, "CalMediConnect: How Have Health Systems Responded?"[2] echoed these findings, and both

[1] University of California for the SCAN Foundation, *Evaluation of CalMediConnect: Results of Focus Groups with Beneficiaries* (March 2016): http://www.thescanfoundation.org/sites/default/files/cal_mediconnect_focus_group_report_march_2016.pdf
[2] University of California for the SCAN Foundation, *CalMediConnect: How Have Health Systems Responded* (July 2016): http://www.thescanfoundation.org/sites/default/files/cal_mediconnect_health_system_full_report.pdf

reports emphasize that more outreach to communities with high opt-out rates, IHSS social workers, and IHSS providers, is needed.

Other Policy Changes. Several recently enacted policies have also impacted the IHSS program, including:

- **Restoration of the seven percent reduction in service hours.** A legal settlement related to *Oster v. Lightbourne* and *Dominguez v. Schwarzenegger*, resulted in an eight percent reduction to authorized IHSS hours, effective July 1, 2013. Beginning in July 1, 2014, the reduction in authorized service hours was changed to seven percent. The 2015 Budget Act approved $225.9 million in one-time General Fund resources, and related budget bill language, to offset the seven-percent across-the-board reduction in service hours. The 2016-17 Governor's budget uses a portion of the revenues from a restructuring of the existing Managed Care Organization (MCO) tax to restore the seven percent across-the-board reduction beginning July 1, 2016.

- **Minimum wage increases.** Assembly Bill 10 (Alejo), Chapter 351, Statutes of 2013, increased the minimum wage from $8 per hour to $9 per hour in July 2014, with gradual increases until the minimum wage reached $10 per hour by January 2016. 29 counties are impacted by the minimum wage increase in 2016-17.

  In addition, SB 3 (Leno), Chapter 4, Statutes of 2016, will move the state's current $10 per month for minimum wage to $10.50 at the beginning of 2017, and schedules annual increases to $15 for most employers by 2022. SB 3 also provides three paid sick leave days to IHSS workers beginning July 2018, and requires DSS, in conjunction with stakeholders, to convene a workgroup to implement paid sick leave for IHSS providers and issue guidance by December 1, 2017.

- **Fair Labor Standards Act (FLSA)—Final Rule.** FLSA is the primary federal statute dealing with minimum wage, overtime pay, child labor, and related issues. In September 2013, the U.S. Department of Labor issued a final rule, effective January 1, 2015, which redefined "companionship services" and limits exemptions for "companionship services" and "live-in domestic service employees" to the individual, family, or household using the services (not a third party employer). The rule also requires compensation for activities, such as travel time between multiple recipients, wait time associated with medical accompaniment, and time spent in mandatory provider training. Under the final rule, employers must pay at least the federal minimum wage and overtime pay at one and a half times the regular pay if a provider works more than 40 hours per work week. The final rule started implementation in California on February 1, 2016.

  SB 855 (Committee on Budget and Fiscal Review) Chapters 29, Statutes of 2014, established a limit of 66 hours per week for IHSS providers based on the statutory maximum of 283 hours a month for IHSS recipients, and limited travel time for providers to seven hours a week. DSS or counties may terminate a provider in the event of persistent violations of overtime or travel limitations.

GOVERNOR'S PROPOSALS:

The Governor's budget estimates that CCI will no longer be cost-effective and does not meet the statutory savings requirements. With this proposal, the IHSS MOE provisions would no longer be in effect and the IHSS program would return to the prior state-county sharing ratio. Responsibility for collective bargaining also returns to counties. The Administration estimates that eliminating the IHSS County MOE provides $665.6 million General Fund savings in 2017-18. The impact of the proposal on funding is shown in the figure below.

Eliminate IHSS County MOE

Funding (In Millions)	FY 2016-17 Appropriation	FY 2016-17 Revised Budget	FY 2017-18 Governor's Budget	FY 2016-17 Change From Appropriation	FY 2017-18 Change From Appropriation
Total*	$0	$0	$0	$0	$0
Federal	$0	$0	$0	$0	$0
State	-$1,113.5	-$1,117.4	-$1,779.2	-$3.8	-$665.6
County (Reimb)	$1,113.5	$1,117.4	$1,779.2	$3.8	$665.6

*Total TANF/GF impact prior to subaccount funds.

ISSUES TO CONSIDER

What are the effects of the Governor's proposal on recipients and providers who participated in the CCI? Can we learn from any successes of the pilot? One of the goals of the CCI was to integrate long-term services and supports (LTSS) and, by extension, IHSS, into Medi-Cal managed care and improve overall health care coordination for beneficiaries. LTSS provides a type of preventative care that can reduce hospitalizations and help consumers better manage their health conditions in the long-term. While the IHSS model as a whole remains relatively untouched by the dissolution of the CCI, meaning that both recipients and providers are unlikely to notice any changes, it may be worth re-examining why IHSS was included as part of the CCI in the first place, considering if the problems the CCI was trying to solve still exist, and determining if in any way the CCI was able to mitigate some of those issues and improve care for the recipients involved in the program.

What are we losing by ending the development of the Universal Assessment Tool? The development of the UAT will also be halted with the Governor's proposal. The UAT has been in development since 2012, and was expected to pilot sometime in 2017. It is important for the Legislature to consider whether the UAT has any merits and meets larger goals for LTSS and home and community-based care outside of the CCI, and if it makes sense to halt the UAT along with the CCI.

What are the county implications of ending the IHSS MOE and returning to a share-of-cost model? If the MOE reverted to the prior state-county split, it is important for the Legislature to evaluate more closely how the MOE worked for both the county and state, and consider what will change under the Governor's proposal, given that the SOC ratio was established back during 1991 Realignment. The elimination of the MOE raises questions about whether the counties should pay for cost increases that were approved after 2012, including FLSA overtime (which was federally mandated), state minimum wage increases, and paid sick leave. In particular, counties estimate that with current law capping state wage and benefit participation at $12.10 per hour, if state minimum wage increases shift to the counties, costs could grow into the hundreds of millions in the out years.

It appears that the Administration expects that the counties will now pay a share in all of these cost increases. It is likely that counties will have to use 1991 Realignment dollars for this purpose; however, many of these funds are already used to pay for other programs at the county level, including health and mental health programs. Complicating the 1991 Realignment issue further is AB 85 (Assembly Committee on Budget) Chapter 24, Statutes of 2013, which established the Child Poverty and Family Supplemental Support Subaccount, and takes a portion of 1991 Realignment growth revenues. This subaccount currently funds CalWORKs grant increases and the 2016 repeal of the Maximum Family Grant Rule in out years (see CalWORKs discussion in this section for more information). While 1991 Realignment funding, including the subaccount, is currently expected to grow, it is unclear if it will grow enough to cover all of its current costs, in addition to rapidly increasing IHSS costs. Given the complex nature of Realignment funding, the Legislature will need to consider where funding for ending the IHSS MOE will come from and whether that action will have impacts beyond just the IHSS program.

What are the implications of ending statewide bargaining for the seven CCI pilot counties? The Legislature should also evaluate what impact, if any, the elimination of statewide bargaining has for the seven pilot counties and if there are any effects on non-pilot counties.

Child Welfare Services: Continuum of Care Reform

BACKGROUND

The Continuum of Care Reform (CCR) is a multi-year effort to reduce the reliance on group home placements and develop a more robust supply of home-based family settings for foster youth, while providing families with the resources necessary to support foster youth as much as possible. The Child Welfare Services (CWS) branch of the Department of Social Services (DSS), in conjunction with counties, is responsible for overseeing this large-scale overhaul of the foster care system. Implementation began on January 1, 2017, and will continue over the course of the next several years, during which it will be important to ensure that DSS and the counties are communicating and working closely together in order to provide the smoothest transition for foster youth and deliver on the promises of CCR.

Continuum of Care Reform

Significant research documents the poor outcomes of children and youth in group homes, such as higher re-entry rates into foster care, low high school graduation rates, and increased risk of arrest. These group homes are generally more expensive than family placements. The CCR began by trying to find solutions to these problems, but eventually broadened the effort into a more comprehensive set of system changes for the whole foster care system.

In 2012, the Legislature passed SB 1013 (Budget and Fiscal Review Committee), Chapter 35, Statutes of 2012, which authorized the CCR to develop recommendations related to the state's current rate setting system, and to services and programs that serve children and families in the continuum of Aid to Families with Dependent Children-Foster Care (AFDC-FC) eligible placement settings. In January 2015, the department released the report "California's Child Welfare Continuum of Care Reform", which listed recommendations to improve assessment of child and families to make more appropriate initial placement decisions; emphasize home-based family care; support placement with available services; change the goals for group home care placement; and, increase transparency for child outcomes. The Legislature subsequently passed AB 403 (Stone), Chapter 773, Statutes of 2015, to implement the CCR, which codified the recommendations. Some of the main components of AB 403 are:

- Creation of Short-Term Residential Treatment Placements (STRTPs), which are intended to provided short term, therapeutic services to stabilize children so that they may quickly return to a home-based family care setting.

- Foster Family Agencies (FFAs) and STRTPs will be required to ensure access to specialty mental health services and strengthen their permanency placement services.

- Additional integration between child welfare and mental health services.

- FFAs and STRTPs are required to obtain and maintain accreditation from a nationally-recognized body in order to improve quality and oversight. CCR also calls for the development of publicly available FFA and STRTP performance measures.

- Resource Family Approval (RFA) is a new, streamlined assessment that replaces the existing multiple approval, licensing, and certification processes for home-based family caregivers.

- The required use of child and family teams (CFTs) in decision-making.

- The creation of a new, comprehensive strengths and needs assessment upon entering the child welfare system in order to improve placement decisions and ensure prompt access to supportive services.

- New Home-Based Family Care rate structure, which is based on child need.

Child Welfare Services

California's child welfare system seeks to prevent, identify, and respond to allegations of child abuse and neglect. Families who are in the child welfare system receive services so children can remain safely in their homes, and/or children who are temporarily removed from their homes can reunify with their families. In instances when reunification is not possible, permanency may occur through adoption or guardianship.

The core of child welfare services (CWS) is made up of four components:

- <u>Emergency Response</u>: Investigations of cases where there is sufficient evidence to suspect that a child is being abused or neglected.

- <u>Family Maintenance</u>: A child remains in the home, and social workers provide services to prevent or remedy abuse or neglect.

- <u>Family Reunification</u>: A child is placed in foster care, and services are provided to the family with the goal of ultimately returning the child to the home.

- <u>Other Placements</u>: Permanency services to a child who is unable to return home and offers an alternative family structure, such as legal guardianship or independent living.

Temporary placement types. Traditionally, there have been three major temporary placement types — a foster family home (FFH), foster family agency (FFA), or group homes:

- FFHs are licensed residences that provide for care up to six children. This placement type also includes relative caregivers. Under CCR, these families are known resource families.

- FFAs are private, nonprofit corporations intended to provide treatment and certify placement homes for children with higher level treatment needs. Under CCR, FFAs are also considered resource families.

- Lastly, group homes are licensed to provide 24-hour non-medical residential care in a group setting to foster youth from both the dependency and delinquency jurisdictions.

Under CCR, however, group homes are being phased out and STRTPs replace them. As of January 1, 2017, group homes are no longer a placement option (subject to case-by-case exceptions that may allow them to continue to operate for a period of time). STRTPs will provide care, supervision, and expanded services and supports.

Additionally, FFAs and STRTPs will be required to ensure access to specialty mental health services and strengthen their permanency placement services by approving families for adoption, providing services to help families reunify, and giving follow-up support to families after a child has transitioned to a less restrictive placement. AB 403 also requires FFAs and STRTPs to make educational, health, and social supports available.

Duration in placement and placement movements. According to the department's 2015-16 CWS Realignment Report, for the largest age group category, 13-17 years old, of the 4,737 children, the majority (45 percent) move out of group home placements in less than 12 months; longer stays (12-36 or more months) comprise the remaining 55 percent (2,619).

The foster youth in group home care will transition to alternative placements. In 2017-18, the department assumes that 115 group home placements will move to an intensive services foster care placement; 345 group home placements will move to an STRTP placement; and 515 group home placements will move to a family-based setting. The remaining 4,630 group home placements will not yet transition.

Below is a table for 2017-18, based on data from DSS, that shows caseload movement from group homes.

Table 3. HBFC Rate Caseload - Child Welfare Group Home Caseoad Movements.

		FY 2016-17 Caseload	FY 2017-18 Caseload	FY 2018-19 Caseload	FY 2019-20 Caseload	FY 2020-21 Caseload	Assumed Final Distribution
Total Child Welfare GH Caseload		3,637	3,638	3,637	3,637	3,638	
Total Current GH 1-9	*390*						
GH RCL 1-9 Shifting to TFC		-	-	17	19	19	9%
GH RCL 1-9 Shifting to STRTP		-	-	-	-	-	0%
GH RCL 1-9 Shifting to FFA		10	27	83	193	195	92%
GH RCL 1-9 Shifting to FFH/Relative		-	18	66	173	176	83%
GH not Shifting		380	345	224	5	-	0%
Total Current GH 10-12	*2,902*						
GH RCL 10-12 Shifting to TFC		-	67	247	430	435	28%
GH RCL 10-12 Shifting to STRTP		37	200	371	573	580	37%
GH RCL 10-12 Shifting to FFA		-	133	371	1,003	1,016	65%
GH RCL 10-12 Shifting to FFH/Relative		-	133	494	860	871	55%
GH not Shifting		2,865	2,369	1,419	36	-	0%
Total Current GH 14	*346*						
GH RCL 14 Shifting to TFC		-	8	15	51	52	28%
GH RCL 14 Shifting to STRTP		2	24	59	103	104	56%
GH RCL 14 Shifting to FFA		-	16	44	119	121	65%
GH RCL 14 Shifting to FFH/Relative		-	8	44	68	69	37%
GH not Shifting		343	290	183	4	-	0%

*Caseload values are rounded.

Placement costs

Prior to CCR, group home facilities were organized under a system of rate classification levels (RCLs) ranging from 1-14 that are based on levels of staff training and ratios. In practice, a majority of group homes were RCL 10 and above, with nearly 50 percent of groups homes at RCL 12. As of 2015-16, group home placements constituted 13 percent of foster care placement and represented 48 percent of total foster care costs. Group home rates were based on the level of care and services provided, ranging from $2,332 to $9,879 per month.

Reimbursement rates for 14 separate group home levels will be replaced by a new set of rates that is based on the needs of the child, which will be determined by a still in development assessment tool to be used by county social workers and child and family teams, unlike the previous structure which centered around the age of the child. These new rates are intended to reflect the expanded set of responsibilities of STRTPs and FFAs under CCR.

With the passage of the 2016-17 budget, the Legislature approved the Administration's proposed Home-Based Family Care (HBFC) Rate structure shown below:

Continuum of Care Reform (CCR) Summary*

Home-Based Family Care Rate Structure

Based on Level of Care (LOC)

		Basic Level	LOC-2	LOC-3	LOC-4
A	**Pay to Resource Family for Basic Rate**				
	Basic Rate	$889	$989	$1,089	$1,189
B	**Pay to Foster Family Agency**	**Basic Level**	**LOC-2**	**LOC-3**	**LOC-4**
	Basic Rate	$889	$989	$1,089	$1,189
	Social Worker	$340	$340	$340	$340
	Social Services & Support	$156	$200	$244	$323
	RFA	$48	$48	$48	$48
	Administration	$672	$672	$672	$672
	Total	**$2,105**	**$2,249**	**$2,393**	**$2,572**
C	**Pay to Resource Family for Intensive Services FC (ISFC)**				
	ISFC Rate	$2,321			
	Pay to Foster Family Agency including ISFC Administration				
	ISFC Administration	$3,482			
	ISFC Social Services & Support	$200			
	Total	**$6,003**			
D	**Pay to Short-Term Residential Therapeutic Program (STRTP)**				
	STRTP Rate	$12,036			
E	**Pay to Foster Family Agency or Community Based Organizations for Services Only**				
	Total Rate	**$771**			

The FFA rate is separated into two components. The first goes to the family caregiver as an assistance payment, and the second goes to the FFA for administrative and social work activities. Similarly, the Therapeutic Foster Care (TFC) model divides the TFC rate into two components, one of which is paid to the TFC caregiver and the second which is paid to the FFA for administrative and supportive services.

CCR also allows counties to pay FFAs to provide services to children who are not placed in FFAs, allowing children in relative and county-approved homes to access supportive services if the county chooses to provide funding. The rates paid to FFAs to provide these services are called the FFA services only rates.

Realignment. In 2011, Governor Brown and the Legislature realigned several programs, including child welfare and foster care, and shifted program and fiscal responsibility for non-federal costs to California's 58 counties.[1] General Fund revenues, which were formerly provided to the counties for child welfare and probation, have been realigned to counties as a revenue stream in the form of a portion of the state's sales tax. The state retains child welfare oversight and serves as the agency for federal funding and administration. Counties must meet all state and federal mandates in CWS and Probation.

Recent policy and budget actions. Several related policies and budget actions include:

- **Extended foster care.** AB 12 (Beall), Chapter 559, Statutes of 2010, enacted the "California Fostering Connections to Success Act of 2010," which provides an extension for foster youth, under specified circumstance, to remain in care until age 21; increases support for kinship care (opportunities for youth to live with family members); improves education stability; provides coordinated health care services; provides direct child welfare; and, expands federal resources to train caregivers, child welfare staff, attorneys, and more.

- **Katie A.** The *Katie A.* vs. *Bonta* case was first filed on July 18, 2002 as a class action suit on behalf of children who were not given adequate services by both the child protective system and the mental health system in California. The suit sought to improve the provision of mental health and supportive services for children and youth in, or at imminent risk of placement in, foster care in California. Outcomes from the settlement agreement and implementation plan include the creation of the Core Practice Model; and the provision of Intensive Care Coordination, Intensive Home-Based Services, and Therapeutic Foster Care to eligible children.

- **Title IV-E Waiver.** Title IV-E is the major federal funding source for child welfare and related probation services. These funds, which were previously restricted to pay for board-and-care costs and child welfare administration, can be used to provide direct services and supports under the waiver extension. Since Title IV-E funding is based

[1] AB 118, (Committee on Budget), Chapter 40, Statutes of 2011, and AB 16X1 (Committee on Budget), Chapter 13, Statutes of 2011, realigns funding for Adoption Services, Foster Care, Child Welfare Services, and Adult Protective Services, and programs from the state to local governments and redirects specified tax revenues to fund this effort.

solely on actual cost of care, if a county's preventative services are effective and fewer children enter or stay in the foster care system, the county's Title IV-E funding is reduced. Thus, the county is penalized for reducing foster care placements, even though such a reduction is the most desirable outcome. However, under a federal waiver demonstration project in which some counties are participating, Title IV-E funds can be used to provide direct services and supports. This waiver demonstration has been extended for five years, beginning October 1, 2014. The participating counties include: Alameda, Butte, Lake, Los Angeles, Sacramento, San Diego, San Francisco, Santa Clara, and Sonoma.

- **Commercial Sexual Exploitation of Children (CSEC) Program.** SB 855 (Budget and Fiscal Review Committee), Chapter 29, Statutes of 2014, established the state CSEC program to enable county child welfare agencies to provide services to child victims of commercial sexual exploitation. Shortly after the state program was enacted, federal CSEC legislation was enacted with statewide requirements.

- **Relative Caregiver Funding.** Effective January 1, 2015, counties who opted-in to the Approved Relative Caregiver (ARC) Funding Program paid an approved relative caregiver a per child, per month rate, in return for the care and supervision of a federally ineligible Aid to Families with Dependent Children-Foster Care (AFDC-FC) child placed with the relative caregiver, equal to the base rate paid to foster care providers for a federally-eligible AFDC-FC child. With the implementation of CCR, however, the ARC payment will be equal to the home-based family care rate basic level.

- **CCR Clean-Up.** AB 1997 (Stone), Chapter 612, Statutes of 2016, cleans up elements of AB 403 which implemented the CCR effort. This bill includes changes to the requirements for mental health certification of an STRTP and modifications to probation placement oversight, establishes additional protocols around the RFA process, which moves from a pilot program to a statewide mandate in January 2017, and makes other technical changes.

Implementation Update.

Several components of CCR were implemented on July 1, 2015, including the foster family agency social worker rate increase and foster parent recruitment, retention, and support activities for resource families and foster parents. Accreditation of STRTPs and FFAs, and the RFA process in thirteen counties, began on July 1, 2016.

Other implementation activities of the CCR have been split into Phase I and Phase II. Phase I began to implement January 1, 2017, and includes the basic level of the rate paid to families and the series and supports components of the FFA payment, the utilization of CFTs, and the remainder of counties beginning to use the RFA process. Phase II is slated to implement on July 1, 2017, and includes all levels-of-care (LOCs) of the HBFC rate structure.

However, implementation is an ongoing, evolving effort that will take at least several years to fully and successfully roll out all components.

GOVERNOR'S PROPOSALS

The 2017-18 Governor's budget proposes $217.3 million ($163.2 million General Fund) to continue implementation of CCR activities.

The table below provides a detailed breakdown of the proposed funding.

Continuum of Care Reform (CCR) Summary*

The CCR has costs listed in several sections in the budget tables. This chart provides a consolidated view of all of the costs included in the budget tables for FY 2016-17 and FY 2017-18 for the CCR.

(in 000's)

	2017-18 Governor's Budget					
	FY 2016-17			FY 2017-18		
Item	Total	Federal[1]	Non-Federal	Total	Federal[1]	Non-Federal
Home-Based Family Care Rate	$22,212	$1,117	$21,095[2]	$10,574	-	$10,574[3]
Foster Family Agency – Social Worker Rate Increase	$3,786	-	$3,786	-	-	-
Accreditation	$2,827	$1,414	$1,413	$2,827	$1,414	$1,413
Contracts	$10,485	$4,929	$5,556	$11,925	$5,650	$6,275
Second Level Administration Review	$29	$6	$23	$62	$12	$50
Child and Family Teams	$27,441	$5,423	$22,018	$54,399	$10,643	$43,756
Foster Parent Recruitment, Retention and Support	$54,729	$11,469	$43,260	$57,080	$13,913	$43,167
Automation	$500	$250	$250	-	-	-
RFA	$12,042	$4,012	$8,030	$24,904	$8,169	$16,735
SAWS	$6,101	$3,550	$2,551	-	-	-
CDSS Local Assistance Total	**$140,152**	**$32,170**	**$107,982**	**$161,771**	**$39,801**	**$121,970**

Note:
1 Federal Title IV-E funds are not included for the CDSS Title IV-E California Well-Being Project Counties, as federal funds for the Project are capped.
2 Includes $34,000 of county funds for Kin-GAP cases.
3 Includes $94,000 of county funds for Kin-GAP cases.

The table below provides a high-level summary of changes between the 2016-17 Budget Act and the 2017-18 Governor's budget:

Continuum of Care Reform (CCR)

Funding (In Millions)	FY 2016-17 Appropriation	FY 2016-17 Revised Budget	FY 2017-18 Governor's Budget	FY 2016-17 Change From Appropriation	FY 2017-18 Change From Appropriation
Total	$152.7	$140.2	$161.8	-$12.5	$9.1
Federal	$33.3	$32.2	$39.8	-$1.1	$6.5
State	$119.3	$107.9	$121.9	-$11.4	$2.6
County (Reimb.)	$0.1	$0.1	$0.1	$0	$0

ISSUES TO CONSIDER

Ensuring access to mental health services. Providing mental health services for foster youth is a key component of CCR, and one that requires intensive and ongoing coordination between the DSS and the Department of Health Care Services (DHCS), as well as local child welfare and mental health services agencies. Mental health services must also be trauma-informed, and many involved in providing these mental health services to foster youth still need education and training in trauma-informed therapies. The Legislature should closely monitor how this collaboration is working and whether foster children are receiving appropriate access to necessary mental health services.

What do the final level-of-care protocol and assessment tools look like? The LOC protocol is designed to be used by county child welfare and probation staff to identify the care and supervision needs of a foster child. The assessment tool will be used to inform placement and LOC decisions made by the CFT. These two critical pieces are not yet finalized or available to the public. The LOC protocol is still in draft form and receiving feedback from stakeholders and has an assumed release of February 2017. The two assessment tools being tested – Treatment Outcome Package (TOP) and the Child and Adolescent Needs and Strengths (CANS) – are still in a pilot phase in select counties, and a recommendation for a single statewide assessment tool is expected in spring of 2017. Given that the utilization of the HBFC rate structure is based around these tools, it is important that the Legislature review these tools carefully and ensure that they work to further the overall goals of the CCR.

Taking a closer look at the new rate structure. Last year, the release of the rate structure was delayed until the May Revision process. The Legislature and advocates were concerned that there had not been sufficient time to review the new rates, and approved the new rate structure with the intent to revisit the rates in the 2017-18 budget cycle. The Legislature should make it a priority to discuss with both the department and advocates how the rates have been received by those implementing them, and consider whether or not the new rate structure is appropriate to support the CCR.

Monitoring consistency and outcomes across counties. There are so many moving pieces to CCR and so much discretion among counties, it is important that DSS give clear and timely guidance to counties so that CCR can be implemented as uniformly as possible across the state. The Legislature needs to make sure that DSS is also monitoring CCR implementation across counties and has a plan for ensuring consistency so that all foster youth share in the benefits of the CCR. The Legislature should also consider if there are specific goals that they would like monitored, and revisit what kind of data would be helpful in measuring the CCR's overall success. For example, tracking of recruitment and retention of home-based family care options and how successful counties are spending those dollars is important, as home-based care is the centerpiece of CCR.

Looking out for special populations. Among foster youth, there are many subpopulations that face even more obstacles than a typical foster youth, including the CSEC population, homeless youth, and probation youth. Also, among caregivers, relatives are a unique population that need special consideration to ensure they receive adequate support, as they are another critical key in the overall goals of CCR. The Legislature should make sure the department has separate plans to monitor how these populations are doing and has the flexibility within CCR to make adjustments to help these populations if they are identified as needing help.

California Work Opportunity and Responsibility to Kids: Program Update

BACKGROUND

California Work Opportunities and Responsibilities to Kids (CalWORKs), the state's version of the federal Temporary Assistance for Needy Families (TANF) program, provides cash assistance and welfare-to-work services to eligible low-income families with children. In relatively short matter of time, CalWORKs has undergone several major programmatic changes and restructuring. This section will consider the impact of those program changes.

Caseload trends. Prior to federal welfare reform in the mid-1990s, California's welfare program was providing aid to more than 900,000 families. By 2000, the caseload had declined to 500,000 families. During the recent recession the caseload grew, but at an estimated 563,500 families in 2012-13, it was not anywhere close to the levels of the early 1990s. Most recently, the 2016-17 caseload is projected to decline by 6.5 percent from the previous year to 463,000 average monthly cases.

Child-Only Caseload. In more than half of CalWORKs cases (called "child-only" cases), the state provides cash assistance on behalf of children only and does not provide adults with cash aid or welfare-to-work services. There is no time limit on aid for minors.

Welfare-to-Work (WTW) program. Adults eligible for CalWORKs are subject to a lifetime limit of 48 months of assistance. Unless exempt for reasons such as disability or caregiving for an ill family member, adults must participate in work and/or other welfare-to-work (e.g., educational) activities. Depending on family composition, these activities are required for 20, 30, or 35 hours per week. The program also offers supportive services, such as childcare and housing support. Effective January 1, 2013, clients are subject to the the WTW 24-month clock, which provides 24 months of flexibility around how to meet work requirements, but after the initial 24-months, imposes stricter work requirements to receive assistance, and a limit on the number or recipients who can participate in the second 24-month period.

Federal Context and Work Participation Rate. Federal funding for CalWORKs is part of the TANF block grant program. TANF currently requires states to meet a work participation rate (WPR) for all aided families, or be penalized by a reduction of their block grant. States can, however, reduce or eliminate penalties by disputing them, demonstrating reasonable cause or extraordinary circumstances, or planning for corrective compliance. It is also important to note that federal formulas for calculating a state's WPR have been the subject of much criticism. For example, the federal government does not give credit for a significant number of families who are partially, but not fully, meeting hourly work requirements.

CalWORKs child care. CalWORKs participants are eligible for child care if they are employed or participating in WTW activities. CalWORKs child care is administered in three stages:

- Stage 1. Provides care to CalWORKs families when first engaged in work or WTW activities, and is provided by the Department of Social Services (DSS).

- Stage 2. Once counties deem the family "stable," CalWORKs families move to this program. Families remain in Stage 2 until they have not received assistance for two years. The California Department of Education (CDE) administers this program.

- Stage 3. Families transition to this program after Stage 2. CDE also administers this program.

Stages 1 and 2's services are considered entitlements, whereas Stage 3's services are available based on funding levels. Families receiving CalWORKs assistance, those considered "safety net," or families who are sanctioned are not required to pay family fees.

Major Program Changes.

Welfare to Work. SB 1041 (Budget and Fiscal Review Committee), Chapter 47, Statutes of 2012 made significant changes to CalWORKs' welfare-to-work rules, including:

- Creation of a 24-month time limit with more flexible welfare-to-work activities (including employment, vocational education; job search; job readiness; job skills training; adult basic education; secondary school; or barrier removal activities) before the time limit has been reached, and stricter requirements afterward (up to 48 total months).

- A two-year phase-out of temporary exemptions from welfare-to-work requirements for parents of one child from 12 to 24 months old or 2 or more children under age 6, along with a new, once in a lifetime exemption for parents with children under 24 months.

- Changes to conform state law to the number of hours of work participation (20, 30, or 35, depending on family composition) required to comply with federal work requirements.

Counties may provide extensions of the more flexible rules for up to six months for up to 20 percent of participants. This 20 percent extender is not a cap, but a target.

Early Engagement Strategies. SB 1041 also required DSS to convene stakeholder workgroups to inform the implementation of the above changes, as well as the following three strategies intended to help recipients to engage with the WTW component, particularly given the new time limits and rule changes:

- Expansion of subsidized employment. Under subsidized employment, counties form partnerships with employers, non-profits, and public agencies to match recipients with jobs. Wages are fully or partially subsidized for six months to a year.

- Family stabilization. Family stabilization (FS) is intended to increase client success during the flexible WTW 24-Month Time Clock period by ensuring a basic level of stability for clients who are especially in crisis, including intensive case management and barrier removal services. Clients must have a “Stabilization Plan” with no minimum hourly participation requirements. Six months of clock-stopping is available, if good cause is determined.

- Online CalWORKs Appraisal Tool (OCAT). OCAT is a standardized statewide WTW appraisal tool that provides an in-depth assessment of a client’s strengths and barriers, including: employment history, interests, and skills; educational history; housing status and stability; language barriers; child health and well-being; and, physical and behavioral health, including, but not limited to, mental health and substance abuse issues.

Eligibility for individuals with previous felony drug convictions. SB 855 (Budget and Fiscal Review), Chapter 29, Statutes of 2014 expanded eligibility for adults who were previously ineligible for benefits due to a prior felony drug conviction, and implemented on April 1, 2015.

Housing and homeless assistance. In the last several budgets, housing and homeless assistance has received more attention and funding as people have become more aware that the lack of affordable housing impacts many CalWORKs recipients.

- The CalWORKs Housing Support Program (HSP) was established in 2014 to provide evidence-based interventions (such as rapid-rehousing) to CalWORKs families that are homeless or at risk of homelessness. Other core components of HSP include housing identification, rent and moving assistance, and focused case management. HSP was augmented in the last two budget cycles.

- The Homeless Assistance Program (HAP) provides a once-in-a-lifetime payment to meet the reasonable costs of obtaining permanent housing, and/or temporary shelter while seeking permanent housing. A typical family is eligible to receive benefits of up to $65 per night for 16 consecutive days of temporary shelter while searching for permanent housing. Families may also be eligible to receive up to two months of rental assistance in order to obtain permanent housing or two months of rental arrearages to prevent eviction. The 2016-17 budget eliminated the HAP the once-in-a-lifetime ban and allows a family to receive HAP assistance once in a 12 month period while maintaining existing exceptions for domestic violence and when existing housing becomes uninhabitable.

Maximum Family Grant (MFG) Repeal. The 2016-17 budget repealed the Maximum Family Grant, a rule which stipulated that a family’s maximum aid payment would not be increased for any child born into a family that had received CalWORKs for ten months prior to the birth of a child. Now, cash grants will be increased to include any child who was not receiving cash assistance because of the MFG. The repeal of the MFG is funded both through revenues in the Child Poverty and Family Supplemental Support Subaccount, which also funds maximum aid payment (MAP) increases, and the General Fund.

Automation. The Statewide Automated Welfare System (SAWS) Consortia is made up of multiple systems which support such functions as eligibility and benefit determination, enrollment, and case maintenance at the county level for some of the state's major health and human services programs, including CalWORKs and CalFresh. The Consortia includes the Los Angeles Eligibility, Automated Determination, Evaluation, and Reporting (LEADER) system, which is now being replaced by the LEADER Replacement System (LRS), the Welfare Client Data System (CalWIN), and Consortium IV (C-IV), which are managed by the Office of Systems Integration (OSI).

- **C-IV Migration into Leader Replacement System (LRS).** In September 2015, Los Angeles County began to rollout LRS, their new eligibility determination system. As of November 2016, the LRS Project has successfully completed countywide implementation for the Department of Public Social Services (DPSS) and the Department of Children and Family Services (DCFS). In addition, C-IV counties (which is another system in the SAWS consortia, and includes 39 counties), will begin migrating over to the LRS system. This migration is expected to be complete in 2019-20.

- **Horizontal Integration of SAWS and CalHEERS.** The goal of the Horizontal Integration effort between the Covered California system (CalHEERS) and SAWS is to allow an applicant applying for health coverage online through Covered California to submit their CalWORKs or CalFresh application online at that time without having to re-respond to some of the questions already asked.

- **Welfare Data Tracking Implementation Project (WDTIP).** The WDTIP provides counties with the automated functionality required to conform to the statewide tracking of time-on-aid requirements, and tracks the 48 and 60-month assistance clock, the 24-month services clock, and WTW exemptions and sanctions.

Monitoring results and outcomes. In July 2014, the RAND Corporation launched a multiyear, evaluation to explore if CalWORKs programmatic reforms achieve desired objectives and report on any unintended consequences. The final report should be completed by early 2018. Initial findings, presented in December 2016, suggest that while the flexibility of SB 1041 changes is generally viewed as positive, CalWORKs participants and welfare staff still struggle to understand the complexities of the 24-month time clock. Findings also indicate that full implementation of SB 1041 components is still underway.

GOVERNOR'S PROPOSAL

The Governor's budget proposes no major programmatic or funding changes to CalWORKs. The budget includes $5.4 billion in federal, state, and local funds for the program, and estimates an average monthly caseload of 459,000 families for 2017-18.

ISSUES TO CONSIDER

Evaluation of early engagement strategies.

- What can the OCAT data tell us about CalWORKs recipients and their needs? How can we use this data to better serve recipients? Are there any obstacles for counties or the state in obtaining or utilizing OCAT data?

- How many subsidized employment placements have led to long-term, living-wage employment? What are counties doing to reach out to local business partners?

- Has the utilization of family stabilization resources increased? How have counties used family stabilization funds?

- Given the flexibility of the activities under the 24-month clock, it was expected that participation would increase in adult education or vocational training. Has this occurred? Why or why not?

What are the state's long-term goals in implementing these types of changes to CalWORKs? What measures, besides the WPR, does the state use or plan to use to determine the success of this program? As these early engagement components of the CalWORKs program begin to see a return of data and increased utilization, the Legislature may wish to consider the best way to use this data, and what outcomes they would like to see, to improve CalWORKs overall.

Do the existing automation systems for CalWORKs adequately support the state and counties' ability to collect data and evaluate the program? Automation for CalWORKs, including program management and utilization data, spans across many different IT systems. The Legislature should continue to monitor these systems, and consider how they can work together or be built upon to provide information on how the program is performing and meeting its goals.

SUBCOMMITTEE NO. 4

STATE ADMINISTRATION and GENERAL GOVERNMENT

State Administration and General Government

Cannabis Regulation

BACKGROUND

The statutorily authorized use of medical cannabis was approved in California in 1996 when voters approved Proposition 215, the Compassionate Use Act (CUA). The CUA provides certain Californians the right to obtain and use cannabis for medical purposes, as recommended by a physician, and prohibits criminal prosecution or sanction against physicians who make medical cannabis recommendations.[1] In 2003, Senate Bill 420 (Vasconcellos), Chapter 875, Statutes of 2003, established the Medical Cannabis Program under the California Department of Public Health, and created a medical cannabis identification card and registry database to verify qualified patients and primary caregivers.

Since 2003, advocates, patients, and local governments recognized some deficiencies in the oversight of medical cannabis and called for additional safety regulations. In June 2015, Governor Brown signed the Medical Marijuana Regulation and Safety Act, comprised of Assembly Bill 243 (Wood), Chapter 688, Statutes of 2015; Assembly Bill 266 (Bonta), Chapter 689, Statutes of 2015; and Senate Bill 643 (McGuire), Chapter 719, Statutes of 2015. The act was later renamed the Medical Cannabis Regulation and Safety Act (MCRSA). Together, these bills established the oversight and regulatory framework for the cultivation, manufacture, transportation, storage, and distribution of medical cannabis in California.

With California having the largest economy in the U.S., many advocates called for the legalization of recreational use of cannabis, predicting an increase of hundreds of millions of dollars in state revenue. In November 2016 voters approved Proposition 64, or the Adult Use of Marijuana Act (AUMA). AUMA legalized nonmedical, adult use of cannabis in California. Similarly to MCRSA, the act creates a regulatory framework for the cultivation, manufacture, transportation, storage and distribution of cannabis for nonmedical use. Below is a table that summarizes the various provisions of MCRSA and AUMA across departments.

[1] Health and Safety Code §11362.5

Cannabis Regulation
Responsibilities by Department

Department	Tasks Assigned by MCRSA	Tasks Assigned by AUMA
Department of Consumer Affairs	License dispensaries, distributors, testing laboratories, and transporters.	License dispensaries, distributors, and microbusinesses.
Department of Fish and Wildlife	Expand its pilot project to address the environmental impacts of cannabis cultivation.	Expand pilot project to a statewide level and make project permanent.
State Water Resources Control Board	Authorized to address waste discharge resulting from cannabis cultivation.	Authorized to address waste discharge resulting from cannabis cultivation.
Department of Food and Agriculture	License indoor and outdoor cultivation sites. Ensure water diversion and discharge from cultivation does not affect instream flows for fish spawning, migration, or rearing. Establish a medical cannabis cultivation program, with specified criteria. Establish program that identifies a permitted medical cannabis plant by a unique identifier. Develop a separate "track-and-trace" system to report movement of commercial products through distribution.	License indoor and outdoor cultivation sites. Ensure water diversion and discharge from cultivation does not affect instream flows for fish spawning, migration, or rearing. Establish a cannabis cultivation program. Implement a unique identification program for retail cannabis and cannabis products. Expand "track-and-trace" system to include the same level of information for nonmedical products.
Department of Public Health	License cannabis manufacturers. Develop regulations for producing and labeling of cannabis products.	License cannabis manufacturers and testing sites.
Department of Pesticide Regulation	Develop cultivation regulations for pesticide use.	Develop cultivation regulations for pesticide use.

Most departments will have the same responsibilities under MCRSA and AUMA, but there are some differences. For example, the Department of Consumer Affairs is responsible for licensing testing laboratories for medical cannabis, while the Department of Public Health is responsible for licensing testing laboratories for recreational use.

Licensing and fees. Licensing authorities must establish a scale of application, licensing, and renewal fees. The licensing and renewal fees are calculated to cover the costs of regulatory activities and are set on a scaled basis depending on the size of the business. All fees are deposited into an account specific to that licensing authority, which will be established within the Cannabis Control Fund. There are a total of 17 different types of licenses for medical cannabis businesses, while AUMA lists 19 different license types.

Local control. Cities and counties may regulate all cannabis businesses and require them to obtain local licenses. Cities and counties may ban cannabis-related businesses, but not cannabis transportation through their jurisdictions. Unlike medical business, recreational cannabis businesses are not required to have a local license (unless a local jurisdiction takes action to require local licensure), but must abide by local ordinances in order to obtain a state license. Local authorities must send notice to the Bureau of Marijuana Control, or relevant licensing authority, when they revoke a cannabis license.

Penalties and Violations. State law authorizes a civil penalty of up to twice the amount of the license fee for each violation relating to the use of medical cannabis, and a civil penalty of up to three times the amount of the license fee for violations relating to commercial cannabis. The department, state, local authority, or court may also order the destruction of the cannabis associated with the violation. Statute establishes different locations for where the penalties will be deposited, depending on whether the Attorney General, district attorney or county counsel, or a city attorney or city prosecutor brings forth the action.

Taxes. AUMA instituted a new state tax on the cultivation of cannabis that enters the commercial market, as well as a new state retail excise tax. Both of these taxes would affect medical and nonmedical cannabis. AUMA eliminated sales tax on medical cannabis, but recreational cannabis would be subject to existing state and local sales tax. Revenues from these new taxes would be deposited into a new special fund, the California Cannabis Tax Fund. The fund would first be used to reimburse state agencies for cannabis-related regulatory costs, and remaining funds would be distributed as follows:

- $10 million annually, until 2028-29, to evaluate effects of recreational cannabis use.
- $3 million annually, until 2022-23, to develop methods to determine whether an individual is driving impaired.
- $10 million in 2018-19, with a $10 million increase annually until 2022-23, and $50 million annually afterward for a grant program to provide services to communities most affected by past drug policies.
- $2 million annually to study hazards and values of medicinal cannabis.
- After the above allocations, remaining funds would be apportioned as follows: 60 percent for youth programs, 20 percent to mediate environmental damage from cannabis cultivation, and 20 percent for programs to reduce impaired driving and a grant program to reduce negative public health impacts.

GOVERNOR'S PROPOSAL

The budget includes $52.2 million to fund regulatory activities, license processing, and enforcement. Loans from the General Fund have provided initial funding for support of regulatory activities, as licensing fees will not be collected until January 1, 2018. The budget includes several proposals across different departments, including:

- **Department of Food and Agriculture (CDFA) –** The budget proposes $22.4 million and 51 positions to provide administrative oversight for the Cannabis Cultivation Program, establish regulations, issue cannabis cultivation licenses, and perform an environmental impact report. Also, CDFA, with the California Department of Technology and the Board of Equalization, will establish a track and trace program to report the movement of products throughout the distribution chain.

- **Department of Consumer Affairs (DCA) –** The budget includes $22.5 million and 120 positions to augment the Bureau of Marijuana Control, formerly the Bureau of Medical Cannabis Regulation, within DCA.

- **Department of Public Health (CDPH) –** The budget includes $1.4 million for licensing and regulation of medical cannabis product manufacturers.

- **Board of Equalization –** The budget includes $5.3 million and 22 positions to notify businesses of new tax requirements and to update information technology systems. The Board of Equalization is required to administer an excise tax on cannabis sales and a cultivation tax on harvested cannabis that enters the commercial market.

- **Department of Health Care Services –** The budget includes $5 million in 2016-17 for establishing and implementing the public information program that will cover health related topics pertaining to cannabis. The program is to be established and implemented no later than September 1, 2017.

ISSUES TO CONSIDER

Impending deadlines. The Bureau of Marijuana Control, along with other licensing entities, will be responsible for 17 different types of medical cannabis business licenses, including: cultivators, nurseries, processors, testing labs, dispensaries, and distributors. With the passage of AUMA licensing authorities have been charged with issuing 19 other license types for recreational use. The bureau must begin issuing licenses by January 1, 2018, and will need to have regulations in place prior to issuing licenses. To meet this deadline, DCA has already held meetings with other licensing entities, and has educated staff and the public about the new law, including: holding educational tours of cannabis businesses, seeing demonstrations on the track and trace systems, and receiving expert presentations. Pre-regulatory stakeholder meetings were held in September and October of 2016. However, these meetings only related to MCRSA, as AUMA was not approved by voters until November. Even though some of the regulatory framework for medical cannabis can be applied to nonmedical cannabis, there are significant differences that require a different regulatory approach. January 1 is an ambitious timeline for departments to finalize regulations, specifically relating to nonmedical cannabis use, and set up information technology (IT) systems to administer such a large and complex program.

Given the impending deadline, and the lack of recent precedent for establishing an oversight and regulatory scheme of this magnitude,[2] the Legislature may wish to consider the following oversight questions during the subcommittee process:

- As the bureau may begin issuing licenses on January 1, 2018, will the bureau be accepting applications for licenses before that date? If so, is the bureau currently equipped to handle intake of those applications?

- The bureau, CDFA, and CDPH are all charged with various licensing duties and may have different IT systems to handle licenses. Are these departments collaborating to ensure that their systems work with the others?

- How will DCA and other relevant licensing authorities regularly update the Legislature on the regulatory development process?

- What will happen if state agencies are unable to meet the January 1, 2018 deadline?

Dual regulatory frameworks. The passage of Proposition 64 created two different systems for medical and nonmedical cannabis regulation. While there are similarities between the systems, there are also differences. Under MCRSA, license applicants are not subject to residency requirements, and licensing authorities do not evaluate special market considerations when issuing a license. Both of these conditions are requirements for granting licenses for recreational cannabis businesses. Restrictions on vertical integration, or businesses possessing multiple license types, were enacted by MCRSA, but no such restrictions were implemented by AUMA. Further, medical cannabis regulations require businesses to obtain both a state and local license to operate, while only a state license is needed to operate a recreational business. However, recreational businesses must abide by local zoning and other requirements. Many state agencies and businesses, especially businesses that produce both medical and nonmedical products, will likely be confused by these conflicting regulations.

Merging these two frameworks into one may alleviate confusion, and allow more efficient regulation by state agencies. However, there may be merit to keeping the two structures separate. As the sale and distribution of cannabis is illegal under federal law, federal prosecutors may choose to take action against cannabis operations, thus affecting the cannabis industry in California. If there is no distinction between these two structures, then the medical cannabis industry may be affected as well. The Legislature may wish to weigh the benefits and risks of having two different sets of regulations for medical and nonmedical use of cannabis.

[2] The last bureau to be created under DCA was the Professional Fiduciaries Bureau, established in 2007, which only licenses approximately 600 individuals.

Tax Revenue. Beginning January 1, 2018, a new excise tax on cannabis and cannabis products, and a new tax on cannabis cultivation will be imposed. Revenues from these new taxes will be apportioned for various purposes, as mentioned above. Even though taxes have not begun to be collected, many organizations are hoping to receive a share of that funding. AUMA broadly defines how these taxes are to be allocated, but does not specify particular groups or programs for funding. The Legislature may wish to start the discussion around distributing funding and directing departments in how to assign funding to various programs.

California's Veterans' Homes

BACKGROUND

California has more veteran residents than any other state in the country. 1.8 million veterans live in California, over half of whom are over the age of 60. The largest share is veterans of the Vietnam era, and most veterans reside in southern California. The California Department of Veterans Affairs (CDVA) is the agency responsible for statewide veterans' services. A primary responsibility of CDVA is to provide qualified veterans with long-term residential care at one of the eight Veterans Homes of California (VHC), located in Barstow, Chula Vista, Fresno, Lancaster, Redding, Ventura, West Los Angeles, and Yountville. Each home is distinctive and offers unique amenities, healthcare options, and a range of activities. All eight homes have the combined resources to house and care for close to 3,000 veterans. Residents of California who are homeless, aged or have a disability, and were discharged from active duty under honorable conditions are eligible for admission. Spouses of veterans are also eligible for admission, under specific circumstances. Distinguished, wartime veterans and homeless veterans often receive prioritized admission to the homes. VHC residents pay a fee, unless they are low-income or have no income. CDVA is currently in the process of revising regulations that limit the amount of fees VHCs may collect based on a resident's income.

The Yountville home, established in 1884, is the oldest veterans' home in California, and is the largest geriatric facility in the country. The establishment of subsequent VHCs was spurred by legislation in the 1990s, and again in the early 2000s. Homes in West Los Angeles, Barstow, and Chula Vista were the result of the 1990s legislation. The Veterans Bond Act of 2000 specified the building of additional homes in Lancaster and Ventura. In 2004, the Legislature provided funding for the remaining homes in Redding and Fresno.

Levels of Care. The homes are a system of residential care facilities offering a comprehensive plan of medical, dental, pharmacy, rehabilitation services, and social activities within a community environment. VHCs offer up to four levels of care: domiciliary (independent living), residential, intermediate nursing, and skilled nursing. The homes provide medical care, meals, personal care services, therapeutic activities, recreational events, and some transportation for residents.

Veterans Homes of California
Capacity and Level of Care Summary

Campus	Physical Capacity	Budgeted Capacity	Skilled Care	Intermed. Care	Residential Care	Domiciliary
Yountville	1,184	1.021	x	x	x	x
Barstow	400	220	x	x		x
Chula Vista	400	305	x		x	x
West LA*	396	370	x		x	x
Ventura	60	60			x	
Lancaster	60	60			x	
Redding	150	150	x		x	
Fresno	300	296	x		x	
TOTAL	2,950	2.482				

*The West LA campus offers a Transitional Housing Program for veterans. Participants in that program are included in this count.

Specialized Services. Some VHCs provide specialized memory care and transitional housing. The Redding, Fresno, West Los Angeles, and Yountville locations have skilled nursing units focused on memory care. These programs provide supervised environments for veterans who have difficulty making decisions, solving problems or participating in conversations, and symptoms of confusion and memory loss. The transitional housing program at the West Los Angeles VHC is administered in collaboration with the U.S. Department of Veterans Affairs (USDVA). It provides supportive services for frequently homeless veterans and veterans living in unstable housing, and prepares them to maintain a stable living situation.

GOVERNOR’S PROPOSAL

The Governor’s budget proposes total spending of $335.4 million ($306.8 million General Fund) for VHC operations. This is a $6 million dollar decrease from 2016-17 expenditures. Funding is partially offset by reimbursements from USDVA, Medi-Cal, Medicare, and member fees. There were no significant budget changes related to VHCs in the Governor’s budget.

Expenditures for Individual Homes
(Dollars in Thousands)

Campus	Expenditures
Yountville	$96,386
Barstow	$24,008
Chula Vista	$36,002
West LA	$67,568
Ventura	$10,473
Lancaster	$10,472
Redding	$33,976
Fresno	$56,496
TOTAL	$335,381

ISSUES TO CONSIDER

Lack of data. In January 2017, the Legislative Analyst's Office (LAO) released a report summarizing veterans' services in California. The original legislative statement of intent that directed the LAO to compile the report had to be amended once work on the report had begun. Originally, the report was to focus on the role of veterans homes in the 21st century. Much of the data on veterans comes from the USDVA and lacks information on veterans' movements after discharge from service. The LAO determined that there was a lack of available data and the reporting language was revised to direct the LAO to review federal and state veterans' services in specific areas. Before the Legislature can discuss the future of veterans' homes, more data needs to be collected. The Legislature may want to discuss efficient methods for collecting data.

Shifting needs for levels of care. Due to the aging veteran population there is an increased need for skilled nursing and memory care. Wait-lists for these levels of care are the two longest. Many administrators are concerned about not being able to transition residents to the skilled nursing care they need due to the lack of beds. Related to this concern is the changing landscape of long-term care. Historically, veterans have entered homes at domiciliary care and moved up to higher levels as needed. In recent years the long-term care landscape has been shifting towards community-based care and more veterans are choosing to stay in the community for as long as possible. These veterans then move into VHCs at higher levels of care, placing additional strain on capacity for skilled nursing and memory care.

The Legislature may wish to consider how VHC will adapt to the changing demands for levels of care. A specific recommendation from the LAO suggests directing CDVA to assess the location and number of beds that could reasonably be converted into higher levels of care. The Legislature may also want to consider whether some services can be shifted to community-based resources, possibly making room to address demands for higher levels of care. A prioritization of admissions to VHCs may also address these issues, as suggested in the LAO report. The Legislature may consider options for community services, and give precedence to individuals who have fewer community options. Another option is to first focus on veterans receiving skilled nursing services and with a highly rated service-connected disability, capturing those with the most need and drawing in more federal reimbursements for their care.

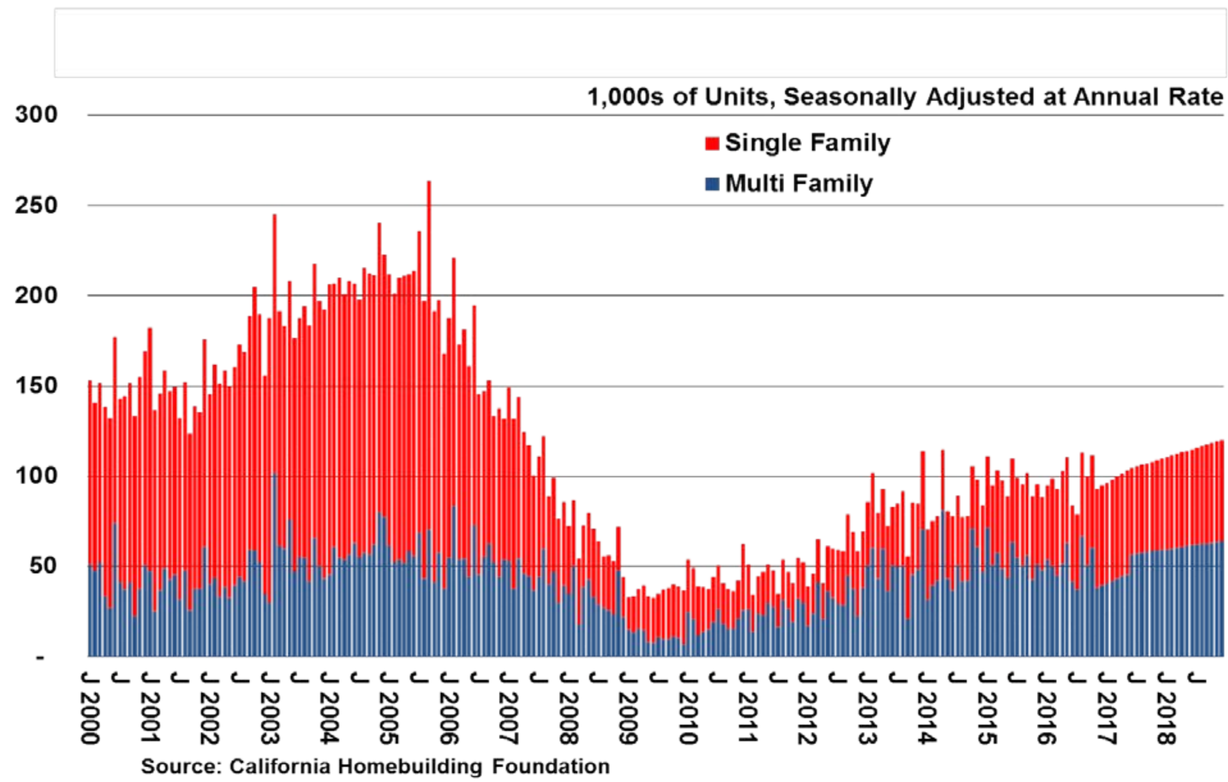
Staff recruitment, retention, and ratios. Administrators at VHCs often experience difficulties in finding and keeping staff. In locations with high competition for entry level staff, individuals will most likely choose higher paying jobs. Staff are state employees, thus VHCs are limited in their ability to make wage changes. Location is another challenge for recruiting staff. Entry level staff may not be able to afford to live in areas with a high cost of living (Yountville, for example), keeping them from accepting jobs at those homes. Issues with staff recruitment also lead to challenges with staff ratios. Overtime mandates and high overtime usage are likely symptoms of staffing challenges. The Legislature may wish to address staffing issues in VHCs, discussing steps that can be taken to enhance recruitment and retention.

Affordable Housing

BACKGROUND

California's high cost of housing is well documented. The Department of Housing and Community Development (HCD) estimates that California built an average of 80,000 new homes a year over the last ten years. However, the department projects that the state will need to produce 180,000 new homes a year between 2015 and 2025 to keep up with housing demand. This undersupply, combined with a growing economy, has pushed housing prices upwards and created a significant affordability gap for many Californians. The figure below illustrates the low housing construction rate in the state.

Housing Construction Permits
2000-2018 (Projection)



The Housing Affordability Gap

Housing affordability depends on both housing prices and household income. According to the US Department of Housing and Urban Development (HUD), housing is considered affordable when a person pays no more than 30 percent of income for housing costs, including utilities. When a person pays more than 30 percent of income they are considered housing cost burdened; when they pay more than 50 percent they are considered severely housing cost burdened. Income categories are used to analyze housing affordability because they allow an analysis of similar households adjusted for regional variations. HCD's analysis uses an area's mean income (AMI) to analyze housing affordability. Low-income households are defined as less than 80 percent of an area's AMI (with extremely low-income households having 0-30 percent of AMI), moderate income households as 80 – 120 percent AMI, above moderate income households as greater than 120 percent AMI. The figure below quantifies the number of households in each category experiencing rent burden in California.

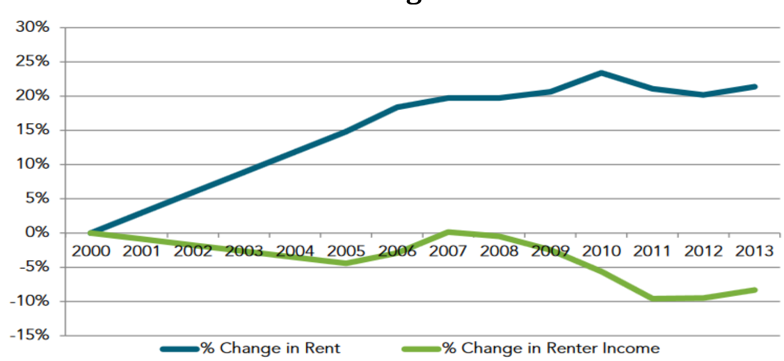
Percentage of California's Renters Experiencing Rent Burden By Income Category

Income	Total Renter Households (million)	% Rent Burdened	% Severely Rent Burdened
Extremely Low-Income	1.27	90%	80%
Very Low-Income	.95	87%	51%
Low Income	1.11	65%	18%
All Lower-Income Renter Households (80% AMI and below) **Subtotal of above**	3.33	81%	51%
Moderate-Income	1.03	35%	4%
Above Moderate-Income	1.54	8%	0%
All Renter Households Total	5.9	54%	30%

Source: 2016 National Low-Income Housing Coalition tabulations of 2014 American Community Survey Public Use Microdata Sample (PUMS) housing file.

Despite the economic recovery that has occurred since the 2008 financial crisis, incomes have not kept pace with housing costs. This issue is particularly acute among renters, who are typically lower income than homeowners. This dynamic has increased the proportion of Californians who are either housing cost burdened or severely housing cost burdened. The figure below highlights the growing gap between income and rental costs.

Renter Income vs. Rental Costs 2000 through 2013



Source: California Housing Partnership analysis of 2000 Decennial Census and 2005-2013 American Community Survey 1 year data. 2001-2004 are an estimated trend. Graphic recreated by HCD.

The affordability issue has become a national problem over the last several years. The National Low Income Housing Coalition estimates that, nationwide, the supply of affordable rental homes can only accommodate 31 of 100 extremely low-income renter households. In California, the current supply of rental housing can only accommodate 21 of every 100 extremely low-income renter households.

The increasing rental burden in California is mirrored in homeownership, where median home prices have increased from $370,405 in 1991 to $526,580 in August of 2016 (adjusted to 2015 dollars). This has resulted in a significant decline in home affordability. According to HCD, as of the first quarter of 2016, California Association of Realtors estimates that only 34 percent of households in California can afford to purchase the median-priced home in the state. The California homeownership rate is currently 53.7 percent, the lowest since the 1940s.

Current Housing Policies

A variety of federal, state, and local policies aim to help close the housing affordability gap in the state. These normally take one of three approaches to the problem: (1) increasing the supply of affordable housing, (2) paying a portion of household rent costs, and (3) limiting the price and rents property owners may charge for housing.

- **Increasing the Supply of Affordable Housing.** The federal and state governments both provide a variety of direct financial assistance, typically tax-credits, grants, or low-cost loans, directly to housing developers for the construction of affordable rental housing. The largest of these programs is the federal and state Low Income Housing Tax Credit (LIHTC), which provides tax credits to affordable housing developers. The LAO estimates that the LIHTC subsidizes the construction of roughly 7,000 units of new housing per year.

- **Paying a Portion of Household Rent Costs.** The federal government makes payments to landlords, known as housing vouchers, on behalf of low-income households in California. These payments generally cover the portion of a renting household's monthly cost that exceeds 30 percent of that household's income.

- **Limiting the Price and Rents Property Owners May Charge.** Some local governments have policies that require property owners to charge below-market rate rents, or that limit the amount landlords can raise rents by in any single year. In most cases, these housing units are then limited to low-income renters. About 15 cities in California currently have such rent control laws, and the California Housing Partnership Corporation estimates that 478,654 such "deed-restricted" affordable units exist in the state.

Previous affordable housing programs have been largely bond-financed. The state continues to pay debt service on the Housing and Emergency Shelter Trust Fund Act of 2002 (Proposition 46) and the Emergency Shelter Trust Fund Act of 2006 (Proposition 1C). The proceeds provided by these bonds have largely been expended for the construction or rehabilitation of roughly 80,000 affordable housing units. However, the state will also pay roughly $355 million from the General Fund for debt service for these bonds in 2017, part of the estimated $10.7 billion in total debt service for these bonds over their life. Recent state actions have also funded a variety of affordable housing programs, including the No Place Like Home Program, which provides

$2 billion in bond authority for housing for the chronically homeless and mentally ill, supported by Proposition 63 Mental Health Services Act funding. Several housing-related bills were approved in 2016, including bills that streamlined approvals for accessory dwelling units and provided density bonuses for affordable housing developers.

GOVERNOR'S PROPOSAL

The Administration's budget proposes $3.2 billion for a variety of affordable housing programs. This includes $262 million for the No Place Like Home Program, $1.25 billion for the California Housing Finance Agency's (HFA) Single Family 1st Mortgage Lending Program, roughly $340 million in both federal and state LIHTC, and $75 million for veteran's housing. This does not include the $355 million in General Fund debt service for previously-approved affordable housing bonds.

ISSUES TO CONSIDER

Funding for Affordable Housing Programs Alone May Not Solve Problem
As noted above, HCD estimates that California will require 180,000 new homes per year from 2015 to 2025 to address population growth. However, the state averaged only 80,000 new units per year over the previous ten years. This has resulted in a significant shortage of housing, which has strongly contributed to the current affordability gap. Zoning, land use, and permitting decisions are predominantly made at the local level. While the state may incentivize the planning or construction of additional housing, or streamline the planning and permitting process, the state's ability mandate the construction of housing, affordable or not, is limited.

As noted above, one option the state has is to directly subsidize the construction of additional units of affordable housing. Such an approach is likely to be prohibitively expensive. The LAO estimates that it costs roughly $165,000 to subsidize an affordable housing unit in coastal areas of the state. At this cost, subsidizing construction of affordable homes for the 1.7 million lower-income households HCD estimates to be severely rent burdened would cost the state roughly $280 billion.

Dedicated Funding Source for Affordable Housing
The current approach to funding affordable housing programs suffers from an unpredictable funding situation. Affordable housing programs are largely funded by a patchwork of funding sources, such as state General Fund (which faces competition from a variety of other programs) and bond funds. Rarely does any single housing program provide sufficient resources for a given affordable housing development. This requires developers to pull together funding from a variety of programs and sources, slowing down and injecting significant uncertainty into the development process, while leaving programs that help low-income households defray housing costs with a limited and variable level of funding from year to year. Federal funds have been a consistent feature of housing programs for decades, but have declined significantly in recent years. This unstable funding picture has made it difficult for developers and local governments to plan ahead, creating further barriers to the development of affordable housing. The Legislature

may therefore want to consider creating or setting aside a dedicated funding source for affordable housing to inject some certainty into affordable housing projects statewide.

Federal Funding is Uncertain and Declining

As stated above, federal funds have been a consistent source of funding for affordable housing for decades. However, these funds have declined significantly in recent years. Between 2003 and 2015, the Community Development Block Grant (CDBG) program declined from $730 million to $357 million, while the HOME Investment Partnership Program declined from $351 million to $121 million. This decline is likely to continue under the current Administration. Given this negative outlook, the Legislature may want to consider ways to backfill federal funds to preserve priority programs, including redirecting from other programs or creating a dedicated source of funding for affordable housing programs.

The Lifecycle of an Emergency

BACKGROUND

With 39 million residents, California is the most populous state in the nation, and has the third largest land area among all states. The state is richly diverse culturally, economically, and ecologically. This diversity makes the state vulnerable to numerous risks and threats. Potential threats include hazardous material spills, civil unrest, flood, fire, earthquake, energy disruption, cyber-attack, severe weather, food and/or agricultural emergency, pandemic/epidemic, and dam or levee failure.

California has long been a leader in emergency preparedness. In fact, California's Standardized Emergency Management System (SEMS), which facilitates communication in the event of a disaster, was used as the basis for the National Incident Management System. The role of the California Governor's Office of Emergency Services (Cal OES) is to address risks and threats, maintain a state of readiness, and plan for and mitigate impacts. Cal OES coordinates the state agency response to major disasters in support of local governments, and homeland security activities throughout the state.

California State Warning Center (CSWC). Before an emergency or disaster occurs, officials at multiple levels are monitoring to identify potential threats. This provides an opportunity to increase readiness once an emergency happens. CSWC acts as the central information hub for emergency communications across the state. The center is staffed twenty-four hours a day, seven days a week, and tracks a variety of potential emergencies, not only in California but around the world. CSWC is responsible for informing local governments and the federal government of emergencies. This past year, staff sent out over a million notifications to federal, state, and local government agencies about events that could impact emergency management.

Standardized Emergency Management System. SEMS is the cornerstone of California's emergency management system. It joins all the separate parts of California's emergency management system into an integrated structure and standardizes its elements. State agencies are required to use SEMS and local governments must use SEMS to be eligible for reimbursement under the state's disaster assistance programs. SEMS is organized into five different levels: field, local government, operational area (OA), region, and state. SEMS requires that each level apply the following five functions: management, operations, logistics, planning/intelligence, and finance/administration. The management section provides overall direction and sets priorities for an emergency. Operations implements the priorities established by management. The planning/intelligence section gathers and assesses information. Logistics obtains the resources to support operations, and finance/administration tracks all costs related to operations.

Activation of emergency operation centers. Response activities begin in the field at the local level. Local officials have the primary responsibility to employ emergency plans and take action to mitigate risk. SEMS is utilized when the local government activates its emergency operations center (EOC) and/or a local emergency is declared, as defined in Government Code 8558(c).

Some disasters and emergencies require more resources than a single local government can provide. Neighboring jurisdictions provide assistance in these cases, under mutual aid agreements. When additional assistance is needed, the field alerts the OA. The OA can then manage the need for resources itself or seek assistance through the mutual aid system. County boundaries define OAs. Activation of an OA EOC triggers activation of its regional EOC, which then triggers activation of the state-level EOC. Emergency proclamations by cities, counties, or the governor also trigger activation of the relevant EOCs.

Recovery. As the emergency continues and operational priorities are met, officials begin to consider needs for recovery. Recovery from an emergency is defined as a return to normal activities. Short-term recovery activities include a restoration of services and implementation of infrastructure recovery plans. Long-term activities build on these short-term actions and include facility and infrastructure reconstruction, community planning, assistance to displaced individuals, and integration of mitigation strategies. The private sector, non-governmental organizations, and every level of government may take part in these recovery activities, depending on the magnitude of the incident.

The California Disaster Assistance Act (CDAA) authorizes the director of Cal OES to administer a disaster assistance program that provides financial assistance from the state for costs incurred by local governments as a result of a disaster event. The Recovery Operations unit within Cal OES coordinates local, state, federal and nonprofit partners to provide recovery assistance to individuals and households under the Individual Assistance program; technical assistance to ensure affected jurisdictions receive state and federal support in an efficient and timely manner through the Public Assistance program; and financial reimbursement and technical assistance to affected jurisdictions to mitigate future disaster effects through the Hazard Mitigation Grant program. Disaster assistance programs provide matching fund assistance for cost sharing required under federal public assistance programs in response to a presidential major disaster or emergency declaration.

Standardized Emergency Management System
Levels, Responsibilities, and Conditions for Activation of Emergency Center

Level	Responsibilities	Conditions for Activation of EOC
Field	Tactical decisions and activities in direct response to incident.	An emergency occurs.
Local Government (County, city, or special district)	Manages and coordinates overall response and recovery within jurisdiction.	A local emergency is declared or the local government declares activation is necessary based on the need for more coordinated management of the emergency.
Operational Area	Manages and coordinates resource requests between local governments. Also acts as a link between local governments and regional areas.	1. A local government has activated its EOC and requested activation of the OA EOC. 2. Two or more cities within OA have declared a local emergency. 3. The county has declared a local emergency. 4. The county or cities within the county have requested a Governor's emergency proclamation. 5. The Governor declares a state of emergency for the county or two or more cities within the county. 6. OA has requested resources from outside its boundaries. 7. OA has received resource requests from outside its boundaries.
Regional[1]	Manages and coordinates information and resource requests between operational areas within the mutual aid region, and provides coordination between operational areas and state.	An OA EOC within its region is activated.
State	Manages statewide resource coordination, integrated with federal agencies. Continuously monitors situations and provides reports to state officials as appropriate.	1. A regional EOC is activated 2. The governor proclaims a state of emergency. 3. The governor proclaims an earthquake or volcanic prediction.

[1]California is divided into three regional areas, which are further divided into a total of six mutual aid regions.

Lead Departments in Emergencies and their Duties

Department	Duty
California Department of Transportation and the California Highway Patrol	Manage transportation systems and infrastructure during domestic threats or in response to incidents.
California Department of General Services	Organize the capabilities and resources of the state to facilitate the delivery of services, technical assistance, engineering, expertise, construction management and other support to local jurisdictions. Coordinate emergency use and repair of state facilities and properties.
Cal OES[1]	Perform executive functions to support all phases of emergency management. Support the restoration and maintenance of emergency communication mediums. Monitor the status of fire mutual aid activities, and coordinate support activities related to the detection and suppression of fires and emergency incident scene rescue activities. Provide personnel, equipment, and supplies to support local jurisdictions. Coordinate state law enforcement personnel and equipment to support law enforcement agencies, search and rescue, coroner activities, and public safety. Provide timely, accurate, and coordinated public information to affected audiences.
California Department of Social Services	Coordinate actions to assist jurisdictions in meeting the needs of victims displaced during an incident.
California Department of Public Health and the Emergency Medical Services Authority	Coordinate public health and medical activities and services statewide in support of resource needs for preparedness, response, and recovery.
California Environmental Protection Agency	Coordinate state resources and support the local jurisdiction in conducting all phases of emergency management in response to and recovery from a release of potential or actual hazardous materials.
California Department of Food and Agriculture	Coordinate stakeholders to provide emergency management impacting the agriculture and food industry. Support recovery of impacted industries and resources.
California Natural Resources Agency and California Utilities Emergency Association	Provide emergency management resources and support related to utility infrastructure system damage and outage response, as well as restoration of service.
California Volunteers	Support jurisdictions in ensuring the most efficient and effective use of volunteers, organizations, and monetary and donated resources to support incidents requiring a state response.

[1]These functions are delegated to various departments within Cal OES.

Cal OES Funding. The Governor's budget proposes total expenditures of $1.4 billion ($173.4 million General Fund) for Cal OES. This is a $1 million decrease from 2016-17 total expenditures. Approximately $217 million of total expenditures is proposed for Cal OES operations and the remainder is to be used for local assistance.

ISSUES TO CONSIDER

In addition to its role in emergency management, Cal OES implements and facilitates the state's counter-terrorism strategy and homeland security. Cal OES also serves as the state administering agent for federal homeland security, emergency management, and victim services grants. The responsibilities and functions outlined above are only a small sample of the duties Cal OES is charged with carrying out. Yet, many of these other functions are not immediately obvious. The Legislature may wish to conduct oversight of OES to gain a better understanding of its responsibilities before, during, and after an emergency.

Local Government Mandates

BACKGROUND

The proposed funding for non-education mandate payments to local governments is included in the budget of the Commission on State Mandates. The commission is responsible for determining whether a new statute, executive order, or regulation contains a reimbursable state mandate on local governments, and for establishing the appropriate reimbursement to local governments from a mandate claim. The California Constitution generally requires the state to reimburse local governments when it mandates that they provide a new program or higher level of service.

Activities or services required by the Constitution (as opposed to statute) are not considered reimbursable mandates. The Constitution, as amended by Proposition 1A of 2004, generally requires that the Legislature either fund or suspend local mandates. In most cases, if the Legislature fails to fund a mandate, or if the Governor vetoes funding, the legal requirements are considered suspended pursuant to the Constitution. However, one exception to this is payment of costs related to labor relations-related mandates, which may be deferred while still retaining the mandate's requirements.[1]

Mandate reimbursement claims are filed with the commission for the prior fiscal year – after that fiscal year is completed and actual costs are known. The state pays the mandate claims in the following fiscal year. For example, local costs incurred in 2015-16 are reported and claimed in 2016-17, and the state will reimburse locals for these costs as part of the 2017-18 budget. Suspending a mandate does not relieve the state of the obligation of reimbursing valid claims from prior-years, but it does allow the state to defer payment on these claims. For example, several elections-related mandates were suspended for the first time in the 2011-12 budget. This means the activities for locals were optional in 2011-12 and locals cannot claim reimbursement for any new costs incurred in 2011-12. However, the mandate claims for these costs in 2009-10 and 2010-11 are still due – either over time or all at once in a year when the mandate suspension is lifted. The state owes local governments approximately $1.0 billion in non-education mandate payments. All of this is related to post-2004 mandate claims.

GOVERNOR'S PROPOSAL

Funded Mandates

The Governor's mandate proposal is largely a continuation of the status quo in terms of mandates in effect and mandates not in effect. The budget proposes expenditures of $34.5 million related to funding non-education mandates. The budget would continue to fund the

[1] Payments for mandate costs incurred prior to 2004 were allowed to be repaid over time, and statutorily required to be fully paid by 2020-21. As of December 2015, the pre-2004 mandate debt (pursuant to Government Code Section 17617) was paid off as a result of appropriations made in the 2014 Budget Act.

19 mandates that were kept in force for 2016-17, the payments on which constitute the bulk of the General Fund cost. Most mandates funded in the budget concern public safety or property taxes. Funded mandates are listed in the following table.

Mandate Funding in Governor's Budget
General Fund
(Dollars in Thousands)

Mandate Title	Amount
Accounting for Local Revenue Realignments	$ 97
Allocation of Property Tax Revenues	570
California Public Records Act	-
Crime Victims' Domestic Violence Incident Reports	164
Custody of Minors-Child Abduction and Recovery	12,555
Domestic Violence Arrest Policies	7,756
Domestic Violence Arrests and Victims Assistance	1,896
Domestic Violence Treatment Services	2,379
Health Benefits for Survivors of Peace Officers and Firefighters	2,413
Local Agency Ethics	5
Medi-Cal Beneficiary Death Notices	14
Medi-Cal Eligibility of Juvenile Offenders	3
Peace Officer Personnel Records: Unfounded Complaints and Discovery	678
Post Election Manual Tally	-
Rape Victim Counseling	444
Sexually Violent Predators	3,693
Sheriff Court-Security Services	803
State Authorized Risk Assessment Tool	629
Threats Against Peace Officers	1
Tuberculosis Control	97
Unitary Countywide Tax Rates	313
Total	**$34,510**

Budget Savings

The budget incorporates a total of $985.1 million in savings from maintaining mandate suspensions or deferring payment of claims. Some 56 mandates are suspended under the budget proposal. In addition, payments on another 21 mandates that have been deferred or have expired have been delayed. The savings breakdown is as follows: (1) $284.1 million savings from deferring payment of post-2004 mandate claims for mandates that have since expired or are otherwise not in effect; (2) $596.1 million savings by continuing the suspension of certain local mandates; and, (3) $104.9 million savings from deferring payment on employee-rights mandates in effect. In prior years, there have been proposals to repeal certain mandates, but no such repeal is proposed in the budget. Repealing mandates does not offer any additional budget savings relative to suspension; however, if the mandate will otherwise be suspended indefinitely, the repeal of statutory provisions cleans up the code, improves statutory transparency, and provides more certainty to local governments.

ISSUES TO CONSIDER

Election Mandates

The state currently has in place six local government mandates that govern the conduct and activities associated with state and local elections. The first of the activities determined to be a mandate was adopted in 1975 and the most recent mandate was adopted in 2009. Three of the six mandates have been suspended in the budget (and thus not required to be conducted by local governments) since 2011 and the remaining three were suspended beginning in 2013. The Governor's budget proposes to continue the suspension of all six election mandates.

Under legislation adopted along with the 2015 Budget Act, the Department of Finance (DOF) was required to submit a report to the Legislature regarding the funding of the election mandates. The language in SB 84 (Committee on Budget and Fiscal Review), Chapter 25, Statutes of 2015, states:

> *"The Department of Finance, in collaboration with the Secretary of State and the Legislative Analyst's Office, shall convene a working group to evaluate alternatives for funding election-related mandates. The working group shall commence no later than September 1, 2015. By September 1, 2016, the Department of Finance shall submit to the Legislature a report that summarizes the findings of the working group, including recommendations to the Legislature."*

The report was provided to the Legislature in October of 2016. Prior to 1979 and the passage of Proposition 4, local election officials primarily used property tax revenues to pay for election costs. After that, local governments typically have submitted claims for the reimbursement of election costs associated with mandates imposed by legislation. As noted above, Proposition 1A requires the state to either fund or suspend local mandates, including those associated with elections. The six election mandates are:

- **Absentee Ballots.** Requires that absentee ballots be available by election officials to any registered voter.
- **Absentee Ballots – Tabulation by Precinct.** Requires that an election official's listing of absentee voters include the voter's precinct.
- **Modified Primary Election.** Requires voter registration cards to include a notice to decline-to-state voters of their ability to vote on a party ballot if allowed by the party.
- **Permanent Absent Voters.** Requires election officials to allow any voter to apply for permanent absent voter status.
- **Voter Identification Procedures.** Requires election officials to compare the signature on each provisional ballot with the signature on the voter's affidavit of registration using specified procedures.

- **Voter Registration Procedures.** Requires county clerks to accept affidavits of registration at any time up to 28 days immediately preceding the election.

The budget acts of 2015 and 2016 suspended the six election mandates. The date of suspension, along with the balance of amounts owed to local governments and the annual costs of funding the mandates, are shown in the table below. Note that if the mandates are "reactivated", the state must pay all past accrued costs, not just annual costs.

Election Mandates
Balance and Annual Costs
(Thousands of Dollars)

Mandate Title	Date Initially Suspended	Accrued Balance 2016	Estimated Annual Cost
Absentee Ballots	2011	$49,608	$24,800
Absentee Ballots – Precinct Tabulation	2011	68	34
Modified Primary Election	2013	1,817	316
Permanent Absent Voters	2013	11,907	4,700
Voter Identification Procedures	2013	10,075	1,600
Voter Registration Procedures	2011	2,481	1,300
Total Outstanding Balance and Annual Costs		**$75,956**	**$32,750**

The DOF report notes that data indicates a trend of voters moving away from traditional polling places and gravitating to a vote-by-mail system with a preference for permanent absentee voter status, and observes that state election laws have not adapted to these changing trends. With these considerations, and after discussions with stakeholders, the DOF report presents the following alternatives to funding the mandates:

- **Legislative Changes.** The report indicates that several of the mandates, together with existing election laws, result in redundancies, inhibit cost-effective election procedures, and may reduce the natural migration of voters to permanent absent voters. Specially, the report indicates that:
  - The Absentee Ballots mandate could potentially be repealed and voters encouraged to obtain permanent absent voter status. This would relieve local governments of significant ballot printing and polling place staffing costs.
  - Repealing the Absentee Ballots mandate could also render the need for the Absentee Ballots – Precinct Tabulation mandate moot. The non-reimbursable duty of local officials to maintain accurate voter lists would allow them to make needed precinct adjustments.
  - Repealing the Voter Identification Procedures mandate could reduce costs without compromising the intent of the legislation, since prior law already directs local

election officials to "examine the records" associated with provisional ballots.

- **Voting Methods.** The report suggests a careful examination of the vote-centered method of voting, that would allow counties to send voters a ballot prior to election day, permit in-person voting before and through election day, and allow voting to occur at established centers for all voters, irrespective of the voters' county of residence. This approach would reduce dramatically the number of polling places and their associated costs.[2]

- **Competitive Grant Program.** The report recommends consideration of a competitive grant program (with a matching requirement), with a goal to develop innovative and outcome based processes at the local level to reduce election costs. Cost-saving activities could include system upgrades for processing, increasing uniformity implementing mandates, and development of best practices.

It is apparent that election laws have not evolved as quickly as election behavior, particularly with respect to absentee ballots, which now represent 60 percent of voters. While this trend suggests that the state should consider adjustments that align election laws with voter behavior, DOF acknowledges that additional research is needed. As a follow-up activity to the report, DOF will conduct a survey to determine which of the six mandated activities would continue to be provided by local jurisdictions, absent the mandate, and indicates that it will conduct a survey in that regard in compliance with the legislation.

The DOF report provides a good starting point to address the significant budgetary impacts of election mandates, while being mindful of the sensitivity of the issues and the importance of election participation. Election law is a crucial policy area for the Legislature, and any changes in these laws should be based on extensive deliberation and analysis. While there is a significant budgetary impact in the decision to fund or not fund any election mandate, the policies surrounding such mandated activities should be considered in conjunction with the existing legislative policy-making procedures.

Carry-Over Debt

As indicated, as part of its debt reduction plan, the Administration has paid off the pre-2004 mandate amounts owed to local governments prior to the Constitutionally-required date of 2020-21 required by the Constitution. However, the state has accrued considerable debt on mandates that were in effect during the period after 2004. Some $1.1 billion is owed to local governments for these post-2004 mandates, including $255.8 million for Handicapped and Disabled Students, $152.0 million for Crime Statistics Reports for Department of Justice, and $107.5 million for Open Meetings Act. The Administration has not put forward a plan to address these amounts owed; the absence of such a plan could begin to exacerbate state-local government relations.

Delays in the Process

Determining whether a particular requirement is a state-mandated local program, and the process by which the reimbursable cost is determined, is an extensive, time-consuming, and multi-stage undertaking. Previously, state and local officials have expressed significant concerns about the

[2] Colorado has implemented a vote-centered system and experienced substantial cost–savings. Data from the state indicates the cost of $16.00 per voter in 2008 was reduced to $9.56 per voter in 2012.

mandate determination process, especially its length and the complexity of reimbursement claiming methodologies. Addressable administrative delays in the mandate process have largely been eliminated as a result of previous budget augmentations for the commission and strong efforts on the part of commission staff. However, the process remains time-consuming and any improvements are expected to fall short of meeting the statutory time frame, due largely to unavoidable constraints in the determination process. In addition, the process itself is awkward from a budgetary perspective, in that it calls on the Legislature (and the Administration) to make decisions based on factors and estimates that are preliminary in nature. The approach presents several difficulties that affect both the state and local governments. Among the most important are flip sides of the same coin, specifically:

- State mandate liabilities accumulate during the determination period and make the amount of state costs reported to the Legislature higher than they would be with an expedited process. Policy review of mandates is hindered because the Legislature receives cost information for a mandate years after the debate regarding its imposition.

- Local governments must carry out the mandated requirements without reimbursements for a period of some years, plus any additional time associated with development of the mandate test claim, appropriation of reimbursement funds, and the issuance of checks.

The state could deal with some fiscal uncertainty by conducting an initial legal analysis of the potential mandate, carry-out a preliminary cost estimate, and annually pre-fund the mandate pending a final determination. A recent statute provides a template for this approach. Last year, the Governor signed Assembly Bill 953 (Weber), Chapter 466, Statutes of 2015, which revises the definition of racial profiling and, among other things, requires the Attorney General to report on citizens' complaints alleging racial or identity profiling. Beginning in 2018-19, local agencies will be required to report data on all stops conducted by the agencies' peace officers, including the time, date, location, and justification. The budget includes $10.0 million in anticipation of state costs in the likely event that at least a portion of the statutory requirements are determined to be a reimbursable mandate.

Transparency and Reform

One of the more troubling aspects of mandate law, and the mandate process, is the lack of transparency regarding the obligations of local governments. The process of mandate suspension, which allows the state to not fund the mandate, leaves in place the statutory requirement regarding the activity. Consequently, a reading of the relevant statute would indicate that such a mandated activity is required to be carried out by local governments; however, unless the mandate is funded in the budget, it is deemed to be suspended, relieving local governments of the obligation to conduct the activity. The LAO has gone on record regarding the confusion and misunderstanding caused by this inconsistency for local governments and the public.

There have been two recent attempts to reconcile this information and eliminate the inconsistency with respect to suspended mandates. As part of the 2012-13 budget, the Governor proposed repealing 32 of 56 long-suspended mandates. Although the proposal was heard in appropriate budget subcommittees, ultimately the Legislature did not act on the proposal through the budget process, with the general view expressed that the policy committee process was the appropriate venue. As part of the 2013-14 budget, the Governor approached the mandate issue with a more nuanced proposal and the Legislature, to a large extent, initially agreed to this more surgical approach. In budget trailer bill, the Administration proposed ‘making permissive’ five mandates that had been suspended at least since 1990, consisting of: Adult Felony Restitution, Minors’ Victims Statements, Deaf Teletype Equipment, Pocket Masks, and Domestic Violence Incident Reporting. All were initially approved to be made permissive, but the Domestic Violence Incident Reporting statutory language was subsequently reinstated.

Cost Determination

In addition to the delays that characterize the mandate review and determination process, there are other significant issues. On the cost determination side, since most mandates relate to expanding existing programs (rather than instituting completely new ones), local governments have difficulty in measuring the marginal costs. The complexity of the claiming methodologies means local governments’ claimed costs frequently are not supported by source documents showing the validity of such costs, or are not allowable under the mandate’s reimbursement methodology. Accordingly, the State Controller's Office has disallowed a significant number of reimbursement claims over the last few years, leading to frequent appeals, more uncertainty and mounting bills.

General Obligation Bonds

BACKGROUND

The state uses general obligation (GO) bonds to borrow funds for spending – primarily for infrastructure and other capital investments. The use of bonds to accelerate capital projects is a commonly-used practice of government entities. GO bonds must be approved by voters and bond proceeds are either continuously appropriated (immediately available for expenditure) or require an appropriation from the Legislature. All bond debt service is continuously appropriated and, therefore, not considered in the annual budget bill process except as an informational item. Based on December 2015 data, the state has $73.7 billion in outstanding GO bond debt (including self-liquidating bonds). Another $35.6 billion in bonds are authorized, but remain unissued. In most instances, bonds are sold at different lengths of maturity such that repayment is spread over about 30 years. The chart below displays the state's authorized, outstanding and unissued bonds by program area.

General Obligation Bonds Authorized and Not Issued
(Dollars in Millions)

Activity or Program	Authorized	Outstanding	Unissued
Health and Hospitals	$1,730	$1,272	$352
Water Quality/Disaster Preparation	31,073	12,950	12,189
Higher Education	14,462	8,474	2,106
K-12 Education	49,785	28,469	7,522
Housing	5,700	1,809	1,519
Stem Cell	3,000	1,166	1,032
Transportation/Air Quality	34,865	19,152	10,752
Other Infrastructure	3,734	429	81
Total	**$144,722**	**$73,722**	**$35,564**

[1] Non self-liquidating.

The state generally goes to market to sell GO bonds twice annually – once in the spring and once in the fall. Bond structures are often tailored to meet market demand and investor appetite. This tailoring includes tinkering with variables such as fixed and variable rates, call features and premiums, and various security enhancements. Bonds are sold in amounts necessary to meet expenditure needs, plus an additional cash cushion to account for flexibility reflecting how fast projects will expend funds and uncertainty about the timing of the next bond sale. Based on November 2016 data, there is about $1.4 billion in bond cash on-hand, distributed across various bond programs. This is about the same level of unspent bond proceeds as there was at this same time last year. Reducing the level of unused bond proceeds is generally considered to constitute wise bond-proceeds management, as it minimizes the amount of idle cash upon which interest must continue to be paid.

GOVERNOR'S PROPOSAL

General Obligation Bonds and Debt Service

Expenditure of bond proceeds is reflected in the budgets of individual departments, with the payment of bond debt service consolidated in Item 9600 in the Governor's budget. It is the repayment of bond debt that is reflected as a General Fund expense. Some bond costs are offset by special funds or federal funds. Other bonds are 'self-liquidating,' or have their own dedicated revenue source.

The Governor's budget includes $4.8 billion in General Fund costs for GO bond debt service and related costs. In addition, about $1.9 billion in debt costs are scheduled to be funded from special funds. Finally, federal bond subsidies, through the Build America Bonds (BABs) program, will provide an estimated $352 million in 2017-18, allowing for a reduction in General Fund expenses. The Governor's proposed budget includes about $124 billion in General Fund available for debt service – including carry-over balances, but excluding amounts to be transferred to the state's Budget Stabilization Account (BSA). The net General Fund debt service for GO bonds, as a percentage of General Fund resources, is less than four percent.

Governor's Budget for General Obligation Bond Debt
(Dollars in Millions)

Category	2015-16 Actual Cost	2016-17 Estimated Cost	2017-18 Forecasted Cost
Gross Debt Service[1]	$6,577	$6,777	$7,102
Other Funds and Department Costs[2]	-1,492	-1,665	-1,879
Federal Subsidy[3]	-327	-343	-352
Total Net Debt Service	**$4,759**	**$4,769**	**$4,872**

[1] Includes variable rate bond and commercial paper expenses.
[2] Debt incurred for transportation, higher education and water resources purposes.
[3] Build America Bonds subsidy.

Debt service is expected to be relatively stable in the budget year based on past bond sales and anticipated issuances. The State Treasurer's Office (STO) plan includes an assumption that $4.1 billion in GO bonds will be sold (or have been sold) in 2016-17, and that $4 billion will be sold in 2017-18. In recent years, the state's GO bond debt service cost per borrowed dollar had been declining, although in the last year there has been a slight uptick in rates. This general post-recession decline has occurred not only because of the general decline in interest rates, but also the state's improved credit rating based on sound financial management. In 2010, the spread between California's 30-year borrowing costs was 150 basis points (1.5 percent) higher than term-comparable AAA-rated paper; while the current spread is closer to 10 basis points. The STO has taken advantage of this dynamic and maintained an active refinancing program.

Infrastructure Plan

Infrastructure is one of the core missions of state government. It is also a core foundation of economic growth for the state, as we discussed in the *Overview of the 2015-16 Budget Bill.*[1] The California Infrastructure Planning Act requires the Governor to annually submit a five-year infrastructure plan to the Legislature for consideration with the budget bill. The Governor's *2017 California Five-Year Infrastructure Plan* calls for an investment of $43 billion over the next five years, using a variety of financing methods. The great bulk of this is in the transportation area. Unlike last year, there is less in General Fund resources available for infrastructure, and the plan reflects a greater reliance on debt issuance to make critical infrastructure investments. The plan also reflects the Governor's proposed transportation package, discussed in the transportation section of this report under *Transportation Funding*. The plan financing and the uses of the funding are presented below:

2017 Five-Year Infrastructure Plan
(Dollars in Millions)

Funding Sources	**Amount**
General Fund	$524
Special Funds	8,100
Lease Revenue Bond Funds	1,700
General Obligation Bond Funds	$338
Federal Funds	13,600
Reimbursements and Cost Funds	4,100
High-Speed Rail Funds	14,600
Total	**$42,962**
Spending Plan	**Amount**
Transportation and High-Speed Rail	$39,647
Natural Resources	869
California Environmental Protection Agency	413
Health and Human Services	44
Corrections and Rehabilitation	197
Education	182
General Government	1,534
Total	**$42,886**

In addition to the identification of capital financing, the plan also identifies some $78 billion in deferred maintenance needs across the state. Of this amount, 72.9 percent is in transportation, 16.6 percent in water resources, 4.5 percent in higher education, and 1.5 percent in parks and recreation. The Governor notes that the 2015 and 2016 budgets allocated slightly under a billion dollars to address this maintenance backlog. The proposed budget for 2017-18 does not provide additional funds for these purposes.

[1] Senate Committee on Budget and Fiscal Review, *Overview of the 2015-16 Budget Bill*, February 2015, http://sbud.senate.ca.gov/sites/sbud/senate.ca.gov/files/overview/2015overview2015-16Budget.pdf.

ISSUES TO CONSIDER

Budget and Bonds

Paying GO bond debt is a significant General Fund expense. State and federal tax exemptions for interest income received by investors ensure that GO bond debt is a low-cost financing alternative. To the extent bond costs do not exceed a government's long-term ability to fund other commitments, bonds typically allow the public to enjoy the benefits of infrastructure investment more quickly than would otherwise be the case. The Legislative Analyst's Office (LAO) indicates that the state's gross debt service requirements for infrastructure for bonds already sold will drop steadily over the next few years to around three to four percent of General Fund revenues, resulting in a cost of roughly $6 billion annually over the same time period. This issue is discussed further below.

Voters must authorize GO bonds, but the timing of the issuance of the bonds is the responsibility of the STO. In November 2016, voters approved over $9 billion in additional school bonds. During difficult budget times, such as the recent great recession, bonds enable the state to invest in infrastructure while the need for economic stimulus is most acute, borrowing costs are low, and construction procurement is favorable. Despite the benefits of bonds, they come with the cost of many years of debt service. Assuming that a bond carries an interest rate of five percent, the cost of paying it off with level payments over 30 years is close to $2 for each dollar borrowed – $1 for repaying the amount borrowed and close to $1 for interest. This cost, however, spread over a 30-year period, after adjusting for inflation is considerably less – about $1.30 for each $1 borrowed (based on the current inflation range). The Legislature can increase or limit bond funding through the budget process as overall expenditures are prioritized.

Despite the interest costs associated with debt, the decision to issue bonds comes with numerous advantages, as outlined above. In addition to these benefits, the current interest rate environment, which continues to display very low long-term rates, presents unique advantages for the issuance of long-term debt for the state. For California AA-rated twenty year paper, the representative yield is 3.28 percent[2] (compared to 2.93 percent for municipal AAA paper). California bond yields are up slightly from the comparable figure 3.05 percent of last year, but are still in the historically low range. However, this could change if the economy continues to improve and places upward pressure on interest rates.

The Administration proposes maintaining its current market level of bond issuance and, given the budget problem identified by the Administration, has pulled back on some of its previous commitment of cash for substantial capital improvements. While California should guard its vastly improved credit rating and lower interest costs, the Legislature could also consider initiatives that take advantage of the continuing low interest rate environment. In particular, the significant backlog of deferred maintenance of almost $80 billion would benefit from a sustained effort of reinvestment in these capital assets. Without such a sustained effort, the backlog will continue to grow – and at an increasingly rapid rate.

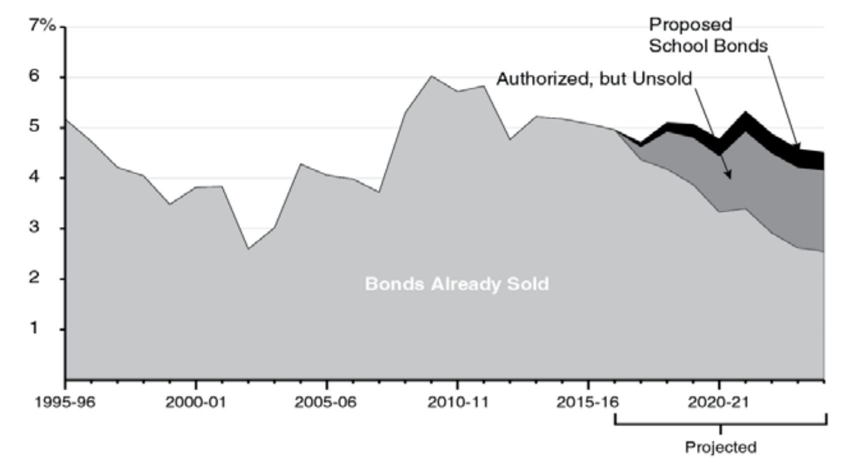
[2] California's current long-term General Obligation bond ratings from the three major services are: Moody's Aa3; Standard & Poor's AA-; Fitch A+.

Debt Capacity
One indicator of the state's debt situation is its debt service ratio. This ratio indicates the portion of the state's annual General Fund revenues that must be set aside for debt-service payments on infrastructure bonds and, therefore, are not available for other state programs. As shown in the LAO figure below, the debt service ratio is now about five percent of annual General Fund revenues. Assuming the state's schedule of GO bond issuance is similar to past years, the approval of the school bond in November 2016, and the continued issuance of previously authorized bonds, will result in debt service remaining at about the five percent over the next several years, and declining thereafter. Thus, these bond sales would increase the debt service ratio by about one-third of a percentage point compared to what it would otherwise have been. The state's future debt service ratio would be higher than those shown in the figure if the state and voters approve additional bonds in the future.

Figure 1

General Fund Debt-Service Ratio

Percent of General Fund Revenues Spent on Debt Service



Source: Legislative Analyst's Office

An alternative measure of debt affordability is the ratio of total state debt to personal income. Among the ten most populous states, California is in the upper tier with state debt accounting for 4.7 percent of personal income in 2016. With respect to this measure, New York was the highest with debt equal to 5.7 percent of personal income, followed by Illinois at 5.2 percent. It should be noted that California's percentage has dropped steadily from 6.0 percent in 2012 to 5.4 percent in 2014, then to its current level in 2016. This ratio is a key component of credit analysis conducted by the various bond rating agencies. California's improved ratio can have an impact on bond ratings and thus directly affect the interest costs associated with the issuance of debt.

Bond Management
As the state's cash situation deteriorated with the steep recession, the Administration changed the methodology for managing bond cash. Prior to the recession, reserve cash funded project costs in advance of bond sales, and then bond sales replenished cash reserves. When reserve cash declined, the state had to instead sell bonds in advance of expenditures. Due to project expenditures occurring slower than anticipated at the time of bond sales, large bond cash

balances developed – about $9.7 billion as of December 2011. As a result, the Administration implemented a plan to utilize commercial paper to aid cash flow, thus reducing the need to carry large bond cash balances. As part of this effort, the Administration requires GO bond programs to demonstrate an immediate need for additional bond proceeds prior to issuing new bonds. Progress has been made to reduce bond cash, and cash reserves have dropped to just under $1.4 billion by the end of December 2016. At budget hearings, the Administration could be asked to discuss their management of bond proceeds, forecasts of project expenditures, and the optimal level of cash balances.

Debts and Liabilities

BACKGROUND

Through budget actions over the last decade, the state borrowed from special funds, deferred various payments to schools and other entities, and took certain other actions in order to help balance the state budget. By the close of 2010-11, the Department of Finance (DOF) indicates that a total of $34.7 billion in loans and deferrals had accumulated and remained unpaid. This amount largely represents the debt overhang from prior year budgets adopted under the previous Administration and was formerly referred to as the "wall of debt". The DOF no longer formally calculates the "wall of debt"; however, the amount formerly included in this calculation is expected to be reduced to a total of about $3.1 billion by the inception of 2017-18.

Some of these obligations have required repayment in specified years due to constitutional requirements or due to scheduled bond debt service. Other debt payments are more flexible and can be repaid over time depending upon the budget condition, as long as borrowing does not interfere with the activities that a special fund loan supports. The General Fund is typically used to pay off budgetary debt. In addition to these budgetary obligations, the state has accumulated liabilities for retirement costs for state employees, teachers, judges, and University of California employees. These latter liabilities will total an estimated $236.5 billion at the start of 2017-18. Some of these unfunded liabilities are being addressed with routine annual payments over time.

Proposition 2, which revised the state's Budget Stabilization Account (BSA), was approved by the voters in November 2014. The measure changes the way the state pays down debts and liabilities, as well as how it sequesters money in reserves. According to the Legislative Analyst's Office, Proposition 2 could result in roughly $15 to $20 billion being used to pay down certain state debts through the duration of the measure's debt payoff requirement. Choices about how calculations are made under Proposition 2 determine the amount of funds that are split evenly between the BSA and debt pay-down. Both the state's debts and liabilities represent budget challenges, as payments on these restrict legislative discretion and displace funding for ongoing or expanded program costs.

GOVERNOR'S PROPOSAL

Under the Administration's calculations, Proposition 2 captures a total of $2.4 billion in the budget year. Proposition 2 requires that this amount be split evenly between paying down existing state debt and the reserve. As shown in the figure below, the Governor proposes to spend the required $1.2 billion on paying down $252 million in special fund loans, $400 million in prior-year Proposition 98 costs known as "settle-up" and $235 million in transportation loans. In addition, the Governor's plan would use $100 million for state retiree health and $169 million for University of California employee pensions. The Administration's multi-year budget plan proposes to fully repay transportation loans by 2019-20, and payoff special fund loans and Proposition 98 settle-up by the end of 2020-21. Due to the dynamic nature of budgeting and changing fiscal circumstances, the pay-off schedule always changes somewhat from year to year. Detail on the Governor's current plan is displayed in the table below.

Proposal for Debts and Liabilities Payments
(Dollars in Millions)

Category	Amount Beginning of 2017-18	Payment in 2017-18
Budgetary Borrowing		
Special Fund Loans and Interest[1]	$1,365	$252
Proposition 98 Settle-Up Underfunding[1]	1,026	400
Transportation Loans (Pre-Proposition 42)[1]	706	235
Subtotal Debt	**$3,097**	**$887**
Retirement Liabilities		
State Retiree Health[1]	74,103	100
State Employee Pensions	49,592	0
Teacher Pensions	72,626	0
Judges' Pensions	3,279	0
CalPERS Deferred Payment	627	0
UC Employee Pensions[1,2]	15,141	169
UC Retiree Health[2]	21,087	0
Subtotal Liabilities	**$236,455**	**$269**
Grand Total	**$239,552**	**$1,156**

[1] Payment under Proposition 2.
[2] Not a state government liability.

The special fund loans that would be repaid under the Governor's budget are shown below.

Governor's Proposal for Repayment of Special Fund Loans
(Dollars in Millions)

Fund Name	Amount
Greenhouse Gas Reduction Fund	100,000
Immediate and Critical Needs Account	90,000
Hospital Building Fund	15,000
False Claims Act Fund	12,700
Contingent Fund of the Medical Board of California	9,000
Behavioral Science Fund	6,300
Firearms Safety and Enforcement Special Fund	4,900
Registry of Charitable Trust	2,700
Environmental Water Fund	2,400
California Water Fund	1,100
Total	**$244.1**

ISSUES TO CONSIDER

The Governor has prioritized using Proposition 2 funds to pay off special fund loans and prior-year Proposition 98 settle up obligations. However, alternative uses of these funds could pay down certain liabilities faster or potentially free up General Fund dollars for other purposes. For example, prior years highlighted the $74 billion unfunded liability for retiree health care costs. The Governor has instead pursued a plan – to this date, largely successful – substantially reliant upon employee bargaining to eliminate the liability over a 30 year period. While the Administration could have used more of the Proposition 2 funds to pay down some of the retiree health care unfunded liability, the Governor proposes to begin working down this debt with a relatively minor initial commitment of $100 million, which then ratchets up to reach $300 million in 2020-21.

In addition, the state could pay off more or less special fund loans now than the Governor proposes. Some of the loan repayments proposed are fiscally necessary and some of the loans could be repaid to help meet the desired program objectives; however, some repayments are unnecessary to make at this time, as the programs have been operating for many years without the funds. While working down the smaller amounts of special loan repayments cleans-up the state's balance sheet, augmenting resources devoted to pension liabilities sooner can have a substantial impact on future state liabilities.

Cash Management

BACKGROUND

The state's receipts and disbursements of cash occur unevenly throughout the fiscal year. As a consequence, the General Fund borrows for cash flow purposes in most years, even though each budget is balanced when enacted and funds are repaid within the fiscal year. Given that the state receives revenues on an uneven basis throughout the year, the state's cash position varies. Maintaining an adequate cash balance, by using both internal and external borrowing, allows the state to pay its bills in a timely fashion. Interest is paid on internal borrowing (such as cash flow loans from special funds) and external borrowing (such as Revenue Anticipation Notes [RANs]). For the current year, the state's cash position did not require the issuance of a RAN.

Total monthly borrowable internal resources from over 700 funds are typically in the range of $20 billion, although these amounts have increased during the recovery period. The state also established a cash flow tool in the form of the Voluntary Investment Program (VIP) in 2012. This program provides an additional means to assure cash flow continuity by establishing a new account for voluntary participation by local governments. Another cash management tool for the state is the State Agency Investment Fund (SAIF), which attracts deposits from entities not otherwise required to deposit funds with the state. The VIP and SAIF were not used in the current year.

An additional tool in managing cash is deferrals of payments within the fiscal year to K-12 and higher education, local governments, and other entities. The fiscal impact of these deferrals varies from entity to entity, depending upon their own cash positions. In past years, flexible deferrals have been enacted in statutes that allow specified deferrals, if necessary to maintain a prudent balance for bond debt and other priority payments. The 2014-15 budget included a statutory provision providing that any increases in the Proposition 98 minimum guarantee first be used to pay down late payments to schools and community colleges. In the current year, the state was able to shift education payments back to the appropriate year, as additional revenues allowed for activating a trigger mechanism that eliminated all K-14 deferrals.

GOVERNOR'S PROPOSAL

The Governor's budget does not anticipate engaging in external borrowing (RAN) in 2017-18 and assumes that internal borrowing will be adequate to cover any low points in the state's cash position. This is the third year in a row that the state will avoid costs of external borrowing and reflects the state's improved cash position and, if projections hold, would be only the fourth year since the mid-1980 that the state has not issued a RAN. Given the improvement in the cash status, no new education or other payment deferrals are incorporated in the budget. Based on the cash flow statements of the Administration, the cash low points will occur in July and March, requiring a draw on internal cash resources of $6.0 billion and $6.7 billion, respectively. Total unused internal cash resources are substantial over the budget year, and range from a low of $37.4 billion in January 2018 to a high of $41.7 billion in September 2017.

The state anticipates engaging in its typical internal cash-borrowing, with all internal cash flow borrowing managed such that the programs supported by these special funds are completely unaffected. The budget includes $20 million for interest costs associated with internal borrowing. As mentioned earlier, the Administration has not proposed a RAN, and the budget does not include any costs associated with external borrowing for cash flow purposes. There is also no anticipated need for the VIP or the SAIF in the Governor's budget. The Administration has not incorporated any new deferrals as part of the budget plan; however, the Governor's budget assumes smoothing of payments to UC and CSU in a manner similar to the past years. The cash management strategy for higher education is funding one-twelfth of the total appropriation in each month.

ISSUES TO CONSIDER

Maintaining an emphasis on cash flow borrowing from special funds is good fiscal policy that reduces the need for more expensive external borrowing. Cash deferrals to other government units – such as K-12 education – are generally among the least desirable of the cash management tools, in that these can cause cash flow stress on other governmental entities. (The Governor has proposed a deferral for K-12 to address the over-appropriation, but not for cash flow purposes.) Although deferrals for cash flow may have been necessary in the past – especially in order to limit the magnitude of external borrowing – not having to rely on this measure in the current and coming year is a positive development. The Administration's proposal appears to be a suitable approach to cash flow management and the lack of external borrowing reflects the state's continued overall fiscal health.

Information Technology and FI$Cal

BACKGROUND

The State of California invests a significant amount of resources in information technology (IT) projects annually. Given technological trends and the pressure to continuously upgrade and improve its technological infrastructure, the state's IT resource needs are likely to continue to increase in the future. The California Department of Technology (CDT) is the state's central IT entity and has broad responsibility and authority over all aspects of technology in California state government, including: policy formation, interagency coordination, IT project oversight, information security, technology service delivery, and advocacy. The director of the CDT, who also serves as the state chief information officer, advises the Governor on the strategic management and direction of the state's IT resources. While CDT provides project oversight, because of the diversity in project designs, schedules and costs, procurement and implementation is generally the responsibility of individual departments.

Status of Projects

As shown in the chart below, the estimated cost of current IT projects committed to by the state total almost $3.5 billion over the period of acquisition of the projects. These individual project costs range from $2.6 million for the Renewable Portfolio Standards Database (RPS) for the Energy Resources Conservation and Development Commission to over $910 million for the statewide Financial Information System for California (FI$Cal). As we discuss further below, IT projects can be quite dynamic and, as a consequence, their associated costs are typically revised and refined throughout the acquisition and implementation period.

California Information Technology Projects
Costs and Status
December 2016

Department	Project Number And Project Name	Total Project Cost	Criticality Rating	Complexity Zone	Score Card Rating
Board of Equalization, State	0860-094 Centralized Revenue Opportunity System (CROS)	$343,383,931	High	IV	Green
Board of Equalization, State	0860-097 AB 1717 Prepaid Mobile Telephony Services Surcharge (MTS)	$4,407,435	High	II	Green
California Correctional Health Care Services	5225-146 Electronic Health Record System Project	$386,462,158	High	IV	Green
Commission on Teacher Credentialing	6360-098 Streamline and Strengthen the Accreditation Process (SSAP)	$6,471,434	Medium	II	Green

Department	Project Number And Project Name	Total Project Cost	Criticality Rating	Complexity Zone	Score Card Rating
Conservation Corps, California	3340-013 California Conservation Corps C³ Project	$8,112,282	Medium	II	Yellow
Department of Corrections and Rehabilitation	5225-157 Automated Re-entry Management System (ARMS)	$62,929,901	Medium	II	Yellow
Department of Corrections and Rehabilitation	5225-162 Career Technical Education (CTE)	$20,024,880	Medium	II	Green
Energy Resources Conservation and Development Commission	3360-071 Renewable Portfolio Standards Database (RPS)	$2,633,817	Medium	II	Green
Finance, Department of	8860-030 Financial Information System for California (FI$Cal)	$909,967,933	High	IV	Yellow
Health Care Services, Department of	4260-200 CA Medicaid Management Information System (CA-MMIS)	$458,591,056	High	IV	Green
Human Resources, Department of	7501-001 Examination and Certification Online System (ECOS)	$9,946,210	Medium	II	Green
Insurance, Department of	0845-042 CDI Menu Modernization Project (CMMP)	$21,391,153	High	IV	Green
Motor Vehicles, Department of	2740-191 Centralized Customer Flow Management and Appointment System	$17,862,420	High	IV	Green
Motor Vehicles, Department of	2740-190 Automated Knowledge Testing Expansion System	$9,768,595	Medium	IV	Yellow
Pesticide Regulation, Department of	3930-012 Product Registration Data Management System (PRDMS)	$6,037,903	Medium	II	Green
Public Health, Department of	4265-028 Women, Infants and Children Management Information System (eWIC-MIS)	$90,288,809	High	IV	Green
Public Health, Department of	4265-019 Women, Infants and Children Management Electronic Benefit System (eWIC-EBT)	$46,685,330	High	III	No Report Available

Department	Project Number And Project Name	Total Project Cost	Criticality Rating	Complexity Zone	Score Card Rating
Public Health, Department of	4265-021 California Immunization Registry (CAIR) 2.0	$11,856,841	High	IV	Green
Public Utilities Commission	8660-068 Transportation Carrier Application and Equipment e-Filing Portal (TCP)	$3,548,849	Medium	II	No Report Available
Public Utilities Commission	8660-080 eFiling Administration Support (eFast)	$5,684,942	Medium	II	Green
Rehabilitation, Department of	5160-047 Enhanced Maintenance and Operations	$11,823,889	Medium	II	Green
Secretary for California Health and Human Services Agency	0530-200 LEADER Replacement System (LRS)	$484,812,905	High	IV	Green
Secretary for California Health and Human Services Agency	0530-211 Child Welfare System (CWS) New System (CWS- NS)	$420,744,069	High	IV	No Report Available
Secretary of State	0890-047 California Business Connect	$53,350,155	High	III	Green
Social Services, Department of	5180-153 County Expense Claim Reporting Information System (CECRIS)	$10,583,093	Medium	II	Green
Social Services, Department of	5180-186 State Hearings Appeals Case Management System (ACMS)	$18,843,759	High	IV	Green
State Treasurer	0950-019 Debt Management System II	$19,773,758	High	II	Green
Total Cost : $3,445,987,507					

Source: Department of Technology

The projects listed in the chart have a "Score Card Rating," with the rating generally based on the degree to which they remain on schedule with respect to timing and costs. The rating is compiled from various strategic, tactical, and work environment indicators, and is derived from the evaluation tools provided in the Statewide Information Management Manual (SIMM). The CDT defines the rating categories as the following:

- **Green** – Indicates a fairly healthy project.
- **Yellow** – Indicates a project that is slipping.

- ■ **Red –** Indicates a project that is in need of immediate intervention.

- **Not Indicated –** Indicates that a Project Status Report was submitted, but the so-called "vital signs" portion of the Status Report was not completed.

- **No Report Available –** Indicates that a Project Status Report is not available for publishing for the reporting period.

Most of the projects listed in the chart are proceeding according to current plan, at least based on the most recent assessments. However, we would note that the scorecard rating is based on performance relative to the current existing projects. For some of the items listed (for example, the Board of Equalization's Centralized Revenue Opportunity System [CROS]), the project listed represents only the most recent attempt to address this particular IT need of the agency; there have been other previous projects designed to address this issue. In addition, the status chart appears to be compiled on the basis of the most recent documents received (including revisions) and is not necessarily reflective of the original timeline established for the project.

It is worth considering the number and magnitude of the IT projects that have been discontinued entirely in the past. In recent years, the state has had a number of challenges delivering on-time and on-budget IT projects. Several high-profile projects have experienced significant revisions, delays, and cost overruns. The numerous setbacks have been the topic of several legislative oversight hearings, and have led to organizational and process changes within the Administration. One of the more significant changes was the Legislature's approval of a statewide project management office within the CDT.

Budget Subcommittee Review

In previous years, the Senate Budget and Fiscal Review Subcommittee No. 4 has conducted an extensive review of the state's IT procurement and project implementation process. Other budget subcommittees have also conducted reviews of IT projects that fall under their jurisdictions. Subcommittee No. 4 included in its review, the procurement and project implementation of the State Controller's 21st Century Project. The 21st Century Project, which was intended to unify an automated statewide payroll disbursement system, was originally estimated to cost $84 million. Prior to its suspension in 2013, overall project costs were estimated to be over $300 million. Over the project's nine-year lifespan the project costs ballooned by over 350 percent.

While the focus of the subcommittee was on the 21st Century Project, it also looked at several other high-profile IT projects that were also experiencing difficulty. For example, the California Department of Motor Vehicles' $200 million IT modernization project was also suspended in 2013. During its oversight hearings, Subcommittee No. 4 questioned whether or not there was an underlying issue that has handicapped the state's ability to deliver an IT project on time and on budget. The subcommittee came to a primary conclusion that was similar to the Administration's – that the individuals with responsibility for implementing complex IT projects often lack the necessary experience and technical capabilities for project success.

In addition to the lack of adequate staffing, IT project design, procurement and management is a very dynamic process with numerous unknowns. The process and the approach for IT necessarily lacks many of the characteristics typical of more traditional capital procurement. There are numerous complexities and developments that require fairly regular adjustments in timing, staffing and costs. Projects can also be altered or significantly redesigned after the project has been initiated. In other situations, mid-year budget adjustments are necessary to achieve project success. What this process suggests is that project success requires personnel and project contracts to be flexible enough to adapt and respond to changing circumstances and demands.

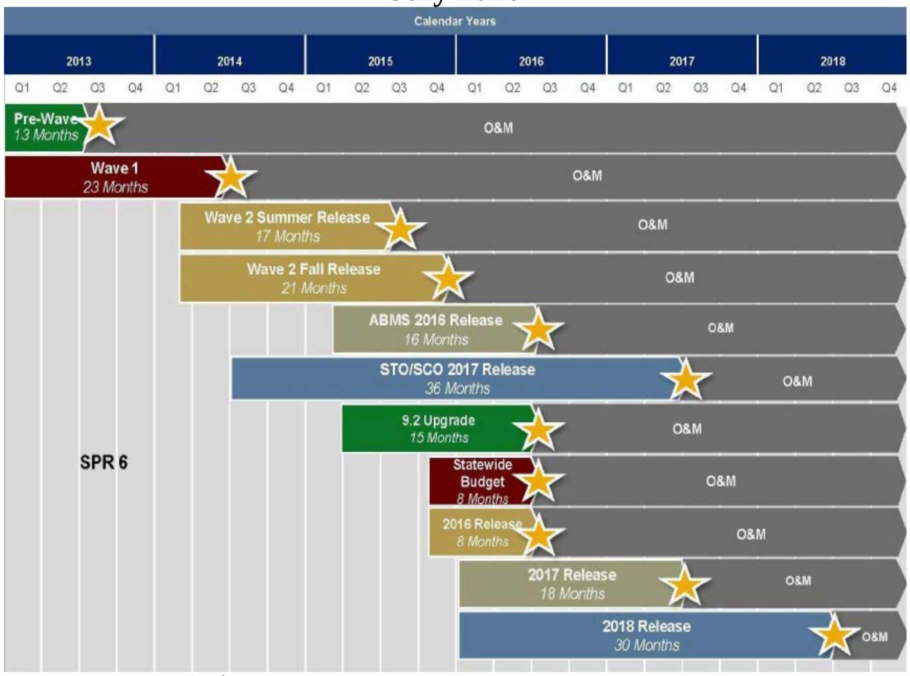
Focus on FI$Cal

One of the most vital projects for the state is FI$Cal, the statewide project being undertaken to integrate and re-engineer the statewide business processes related to budgeting, accounting, procurement and cash management. The goal of the project is to provide a unified and consistent financial system the will be used by virtually all state entities. System integration for the project is being provided by Accenture LLP; independent project oversight (IPO) by the CDT; and, independent verification and validation (IV&V) by the Public Consulting Group. Last year the Legislature approved a permanent administrative structure for FI$Cal, establishing it as a stand-alone department. As noted in the chart above, the project report rating for FI$Cal is ‘yellow,’ indicating that the project is ‘slipping.’

FI$Cal is an ambitious and complex project, and in reflection of this, the project has undergone numerous changes in scope, schedule and cost. These various changes have been incorporated and documented in special project reports (SPRs) with the project currently working under the rubric of SPR 6, approved last year. Under the previous SPR 5, a series of waves were to be set in motion, with each wave consisting of additional departments and system functionality. The Legislative Analyst’s Office (LAO) notes that there were some ‘early successes’ in this process, but later some difficulties and delays occurred. Overall, the LAO notes that project changes to date have led to schedule extensions and cost increases, but have also led to modifications that have mitigated project risk and made project objectives potentially more attainable.

Project Costs and Schedule. Under the changes in SPR 6, the project transitioned from implementing ‘waves’ to more independent ‘releases’, allowing departments that are not prepared to implement on the scheduled date to come on line at a later time. The amended approach established new programs to assist departments in transitioning to the project, revised the implementation schedule for remaining releases, and allowed more time for knowledge transfer to the state. These changes resulted in increased costs for the project and a two-year delay in the overall timeline for the project. The two-year time extension pushed out project completion from July 2017 to July 2019. The costs also expanded significantly to $910 million, representing an increase of $237 million from those in SPR 5 dated January 2014. The currently timeline is shown in the department’s graphic below.

FI$Cal
Project Schedule
July 2016



Source: Department of FI$Cal

State Auditor's and LAO Concerns. The auditor's most recent Letter Report of January 2017 indicates that the project continues to experience some delays, despite the two year time extension provided in SPR 6. For example, according to the IPO, a key component of the project – testing of the Activity Based Management System (ABMS) – was taking 10 weeks longer than planned as of October 2016. In addition, the IPO indicated that implementation of functionality for both the State Controller's Office and the State Treasurer's Office were delayed, along with a five week delay in the release for other departments.

While the delays represent a continuing concern, it is unclear whether these are the responsibility of FI$Cal or the participating departments, or both. We should note that many of the delays are due to failures on the part of departments to adequately staff the conversion to the new system. Specifically, the most recent Letter Report from the auditor identifies as a significant driver of the most recent SPR, the unanticipated need to provide continuing support from FI$Cal to departments in year-end reconciliation and budget close-out. More recently, in some cases, it appears that delays or time extensions have been necessitated by departments unwilling or unable to make a decision on how to proceed at a certain decision point. The auditor's letter notes that if delays continue and compound, the project may need to extend the schedule again, which could increase the costs by an additional $100 million. Alternatively, not extending the schedule could jeopardize the functionality and quality of the final product.

The auditor 'remains concerned' regarding the number and size of the departments that have yet to implement FI$Cal, as well as the compressed time frame proposed for implementation. Given the challenges that were presented with smaller, fewer and less complex departments, the auditor notes potential issues with the project's ability to implement the next releases (scheduled for July

2017 and July 2018), which consist of major state departments. Citing the project's 21 percent vacancy rate, the auditor notes that "…there is significant risk that the project's resources will be overwhelmed when it tries to implement releases that include large and complex departments."

Last year in conjunction with FI$Cal budget proposals, the LAO weighed in on the overall status of the project. At that time, it expressed the view that the Governor's budget proposal to implement the changes proposed in SPR 6 was a reasonable plan to implement the remaining functions and departments in FI$Cal, and recommended approval of this component of the Governor's budget proposal. However, LAO also noted that the FI$Cal Project involves the development of an extremely ambitious and complex IT system and significant work remains before the system is fully implemented. Given the scope of the remaining work and signals from oversight entities that some project activities continue to track behind schedule, LAO thinks a future SPR is likely that would further extend the project schedule and increase costs.

ISSUES TO CONSIDER

As indicated in the chart that begins this discussion, the state has substantial investment in IT projects across various departments. This level of investment is only going to increase in the future, due to the complexity and accompanying expenses of procuring and implementing its IT plans. By CDT's own assessment, four of the 27 projects identified are slipping, representing an investment of just under $1 billion and 30 percent of the total. Another two projects totaling costs of $470 million have not provided information sufficient to have a rating assigned.

Ensuring FI$Cal Success. The FI$Cal project discussion is provided as an example of a major state project (consisting of numerous sub-projects) that while generally proceeding in a positive manner, has experienced numerous delays and cost increases. These instances have caused several new SPRs to be issued in order to cope with changing circumstances. Given the additional delays that have occurred since the issuance of SPR 6, the project may be in the position to issue a follow-up SPR in order for project plans to track with actual performance. While this would recognize that FI$Cal (and certain departments) have missed milestones, it could allow for the project to refocus on the overall goal to ensure the overall functionality of the system. In this context, the Legislature may want to consider the follow:

- Revisit issues related to resource support for departments, and consider whether additional outside assistance is warranted in the conversion to FI$Cal.

- Examine the process through which balancing costs, functionality and project timeframe need to be addressed in projects of this magnitude.

- Address governance and administrative structures that could improve and enhance the overall accountability for the project.

Oversight and Monitoring. As a component of its oversight responsibilities the budget committee and subcommittees should continue to review the performance of state projects, and consider increasing the level and consistency of oversight activities. The Legislature lacks a dedicated venue for IT oversight and monitoring, and this may be an area where the budget committee should invest in further effort. In particular, oversight could focus on those areas that seem most susceptible to both weaknesses and present opportunities for potential improvements. For projects currently underway, it is clear that the most vital factor for project success is to ensure that these efforts are fully staffed – both state department and project vendor – with the most qualified technical personnel available. The state could consider additional incentives (such as differential pay, as employed by the Department of Finance) in order to attract and retain IT professionals.

Future IT Projects. Going forward, the Legislature, in its oversight capacity, should consider facilitating and encouraging the administrative branch to look to the Government Accountability Office's (GAO) recommendations regarding successful IT projects. The common critical success factors as determined by the GAO are:

- Project staff is actively engaged with stakeholders.
- Project staff has necessary knowledge and skills.
- Senior department and agency directors support the program.
- Users and stakeholders are involved in developing the project requirements.
- Users participate in testing of the functionality throughout project.
- Government and contractor staffing is stable and consistent.
- Program staff appropriately prioritizes project requirements.
- Program officials maintain consistent communication with primary vendor.
- Sufficient and consistent funding is provided.

SUBCOMMITTEE NO. 5

CORRECTIONS, PUBLIC SAFETY, AND THE JUDICIARY

Corrections and Public Safety

Labor

Proposition 57: Criminal Sentencing Reform

BACKGROUND

California law identifies three categories of crimes: felonies, misdemeanors, and infractions. A felony is the most serious type of crime, and an individual convicted of a felony may be sentenced to state prison under certain circumstances. Individuals convicted of felonies who are not sentenced to state prison are sentenced to county jail, supervised by the county probation department in the community, or both.

Existing law classifies some felonies as "violent" or "serious," or both. Examples of felonies currently defined as violent include murder, robbery, and rape. While almost all violent felonies are also considered serious, other felonies are defined only as serious, such as assault with intent to commit robbery. Felonies that are not classified as violent or serious include grand theft (not involving a firearm) and, until the passage of Proposition 47 in November, possession of a controlled substance. In recent years, states have begun reconsidering whether the punishments meted out for various crimes appropriately fit the nature of the crime. Much of this reconsideration came as prisons became overcrowded due to enhanced sentences and as increasingly large portions of state budgets were being dedicated to prison spending.

California's Sentence Enhancements. In 1976, California moved away from the practice of indeterminate sentencing which allowed judges to sentence an individual to prison for a range of time (i.e. five years to life for robbery). In its place, the Legislature passed the determinate sentencing law (DSL), which was designed to provide transparency and uniformity in sentencing. Under the DSL, a judge must impose one of three specified terms for each criminal law violation, and the individual must serve a minimum portion of the term imposed. For example, California's Penal Code specifies terms of two, three, or five years of incarceration for second-degree robbery. The DSL was intended to reduce overcrowding in prisons by fixing sentences for certain crimes and removing judges' ability to lengthen sentences.

Over time, the Legislature passed laws creating sentence enhancements that could be added to the base crime under specific circumstances. Most notably, the Legislature approved the "Three Strikes and You're Out" law in 1994 which is discussed in detail in the following section. In addition, in 1997, the Legislature passed the "Use a Gun and You're Done" law which significant increased the penalty for using a gun during the commission of a crime. As a result of enhancements passed over that last 40 years, determinate sentences that were designed to reduce the prison population by reducing the number of years a person serves for a crime has resulted in a significant increase in prison sentences. For example, there are enhancements related to previous felony convictions, using a firearm in the commission of a crime, committing a crime as part of a street gang, carjacking, crimes causing great bodily injury, and the commission of certain sex crimes.[1] Individuals convicted of crimes eligible for multiple enhancements can often double or triple the amount of time they are required to serve in prison. As an example, an

[1] For more information on enhancements, see Penal Code Title 16. General Provisions, beginning with Section 667.

individual could receive a seven year sentence of manslaughter. However, if the individual used a gun and shot a person standing in the entrance to a house, the perpetrator could receive a 25-year to life sentence enhancement tacked onto the regular sentence for shooting into an occupied dwelling, resulting in a 32-year sentence. Likewise, an individual convicted of attempted murder could receive a 15-year sentence with an additional 25 years to life enhancement for being an ex-felon discharging a firearm and an additional 25 years to life enhancement for being an ex-felon in possession of a firearm. For this particular individual, the base crime carried a 15-year sentence and his conviction included an additional 94 years due to the enhancements.[2]

Research on the impact of enhancements has determined that longer prison sentences does not deter individuals from committing crime, nor is it an effective crime fighting tool. According to the California Budget and Policy Center, studies have shown that communities experience less crime when prison sentences are reduced. Specifically they note that during periods when California, New Jersey, and New York were significantly decreasing their prison populations relative to nationwide trends, these states saw greater reductions in violent crime than did the rest of the country.[3]

California's "Three Strikes" Law. The "Three Strikes and You're Out" law, passed in 1994, imposed a life sentence for almost any crime, no matter how minor, if the defendant had two prior convictions for crimes defined as serious or violent by the California Penal Code. Statistics from the California Department of Corrections (CDCR) indicate that the law disproportionately affects minority populations. Over 45 percent of inmates serving life sentences under the Three Strikes law are African-American. The Three Strikes law is also applied disproportionately to defendants with physical or mental disabilities. California's State Auditor estimates that the Three Strikes law added over $19 billion to the state's prison budget. There has also been widespread criticism that the Three Strikes law has had little, if any, impact on public safety.

According to The Sentencing Project, the United States is the world's leader in incarceration with 2.2 million people currently in the nation's prisons or jails – a 500 percent increase over the past 30 years. This rate of incarceration is far greater than any other industrialized nation and unprecedented throughout the history of the United States. These trends have resulted in prison overcrowding and required states to use increasing shares of their budgets to fund the rapidly expanding penal system.[4] In California alone, the public safety budget has grown from $1 billion in 1984-85, which constituted four percent of the state General Fund budget at the time, to over $13 billion (including realigned revenue) in 2017-18, constituting approximately ten percent of the state's General Fund budget.

National Sentencing Trends. After 30 years of "tough on crime" sentencing, people throughout the country from across the political spectrum have begun rethinking the incarceration of such a large percentage of the population in prisons and jails. States, including California, Texas, and

[2] Examples of enhancements come from a February 26, 2016, news story published by NBC's Bay Area affiliate (http://www.nbcbayarea.com/investigations/Thousands-of-California-Inmates-Face-Extraordinarily-Long-Sentences-Because-of-Enhancements-370335951.html)
[3] Teji, Selina. *Sentencing in California: Moving Toward a Smarter, More Cost-Effective Approach*. California Budget and Policy Center. December 2015.
[4] Information on rates of incarceration comes from www.sentencingproject.org.

New York have found that justice systems focused primarily on punishment rather than treatment and rehabilitation, is not sustainable or necessarily healthy for society. According to a recent *New York Times* article, experts have found that longer sentences and mandatory minimum sentences, which have been the trend over the last few decades, have had a minimal effect on reducing crime. The critics argue that imprisoning more people for long periods of time does not necessarily make society safer.[5]

According to testimony presented to the Senate Budget and Fiscal Review Committee last January by former California Assembly Member Chuck DeVore, who is now the Vice President of the Texas Public Policy Foundation and oversees the Right on Crime Initiative, Texas, despite its long-standing reputation as a "law and order" state, started implementing criminal justice reforms in 2007. Those reforms primarily focus on diverting low-level, non-violent offenders away from prison toward treatment or other supportive, rehabilitative, services. Since this shift away from incarceration toward other alternatives, such as substance abuse and mental health treatment, Texas has seen its crime rate drop faster than the national average. In addition, as of 2013, Texas had closed three of its prisons and has saved more than $2 billion by avoiding the need to build 17,000 additional prison beds.[6]

Three-Judge Panel. In 2009, a federal three-judge panel declared that overcrowding in the state's prison system was the primary reason that the CDCR was unable to provide inmates with constitutionally adequate health care. The court ruled that in order for CDCR to provide such care, overcrowding would have to be reduced. Specifically, the court ruled that by June 2013 the state must reduce the inmate population to no more than 137.5 percent of the design capacity in the 33 prisons operated by CDCR. Design capacity generally refers to the number of beds CDCR would operate if it housed only one inmate per cell and did not use temporary beds, such as housing inmates in gyms. Inmates housed in contract facilities or fire camps are not counted toward the overcrowding limit. In May 2011, the U.S. Supreme Court upheld the three-judge panel's ruling. Since that time, the state has made significant changes designed to reduce the number of people in the state's prison system.

Public Safety Realignment. In 2011, the Legislature approved a broad realignment of public safety, health, and human services programs from state to local responsibility. Included in this realignment were sentencing law changes requiring that certain lower-level felons be managed by counties in jails and under community supervision rather than sent to state prison. Generally, only felony offenders who have a current or prior offense for a violent, serious, or sex offense are sentenced to serve time in a state prison. Conversely, under realignment, lower-level felons convicted of non-violent, non-serious, and non-sex-related crimes (colloquially referred to as "non-non-nons") serve time in local jails. In addition, of those felons released from state prison, generally only those with a current violent or serious offense are supervised in the community by state parole agents, with other offenders supervised by county probation departments. Responsibility for housing state parole violators was also shifted from state prisons to county jails.

[5] Eckholm, Erik. "In a Safer Age, U.S. Rethinks Its 'Tough on Crime' System." New York Times, January 13, 2015.
[6] Testimony of Chuck DeVore before the Senate Budget and Fiscal Review Committee on January 30, 2014.

In adopting this realignment the Legislature had multiple goals, including reducing the prison population to meet the federal court-ordered cap, reducing state correctional costs, and reserving state prison for the most violent and serious offenders. Another goal of realignment was to improve public safety outcomes by keeping lower-level offenders in local communities where treatment services exist and where local criminal justice agencies can coordinate efforts to ensure that offenders get the appropriate combination of incarceration, community supervision, and treatment. For many, realignment was based on the confidence that coordinated local efforts are better suited for assembling resources and implementing effective strategies for managing these offenders and reducing recidivism. This was rooted partly in California's successful realignment reform of its juvenile justice over the last 15 years and the success of SB 678 (Leno), Chapter 608, Statutes of 2009, which incentivized evidence-based practices for felony probationers through a formula that split state prison savings resulting from improved outcomes among this offender population.

Passage of Proposition 36. The passage of Proposition 36 in 2012 resulted in reduced prison sentences served under the Three Strikes law for certain third strikers whose current offenses were non-serious, non-violent felonies. The measure also allowed resentencing of certain third strikers who were serving life sentences for specified non-serious, non-violent felonies. The measure, however, provides for some exceptions to these shorter sentences. Specifically, the measure required that if the offender has committed certain new or prior offenses, including some drug-, sex-, and gun-related felonies, he or she would still be subject to a life sentence under the three strikes law.[7]

February 2014 Court Order. On February 10, 2014, the federal court ordered the state to implement several population reduction measures to comply with the court-ordered population cap and appointed a compliance officer with the authority to order the immediate release of inmates should the state fail to maintain the final benchmark. The court reaffirmed that CDCR would remain under the jurisdiction of the court for as long as necessary to continue compliance with the final benchmark of 137.5 percent of design capacity and establish a durable solution.

The February 10, 2014 order required the CDCR to:

- Increase prospective credit earnings for non-violent second-strike inmates as well as minimum custody inmates.

- Allow non-violent second-strike inmates who have reached 50 percent of their total sentence to be referred to the Board of Parole Hearings for parole consideration.

- Release inmates who have been granted parole by the Board of Parole Hearings but have future parole dates.

- Expand CDCR’s medical parole program.

[7] Legislative Analyst’s Office, “Proposition 36: Three Strikes Law. Sentencing for Repeat Felony Offenders. Initiative Statute.” July 18, 2012.

- Allow inmates age 60 and over who have served at least 25 years of incarceration to be considered for parole (the "elderly parole" program).

- Increase its use of reentry services and alternative custody programs.

SB 260 and 261. In 2013, SB 260 (Hancock), Chapter 312, Statutes of 2013, created a youthful offender parole process. Under this bill, individuals who committed their crimes under the age of 18 would be eligible for parole, even if serving a life sentence. Specifically, the legislation established a youth offender parole hearing which is a hearing by the Board of Parole Hearings for the purpose of reviewing the parole suitability of any prisoner who was under 18 years of age at the time of his or her controlling offense. The bill created the following parole mechanism for a person who was convicted of a controlling offense that was committed before the person had attained 18 years of age:

- If the controlling offense was a determinate sentence the person is be eligible for release after 15 years.

- If the controlling offense was a life-term of less than 25 years then the person is eligible for release after 20 years.

- If the controlling offense was a life-term of 25 years to life then the person is eligible for release after 25 years.

In 2015, SB 261 (Hancock), Chapter 471, Statutes of 2015, expanded the youthful parole process to include people who were convicted of committing a crime prior to attaining the age of 23.

Passage of Proposition 47. In November 2014, the voters approved Proposition 47, the Reduced Penalties for Some Crimes Initiative, which requires misdemeanor rather than felony sentencing for certain property and drug crimes and permits inmates previously sentenced for these reclassified crimes to petition for resentencing.

Proposition 47 requires that state savings resulting from the proposition be transferred into a new fund, the Safe Neighborhoods and Schools Fund. The new fund will be used to reduce truancy and support drop-out prevention programs in K-12 schools (25 percent of fund revenue), increase funding for trauma recovery centers (10 percent of fund revenue), and support mental health and substance use disorder treatment services and diversion programs for people in the criminal justice system (65 percent of fund revenue). The Director of Finance is required on or before July 31 of each fiscal year to calculate the state savings for the previous fiscal year compared to 2013-14.[8]

In the proposed budget, the Administration estimates that the 2016-17 savings associated the Proposition 47, will be $42.9 million in 2016-17, an increase of $3.5 million in savings over 2015-16. On-going savings are estimated to be $69 million.

[8] 2015-16 Governor's Budget Summary

Crime and Arrest Rates. According to the California Attorney General's open justice database, California's crime rate has reached its lowest rate in 47 years. Every violent and property offense has decreased in both overall number and rate per population. California's property crime rate which includes burglary, motor vehicle theft, and larceny-theft, also declined dramatically between 1982 and 2014 for each offense. During this period, rates for burglary decreased by 74 percent, motor vehicle theft 41 percent and larceny-theft by 59 percent. Since 1980, California has seen an overall dramatic decrease in its violent crime rate, which includes homicide, rape, robbery, and aggravated assault. When comparing 1982 to 2014, rates for homicide decreased by 61 percent, rape 52 percent, robbery 66 percent and aggravated assault 37 percent.[9]

In 2014, there were 1.42 million total arrests, at a rate of 3,641 arrests per 100,000 residents. Since 1990, misdemeanor arrest rates have steadily declined and felony arrests rates have slightly decreased.[10] In 2015, the arrest rate in California overall was 4.4 percent lower than the arrest rate in 2014. The majority of the decline was due to a 17.1 percent decline in juvenile arrests. The felony arrest rate decreased by 29 percent, while the total misdemeanor arrest rate increased by 8.8 percent. In 2015, the total violent offense arrest rate increased one percent, the homicide arrest rate remained the same and the robbery and kidnapping arrest rates increased by 6.7 percent and 15.2 percent, respectively. In 2015, 45.4 percent of misdemeanor arrests were either alcohol or drug-related. In 2015, 66.9 percent of felony arrests resulted in a conviction. [11]

California's Prison Population Declines. As described in detail above, California has moved away from prison toward treatment and rehabilitation within the last five years through Public Safety Realignment in 2011; changes in the Three Strikes law in 2012; and the passage of Proposition 47. Thanks in large part to these recent efforts, California's prison population, which peaked at 173,000 in 2007, has declined to 118,560 adult inmates as of January 11, 2017. Currently, the state's prisons are at 133.8 percent of their design capacity. As these sentencing changes continue to be implemented and Proposition 57 is implemented, the population should continue to decline.

PROPOSITION 57

Approved by voters in November, Proposition 57, the California Parole for Non-Violent Criminal and Juvenile Court Trial Requirements Initiative, brings three major changes to sentencing:

- Allows individuals convicted of nonviolent felonies to be considered for parole after completing the sentence for their primary offense.
- Allows CDCR to award additional sentence reduction credits for rehabilitation, good behavior or educational achievements.

[9] California Department of Justice, Open Justice database.
[10] California Department of Justice, Open Justice database.
[11] California Department of Justice, 2015 Crime in California report, p 1-2.

- Requires a judge's approval before most juvenile defendants can be tried in an adult court.

CDCR is currently working on regulations to implement the proposition and anticipates that they will be in place by October 1, 2017.

GOVERNOR'S PROPOSAL

Under Proposition 57, the budget estimates a net savings of $22.4 million General Fund in 2017-18, growing to a net savings of approximately $140 million by 2020-21. Specifically, the budget includes the following costs and savings.

2017-18 Proposition 57 Budget Impact
(Dollars in Thousands)

Cost	
Department of Juvenile Justice Population Increase	$ 4,867
Parole	$ 4,392
Board of Parole Hearlings	$ 1,305
Implementation BCP	$ 5,687
Total Costs	$ 16,251
Savings	
Department of Juvenile Justice Reimbursement from Counties	$ (3,192)
Adult Institutions - Population Reduction	$ (7,382)
Out-of-State Contract Population Reduction	$ (28,078)
Total Savings	$ (38,652)
Net Cost/Savings	**$ (22,401)**

Caseload Impact. The Administration assumes that Proposition 57 will result in 1,959 fewer inmates in 2017-18, growing to 9,956 fewer in 2020-21. In addition, they assume that there will be 1,038 more parolees in 2017-18, growing to 3,545 by 2020-21.

Changes to Credit Earnings. The proposition provided a significant amount of flexibility in terms of awarding inmates additional credits for good behavior and rehabilitation programming. The current proposal assumes that the department will make the following changes to credit earnings:

- Increase and standardize good-time credit earnings. Good-time credits are earned when an inmate avoids violating prison rules.

  - All inmates in fire camps will receive 2-for-1 credit earning (two days off of their sentence for every day spent working in a fire camp).
  - Violent offenders will earn 20 percent. Currently, violent offenders are eligible to earn anywhere from zero to 15 percent, depending upon their crime.
  - Non-violent third-strike offenders will earn 33.3 percent. Currently, inmates serving time for a third-strike felony do not receive good-time credits.

- All inmates, with the exception of life-term inmates without the possibility of parole and condemned inmates, will be eligible to earn milestone credits. Milestone credits are earned when an inmate completes a specific education or training program that has attendance and performance requirements.

- Increase the amount of time an inmate can earn for milestone completion credits from six weeks per year to 12 weeks.

- Create new, enhanced milestone credits for one-time significant earned academic and vocational achievements, such as the earning of Associate of Arts and Bachelor's degrees, high school diplomas, the Offender Mentor Certification Program, and Career Technical Education certifications. Enhanced milestone credits will be applied retrospectively for those credits earned during the inmate's current term.

- Establish new achievement credits for inmates that have sustained participation in other rehabilitative programs and activities. Inmates will be able to earn up to four weeks of achievement credits in a 12-month period.

Credits earned by life-term inmates will be credited towards their Minimum Eligible Parole Date. CDCR does assume that, consistent with current practices, all credit earning will be revocable based on behavior-based violations.

ISSUES TO CONSIDER

Maximizing Sentence Reduction Credits for Volunteer-Led Programs. Currently, inmates are only allowed to earn milestone credits in seven volunteer-led programs. According to the program providers, receiving milestone credits for their programs was a long and cumbersome process. CDCR is currently in the process of making decisions regarding sentence reduction credits, including determining which programs should be eligible for milestone credits. The Legislature may want to work closely with CDCR to ensure that those credits are maximized and that the criteria for determining eligibility is streamlined and allows as many programs as possible, especially innovative, volunteer-led programs, to provide credits.

Program Opportunities for Parole-Eligible Individuals. One of the criteria for parole eligibility is being able to demonstrate work toward rehabilitation by participating in programming. Unfortunately, opportunities for programming can be limited and vary widely between prisons and even between housing units within prisons. So, while an inmate who is eligible for parole may have participated in every program offered to him or her, it still may not be enough for the parole board. In addition, until recently, certain programs and treatment were primarily concentrated in 11 prisons that CDCR had designated as “reentry hubs.” Therefore, unless an inmate was housed in one of those 11 facilities, they may not have access to substance use disorder treatment or cognitive behavior therapy treatment, both of which may be required for parole. Unless programming and treatment is expanded throughout the prison system and includes enough slots to satisfy the long list of inmates who are waiting for programs, initiatives like Proposition 57, which expanded eligibility for parole, may not reach as many inmates as possible, thus limiting the state’s ability to stay under the population cap without the use of private prison contracts or construction of new prisons.

Effectiveness and Quality of Rehabilitation Services and Programs. Over the last few years, the Senate has led the way in expanding rehabilitation programs in the prisons. Beginning in 2013 with the passage SB 105 (Steinberg and Huff), Chapter 310, Statutes of 2013, which provided the CDCR with an additional $315 million in General Fund in order to expand prison capacity. Within that legislation was the requirement that any unspent funding be placed in a recidivism reduction fund and be used to increase rehabilitative programming in prisons and provide funding for other programs that have been shown to reduce the likelihood that someone would return to prison after being released. Through that funding, the Legislature established innovative program grants that were designed to expand the number of restorative justice/offender responsibility programs available throughout the prison system.

Beyond those efforts, in recent years, the Legislature has segregated the funding used for rehabilitation programming in CDCR’s budget to ensure that those funds could not be redirected toward increased security staffing or other funding priorities. In addition, in 2014, the Legislature passed SB 1391 (Hancock), Chapter 695, Statutes of 2014, which significantly expanded community college programs throughout the prison system. Perhaps most significantly, the legislation required that CDCR partner with local community college districts to provide in-prison, in-person college level courses.

The Administration has embraced and supported these efforts. In addition, they have expanded them by making innovative program funding a permanent part of the rehabilitation budget and by reinstating the Arts in Corrections program at all 36 state prisons. However, along with these efforts to expand the availability of rehabilitation programing, the question remains as to whether or not the programs and treatment being offered both in prison and upon release are effective and of a high quality. The Legislative Analyst’s Office has continually recommended that the Legislature assess whether or not the $400 million being spent each year on rehabilitation programming is being spent on programs that work to reduce recidivism. Toward that end, CDCR has been partnering with several national organizations to support and evaluate parolee support and recidivism reduction strategies. These partnerships include evaluations of the Second Chance Act Adult Re-entry Demonstration projects with the National Institute of Justice, documentation of community re-entry programs with the University of California, Los Angeles and evaluation of re-entry and parolee programs with the Pew-MacArthur Results First Initiative to provide a cost-benefit analysis of current programs.

The Legislature may wish to ask CDCR to report during legislative budget hearings on the progress of the evaluations and to provide any results they have received. Depending upon the findings of the evaluations, the Legislature may want to examine the way in which rehabilitation funding is being spent and redirect it toward programs that are proven to reduce recidivism and tension in the prisons and improve the prison environment, thus improving people's chance of succeeding once they leave prison and providing a safer and productive environment for the 130,000 individuals confined to the prison system.

Definition of Violent Crime. Proposition 57 allows individuals convicted of nonviolent felonies to be considered for parole after completing the sentence for their primary offense. Under the language of the proposition, a violent felony is defined as those felonies listed under Penal Code Section 667.5(c). In recent months there has been significant debate about what is and is not included on the list of violent felonies. Several bills have been introduced this legislative session to increase the number of crimes that are counted as violent. Therefore, it is likely that the debate will continue through the policy bill process.

California's Use of For-Profit Prison Contracts

BACKGROUND

In the 1970s and 80s, the war on drugs and harsher sentencing policies, including mandatory minimum sentences, fueled a rapid expansion in the nation's prison population. The resulting burden on the public sector led private companies to step in during the 1970s to operate halfway houses. They extended their reach in the 1980s by contracting with the Immigration and Naturalization Service (INS) to detain undocumented immigrants. These forms of privatization were followed by the appearance of for-profit, private prisons. [1]

There are two private, for-profit companies providing the majority of private housing and rehabilitation services to inmates in the United States: 1) Corrections Corporation of America (CCA) (now Core Civic), established in 1983, and 2) Wackenhut Corrections Corporation (now the GEO Group, Inc.), established in 1984. Today, CCA and GEO Group collectively manage the majority of the contracts in the United States, which resulted in combined revenues exceeding $3.2 billion in 2015. CCA, as the largest private prison company, manages more than 89,000 inmates and detainees in 77 facilities. GEO Group, as CCA's closest competitor, operates slightly fewer, with 64 facilities and 74,000 beds.[2] Smaller companies, including Management & Training Corporation, LCS Correctional Services, and Emerald Corrections also hold multiple prison contracts throughout the United States.[3]

As of 2014, over eight percent of U.S. prisoners were held in privately-owned prisons. In 2014, seven states housed at least 20 percent of their inmate populations in private prisons. A total of 131,300 inmates were housed in private facilities between those states and the federal bureau of prisons. This figure represents a decrease of 2,100 prisoners from 2013. According to the federal Bureau of Justice Statistics, since 1999, the size of the private prison population grew 90 percent, from 69,000 inmates in 1999 to 131,000 in 2014. The use of private prisons was at its peak in 2012, when 137,000 inmates (almost nine percent of the total prison population) were housed in private facilities.[4]

In addition to federal prisoners, the United States detains approximately 400,000 immigrants per year. As of 2016, the Detention Watch Network (DWN) reports that 73 percent of detained immigrants were held in private, for profit prisons.[5] That percentage equates to almost 300,000 individuals held in private, for-profit immigration detention facilities throughout the United States, including in California.

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[1] Mason, Cody. *Too Good to be True: Private Prisons in America*. The Sentencing Project, January 2012.
[2] CCA and Geo 2015 Annual Reports.
[3] Mason, Cody.
[4] Prisoners in 2014. Bureau of Justice Statistics, Office of Justice Programs, United State Department of Justice. www.bjs.gov.
[5] Small, Mary, et al. *A Toxic Relationship: Private Prisons and U.S. Immigration Detention*. December 2016. Detention Watch Network.

Concerns about the use of for-profit contractors in state and federal prisons have grown in recent years. Reports detailing physical and sexual abuse, contraband, excessive use of force, inadequate safety measures, lack of adequate healthcare, and lack of programming have surfaced in many states, including federal facilities in California.[6]

In 2010, the American Civil Liberties Union (ACLU) filed a suit against CCA related to their running of the Idaho Correctional Center (ICC) in Boise, Idaho. The suit came about after reports began to surface about violence in ICC. The ACLU's complaint detailed more than 30 assaults that they argued might have been prevented had CCA operated ICC in a responsible manner.[7] In addition, in 2010, the Governor of Kentucky ordered the removal of over 400 female inmates from a CCA run facility after over a dozen women complained of being sexually assaulted by male correctional officers.

CCA, however, is far from alone in complaints about the conditions in their institutions and the treatment of inmates. In 2012, the *New York Times* published a series of investigative articles related to the treatment and oversight of inmates at the Albert M. "Bo" Robinson Assessment and Treatment Center in New Jersey run by Community Education Centers (CEC). The complaints ranged from the sexual assault of inmates by CEC staff to a lack of security that led to inmates assaulting and robbing each other during the night when only one or two staff were assigned to overseeing housing units of 170 inmates. According to the *New York Times*' findings, inmates regularly asked to be returned to a state-run prison where they felt safer.[8]

In Mississippi, a prison run by Management and Training Corporation (MTC) was deemed by one federal judge to be so corrupt that it was "effectively run by gangs in collusion with corrupt prison guards." In 2012, federal judge Carlton Reeves wrote in a 2012 settlement order that it "paints a picture of such horror as should be unrealized anywhere in the civilized world." That prison was shut down in September of 2016.[9]

GEO Corporation has also faced its share of issues over the years. Of particular note are reports on the treatment of immigrants being detained in GEO's detention facility in Adelanto, California. The ACLU, DWN, and Community Initiatives for Visiting Immigrants in Confinement (CIVIC) have all detailed abuses related to the Adelanto facility. In an October 2015 report, CIVIC and DWN outline complaints of medical abuse and neglect relating to at least one preventable death and four instances of physical abuse by GEO staff.

In addition, GEO's Walnut Grove Youth Correctional Facility in Mississippi was under federal investigation in 2012 after receiving hundreds of brutality complaints. The facility was also the subject of a federal lawsuit claiming that inmates "live in unconstitutional and inhumane

[6] To date, the Legislature is unaware of any complaints of excessive use of force or criminal activities related to private facilities housing California inmates. However, as discussed later in the piece, all but one of the contract facilities appears to be providing inadequate medical care.
[7] Pevar, Stephan. *Is CCA Guilty?* March 5, 2014. www.aclu.org
[8] Dolnick, Sam. "At a Halfway House, Bedlam Reigns." *New York Times*. June 17, 2012.
[9] Williams, Timothy. "Privately Run Mississippi Prison, Called a Scene of Horror, is Shut Down." *New York Times*. September 15, 2016.

conditions and endure great risks to their safety and security" due to understaffing, violence, corruption, and a lack of proper medical care.[10]

Generally, complaints about the private prison industry have been focused on the fact that facilities contain too few staff and that they are both underpaid and undertrained for their jobs. Thus as a result of inadequate staffing, inmates in private prisons are subject to more violence and sexual assault, higher rates of contraband, inadequate food, and inadequate medical care.

Federal Bureau of Prisons. In August of 2016, the United States Attorney General's Office of the Inspector General released a report comparing the federal Bureau of Prison-operated institutions to the private prisons under contract with the federal government. The agency found that private prisons were more dangerous and less hygienic than government facilities, citing higher instances of assault, inappropriate use of solitary confinement and inadequate medical treatment. In addition, the report found that the Bureau of Prisons needed to improve how they monitor the contracts.[11] As a result, the Attorney General's Office asked the federal government to phase-out their use of private prisons. In a memo to the Director of the Federal Bureau of Prisons calling for the phasing out of private prison contracts, Deputy Attorney General, Sally Yates noted of private prisons:

> *They simply do not provide the same level of correctional services, programs, and resources; they do not save substantially on costs; and as noted in a recent report by the Department's Office of Inspector General, they do not maintain the same level of safety and security. The rehabilitative services that the Bureau provides, such as educational programs and job training, have proved difficult to replicate and outsource, and these services are essential to reducing recidivism and improving public safety.*[12]

The prior federal Administration intended to begin phasing out the use of for-profit facilities for inmates, and possibly for immigration detainees. It is unclear whether or not the new Administration will continue with that commitment. However, given the stock prices for both GEO and CCA, it appears that the industry and stockholders believe the country will rely more on private prisons, rather than doing away with them. Since the current president was elected, CCA stock has jumped 78 percent and GEO Group Inc., is up 53 percent.[13]

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[10] Mason, Cody. *Too Good to be True: Private Prisons in America*. The Sentencing Project. January 2012.
[11] *Review of the Federal Bureau of Prisons' Monitoring of Contract Prisons*. Office of Inspector General, United States Department of Justice. August 2016.
[12] Memorandum to the Acting Director, Federal Bureau of Prisons, from Sally Q. Yates, Deputy Attorney General. August 18, 2016.
[13] Etter, Lauren. *America's Private Prisons are Back in Business*. Bloomberg. January 10, 2017. https://www.bloomberg.com/news/articles/2017-01-10/trump-deportation-plan-to-hand-windfall-to-a-dying-u-s-industry

Private Prison Facilities. Private, contract prison facilities have been an important tool for California in reducing overcrowding in its prisons in recent years. In September 2013, the Legislature passed, and the Governor signed, SB 105 (Steinberg and Huff), Chapter 310, Statutes of 2013, to address the federal three-judge panel order requiring the state to reduce the prison population to no more than 137.5 percent of design capacity by December 31, 2013. SB 105 provided the California Department of Corrections and Rehabilitation (CDCR) with an additional $315 million in General Fund support in 2013-14 and authorized the department to enter into contracts to secure a sufficient amount of inmate housing to meet the court order and to avoid the early release of inmates, which might otherwise be necessary to comply with the order. The contracts were intended to be short-term in nature and were entered into in lieu of building additional prisons throughout the state. In 2014, the state housed approximately 9,000 inmates in out-of-state, private prisons. Since that time, the state has considerably reduced its reliance on out of state, private prisons and now houses approximately half of the 2014 number of inmates out of state. CCA runs both out-of-state prisons used by California to house 4,722 inmates, 2,580 in Arizona and 2,142 in Mississippi.[14]

In California, GEO and CCA currently operate eight state facilities, including a recent contract with GEO for an 80-bed community re-entry facility in San Francisco. The 2017-18 proposed budget assumes the state will house 7,242 California inmates in private prisons (4,900 in out-of-state prisons and 2,342 in in-state prisons). These totals do not include the estimated 2,381 inmates who will be housed in California City, a prison owned by CCA and run by the state. In addition to prison facilities, the state currently contracts with both GEO and CCA to provide reentry services, parole services, substance use disorder treatment, and cognitive behavioral therapy.

California currently has approximately $330 million in contracts during 2016-17 with for-profit companies providing either housing or rehabilitation services and treatment for CDCR inmates. Of that amount, $240.5 million is for private prison facilities both in state and out of state. The remaining $89 million is for contracts providing substance use disorder treatment, cognitive behavioral therapy, parolee services, and community reentry. Of the total amount, $187 million is for contracts with CCA ($182.4 million for facilities and $4.6 million for cognitive behavioral therapy) and $71 million is for GEO contracts ($58 million for facilities and $12.4 million for rehabilitation and reentry programming). The next largest contractor on the list is CEC for $24 million.

As discussed previously, all three companies have come under considerable scrutiny nationally for their treatment of inmates and treatment of their employees. However, the Legislature has not received any complaints or reports to suggest that the problems reported in the private institutions in other states or under federal jurisdiction exist in the private state facilities in California.

[14] Out-of-state population based on CDCR's weekly population report for the week ending January 18, 2017.

The following table includes all of the companies providing either housing or rehabilitation services in California's prison system.

Private Provision of Housing and Rehabilitation Services

	2017-18 Proposed Budget	2017-18 Estimated Caseload
PRIVATE PRISONS		
In-State Modified Community Correctional Facilities		
Golden State -- GEO Group	$ 15,689,862	683
Desert View -- GEO Group	$ 15,689,862	683
Central Valley -- GEO Group	$ 15,689,862	683
McFarland Female Community Re-entry Facility -- GEO Group	$ 10,040,095	293
Out-of-State Correctional Facilities in Mississippi and Arizona		
La Palma in Arizona -- CCA	$ 75,426,460	3,067
Tallahatchie in Mississippi -- CCA	$ 15,215,540	1,833
Total	**$ 147,751,681**	**7,242**
Privately-Owned Facility Leased to the State		
California City -- CCA*	$ 72,159,958	2,381
	2016-17 Contract Amounts**	
REHABILITATION/REENTRY/PAROLE PROGRAMS***		
Behavioral Systems Southwest -- Parolee Day Reporting Center	$ 1,127,269	
Behavioral Systems Southwest -- Parolee Service Center	$ 2,146,653	
Community Education Centers, Inc. -- Cognitive Behavioral Treatment	$ 7,397,050	
Community Education Centers, Inc. -- Specialized Treatment for Optimal Programming (STOP)	$ 16,884,330	
Corrections Corporation of America (CCA) -- Cognitive Behavioral Treatment	$ 4,599,000	
GEO Group (dba BI Incorporated) -- Parolee Day Reporting Centers	$ 6,304,198	
GEO Group (dba Cornell Corrections of California) -- Parolee Service Center	$ 1,749,185	
GEO Group (dba GEO Reentry Services, LLC) -- Cognitive Behavioral Treatment	$ 3,545,421	
GEO Group -- Cognitive Behavioral Treatment	$ 1,467,440	
GEO Group (dba GEO Reentry, Inc.) -- Male Community Reentry Program	$ 1,432,558	
National Crossroads -- Parolee Service Center	$ 837,310	
Lifesigns Now -- Interpreter Services	$ 160,000	
Interpreting & Consulting -- Video Remote Interpreting	$ 692,640	
Total	**$ 48,343,055**	

*Of the $72 million budgeted for California City, approximately $30 million is for lease payments to CCA.

** CDCR does not project the amount of contracts on a contract-by-contract basis when building their budget.

*** These contracts include those in the Division of Rehabilitative Programming budget and not those in the Division of Parole Operations.

Contract Monitoring of Private Facilities. California does not seem to have encountered the same problems with private facilities as other states and the federal government. One reason for that may be the policies put in place to closely monitor and oversee the running of the private facilities. For example, all inmates housed in private facilities must be supervised in the same manner and under the same rules as the state-run prisons. These rules include an appeals process that all complaints filed by inmates be handled in the same manner as in the state-run prisons. In addition, CDCR has an appeals coordinator and two analysts who monitor the appeals process for all of the contracted facilities. These appeals are also tracked using the state's Inmate Appeals Tracking Systems.

In addition to CDCR's monitoring of contract facilities, the state's Inspector General has the same oversight and authority over private facilities as he does over the state-run prisons. For example, the Office of the Inspector General (OIG) monitors all use-of-force complaints, Prison Rape Elimination Act (PREA) complaints, and surveys rehabilitation programming. In addition, notices are required to be posted throughout the prison providing the information necessary for inmates to contact the OIG directly with complaints and concerns. The OIG, however, does not monitor healthcare in the contract facilities.

Under the state's current healthcare structure, California Correctional Healthcare Services, pursuant the leadership of the federally appointed receiver, monitors medical care at all contract facilities. The receiver's office notes that it audits all of the facilities at least once a year and then posts those audits online for the public to access. According to the introduction for the audit reports, the standardized audit tool is designed to evaluate the effectiveness, efficiency and compliance of the health care processes implemented at each contracted facility. The audit instrument is intended to measure the facility's compliance with various elements of inmate-patient access to health care and to assess the quality of health care services provided to the inmate-patient population housed in these facilities. The audits include both a review of relevant paperwork and interviews with staff and inmates in the facilities.[15]

Inadequate Medical Care. As noted previously, the federal healthcare receiver audits all of the in-state and out-of-state contract facilities each year, and all but one of those facilities is providing inadequate medical care, as indicated in the figure below. The audit findings range from patients not being seen in a timely manner and patients not receiving their medications as required to failing to properly dispose of used needles. In several facilities the nurses did not refer patients to a physician. In addition, in some instances, nurses did not confirm the identity of an individual before administering medications. The responsibility for the quality of medical care falls to CDCR. The federal receiver does not have jurisdiction over the contract facilities; however, he can refuse to allow inmates to be placed in them if the medical care remains inadequate. The receiver's office has expressed concern about the medical care being provided at the contract facilities, particularly the in-state facilities.

[15] http://www.cphcs.ca.gov/ContractPrisonFacilities.aspx

Results of Most Recent Healthcare Audits for Private Contract Facilities

Private Contract Facilities	2016 Audit Results
In-State Modified Community Correctional Facilities	
Golden State -- GEO Group	Inadequate
Desert View -- GEO Group	Inadequate
Central Valley -- GEO Group	Inadequate
McFarland Female Community Re-entry Facility -- GEO Group	Inadequate
Out-of-State Correctional Facilities in Mississippi and Arizona	
La Palma in Arizona -- CCA	Adequate
Tallahatchie in Mississippi -- CCA	Inadequate

The 2016 Budget Act provided $2 million General Fund to increase medical coverage at in-state contract facilities, in addition to the contract amounts noted previously. The funding is intended to provide for a full-time physician and an additional licensed vocational nurse.

Private Immigration Detention Facilities. In California, there are four privately-run detention facilities that hold close to 85 percent of detainees statewide, approximately 3,700 people. The rest are held in county jail facilities that contract directly with federal Immigration and Customs Enforcement (ICE).

Private Detention Centers in California

PRIVATE, FOR-PROFIT IMMIGRATION DETENTION CENTERS IN CALIFORNIA	Capacity
Adelanto Detention Facility - San Bernardino - GEO Group	1,940
Mesa Verde Detention Facility - Bakersfield - GEO Group	400
Otay Mesa Detention Facility - San Diego - CCA	1,482
Imperial Regional Detention Facility - Imperial - Management and Training Corporation (MTC)	782
Total	**4,604**

GOVERNOR'S PROPOSAL

The Governor's budget for in-state and out-of-state contract facilities includes $256 million General Fund for 2016-17 and $229 million General Fund for 2017-18. The reduction is due in large part to the funding for CCA's Tallahatchie prison being reduced from $42 million to $15 million. In the proposed budget, the Governor commits to removing all out-of-state inmates from one facility by the end of 2017-18. In addition, CDCR anticipates returning all inmates from out-of-state facilities by 2020.

ISSUES TO CONSIDER

Oversight and Monitoring Issues in California. As noted previously, in general, a system of oversight and monitoring has been put in place that helps to insure that inmates in private prisons are receiving the same supervision and care and have the same protections as those in the state-run prisons. The one area that may warrant closer oversight, and that has been of concern nationally, is the healthcare provided in the private facilities. As noted previously, all but one of the contract facilities is providing inadequate healthcare to inmates.

Currently, the OIG is responsible for monitoring the medical care for inmates in all of the state facilities. However, that monitoring does not extend to the contract facilities. The Inspector General notes that the reason they do not do medical inspections is because anyone with a serious health condition cannot be housed in a contract facility. However, given the poor quality of medical care found by the receiver, the Legislature may wish to expand OIG medical oversight to include private facilities.

Currently, as noted above, the healthcare receiver's office has an audit unit that monitors all in-state and out-of-state contract facilities' medical care. If the Legislature decides not to have the OIG monitor healthcare at private facilities while the receivership is in place, they may wish to shift the monitoring from the receiver to the OIG once the receivership ends. Absent placing the audit responsibility with the OIG, it is likely those monitoring functions would be transferred to CDCR when the receivership ends. In addition to considering the role of the OIG in monitoring healthcare at contract facilities, the Legislature should have the Administration report during budget hearings on the current state of medical care at each of the contract facilities and the steps they are taking to improve that care.

Ending Private Contracts or Closing a Prison. The 2012 Budget Act included an additional $810 million of lease-revenue bond financing authority for the design and construction of three new level II dormitory housing facilities at existing prisons. Two of these new dormitory housing facilities are located adjacent to Mule Creek State Prison in Ione, and the third is located adjacent to Richard J. Donovan Correctional Facility in San Diego. All three infill projects have been completed and activated. At the time the Legislature approved the infill projects, the understanding was that the cost of operating the facilities would be offset by the closure of the California Rehabilitation Center (CRC) in Norco. CRC is one of the state's most dilapidated prisons and it is in need of several hundred million dollars in repairs. Therefore, the new infill projects would replace the prison beds at CRC. That closure would have saved the state approximately $160 million in General Fund per year.

However, in budget discussions over the last two years, the Administration has successfully argued that CRC needed to be kept open in the short-term in order to insure that the state would stay safely below the federal population cap of 137.5 percent of the state's prison capacity. While it may be prudent to get rid of the state's contract facilities as quickly as possible, it is unlikely the state would be able to end the contracts *and* close a prison in the near future. Therefore, if the contracts are terminated prior to a closure of one of the state's prisons, it is unlikely that a prison will be closed. It is more likely that the state will need to invest in the repair and rebuilding of CRC.

If the ultimate goal of the Legislature continues to be achieving long-term savings through the closure of one of the state's prisons, they may need to prioritize that over ending the use of private contract facilities. In the long-term, that strategy will achieve greater General Fund savings. Not only will the state save a minimum of $160 million per year by reducing the number of prisons, but the state can also save over time as the number of contract beds are reduced. Unlike the budget for the state prisons, where the number of security staff is based upon the design of the facility rather than the number of inmates, the state pays for contract beds on a per-inmate basis.

Treatment and Rehabilitation Programming Provision by For-Profit Companies. While many of the investigations throughout the country have focused on the treatment of inmates housed in private prisons, these companies are also providing rehabilitative treatment in state-owned facilities and are running community reentry facilities. As the state works toward a durable solution for reducing its prison population, short of building more prisons and contracting for more private beds, the state must look toward changing sentences (as it has done) and must provide high quality, effective rehabilitation and reentry programming and treatment to ensure that people leaving prison do not return.

Given the vital importance of this aspect of the state's correctional system, the use of for-profit entities to provide critical programming and treatment for inmates has created a significant amount of concern. The Drug Policy Alliance and other advocates and non-profit service providers throughout the state have strongly objected to the use of for-profit companies to provide these services. Therefore, the question before the Legislature is whether or not a company whose primary responsibility is making a profit for its shareholders and investors is capable of providing quality, effective programming and treatment or does that mission run contrary to their bottom line need to cut costs in order to return a profit.

Arts in Corrections

BACKGROUND

Prior to the most recent recession, California had pioneered the concept of art-as-rehabilitation. In 1977, artist Eloise Smith, then the director of the California Arts Council, proposed the idea of art[1] in prison as a way to "provide an opportunity where a man can gain the satisfaction of creation rather than destruction." She found private funding to launch an arts program in one prison, and it grew to six prisons.[2] In 1980, Arts in Corrections (AIC) was established by the Legislature and California became the first state to fund a professional arts program throughout its prison system. The AIC program was designed to improve the quality of the prison experience for both inmates and staff, as well as encourage better institution-community relationships through community service art projects and concert series.

The original AIC program included individual and group instruction in visual, performing, literary and media arts, and fine craft disciplines. Originally, the AIC program was a unit of the California Department of Corrections and Rehabilitation (CDCR) Resources Development Division. The 1981-82 budget for the program was $449,784, which provided for six full-time artist/facilitators who were responsible for teaching, management of programs, screening and orientation of instructors, and who served as liaisons with contractors and outside art organizations. The six facilitators served six prisons: California Medical Facility (Vacaville), San Quentin State Prison, Correctional Training Facility (Soledad), California Men's Colony (San Luis Obispo), California Institution for Women (Corona), and California Institution for Men (Chino). The director of AIC was housed in Sacramento and was tasked with coordinating the program at the six remaining state prisons and with overseeing the artist/facilitators and the regional contractors.

The initial budget also called for contracting with professional artists and community arts organizations to provide workshops and demonstrations, as well as funding for supplies and equipment. The artist/facilitators and program and program providers also were required to actively solicit volunteers and donations.[3]

In 1983, University of San Francisco professor Lawrence Brewster performed a financial analysis at four prisons that found benefits from the program were more than double the costs. He also found that inmates in the arts program were 75 percent less likely than others to face disciplinary actions. "It's critically important," Brewster says of the program he's now studied for three decades. He went on to note, "It instills a work ethic and self-confidence. "People in the arts programs don't cause problems because they don't want to lose the privilege of being in the program."

[1] "Art" throughout this analysis refers to art in the broad sense, including visual arts, dance, theater, creative writing, and music.
[2] The Orange County Register. "The state is reviving an arts program for inmates. Can it help?" August 17, 2015.
[3] Brewster, Lawrence G. (1983) *An Evaluation of the Arts-in-Corrections Program of the California Department of Corrections.*

By 2000, state budget cuts began to significantly reduce the AIC program. In 2003, the program lost most of its funding, and by 2010 it had lapsed altogether. A few arts programs continued to work with inmates – the Prison Arts Project, the Marin Shakespeare Company and the Actors' Gang – but they were all privately funded.

The Current Arts in Corrections Program. The state's new AIC program began as a one-time, two-year pilot program in 2014, using $2.5 million unspent CDCR rehabilitation funds and administered by the California Arts Council. The Arts Council worked closely with the Department of General Services to develop a request-for-proposal (RFP). Under an expedited time frame, the Arts Council, over a three to four month period beginning in February 2014, was able to develop an RFP, solicit applications, review applications, award funding and begin the pilot program by June 2014. The renewed program offers arts to offenders in many forms such as literary, visual arts, performing arts, and media arts, as well as drawing, painting, and sculpting. Despite one year remaining in the pilot project, the 2015-16 budget included $2 million General Fund to expand the pilot into an on-going program.

In its fourth year, AIC programs currently offer an array of performing, literary, and visual arts disciplines, such as theater, music, creative writing, poetry, painting, drawing, and sculpture at 23 state prisons. Programming is provided by professional artists who are recognized as experts by their peers in the arts field and who are professionally trained in leading rehabilitative programs that are sensitive to inmate populations.

AIC programs are diverse depending on the artistic discipline, the curriculum, the arts providers, the space and the institution. Programs run anywhere from 12 weeks to 36 weeks for a group of inmates, with workshops and classes ranging from two hours twice a week to six hours one time a week. There is a maximum of 12 inmates per AIC instructor, but many programs have more than one instructor and therefore are available to more inmates. An informal survey conducted by CDCR suggests that there are approximately 1,000 inmates on waiting lists for the programs throughout the 23 institutions.

To date, more than 2,000 inmates have participated in an AIC program. Along with the regular AIC program, the Arts Council is conducting 15 AIC demonstration projects that are designed to address specific rehabilitative efforts such as mental health and preparation for reentry into society. Research on the impact of AIC programs is being conducted by the William James Association.

The 2016 budget act included funding to expand AIC programs to all 36 CDCR adult institutions in 2017, and allows the Arts Council to provide more robust programming at current facilities, strengthening existing AIC programs to reach more inmates on more yards. A multi-phased program expansion plan is currently being implemented by the Arts Council, in collaboration with CDCR. As of January 2017, the Arts Council is waiting for contract approval for the first phase of the expansion which will bring AIC programming into all 36 CDCR adult facilities. Contractors are ready to begin the implementation process once the contracts are finalized. In mid-2017, the Arts Council intends to issue an RFP for new contractors in order to increase the local resources, art forms, and arts organizations providing services throughout the prison system.[4]

Current service providers. In partnership with CDCR, the California Arts Council has contracted with the following organizations to provide rehabilitative arts services in state correctional facilities.

Actors' Gang - Los Angeles, CA
Alliance for California Traditional Arts (ACTA) - Fresno, CA
Dance Kaiso - San Francisco, CA
Fresno Arts Council – Fresno, CA
Inside Out Writers – Los Angeles, CA
Marin Shakespeare Company - San Rafael, CA
Muckenthaler Cultural Center - Fullerton, CA
Red Ladder Theatre Company / Silicon Valley Creates - San Jose, CA
Strindberg Laboratory - Los Angeles, CA
William James Association- Santa Cruz, CA

Artist/Facilitators. According to the state's job description for artist/facilitators, as distinguished from resident artists located at institutions/hospitals through grants, the artist/facilitator represents the arts program and gives that program a breadth beyond the artist/facilitator's own arts discipline. Artist/facilitators serve as a local artist for an institution, doing art and performing arts processes that involve inmates in the arts. The facilitator presents art programming for inmates and staff. In addition, the artist/facilitator is responsible for setting up studios and workshops and coordinating support for the creative processes.

Depending upon the artist/facilitators specialty, the facilitator is responsible for the following:

- As a graphics (visual) artist, sets up art studios, and with inmates, produces pieces for a show.

- As a literary artist, writes and locates written works of other institutional writers (pieces that could be used in an anthology to be printed by that institution).

- As a dramatist, directs the writing, rehearsal and performance of a play or creative dramatic production.

- As a musician, form musical groups to perform work inside or outside of the prison.

Artist/facilitators are expected to emphasize the ethnic and cultural diversity of particular prisons. They are also required to identify and facilitate using arts resources available from local public or private community resources. In addition, he or she represents the arts program at staff meetings. Finally, he or she facilitates the functioning of artists of other disciplines in the prison.[5]

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[4] California Arts Council, *Arts in Corrections Overview – 2017*.
[5] http://www.calhr.ca.gov/. Institutions Artist/Facilitator (5658).

As noted previously, a key component of the success of the old AIC program was the existence of an artist facilitator, or artist-in-residence, at every institution. Under the new program, there are no artist/facilitators coordinating the programs or teaching in the prisons. Instead, the job of facilitating the arts program has fallen to each institution's community resource manager (CRM). The AIC providers have expressed concern that the lack of an artist/facilitator limits their ability to successfully implement their programs.

Community Resource Managers. As noted previously, under the current AIC program, CRMs have taken on the role of facilitating the AIC programs at each institution. This added responsibility is in addition to their current responsibilities, which include:

- Developing, allocating, coordinating, and controlling all community resources within a prison.
- Making resource availability/priority decisions within the institution.
- Designing and implementing new and innovative programs to benefit the inmates and institution.
- Soliciting community support and resources by working with community leaders and agencies, including making presentations and follow-up visits; implementing community-sponsored activities for inmates; and designing and implementing special events to inform the community of CDCR's role in the community and society at large.
- Negotiating contracts with public entities who wish to use inmate support services.
- Developing and implementing all volunteer training and orientation procedures; monitors and reports total number of volunteer hours; serves as staff liaison to the legislatively-mandated Citizens' Advisory Committee.
- Designing, coordinating, and monitoring at-risk youth intervention programs, self-help programs and innovative programming such as Narcotics Anonymous, Insight-Out, and Center for Council.
- Supervising chaplains, coordinating, monitoring, and supporting all religious programs, including, monitoring the implementation of court- mandated religious services such as the provision of inmate religious dietary needs.
- Monitoring gate clearances and institutional contractor identification cards for contractors and volunteers.[6]

[6] http://www.calhr.ca.gov/. Community Resources Manager, Department of Corrections (9608).

Arts in the State's Juvenile Justice Facilities. The Division of Juvenile Justice (DJJ) provides education and treatment to California's youthful offenders up to the age of 25 who have the most serious criminal backgrounds and most intense treatment needs. Most juvenile offenders today are committed to county facilities in their home community where they can be closer to their families and local social services. As a result, DJJ's population represents less than one percent of the 87,000 youths arrested in California each year. This population has committed serious and/or violent felonies that require intensive treatment services conducted in a structured and secure environment. There are approximately 700 youth (678 males and 26 females) committed to four juvenile facilities in the state: N.A. Chaderjian Youth Correctional Facility (Stockton); O.H. Close Youth Correctional Facility (Stockton); Pine Grove Youth Conservation Camp (Pine Grove); and Ventura Youth Correctional Facility (Camarillo).

According to CDCR's most recent report to the Legislature on their annual performance measures, juveniles have a significantly higher rearrest and recidivism rate than adult offenders. For example, after three years, 51.3 percent of adults have been convicted of a new crime. For juveniles, however, the conviction rate after three years is 60.1 percent. While 75.1 percent of adults are arrested within three years of their release, 84.2 percent of juvenile wards have been arrested during the same time period. In addition, 38.1 percent of juvenile offenders are committed to an adult prison within three years of their release from a DJJ facility.[7]

In 2015-16, the state, on average, spent $153,000 per juvenile. In contrast, the state averages roughly $60,000 per year for each adult inmate. According to CDCR's website, DJJ provides academic and vocational education and treatment programs that address violent and criminogenic behavior, sex offender behavior, substance abuse and mental health problems, and medical care. This treatment and programming description is similar to what the CDCR provides for adult inmates. However, the actual rehabilitation programming is significantly different.

Currently, however, the AIC program is only available for adult inmates and the state provides little in the way of an organized, formal arts program to the 700 juveniles confined to the three juvenile justice facilities. Through their schooling, students are required to take 10 hours of fine arts credit to meet California graduation requirements. In addition, the O. H. Close Youth Correctional Facility School has a band, recreational therapists are providing informal arts and crafts, and the Sexual Behavior Treatment Program has an arts component.

The Benefits of Arts Program. Recent research demonstrates that involvement in arts activities has significant impact on health-related outcomes, both physical and mental, including, but not limited to, reduction in anxiety, stress, and pain levels for participants, as well as increases in overall cognitive functioning and psychological health. Arts engagement enhances resilience and coping skills, and it has been associated with cutting the length of hospital stays and decreasing health care-related infection rates and the need for pain treatments. In addition, engagement in the arts has been shown to reduce depression and increase self-esteem.[8] Studies have also shown that seniors who regularly participate in art programs report better health, fewer doctors' visits

7 *Supplemental Report of the 2015-16 Budget Package Annual Performance Measures Report*. January 13, 2017.
8 Stuckey, Heather L., DEd, and Jeremy Nobel, MD, MPH. *The Connection Between Art, Healing, and Public Health: A Review of Current Literature.* American Journal of Public Health, February 2010.

and less medication usage. The arts can also help ameliorate age-related conditions, such as dementia and cognitive decline.[9]

Along with the physical, mental and cognitive health benefits of arts engagement, numerous studies have shown the value of arts for various at-risk and vulnerable populations. University of Pennsylvania researchers have demonstrated that a high concentration of the arts in a city leads to higher civic engagement, more social cohesion, higher child welfare, and lower crime and poverty rates.[10]

Impact on Incarcerated Individuals. When California first invested in AIC in the 1980s, the California Department of Corrections investigated its impact for inmates who returned to society. The Arts in Corrections Recidivism Study, spanning 1980-87, showed a significant impact on recidivism. The bottom line conclusion was that participants in AIC were more likely to stay out of jail or prison than those who did not participate.

Other aspects of the benefits of AIC were examined in the 1980s as well, including a cost-benefit analysis. Analysis from that time showed that an investment in AIC resulted in savings for the state. Researchers compared the costs of having an AIC program that included artist facilitators on staff and outside artists providing AIC services to the benefits derived from inmates' engagement with the arts. The benefits included the direct services, but also included reduced institutional tension, cost avoidance, institutional enrichment and community service. The analysis showed that an expenditure (in 1982 dollars) of $162,790 led to a benefit of $228,522 – a cost benefit of over $70,000, or 40 percent over the investment in AIC. In today's dollars, that is equivalent to a $700,000 benefit for every $500,000 spent. The relationship between AIC participation and reduced disciplinary actions were especially compelling for the researchers. At the four institutions investigated, the decrease in disciplinary actions reduced disciplinary administration time by 4,553 hours, which was worth $77,406 in 1983. [11]

A more current analysis (2014) included the direct impact on the inmates – specifically their behavior and their attitudes about themselves.[12] This analysis showed that a significant majority of inmates attributed their greater confidence and self-discipline to pursue other academic and vocational opportunities to their participation in arts programs, signaling a pathway for overall personal growth. Specific results indicated:

- A strong correlation between participation in visual and performing arts and;
    - ✓ Improved time management.
    - ✓ Achievement motivation.
    - ✓ Intellectual flexibility.
    - ✓ Active initiative.
    - ✓ Self-confidence.

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[9] Cohen, Gene D. M.D, Phd, et al. *The Creativity and Aging Study: The Impact of Professionally Conducted Cultural Programs on Older Adults.* The Center on Aging, Health & Humanities, George Washington University. April 2006.
[10] *Top 10 Reasons to Support the Arts in 2015*. www.americansforthearts.org , Mar 13, 2015
[11] Brewster, Lawrence G. (1983) *An Evaluation of the Arts-in-Corrections Program of the California Department of Corrections.*
[12] Brewster, Lawrence G. (2014) *The Impact of Prison Arts Programs on Inmate Attitudes and Behavior: A Quantitative Evaluation*. http://williamjamesassociation.org/

- Participants who had previously studied or practiced visual, performing and literary arts were statistically more likely to pursue other educational and/or vocational programs than those without arts experience.

- A significant majority of participants reported that the arts programs helped them to relieve stress, feel happier, and gain valuable insights.

- Family relations were improved. Over half (58 percent) said their art brought them closer to family; enriching their conversations and nurturing a new identity as an artist, rather than as a convict. [13]

Impact of the Arts on Trauma Survivors. Researchers and therapists have found that the arts can play a significant role in treating individuals with post-traumatic stress disorder and other trauma-related disorders. According to scientists, it takes a lot of effort for the brain to deal with trauma. Whether because of post-traumatic stress disorder or the many adaptive behaviors that victims use instinctively in threatening situations, the traumatized brain is constantly on high-alert, particularly its lower regions, where survival instincts originate. When the lower-brain's instincts are over-activated, they can inhibit people's ability to perform higher cognitive functions until they have started healing from the trauma. Simple artistic activities like drawing or sculpting clay can soothe those lower regions, which is why art therapy can help trauma victims calm down and release some of that mental tension. Given these findings, art therapist treating trauma survivors use creativity to raise victims' awareness of their physical and mental states and build resilience and a sense of safety.[14]

Researchers have suggested that a trauma-based approach be used when working with inmates because much of their criminogenic behavior can stem from trauma early in their lives. Researchers have found that institutional environments and practices – including the constant presence of authorities and the frequent discipline they impose, the lack of privacy, restricted movement, pat downs, and strip searches – may trigger trauma-related memories and symptoms among prisoners and threaten not only the stability of individuals but also the overall safety of corrections facilities. Prisoners with any type of trauma history may have symptoms – emotional numbing, dissociation, and hyper-responsiveness to perceived threats – that make it more difficult to adjust to the institution and deal with other inmates and staff.[15] Therefore, the use of intensive arts engagement in prisons could assist in reducing trauma-induced behaviors.

Impact on At-Risk Youth. A 2012 National Endowment for the Arts research study used data from four longitudinal databases to determine the relationship between arts involvement and academic and social achievements. The study concluded that teenagers and young adults who come from a low socio-economic background and have a history of in-depth arts involvement show better academic outcomes than their peers who have less arts involvement. Specifically,

[13] Information in the impact of Arts in Corrections was compiled with the assistance of the California Arts Council for use during the 2016-17 legislative budget hearings. www.arts.ca.gov.

[14] *Calm Through Creativity: How Arts Can Aid Trauma Recovery*. National Clearinghouse on Families and Youth, December 2013.

[15] Miller, Niki, and Lisa Najavits. *Creating Trauma-Informed Correctional Care: A Balance of Goals and Environment.* European Journal of Psychotraumatology. 2012. http://community.nicic.gov/blogs/mentalhealth/archive/2013/09/09/trauma-informed-correctional-care-promising-for-prisoners-and-facilities.aspx

students with high arts involvement had higher test scores, better grades, were more likely to graduate from high school and attend college, participated in student government and extracurricular activities at a higher rate, were more likely to have volunteered recently, and were more likely to vote or participate in political campaigns.

Essentially, the report found that socially and economically-disadvantaged children and teenagers who have high levels of art engagement or arts learning show more positive outcomes in a variety of areas than their low arts engaged peers. In fact, at-risk teenagers or young adults with a history of intensive arts experiences show achievement levels closer to, or in some cases exceeding, the levels shown by the general population.[16]

The 2016 Budget Act. The 2016 Budget Act included a comprehensive arts package designed to expand access to the arts not only within state prisons, but also in communities that have traditionally been underserved by the arts. Specifically, the 2016 budget act included:

- Two permanent positions and $4 million General Fund in 2016-17 and $6 million General Fund in 2017-18 and ongoing, to expand the AIC program to all state prisons. The funding was included in the CDCR budget and provided to the California Arts Council through an interagency agreement.

- $6 million in one-time General Fund to increase art programs in underserved communities. Related budget bill language defined underserved communities as "communities who are traditionally underrepresented in the arts and generally have reduced access to arts programs. Those populations may include, but are not limited to, rural, low-income, or inner city communities, historically underserved ethnic and cultural communities, people with disabilities, veterans, youth in the juvenile justice system, people who are homeless or people with mental illnesses."

- $800,000 in one time General Fund to the Arts Council to establish a reentry/bridging grant program to facilitate and expand arts programs designed to help inmates transition from prison back into their community.

GOVERNOR'S PROPOSAL

The Governor's budget includes $8 million General Fund to provide AIC programming at all 35 state prisons. However, the budget does not include funding to continue the expansion of arts programs to underserved communities or to continue the prison reentry/bridging grant program.

[16] Catterall, James S., et al. *The Arts and Achievement in At-Risk Youth: Findings from Four Longitudinal Studies*. National Endowment for the Arts, 2012.

ISSUES TO CONSIDER

Restoring Artist/Facilitators. As discussed earlier, artist/facilitators teach classes for the inmates and serve as the liaisons between outside providers, the Arts Council and the institutions. In recent years, the Legislature has invested significant funding in the CDCR budget for innovative programming, including the AIC program. The Governor's budget largely maintains that investment. However, unless the people and organizations that provide the programming are properly supported in the institutions, it can become very difficult for those programs to operate effectively.

Community groups and volunteer groups throughout the state's prison system have expressed widespread concern for the CRMs' ability to successfully carryout their long list of duties, much less the added workload associated with coordinating and running a successful AIC program. In addition, some groups have noted that CRMs at some institutions are actually blocking their access to the prisons, rather than facilitating innovative programs and arts programs.

The Senate's version of last year's budget shifted funding from the Governor's proposed augmentations in the CDCR budget to restore the artist/facilitators to all 36 institutions. However, the final budget did not include these positions. The Senate may wish to once again augment the budget by $3.5 million General Fund, either by redirecting funding from the Governor's proposed budget or providing an augmentation. This would allow for additional art instruction and also provides the arts contractors and the Arts Council with an artist liaison in each institution to facilitate the programs and ensure that they are being fully utilized, rather than relying on overly burdened CRMs. Reestablishing artist/facilitators will also allow the arts programs to expand, reducing waiting lists.

Establish an Arts Program at the State's Juvenile Justice Facilities. Efforts to reestablish the Arts in Corrections program have not included the state's four juvenile justice facilities. As noted earlier, extensive research has shown the myriad of ways that intensive and regular exposure to the arts can help at-risk youth succeed. Essentially, exposure to the arts improves academic outcomes, community engagement, and the treatment of trauma-based disorders. Studies of arts programs in juvenile justice settings have documented that participants with ongoing artistic engagement demonstrate significant decreases in levels of disengaged or disruptive behaviors; build stronger positive social networks; and are more likely to earn high school credit while in an institution.[17]

In addition, researchers have found that providing trauma-informed arts therapy at a younger age can help significantly reduce the impact of the trauma. In *Calm Through Creativity: How Arts Can Aid Trauma Recovery*, the authors note that, "Expressive arts support trauma recovery, especially for those victims who were traumatized or seek treatment at a young age, because they engage the regions of the brain that develop earlier in life." Essentially, young people may not have communication skills that allow them to access and discuss earlier traumas. However, they do have the ability to express themselves through pictures, music or other means of artistic

[17] Wolf, D.P. & Holochwost, S. (2014) *Our Voices Count: The Potential Impact of Strength-Based Music Programs in Juvenile Justice Settings*. Washington D.C.: National Endowment for the Arts.

expression. Tapping into the young brain's ability to process information through pictures, allows young people to process and heal from traumas that they otherwise may not be able to access until much later in life. It also allows young people to reconnect with that image-based part of the brain, a process which calms the parts of the brain that have been overworked by trauma.[18]

Currently, the Arts Council provides funding for a number of programs directed at juveniles, both in schools and in the community. Among their programs specifically targeted at youth are: JUMP StArts, which provides art programs for youth involved in the juvenile justice system; Poetry Out Loud, which helps students master public speaking skills and build self-confidence; and, Artists in Schools, which supports projects that integrate community arts resources into comprehensive, standards-based arts-learning at school sites.

Given the proven benefits of arts engagement for incarcerated individuals and at-risk youth and the existence of AIC and multiple programs funded by the Arts Council targeted at youth, including those involved in the juvenile justice system, the Legislature may wish to establish an AIC program specifically designed for at-risk youth who are currently committed to the state's juvenile justice facilities.

On-going Investment in the Arts. Along with artist/facilitators and the expansion of AIC, the Senate's version of the 2016 budget included permanent funding for underserved communities and grants for arts-based prison reentry and bridging programs. Specifically, the Senate's comprehensive arts package included the following components:

- 36 permanent institution artist/facilitator positions to CDCR and $3.3 million General Fund in 2016-17, and $3.1 million General Fund in 2017-18 and on-going to provide artist/facilitators at each state prison.

- $6 million on-going General Fund and two permanent positions to the Arts Council to increase art programs in underserved communities through such programs as Local Impact, Artists Activating Communities and Arts in Schools.

- $800,000 on-going General Fund to the Arts Council to establish a reentry/bridging grant program to facilitate and expand arts programs designed to help inmates transition from prison back into their community.

As noted previously, the final budget included one-time funding to the Arts Council expansion and the reentry arts programs. The Legislature may wish to consider making that funding on-going.

[18] *Calm Through Creativity: How Arts Can Aid Trauma Recovery*. National Clearinghouse on Families and Youth, December 2013.

Changes in Gun Control Laws

BACKGROUND

California has some of the most stringent gun control laws in the United States. Over the last 25 years, California has steadily increased gun control regulations, beginning in 1990 with Governor George Deukmejian supporting a ban on assault weapons after a 1989 mass shooting at a Stockton schoolyard killing five children and wounding 30 others. These stringent regulations have likely played a significant role in the decline in gun deaths in California, which have fallen 20 percent since 2000, while nationally they have remained relatively steady.[1] This past fall, through the passage of Proposition 63, Background Checks for Ammunition Purchases and Large-Capacity Ammunition Magazine Ban (2016), and the enactment of a series of firearms bills, California has moved to further regulate the sale and ownership of guns.

Statistics on Gun Violence. The Centers for Disease Control reports that in 2015, 33,390 people died in firearms-related deaths in the United States. That equates to 10.2 people out of every 100,000. In California, 2,935 people died in firearms-related deaths, which equates to 7.4 people out of every 100,000. According to statistics gathered by the Brady Campaign to Prevent Gun Violence, over 100,000 people a year in the United States are shot.[2] According to the latest United States Department of Justice data, in 2011, about 70 percent of all homicides and eight percent of all nonfatal violent victimizations (rape, sexual assault, robbery and aggravated assault) were committed with a firearm, mainly a handgun. A handgun was used in about seven in ten firearm homicides and about nine in ten nonfatal firearm violent crimes in 2011. In the same year, about 26 percent of robberies and 31 percent of aggravated assaults involved a firearm, such as a handgun, shotgun or rifle.[3]

Firearms in California. Under California law, in order to purchase a firearm, an individual must provide a licensed gun dealer with proof of age (21 years for handguns and 18 years for long guns), pass a background check, pay a $25 fee, and wait for 10 days. In addition, a person purchasing a gun must provide proof that he or she passed the gun safety exam. All firearms must be sold with a locking device. Under certain circumstances, individuals are prohibited from owning or possessing firearms. Generally, a person is prohibited from owning guns if any of the following apply:

- If the individual is on probation or parole.
- If the individual has been convicted of a felony or of certain misdemeanors.

[1] Skelton, George. "If California voters approve stronger gun control, the message sent at the ballot box will be heard across the U.S." *Los Angeles Times*, October 24, 2016.
[2] Brady Campaign to Prevent Gun Violence. *Key Gun Violence Statistics*. www.bradycampaign.org.
[3] Firearm Violence, 1993-2011. www.bjs.gov

- If the individual has been proven to be a danger to himself or herself or to others due to a mental illness.

- If the individual has been restrained under a protective order or restraining order.

- If the individual has been convicted of certain crimes as a juvenile and adjudged a ward of the state.

In recent years, there has been a continued and substantial increase in gun purchases, extending through 2016. In fact, for the first time in the state's history, in 2016, over one million guns were sold. This represents an increase of almost 50 percent over sales in 2015. The number of long guns nearly doubled in sales and handgun sales increased by 18 percent. The table that follows illustrates the annual number of overall purchases of firearms in the state.

Firearms in California
Purchases and Denials

Year	Hand Guns Purchased	Hand Gun Denials	Long Guns Purchased	Long Gun Denials	Total Guns Purchased	Total Denials
2004	145,335	1,497	169,730	1,828	315,065	3,325
2005	160,990	1,592	183,857	1,878	344,847	3,470
2006	169,629	2,045	205,944	1,689	375,573	3,734
2007	180,190	2,373	190,438	1,926	370,628	4,299
2008	208,312	2,737	216,932	2,201	425,244	4,938
2009	228,368	2,916	255,504	2,221	483,872	5,137
2010	236,086	2,740	262,859	2,286	498,945	5,026
2011	293,429	3,094	307,814	2,764	601,243	5,805
2012	388,006	3,842	429,732	3,682	817,738	7,524
2013	422,030	3,813	538,419	3,680	960,179	7,493
2014	512,174	4,272	418,863	4,297	931,037	8,569
2015	483,372	5,417	397,231	4,252	880,603	9,669
2016	572,644		758,678		1,331,322	

Firearms Regulation Funding. Every individual purchasing a firearm in California is required to pay a $25 assessment. The funds primarily go toward supporting firearm safety and regulation within the Department of Justice (DOJ). The $25 total is the sum of three separate state fees:

- $19 background check fee payable to the Dealer Record of Sale (DROS) Special Account.

- $5 payable to the Firearms Safety and Enforcement Special Fund (FS&E).

- $1 firearm safety device fee payable to the Firearms Safety Account (FSA).

Beginning in 1999, the DOJ Bureau of Firearms began to study some of California's high-profile shootings in an effort to determine if there were remedial measures that could be enacted to curtail instances of gang violence and other similar violent events. The study found that many of the offending individuals were law-abiding citizens when they purchased the firearms, and were subsequently prohibited from gun ownership. At the time of the study, DOJ lacked the capacity to determine whether or not an individual who had legally purchased a firearm, and subsequently became prohibited from such ownership, was still in possession of a firearm. In addition, even if such a determination could have been made, the DOJ lacked the authority to retrieve that weapon from the prohibited person.

In 2001, the Legislature created the Prohibited Armed Persons File to ensure otherwise prohibited persons do not continue to possess firearms SB 950 (Brulte), Chapter 944, Statutes of 2001. SB 950 provided DOJ with the authority to cross-reference their database of individuals who own handguns with their database listing of prohibited individuals. The 2002 Budget Act included General Fund support of $1 million for DOJ to develop the Armed Prohibited Persons System (APPS). The database was complete in November 2006, with continued funding to support the program provided from the General Fund. Further legislation, SB 819 (Leno) Chapter 743, Statutes of 2011, allowed the department to utilize funds within the DROS Account for firearm enforcement and regulatory activities related to the Armed Prohibited Persons System.

Proposition 63: Background Checks for Ammunition Purchases and Large-Capacity Ammunition Magazine Ban (2016). On November 8, 2016, Proposition 63, the Background Checks for Ammunition Purchases and Large-Capacity Ammunition Magazine Ban (2016), was approved by a wide margin with over 63 percent of voters voting "yes." Proposition 63 establishes a regulatory process for ammunition sales, creates a new court process to ensure the removal of firearms from prohibited persons after they are convicted of a felony or certain misdemeanors, and tightens the restrictions around the ownership and use of large capacity magazines. Additionally, Proposition 63 states that the Legislature can change its provisions if such changes are "consistent with and further the intent" of the measure. Such changes can only be made if approved by 55 percent of the members of each house of the Legislature and the bill is enacted into law.

Regulation of Ammunition Sales. Proposition 63 includes various regulations related to the sale of ammunition. Some of the regulations would replace existing law with similar provisions. However, other regulations proposed by Proposition 63 are different, as discussed below.

- **Requirements to Buy Ammunition.** Proposition 63 includes various requirements for individuals seeking to buy ammunition and for DOJ to regulate such purchases. Specifically, the measure:
    - Requires individuals to obtain a four-year permit from DOJ to buy ammunition and for ammunition dealers to check with DOJ that individuals buying ammunition have such permits.
    - Requires DOJ to revoke permits from individuals who become prohibited.

- Allows DOJ to charge each person applying for a four-year permit a fee of up to $50 to support its various administrative and enforcement costs related to ammunition sales.

The state, however, enacted legislation in July 2016 to replace the above provisions with alternative ones. Specifically, under the legislation, (discussed in more detail below):

- Ammunition dealers would be required to check with DOJ that individuals seeking to buy ammunition are not prohibited persons at the time of purchase.

- DOJ could charge individuals up to $1 per transaction.

- **Licenses to Sell Ammunition.** Proposition 63 requires individuals and businesses to obtain a one-year license from DOJ to sell ammunition.

- **Other Ammunition Requirements.** The proposition prohibits most California residents from bringing ammunition into the state without first having the ammunition delivered to a licensed ammunition dealer, beginning in January 2018.

New Court Process for Removal of Firearms. Proposition 63 created a new court process to ensure that individuals convicted of offenses that prohibit them from owning firearms do not continue to have them. Beginning in 2018, the measure requires courts to inform offenders upon conviction that they must (1) turn over their firearms to local law enforcement, (2) sell the firearms to a licensed firearm dealer, or (3) give the firearms to a licensed firearm dealer for storage. The measure also requires courts to assign probation officers to report on what offenders have done with their firearms. If the court finds that there is probable cause that an offender still has firearms, it must order that the firearms be removed. Finally, local governments or state agencies could charge a fee to reimburse them for certain costs in implementing the measure (such as those related to the removal or storage of firearms).

Currently, local law enforcement agencies are provided monthly information regarding the armed and prohibited persons in the agency's jurisdiction. Given this access, once the armed and prohibited person is identified, DOJ and local agencies could coordinate to confiscate the weapons. However, at the present time, many agencies are relying on assistance from DOJ's criminal intelligence specialists and special agents to work APPS cases. This proposition shifts the burden from DOJ to local law enforcement and the courts by requiring probation officers to report to the court on the disposition of the firearms owned by prohibited persons.

Large Capacity Magazines. Since 2000, state law has generally banned individuals from obtaining large capacity magazines (defined as those holding more than ten rounds of ammunition). The law, however, allowed individuals who had large capacity magazines before 2000 to keep them for their own use. Beginning July 2017, recently enacted law will prohibit most of these individuals from possessing these magazines. Individuals who do not comply are guilty of an infraction. However, there are various individuals who will be exempt from this requirement—such as an individual who owns a firearm (obtained before 2000) that can only be used with a large capacity magazine. Proposition 63 eliminates several of these exemptions, as well as increases the maximum penalty for possessing large capacity magazines. Specifically, individuals who possess such magazines after July 2017, would be guilty of an infraction or a misdemeanor.

Reporting Requirements. The measure includes a number of reporting requirements related to firearms and ammunition. For example, the measure requires that ammunition dealers report the loss or theft of ammunition within 48 hours. It also requires that most individuals report the loss or theft of firearms within five days to local law enforcement. An individual who does not make such a report within five days would be guilty of an infraction for the first two violations. Additional violations would be a misdemeanor. This measure also reduces the penalty for an individual who knowingly submits a false report to local law enforcement from a misdemeanor to an infraction and eliminates the prohibition from owning firearms for ten years for such an individual.

Penalty for Theft of Firearms. Under current state law, the penalty for theft of firearms worth $950 or less is generally a misdemeanor punishable by up to one year in county jail. Under Proposition 63, such a crime is a felony and could be punishable by up to three years in state prison. Additionally, individuals previously convicted of a misdemeanor for the theft of a firearm would be prohibited from owning firearms for ten years. Currently, there is no such prohibition for a misdemeanor conviction for theft of firearms.[4]

2016 Legislative Gun Package. In 2016, the Legislature passed a series of firearm safety laws designed to strengthen the state's gun control laws. Among those laws were the following statutory changes:

- **Bullet Buttons – Senate Bill 880 (Hall and Glazer), Chapter 48, Statutes of 2016, and Assembly Bill 1135 (Levine), Chapter 40, Statutes of 2016.** California law bans, as assault weapons, semiautomatic rifles and handguns with the capacity to accept a detachable ammunition magazine and which also have any one of the enumerated weapon characteristics (e.g., folding stock, flash suppressor, pistol grip, or other military-style features). Under state regulation, if a tool is required to release the magazine, it is not considered "detachable." In response to this definition, firearm manufacturers have developed the bullet button to make military-style weapons compliant in California. The bullet button is a device that allows gun owners to detach their magazines quickly by inserting the tip of a bullet or some other small tool into a button on the side of their weapons, undermining the intent and effect of the state's assault weapon ban.

  These bills closed the loophole in existing law by redefining assault weapon in statute to include a semiautomatic, centerfire rifle or pistol that does not have a fixed magazine but does have one of the other enumerated military-style features. They further defined a fixed magazine to mean an ammunition feeding device contained in, or permanently attached to, a firearm such that it cannot be removed without disassembling the firearm action.

[4] Legislative Analyst's Office, *Proposition 63: Firearms. Ammunition Sales. Initiative Statute.* November 8, 2016.

The legislation exempts those firearms that are assault weapons that do not have a fixed magazine if they were lawfully purchased and possessed before January 1, 2017, so long as the firearm is registered with DOJ.

- **Ghost Guns – Assembly Bill 857 (Cooper), Chapter 60, Statutes of 2016.** Under federal law, it is illegal for an unlicensed person to make a firearm for sale or distribution. A loophole in the law, however, allows for the construction of firearms by unlicensed individuals so long as the firearms are made for personal use and not sold or transferred. These homemade guns are assembled through the purchase of unfinished receivers, or 80 percent completed lower receivers. Unfinished receivers, in many ways the engine of a firearm, are not technically considered firearms because of their incomplete stage and thus do not require a serial number or background check for purchase. With an unfinished receiver, a firearm parts kit, and basic drilling machinery, an individual can assemble a fully-functional firearm without being subject to the requirements placed on all other firearms transactions. Moreover, when homemade guns are seized from prohibited people, law enforcement agencies are put in the impossible situation of identifying and cataloging the firearm, as required for administrative purposes, because of a lack of any unique serial number or identifying mark. This is particularly burdensome when law enforcement seizes a large quantity of homemade guns, an occurrence that is becoming more commonplace.

  AB 857 requires a person, commencing July 1, 2018, to apply to and obtain from DOJ a unique serial number or other mark of identification prior to manufacturing or assembling a firearm; and requires by January 1, 2019, any person who, as of July 1, 2018, owns a firearm that does not bear a serial number assigned to it to obtain a unique serial number or other mark of identification.

- **Regulation of Ammunition – Senate Bill 1235 (de Leon), Chapter 55, Statutes of 2016.** California had enacted legislation designed to keep guns out of the hands of criminals, but until 2016, it had done little to prevent criminals, gang members, and other prohibited people from procuring the ammunition that fuels gun violence. Several cities require vendors to keep records of ammunition sales, leading to the arrest of thousands of armed and dangerous criminals. Similarly, California enacted statewide legislation requiring vendors to record handgun ammunition sales, but this law has been tied up in litigation involving the statutory definition of handgun ammunition. Consequently, as the result of a court injunction preventing enforcement of the law, any criminal can purchase ammunition, no questions asked.

  This legislation replaced the language in Proposition 63 and required vendors to obtain a state license to sell ammunition, log information about ammunition transactions, and screen the ammunition purchaser for any prohibitions at the point of sale. There are three main components to the legislation: vendor licensing, purchase authorization, and purchase information collection.

- **Gun Violence Research – Assembly Bill 1602 (Committee on Budget), Chapter 24, Statutes of 2016.** Too little is known about firearm violence and its prevention. The dearth of research in this field is due, in substantial part, to the congressional limits placed on the

Centers for Disease Control and Prevention that, in effect, curtail federal funding for firearm violence research. The need for more – and more sophisticated – research, however, still remains so that California, and the nation, can mount effective, evidence-based responses to combat gun violence.

The Budget Act of 2016 included $5 million one-time General Fund over five years to establish a firearm violence research center at the University of California. Budget trailer bill language specified the research include, but not be limited to, the effectiveness of existing policies and laws, and efforts to promote the responsible ownership and use of firearms. Under the legislation, the center will be housed in the University of California system and operate under the following principles:

- Interdisciplinary work of this center should address the nature of firearm violence; individual and societal determinants of risk for involvement in firearm violence, whether as a victim or a perpetrator; the individual, community, and societal consequences of firearm violence; and the prevention and treatment of firearm violence.
- The center should conduct basic, translational, and transformative research with a mission to provide the scientific evidence on which sound firearm violence prevention policies and programs can be based. Its research should extend to firearm violence as a form of terrorism.
- The center should work on a continuing basis with policy makers in the California Legislature and state agencies to identify, implement, and evaluate innovative firearm violence prevention policies and programs.

- **Gun Lending – Assembly Bill 1511 (Santiago and Chiu), Chapter 41, Statutes of 2016.** Prior to passage of this legislation, people were allowed to loan firearms to a person personally known to the gun owner for up to 30 days. This category of individuals was extremely broad. AB 1511 limited a gun owner's ability to loan firearm only to his or her family members.

GOVERNOR'S PROPOSAL

Proposition 63 Implementation. Proposition 63 included a $25 million General Fund loan for the DOJ to begin implementing the changes included in the proposition. The Governor's proposed budget does not include any information on how the department intends to spend the funds or the costs associated with implementation.

The Judicial Council estimates that Proposition 63 will cost the trial courts approximately $11.4 million per year for the new court processes that require the court to ensure that individuals convicted of a prohibiting offense have relinquished their firearms. The Governor's budget, however, does not include any additional funding for the courts to cover this cost.

Senate Bill 880 (Hall), Chapter 48, Statutes of 2016, and Assembly Bill 1135 (Levine), Chapter 40, Statutes of 2016 – Assault Weapon Registration/Bullet Buttons. The budget proposes an increase of $2.6 million and 27 positions in DROS Special Fund spending authority to implement the provisions of Senate Bill 880 and Assembly Bill 1135. The requested funding would be loaned from the FS&E Special Fund, and would be repaid no later than June 30, 2021, by revenue in the DROS fund.

AB 857 (Cooper), Chapter 60, Statutes of 2016 – Ghost Guns. The budget proposes an increase of $1.4 million in 2017-18, $1.0 million in 2018-19, $866,000 in 2019-20 and $820,000 on-going in DROS Special Fund spending authority to support eight positions to implement the provisions of AB 857. The requested funding would be loaned from the FS&E Special Fund, and would be repaid no later than June 30, 2021, by revenue in the DROS fund.

ISSUES TO CONSIDER

Require a Detailed Accounting of $25 million General Fund Appropriated through Proposition 63. As noted previously, Proposition 63 included a $25 million appropriation as a General Fund loan for the DOJ to begin implementation of the requirements of the proposition. The Governor's proposed budget, however, does not include any details on how those funds will be spent. The Legislature may wish to include oversight of the $25 million loan in its annual budget process by requiring the DOJ to submit a report on the implementation of Proposition 63 and the related expenditures during budget subcommittee hearings.

Require an Annual Report to the Legislature on the Removal of Guns from Armed Prohibited Persons. Over the last several years, the Legislature has expressed concerns related to the backlog of individuals in the Armed Prohibited Persons System who had not surrendered their firearms. During those discussions, the Legislature considered creating a partnership between DOJ and other state and local law enforcement to assist in the retrieval of prohibited firearms. Proposition 63 creates such a partnership by establishing a new court process related to prohibited persons. The Legislature may wish to require annual updates from DOJ and the Judicial Council related to the removal of guns from prohibited persons.

Retiree Healthcare

BACKGROUND

Since 1961, California has provided health benefits to eligible retired state employees. The health plans available to retired state employees are the same plans available to active employees, including supplemental plans for people enrolled in Medicare. Since 1978, the maximum contribution available to retired state employees covers 100 percent of an average of California Public Employment Retirement System (CalPERS) premium costs plus 90 percent of average CalPERS premium costs for enrolled family members, this is often referred to as the 100/90 formula. Retired state employees now generally are eligible to receive this contribution after 20 years of state service. Retired employees with ten years of state service receive 50 percent of this amount, increasing five percent annually until the 100 percent level is earned. Most state retirees receive the 100/90 contribution. In 2017, the 100/90 formula entitles retirees to a maximum state contribution towards their health care of $707 per month for single coverage. About two-thirds of retirees are enrolled in Medicare and a state-sponsored Medicare supplemental plan, the rest are enrolled in one of the plans offered to active employees. The state contribution for the typical retiree who is enrolled in Medicare is sufficient to pay the monthly CalPERS Medicare health plan premium and Medicare Part B premium costs—$134 per month for the typical Medicare enrollee.

Instead of setting aside money during an employee’s career to pay for the future cost of retiree health care, the state has—until recently—funded the cost of retiree health benefits on a pay-as-you-go basis after an employee retires. This means that later generations pay for benefits of past public employees. This has resulted in large unfunded state liabilities for the benefits. Unfunded liabilities can emerge even if the state were to set aside the amount of money actuaries determine is necessary to fully fund the benefit, if assumptions used by actuaries in their calculations do not materialize in the future. For example, unfunded liabilities in the CalPERS pension system grew over the past decade or so largely because (1) investment returns fell short of what actuaries assumed and (2) employees are living longer in retirement than actuaries had assumed. In the case of the state’s retiree health benefit, the State Controller’s Office determined that the total unfunded liability resulting from retiree health benefits earned by all current employees and retirees is about $76.7 billion. With the state paying for these benefits on a pay-as-you-go basis, these unfunded liabilities have grown each year. The largest contributing factors to the rapid growth in these costs are the rising cost of health premiums and the growing number of people receiving this benefit as more employees retire and people live longer.

The following table displays the Governor’s budget expenditures for health and dental benefits for retirees (excluding employees who work for the California State University).

Health and Dental Benefits Funding

FUNDING	2015-16*	2016-17*	2017-18*
0001 General Fund	$1,551,749	$1,642,229	$1,778,518
0950 Public Employees Contingency Reserve Fund	4,600	4,600	4,600
TOTALS, EXPENDITURES, ALL FUNDS	**$1,556,349**	**$1,646,829**	**$1,783,118**

The following table reflects Governor's budget augmentations for state employee compensation. Included in this figure is $1.2 billion ($602.3 million General Fund) for employee compensation and prefunding of other post-employment benefits (OPEB) for active employees and state employees of the judicial branch.

Budget Augmentations for State Employee Compensation

FUNDING	2015-16*	2016-17*	2017-18*
0001 General Fund	$-	$196,926	$799,255
0494 Other - Unallocated Special Funds	-	151,280	530,234
0988 Other - Unallocated Non-Governmental Cost Funds	-	74,511	261,160
TOTALS, EXPENDITURES, ALL FUNDS	**$-**	**$422,717**	**$1,590,649**

Over the last several years, the Administration has been focused on paying down the state's unfunded liabilities, in particular, the unfunded liabilities associated with retiree healthcare. Until recently, most state worker groups – as well as the state - did not partially prefunded retiree health benefits. The Administration's 2015-16 budget proposal sought to implement sweeping reforms to retiree healthcare. As a result, the Administration, through the collective bargaining process, has required state employees to begin contributing to retirement healthcare obligations. The strategy for addressing the liability includes (1) equal cost-sharing between the employee and employer to prefund retiree health benefits, and (2) for new employees, extending the period to qualify for retiree health and dental benefits from 20 to 25 years and reducing the amount of money the state contributes towards these future employees' healthcare in retirement. Bargaining agreements reached in the past year have all included these retiree health provisions. Thus far, the Legislature has ratified agreements with Bargaining Unit 2 (Attorneys and Hearing Officers), 6 (Corrections), 7 (Protective Services and Public Safety), 9 (Professional Engineers), and 10 (Professional Scientific).

These ratified agreements change future retiree health benefits for employees first hired in 2017 and thereafter. Unlike the benefit received by current retirees, retired future employees will receive a significantly smaller amount of money from the state to pay for healthcare. Specifically, instead of the 100/90 formula, (1) the maximum benefit available to retirees not eligible for Medicare will be up to 80 percent of the weighted average premium cost of CalPERS health plans available to active employees and (2) the maximum benefit available to employees eligible for Medicare will be up to 80 percent of the weighted average premium cost of CalPERS Medicare plans and retirees will be responsible for paying the full Medicare Part B premium. Using current premiums for comparison, whereas a typical current retiree enrolled in Medicare has no premium costs, a retired future employee enrolled in Medicare would be responsible for paying more than $1,800 per year to pay Medicare Part B premiums and CalPERS Medicare plan premiums. This is more than five percent of the average pension received by retired state employees in 2014-15. Moreover, under the agreements, employees will have to work five years longer (25 years) to receive the maximum benefit in retirement.

The agreements begin to address unfunded retiree health benefits for employees. While the Administration's plan seems to keep making pay-as-you-go benefit payments for many years, the new arrangement would begin to fund "normal costs" each year for the future retiree health benefits earned by today's workers. The agreements establish a "goal" that employees and the state each regularly contribute half of the normal costs by a specified date. The agreements deposit these payments in dedicated accounts in an invested trust fund managed by CalPERS. These accounts would generate earnings and gradually reduce unfunded liabilities over the next three decades or so.

Currently, the state has approximately $400 million set aside in the prefunding trust fund to pay for future retiree health benefits. By the end of 2017-18, the trust fund balance will more than double and approach $1 billion in assets. Additionally, as part of AB 133 (Committee on Budget), Chapter 2, Statutes of 2016, the 2015 Budget Act included a one-time allocation of $240 million to pay down the state's unfunded liability for retiree health care. This amount was to be apportioned to the trust fund accounts of bargaining units that had reached a memorandum of understanding with the Administration by November 1, 2016, and where such agreement includes employer and employee contributions for prefunding retiree health care. Pursuant to the requirements of AB 133, the $240 million appropriation has been apportioned to the Attorneys and Administrative Law, California Highway Patrol, Correctional Officers, Public Safety Officers, Professional Engineers, and Professional Scientists units.

GOVERNOR'S PROPOSAL

The budget includes $1.6 billion ($799 million General Fund) for employee compensation, health care costs for active state employees, and retiree health care prefunding for active employees. Included in these costs are salaries and benefit increases as a result of contract negotiations and pay increases related to minimum wage changes in Senate Bill 3 (Leno), Chapter 4, Statutes of 2016. Funding is also included for 2018 calendar year increases in health care premiums and enrollment.

California State University (CSU) Health Benefits for Retired Annuitants. The budget proposes $295.3 million General Fund to fund health benefit services for retired CSU employees and their dependents.

University of California (UC) Retirement. The budget includes $169 million Proposition 2 funds for the unfunded liability of the UC retirement plan. The amount represents the final installment of a total of $436 million in one-time funds provided over a three-year period.

ISSUES TO CONSIDER

Since the 2016 Budget Act, the Administration has negotiated contract agreements with the bargaining units represented by the Service Employees International Union (SEIU), attorneys and administrative law judges, public safety officers, craft and maintenance workers, stationary engineers, health and social service professionals, psychiatric technicians, and firefighters. These MOUs are currently pending in the Legislature. These agreements include employer and employee prefunding for retiree healthcare, and extended vesting schedule for retiree healthcare and dental benefits. The Administration will continue bargaining with the unit representing physicians and dentists, which is the only bargaining unit that is working under an expired agreement.

Pension Costs Will Increase. At its December 2016 meeting, the CalPERS board voted to change a key assumption used in calculating how much money employers and employees must contribute to the pension system each year. Specifically, the board voted to lower the discount rate from seven and a half percent to seven percent over the next three years. This lower discount rate means that CalPERS calculations of plan assets and liabilities will assume investments will have lower returns. By assuming less money comes into the system through investment gains, the state will be required to contribute significantly more money to pay for higher normal costs and a larger unfunded liability.

OPEB Contribution Rates Likely Will Need to Be Changed in Future. The bargaining agreements establish state and employee contributions to prefund retiree health benefits as a percent of pay. These contributions are based on current assumptions - including assumptions related to investment returns. The trust fund used to prefund retiree health benefits is administered by CalPERS. CalPERS indicated that it expects investment returns over the next ten years to be lower than the state assumed in the past. While CalPERS took action to lower the discount rate for pension, it did not adjust the OPEB discount rate, and the Legislative Analyst's Office indicates that the current investment return assumption for OPEB might need to be lowered. Similar to the pension discount rate, lowering this assumption could significantly increase the amount of money that needs to be contributed to fully fund retiree health benefits.

Effect of Retiree Health Prefunding on Recruitment and Retention. The Legislature may wish to consider how these bargaining agreements might affect employee recruitment or retention. Requiring current employees to make contributions towards retiree health benefits reduces employees' take home pay. This, in turn, could make it more difficult for the state to recruit or retain certain employees. Younger people, for example, might find state employment less attractive because they would be required to make contributions as well as work longer to obtain the benefits. Older employees, conversely, might retire earlier than they would otherwise. This is because, in retirement, these employees would not be required to make payments towards prefunding the benefit.

APPENDIX

TIMELINE FOR THE 2017-18 BUDGET BILL

Tuesday	January 10	Governor submits State Budget to the Legislature.
Tuesday	January 10	Committee releases *Summary of Governor's Proposed 2016-17 Budget.*
Friday	January 13	Legislative Analyst submits *Overview of the Governor's Budget.*
Tuesday	January 17	Committee conducts overview hearing of the Governor's Proposed 2016-17 Budget.
Thursday	February 9	Full Budget Committee holds oversight hearing – Information Technology: Focus on Financial Information System for California (FI$Cal)
Monday	February 13	Committee releases *Overview of the 2017-18 Governor's Budget.*
Thursday	February 16	Full Budget Committee holds oversight hearing – Marijuana in California: Revenue, Budget and Community Impact.
Monday	February 23	Full Budget Committee holds oversight hearing – California Correctional System.
Thursday	March 2	Subcommittee budget hearings begin.
Monday	April 3	Department of Finance submits Finance Letters.
Thursday	April 6	Spring Recess begins.
Monday	April 17	Legislature reconvenes from Spring Recess.
Thursday	May 11 (est.)	Governor delivers May Revision to the Legislature.
Thursday	June 15	Legislature must pass budget to meet constitutional deadline for passage of the budget.
Thursday	June 30	Governor signs 2017-18 Budget

STAFF ASSIGNMENTS

OVERALL BUDGET	MARK IBELE JOE STEPHENSHAW
CORRECTIONS AND PUBLIC SAFETY	JULIE SALLEY-GRAY
DEVELOPMENTAL SERVICES	RENITA POLK PEGGY COLLINS
EDUCATION	
K-12 EDUCATION	ELISA WYNNE
HIGHER EDUCATION	ANITA LEE
EARLY CHILDHOOD EDUCATION	ELISA WYNNE
ENERGY	JAMES HACKER
ENVIRONMENTAL PROTECTION	JOE STEPHENSHAW
HOUSING AND COMMUNITY DEVELOPMENT	JAMES HACKER
JUDICIARY	JULIE SALLEY-GRAY
LABOR AND EMPLOYEE COMPENSATION	ANITA LEE
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RESOURCES	JOE STEPHENSHAW
TAXES AND REVENUES	MARK IBELE
STATE ADMINISTRATION	RENITA POLK MARK IBELE
TRANSPORTATION	JAMES HACKER
VETERANS AFFAIRS	RENITA POLK
COMMITTEE SECRETARY	SANDY PEREZ
COMMITTEE ASSISTANT	MARY TEABO

CALIFORNIA STATE BUDGET HISTORY

Fiscal Year	Bill and Chapter No.	Date Passed and Chaptered		Total Budget ($ Billions)
1965-66	AB 500/757	6-18	6-30	4.0
1966-67[a]	SB 1XX/2	6-30	6-30	4.7
1967-68	AB 303/500	6-29	6-30	5.0
1968-69	SB 240/430	6-28	6-29	5.7
1969-70	SB 255/355	7-3	7-3	6.3
1970-71	AB 525/303	7-4	7-4	6.6
1971-72[b]	SB 207/266	7-2	7-3	6.7
1972-73[c]	SB 50/156	6-15	6-22	7.4
1973-74	AB 110/129	6-28	6-30	9.3
1974-75	SB 1525/375	6-28	6-30	10.3
1975-76	SB 199/176	6-26	7-1	11.5
1976-77	SB 1410/320	7-1	7-2	12.6
1977-78	AB 184/219	6-24	6-30	14.0
1978-79	AB 2190/359	7-5	7-6	18.8
1979-80	SB 190/259	7-12	7-13	21.5
1980-81	AB 2020/510	7-16	7-16	24.5
1981-82c	SB 110/99	6-15	6-28	25.0
1982-83	AB 21/326	6-30	6-30	25.3
1983-84	SB 123/324	7-19	7-21	26.8
1984-85c	AB 2313/258	6-15	6-27	31.0
1985-86c	SB 150/111	6-13	6-28	35.0
1986-87c	AB 3217/186	6-12	6-25	38.1
1987-88	SB 152/135	7-1	7-7	40.5
1988-89	AB 224/313	6-30	7-8	44.6
1989-90	SB 165/93	6-29	7-7	48.6
1990-91	SB 899/467	7-28	7-31	51.4
1991-92	AB 222/118	6-20/7-4	7-16	55.7
1992-93	AB 979/587	8-29	9-2	57.0
1993-94	SB 80/55	6-22	6-30	52.1
1994-95	SB 2120/139	7-4	7-8	57.5
1995-96	AB 903/303	8-2	8-3	56.8
1996-97	SB 1393/162	7-8	7-15	61.5
1997-98	AB 107/282	8-11	8/18	67.2
1998-99	AB 1656/324	8-11	8-21	71.9
1999-00	SB 160/50	6/16	6/29	81.3
2000-01	AB 1740/52	6/22	6/30	99.4
2001-02	SB 739/106	7/21	7/26	103.3
2002-03	AB 425/379	9/1	9/5	98.9
2003-04	AB 1765/157	7/29	8/2	98.9
2004-05	SB 1113/208	7/29	7/31	105.3
2005-06	SB 77/38	7/7	7/11	117.3
2006-07	AB 1801/47	6/27	6/30	131.4
2007-08	SB 77/171	8/21	8/24	146.5
2008-09	AB 1781/268 & AB 88/269	9/16	9/23	144.5
2009-10	SBx3 1/Ch 1 & ABx4 1/Ch 1	2/20 – 7/23	2/19 - 7/28	119.2
2010-11	SB 870/Ch 712	10/7	10/8	125.3
2011-12	SB 87/Ch 33	6/28	6/30	129.5
2012-13c	AB 1464/Ch 21 & AB 1497/Ch 29	6/15	6/27	142.4
2013-14c	AB 110/Ch 20	6/14	7/1	145.3
2014-15c	SB 852/Ch. 25	6/15	6/20	156.4
2015-16c	AB 93/Ch 10, SB 97/Ch 11, and SB 101/Ch 321	6/15, 6/19 9/11	6/19, 6/24 and 9/22	167.6
2016-17	SB 826/Ch 23, AB 1622/Ch 44, AB 1623/Ch 318, AB 1613/Ch 370	6/15, 6/30, 8/24, /31	6/27, 7/1, 9/13, and 9/14	170.9

[a] *1966 Second Extraordinary Session.*
[b] *First year budget was to be enacted by June 15.*
[c] *June 15 constitutional deadline met (8).*

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

		2016-17	2017-18	2018-19	2019-20	2020-21
1	**Major Revenues**					
2	Alcoholic Beverage Taxes and Fees	370	372	374	376	378
3	Corporation Tax	10,389	10,878	11,348	11,937	12,497
4	Cigarette Tax	79	65	63	61	59
5	Insurance Gross Premiums Tax	2,309	2,368	2,431	2,774	2,839
6	Mobile Home in-lieu Tax	1	1	1	0	0
7	Personal Income Tax	83,136	85,865	89,078	93,169	97,490
8	Retail Sales and Use Taxes	24,994	25,179	26,232	27,153	28,100
9	**Total Major Revenues**	**$121,278**	**$124,728**	**$129,527**	**$135,470**	**$141,363**
10	**Minor Revenues/Transfers**					
11	Misc Revenue from Local Agencies	171	167	167	167	167
12	Income from Pooled Money Investments	60	97	160	237	281
13	State Lands Royalties	55	38	72	83	115
14	Abandoned Property	371	378	386	387	399
15	Miscellaneous Revenues	53	53	50	50	50
16	Tribal Gaming Revenues	192	11	11	11	11
17	Penalty Assessments - Other	32	32	32	32	32
18	Loan Repayments to Other Funds	-413	-244	-396	-367	-234
19	Weight Fee Transfers	-106	-380	-319	-373	-319
20	All Other Transfers and Loans	27	69	59	-25	211
21	Transfer to BSA for Rainy Day Funds	-3,184	-1,156	-1,191	-1,195	-1,201
22	Remaining Others	229	234	232	232	231
23	**Total Minor Revenues/Transfers**	**-$2,513**	**-$701**	**-$737**	**-$761**	**-$257**
24	**Total Revenues and Transfers**	**$118,765**	**$124,027**	**$128,790**	**$134,709**	**$141,106**

General Fund Multi-Year N98 Expenditures by Agency
at 2017-18 Governor's Budget

(Dollars in Millions)

	2016-17	2017-18	2018-19	2019-20	2020-21
N98 excludes Capital Outlay, Debt Service					
Legislative, Executive	$1,318	$1,267	$1,209	$1,213	$1,184
Courts	2,042	1,919	1,917	1,913	1,913
Business, Consumer Services, and Housing	77	31	30	30	30
Transportation	4	-	-	-	-
Natural Resources	2,036	1,742	1,567	1,554	1,545
Environmental Protection	82	82	75	74	71
Health and Human Services	35,010	33,826	36,569	40,590	43,056
Interim Affordable Care Act County Offset	(-586)	(-546)	(-546)	(-546)	(-546)
Final Reconciliation for Affordable Care Act County Offset[1/]	(164)	(-246)	(0)	(0)	(0)
Corrections and Rehabilitation	10,326	10,501	10,520	10,547	10,609
AB 109 Savings	(-1,544)	(-1,544)	(-1,544)	(-1,544)	(-1,544)
Receiver's Costs	(1,976)	(2,017)	(2,039)	(2,058)	(2,083)
Education	11,846	12,215	12,878	13,701	14,453
STRS Contribution	(2,473)	(2,787)	(3,030)	(3,286)	(3,554)
PERS Contribution (GF) (CSU Only)	(621)	(672)	(730)	(809)	(860)
Labor and Workforce Development	177	122	72	71	71
Government Operations	772	740	721	716	715
General Government	2,169	3,020	4,118	5,179	6,582
Non-Agency Departments	(725)	(632)	(594)	(582)	(582)
Tax Relief/Local Government	(459)	(435)	(428)	(428)	(428)
Statewide Expenditures	(985)	(1,953)	(3,096)	(4,167)	(5,572)
PERS Contribution (GF) (State Only)	(2,506)	(2,784)	(3,104)	(3,542)	(3,878)
Item 9800 Employee Compensation	(197)	(799)	(1,399)	(1,775)	(1,918)
Capital Outlay	1,202	187	120	145	50
Debt Service	5,370	5,518	5,682	5,494	5,269
Total N98 Expenditures	**$72,431**	**$71,169**	**$75,478**	**$81,227**	**$85,548**

[1/]The 2016-17 amount is the repayment to counties for the 2013-14 reconciliation. The 2017-18 amounts is the payment from counties for the 2014-15 reconciliation.

General Fund Prop 98 Expenditures
at 2017-18 Governor's Budget

(Dollars in Millions)

	2016-17	2017-18	2018-19	2019-20	2020-21
Proposition 98 guarantee (GF) (before heatlh care share of EPA)	42,846	44,530	45,361	46,610	47,565
Add GF after heatlh care share of EPA	-	-	N/A	N/A	N/A
Education Protection Account (before health care share of EPA)	7,484	6,821	7,084	7,410	7,743
Minus Health care share of EPA	-	-	N/A	N/A	N/A
Local Property Tax	21,039	22,160	23,301	24,495	25,676
Total Prop 98 guarantee	71,369	73,511	75,746	78,515	80,984
Percent Change to Prior-year	3.93%	3.00%	3.04%	3.66%	3.14%
Prop 98 Test	3	3	3	2	2
General Fund Base	42,846	44,530	45,361	46,610	47,565
Education Protection Account	7,484	6,821	7,084	7,410	7,743
QEIA Payment	0	0	0	0	0
Williams Settlement	0	0	0	0	0
Settle-Up for Old Years	(218)	(400)	291	302	33
Mandate Payments	(335)	(400)	(291)	(302)	(33)
Total General Fund	50,330	51,351	52,736	54,322	55,341
Prop 98 Obligations					
Maintenance Factor Created/Paid (+/-)	864	264	50	-29	-159
Maintenance Factor Balance Prior to Proposition 2	526	543	560	580	505
Maintenance Factor Balance After Proposition 2	838	1,085	1,118	1,069	985
Settle-Up Balance	1,026	626	335	33	0
Budgetary Deferrals Balance	859	0	0	0	0
QEIA Balance	0	0	0	0	0
Mandate Balance	1,835	1,701	1,593	1,493	1,483
Williams Settlement Balance	0	0	0	0	0

General Fund Multi-Year Forecast
at 2017-18 Governor's Budget
(Dollars in Millions)

	2016-17	2017-18	2018-19	2019-20	2020-21
RESOURCES:					
Prior Year Balance	$5,023	$1,027	$2,534	$3,110	$2,270
Revenues/Transfers	$121,949	$125,183	$129,981	$135,904	$142,307
Transfer to the Budget Stabilization Account [1/]	-$3,184	-$1,156	-$1,191	-$1,195	-$1,201
Total Resources	$123,788	$125,054	$131,324	$137,819	$143,376
EXPENDITURES:					
Proposition 98	$50,330	$51,351	$52,736	$54,322	$55,341
Non-Proposition 98	$72,431	$71,169	$75,478	$81,227	$85,548
Unallocated Proposition 2 Debt Payments					(627)
Total Expenditures	$122,761	$122,520	$128,214	$135,549	$140,889
FUND BALANCES:	$1,027	$2,534	$3,110	$2,270	$2,487
Reserve for Encumbrances	$980	$980	$980	$980	$980
Special Fund for Economic Uncertainties	$47	$1,554	$2,130	$1,290	$1,507
Budget Stabilization Account/Rainy Day Fund	$6,713	$7,869	$9,060	$10,255	$11,456
BSA balance as a percentage of General Fund tax proceeds	5.5%	6.3%	7.0%	7.5%	8.1%
Operating Surplus/Deficit with BSA Transfer	-$3,996	$1,507	$576	-$840	$217

[1/] Includes additional $1.840 billion BSA transfer in 2016-17.

Debts and Liabilities Eligible for Accelerated Payments Under Proposition 2
2017-18 Governor's Budget
(Dollars in Millions)

	Outstanding Amount at Start of 2017-18	Proposed Use of 2017-18 Pay Down	Proposed Use of 2018-19 Pay Down	Proposed Use of 2019-20 Pay Down	Proposed Use of 2020-21 Pay Down
Budgetary Borrowing					
Loans from Special Funds	$1,365	$252	$465	$407	$241
Underfunding of Proposition 98—Settle-Up	1,026	400	291	302	33
Repayment of pre-Proposition 42 Transportation Loans	706	235	235	236	0
State Retirement Liabilities					
State Retiree Health	74,103	100	200	250	300
State Employee Pensions	49,592	0	0	0	0
Teachers' Pensions [1/]	72,626	0	0	0	0
Judges' Pensions	3,279	0	0	0	0
Deferred payments to CalPERS	627	0	0	0	0
University of California Retirement Liabilities					
University of California Employee Pensions	15,141	169	0	0	0
University of California Retiree Health	21,087	0	0	0	0
Unallocated Debt Payments		0	0	0	627
Total	**$239,552**	**$1,156**	**$1,191**	**$1,195**	**$1,201**

[1/] The state portion of the unfunded liability for teachers' pensions is $14 billion.

Prop 2 Rainy Day Fund - 2017-18 and Out Years
2017-18 Governor's Budget

(Dollars in Millions)

		2017-18	2018-19	2019-20	2020-21
	1.5% of General Fund Revenues & Transfers				
1	General Fund Revenues and Transfers (before BSA transfer)	$125,183	$129,981	$135,904	$142,307
2	1.5% of General Fund Revenues & Transfers	$1,878	$1,950	$2,039	$2,135
	Capital Gain Revenues (Sec 20(b))				
3	General Fund Tax Proceeds	$125,285	$129,963	$135,990	$141,932
4	Personal Income Taxes from Capital Gains	$10,888	$10,829	$11,317	$11,827
5	% of General Fund Tax Proceeds	8.7%	8.3%	8.3%	8.3%
6	8% of General Funds Tax Proceeds	$10,023	$10,397	$10,879	$11,355
7	Personal Income Taxes from Capital Gains in Excess of 8% General Fund Tax Proceeds	$865	$432	$438	$472
8	Prop 98 Share of Capital Gains Tax Revenue above 8%	$431	$0	$88	$206
9	Non 98 Share of Capital Gain Tax Revenue above 8%	$434	$432	$350	$266
10	Total Available (Lines 2 and 9)	$2,312	$2,382	$2,389	$2,401
11	**Debt Repayment (50%)**	**$1,156**	**$1,191**	**$1,195**	**$1,201**
12	**Deposit to Rainy Day Fund (50%)**	**$1,156**	**$1,191**	**$1,195**	**$1,201**
13	**Additional Transfer to the BSA**	**$0**	**$0**	**$0**	**$0**
14	**Cumulative Balance in Rainy Day Fund** [1/]	**$7,869**	**$9,060**	**$10,255**	**$11,456**
15	**BSA Balance as a Percentage of General Fund Tax Proceeds**	**6.3%**	**7.0%**	**7.5%**	**8.1%**

[1/] Includes balance of $1.606b from 2014-15, $1.923b from 2015-16, and $3.184b (includes $1.840b additional transfer) from 2016-17.

Recap of General Fund Solutions
in 2017-18 Governor's Budget

(Dollars in Millions)

	2016-17 & Prior	2017-18	2018-19	2019-20	2020-21
Proposition 98	$1,054.4	$640.6	$660.0	$683.4	$705.0
Recapture 2016 Allocations	572.8	333.8	33.8	0.0	0.0
Constrain Spending Growth	2.6	550.9	331.0	434.8	441.1
Total	$1,629.8	$1,525.3	$1,024.9	$1,118.2	$1,146.1
Two-Year Total		$3,155.1			

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