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Budget Update

Governor Releases Revised FY 2015-16 Budget with General Fund Revenues \$6.7 Billion Higher than January Budget

Cap and Trade Allocations Rise to \$2.2 Billion; Additional Funds for Drought Relief; Analysis of Revised Redevelopment Proposal Pending Language Review

Gov. Jerry Brown took to the podium in the Capitol at 10 a.m. this morning to deliver his [May Budget Revise for FY 2015-16](#). As usual, he surrounded himself with large charts illustrating the state's fiscal picture current and historic. Compared to the January projections, revenues for FY 2013-14, FY 2014-15, and FY 2015-16 have increased and the state projects an additional \$6.7 billion through the end of the coming fiscal year. Under Proposition 98, the majority of that money will go to K-12 and community colleges. The Governor presented the upswing in state revenues with caution, warning that the next recession is likely just around the corner. The revised budget comprises \$115.03 billion of General Funding in a total budget of \$162.5 billion.

Several spending priorities dominated the Governor's remarks today — the creation of an Earned Income Tax Credit (EITC) for California's lowest income residents, tuition freezes at the California State University and University of California systems along with repayment of pension debt and a pension cap for new university hires, climate change and drought response.

Expected to benefit 2 million Californians, the EITC would complement the federal program that President Gerald Ford signed into law 1975, when Governor Brown first held California's highest office. It would provide an average household benefit of \$460 with a maximum benefit of \$2,653. "I thought it would be reasonable to establish in California. It is a straight deliverance of funding to people who are working very hard and earning very little money," the Governor told the assembled reporters.

Proposition 2 Rainy Day Fund

Voters in November 2014 tightened criteria to ensure deposits were made into the state's rainy day fund to accumulate reserves and also required payments to be made to reduce existing state debts. Pursuant to Proposition 2, the May Revise deposits \$633 million into the rainy day reserve and makes a payment of \$633 million on the state's debt (for a total of \$1.9 billion). By the end of FY 2015-16, the Governor projects that reserve fund will hold \$3.5 billion.

Mandate Repayments

Under [Prop. 1A \(2004\)](#), the state has until FY 2020-21 to repay mandate reimbursements owed to local governments prior to 2004. In January, the budget projected that the state still owed local agencies \$800 million but revised that amount to \$765 in the May Revise based upon updated interest rate calculations.

As a result of trigger language included with the passage of the FY 2014-15 budget, local agencies are projected to receive the full payment of \$765 million in mandate reimbursements owed to local governments from prior to 2004. This allocation builds upon the [\\$100 million repayment received by cities, counties and special districts as part of the FY 2014-15 budget](#), and is \$232 million more than what was estimated in the Governor's January Budget proposal.

Of the \$765 million, approximately 77 percent would be directed to counties, 22 percent (\$168 million) to cities and 1 percent to special districts. Administration officials later announced that payments to local agencies are expected to begin with 45 days.

Redevelopment Dissolution and Related Proposals

The Governor's May Revise outlines several changes to the comprehensive redevelopment (RDA) dissolution proposal provisions proposed in January. Below is a summary of what was contained in the initial documents released on Thursday morning.

City officials should note that this summary is based upon the Governor's May Revise document; given the complexity of the issues involved, none of these provisions can be adequately analyzed until language is available and thoroughly reviewed.

Changes to Previous RDA Dissolution Proposal

- **Re-Entered Agreements:** Removes a major provision that attempted to retroactively undo reentered agreements that were authorized under AB 26X (2011). These agreements have been upheld in several state appellate courts. On Thursday, the Department of Finance (DOF) announced that it would no longer be contesting litigation filed by local agencies on this matter.
- **Recovering Litigation Expenses:** Slightly alters the previous proposal aimed at undoing existing law that allows successor agencies to recover, as enforceable obligations, the costs associated with due process access to the courts to review DOF decisions. The change still prohibits recovery of such costs as enforceable obligations unless they are paid for from a successor agency's administrative allocation but allows a sponsoring agency to loan money to a successor agency challenging DOF decisions, with the costs recoverable as an enforceable obligation if litigation is successful.

New RDA Dissolution-Related Proposals

- **Post-2011 Bonds:** Authorizes access to post-2011 bonds based upon a "tiered process," with remaining funds used to defease outstanding bonds.
- **Property Tax Override Revenue:** Provides access to certain property tax override revenues, under the following paradigm: if the revenues were previously pledged for RDA debt service, they must be used for that purpose; if the revenues were not pledged for debt service, then they are returned to the entity that levies the override. For override revenues pledged for debt service, once debts are repaid or deemed unneeded, the override revenues will be returned to the levying entity.
- **Highway infrastructure:** Agreements between former RDA and its sponsoring entity for state highway infrastructure improvements are recognized as enforceable agreements.

Non-RDA Proposals Linked to DOF's RDA Package

- **Negative Bailout Counties:** Provides \$6.9 million in budget relief for four "negative bailout counties."
- **Newly Incorporated Cities:** Assists the four recently incorporated cities which have suffered from the loss of vehicle license fees in 2011. The state would pay a \$24 million debt the cities owe to Riverside County by reducing the payments the county makes to CALFIRE for fire protection services.
- **San Benito County:** Forgives \$3.4 million in debts owed by local agencies in the county due to a previous calculation error that caused underpayments by those agencies to ERAF.
- **Santa Clara County Tax Equity Allocations:** Saves approximately \$2 million annually for several cities in Santa Clara County by suspending for a five-year period the requirement for the cities to reimburse the county for ERAF for property taxes those agencies receive under a tax equity allocations.
- **Insufficient ERAF:** Provides \$5.8 million in backfill payments to several cities and counties where there is insufficient revenue in the county ERAF fund to reimburse the agencies for losses due to the VLF Swap and the "Triple-Flip."

The League will be hosting [a webinar](#) on Friday, May 15 at 11 a.m. to brief city officials further on the proposal as more details become available.

Transportation

While the Governor does not offer a specific transportation funding proposal in the May Revise, he does say that he is working with the Legislature on their proposals to develop a funding package by year end. The League continues to be concerned that the Governor is focused on the needs of the state highway system and not the overall system. Local governments continue to argue that the local streets and roads system also needs a statewide funding solution.

There were no changes to other items from the January Budget Proposal related to streamlining highway relinquishments and increasing personnel for project initiation documents. The League notes that the first item, streamlining of highway relinquishments, has been rejected by both Assembly and Senate budget committees. Instead, the Legislature is reviewing the issue through the normal legislative process in SB 254 (Allen).

Changes to the Highway User Tax Account (HUTA) projections are negligible. As such, the League does not plan to release new city-by-city projections. New projections will be published should information should change.

Cap-and-Trade Allocations

The May Revise increases the overall allocation from Cap-and-Trade revenues from \$1 to \$2.2 billion.

The updated proposed allocations include:

- \$400 million for the Affordable Housing and Sustainable Communities Grant program;
- \$350 million for low-carbon transportation programs;
- \$365 million for transit;
- \$500 million for High-Speed Rail; and
- \$622 million for energy efficiency and clean energy, natural resources, and waste diversion as detailed below:
 - \$140 million for energy efficiency upgrades/weatherization and renewable energy projects in low-income dwellings within disadvantaged communities;
 - \$40 million to the Department of General Services for energy efficiency upgrades and weatherization in public buildings;
 - \$60 million for renewable energy and energy efficiency projects in the University of California and California State University systems.
 - \$25 million for the Department of Food and Agricultural for agricultural energy and operational efficiency;
 - \$65 million for the Department of Fish and Wildlife for wetlands and watershed restoration, of which \$40 million will be dedicated to Delta wetland restoration projects;
 - \$30 million to the California Energy Commission and Department of Water Resources for Water and Energy Technology Program, pursuant to the Drought Executive Order;
 - \$30 million for the Energy Commission and Department of Water Resources appliance rebate programs pursuant to the Drought Executive Order;
 - \$60 million to the Department of Water Resources and Department of Food and Agriculture for water and energy efficiency (in addition to the \$30 million allocated with the Drought package earlier this year);
 - \$20 million to the Department of Food and Agriculture for demonstration projects that increase carbon in soil;
 - \$92 million for fire prevention and urban forestry projects; and
 - \$60 million for the Department of Resources, Recycling, and Recovery for waste diversion.

Environmental Quality and Drought Response

2014 Water Bond (Prop. 1)

The January budget proposal allocated \$532.5 million to begin the first year of a multiyear Prop. 1 expenditure plan. Most of these funds were allocated earlier this year when the Legislature passed a series of drought relief measures.

The May Revision allocates an additional \$1.8 billion of Prop. 1 funds over the next three years to be as follows:

- \$160 million for the State Water Resources Control Board (SWRCB) for wastewater treatment projects;
- \$180 million for the SWRCB for safe drinking water in disadvantaged communities;
- \$13 million for the Department of Water Resources (DWR) for consumer rebates for replacement of inefficient appliances;
- \$100 million for the SWRCB for stormwater management;
- \$13 million for the DWR to provide technical assistance, data collection, and applied research that supports long-term water use efficiency in urban and agricultural sectors;
- \$27 million for lawn replacement in underserved communities;
- \$35 million for Department of Food and Agriculture and Department of Water Resources for agricultural water efficiency programs.
- \$10 million to implement the CalConserve Program, which will enable homeowners and businesses to finance water-efficiency upgrades through a revolving-loan program;
- \$50 million for the DWR for desalination projects;
- \$475 million for the SWRCB for water recycling;
- \$60 million the DWR for groundwater sustainability planning; and
- \$784 million for the SWRCB for groundwater contamination.

Emergency Drought Response

In addition to Cap-and-Trade revenues, Prop. 1 bond funds, and the \$1.9 billion that has already been allocated since the Governor declared a drought emergency in January 2014, the May Revision includes \$64.1 million to continue to respond to the drought, including:

- \$4 million General Fund to augment the Save Our Water campaign to target the state's largest residential water users with focused information to reduce their water usage;
- \$23 million Special Funds and General Funds for water conservation projects at state facilities;
- \$22.2 million General Fund for the Office of Emergency Services to support local jurisdictions using the California Disaster Assistance Act program for approved drought-related projects, including, but not limited to, restoring and replacing public infrastructure that sustained drought-related damages, and emergency protective measures such as delivering water to individuals without drinking or potable water;
- \$7.5 million General Fund for the Department of Community Services Development to provide emergency assistance to unemployed farmworkers, including job training and assistance;
- \$6 million General Fund for the Department of Housing and Community Development to assist or relocate households without potable water sources due to drought; and
- \$1.4 million General Fund for SWRCB to increase enforcement of water use restrictions and conduct additional inspections of diversion facilities to verify compliance with water rights laws.

Additional Local Enforcement Authority

The May Revision proposes legislation to enhance local enforcement authority by providing all water agencies and local governments a consistent, minimum set of enforcement authorities to achieve the required water conservation standard. Under the proposed legislation, any monetary penalties from this enforcement will be used for local conservation efforts. Specifically, it allows penalties to be issued administratively by wholesale and retail water agencies, as well as city and county governments, and enables these entities to enforce local water waste restrictions and SWRCB conservation restrictions.

Department of Toxic Substances Control

The budget proposal allocates an additional \$2.44 million to the Department of Toxic Substances Control for the following:

- \$1.4 million to improve the effectiveness and timeliness of the permitting process and reduce the backlog of permit applications; and,
- \$2.1 million increase annually for three years to implement and evaluate approaches to address serious environmental violations that occur in California's most disproportionately impacted communities. This proposal will focus inspection and enforcement resources on metal recycling and hazardous waste transportation activities.

Public Safety

Funding for Local Law Enforcement

The \$40 million allocation for Front-Line Public Safety (local police departments) remains unchanged from the January Budget.

Amnesty Program (Traffic Offenses)

The January Budget included an 18-month amnesty program authorizing people with past due court-ordered debt owed before Jan. 1, 2013 for traffic infractions, to pay delinquent debt at 50 percent reduction if they met specified eligibility criteria (projected to generate \$150 million).

May Revise updates this proposal by also allowing people whose drivers licenses have been suspended due to Failure to Appear or Failure to Pay (again related to traffic offenses) to reinstate their licenses as part of the program — facilitating their legal transport to and from work, and payment of their debt to the court.

- Option to make one payment or sign up for payment plan
- Supported by wage garnishment agreement in event of non-payment
- \$300 court-imposed assessment fee to be waived, and replaced with \$50 amnesty administrative fee for court costs to run the program.

Community Corrections Performance Incentive Grant

This grant program was created by SB 678 (Chapter 608, Statutes of 2009) to provide incentives for counties to reduce the number of felony probationers returned to state prison.

The May Revise augments this grant program by \$1.1 million for a total allocation of \$125 million in FY 2015-16, to provide incentives to counties to continue decreasing the number of offenders returned to prison.

California Department of Corrections & Rehabilitation

The May Revise includes \$73.3 million in General Fund savings for FY 2015-16 due to reduction of 4,000 out-of-state contract beds by June 2016. This assumes the total vacation of two out-of-state facilities and reducing use of other out-of-state facilities to achieve a 2700-bed reduction by December 2015, with another 1,300-bed reduction by the following June.

Further reduction in out-of-state beds beyond 4,000 in FY 2015-16 could jeopardize continuing compliance with court-ordered population cap of 137.5 percent of prison design capacity — due to projected increase in prison population in FY 2016-17 and beyond, despite Prop. 47 impacts which are expected to reduce inmate population by 4,600 inmates, and new parole determination process for non-violent second-strikers.

Adjustments (all in General Fund revenues)

- Adult Population: Decrease of \$21.3 million in FY 2014-15, and \$108.5 million in FY 2015-16 for adult inmate and parole population changes.
- Juvenile Population: Decrease of FY \$494,000 in FY 2014-15 and \$2 million in FY 2015-16 for juvenile population changes, reflecting decrease of two wards in the current year, and 32 wards in the budget year.

- Hepatitis C Treatment: Increase of \$51.8 million in FY 2014-15 and \$60.6 million in FY2015-16 to treat inmates with new Hepatitis C treatments.

Commission on Peace Officer Standards and Training

- Allows the Commission to reinstate reimbursement of travel and per diem costs of \$4.4 million (suspended since January 2014). This change will be offset by:
 - Increasing by \$800,000 the planned reduction in administrative costs of \$5.2 million cited in January Budget;
 - Increasing the previous reduction in contracted, non-mandated training courses by \$1.9 million; and
 - Continuing suspension of reimbursements for local law enforcement to backfill positions when officers are participating in training (\$2.5 million).

California Conservation Corps

The May Revise contains two items of interest for drought-related high fire risk areas:

- \$5 million in the CAL FIRE budget for projects related to Forest Health Improvement, under which CALFIRE will partner with the Corps on projects in the highest fire risk areas in California.
- Butte County Conservation Camp: An additional \$3 million for CAL FIRE to repair the Butte County fire camp that was closed in 2004, to facilitate re-opening it as a Northern California counterpart to Camarillo Camp in South California, and providing corpsmen with training in fire suppression starting in mid-2016.

State Retiree Health Care Costs

The May Revise reflects the Governor's continued commitment to address state retiree healthcare and pension costs through both collective bargaining and legislative efforts. This includes the proposal for state retiree health to be prefunded, similar to pensions. This is estimated to save the state's annual payment for retiree health care benefits approximately \$8 billion.

The revised budget also proposes to have costs be controlled by reducing employer contributions for new employees by requiring those employees to work longer before qualifying for retiree health care benefits. Additionally, there is a proposal for increased oversight on the California Public Employees' Retirement System (CalPERS) and increased employee health care options by adding more low-cost plans.

The budget trailer bill would require state agencies and CalPERS do regular reviews of employees enrolling their dependents in their health care plans and that retirees are enrolling in Medicare plans at age 65.

State Retirement Contributions

The May Revision has updated the expected cost for state retirement contributions, with a \$110 million decrease from the Governor's Budget. The administration has cited the reduction as being a result of "the Public Employees' Pension Reform Act of 2013, strong investment performance, and greater than expected contributions to the system."

Community Services

Literacy

The May Revise includes an increase of \$2 million for the Literacy and English Acquisition Services Program. These funds will be programs in coordination with the adult education consortia.

Broadband Expansion

The May Revise increases funding for the California Public Library Broadband Project by \$1.7 million. Of this amount, \$1.5 million is one-time money for grants to public libraries to upgrade broadband equipment and \$225,000 is for continued administration of contracts for broadband services.

Library Preservation

The May Revise includes \$521,000 to support the state library's efforts to preserve historical items in its possession.

California Arts Council

The May Revise includes a proposal for a permanent funding increase of \$5 million annually to provide grants to local arts organizations. These funds will be used to further the arts in the program areas of Economic and Community Development, Arts Education, Cultural and Community Engagement, and the Creative Economy.

Child Care

The May Revise makes the following adjustments to subsidized child care programs as follows:

- An increase of \$46.8 million to reflect an increase in the number of new Stage 2 beneficiaries and an increase in the cost of providing care. Total base cost for Stage 2 is \$395.4 million;
- An increase of \$2 million to reflect minor adjustments in caseload and the cost of providing care. Total base for Stage 3 is \$265.5 million; and
- A net increase of \$17.7 million federal funds to reflect an increase in ongoing base federal funds for child care and development.

Next Steps

The League will be hosting [a webinar](#) for city officials on Friday, May 15 at 11 a.m. to brief city officials further on the redevelopment proposal. Additional information will be distributed as it becomes available.

The constitutional deadline for the legislature to adopt the budget is June 15, a very short 32 days from now. The Legislature will begin hearings on the May Revise next Monday. In addition to May Revise proposals, legislators will need to act on all other budget items not previously closed out. Hearing agendas are often not released until a day or two before hearings.

City officials should be prepared to make calls and travel to Sacramento to testify on priority items on short notice.

In approximately three weeks, the Legislature will convene the Budget Conference Committee to review differences between the Assembly version and Senate version of the budget. It will then go to the floor for a final vote and to the Governor for signature.