Summary of "The 2016-17 Budget: California's Fiscal Outlook" by the Legislative Analyst's Office

The Legislative Analyst reports that California's General Fund revenues for 2015-16 will exceed projections by $3.6 billion, which will in turn be deposited in the state's Rainy Day fund under Proposition 2. The Analyst projects a surplus of $11.5 billion for fiscal year 2016-17, which would be deposited in the Fund for Economic Uncertainties and the Prop 2 Rainy Day fund as a buffer in the next economic downturn. The total reserves at the end of 2015-16 would be $7.8 billion and at the end of 2016-17 would be $11.5 billion.

The higher revenues in 2015-16 would be from higher income tax revenues partially offset by lower sales tax and corporate revenues than initially projected. Schools would see an increase of $739 million due to Prop 98, Medi-Cal spending would be $47 million less than budgeted, and CalWorks would be $90 million less than budgeted.

Unlike the recent past, Prop 98 school spending increases are being paid for mostly by the increases in property tax revenues generated by the run up in home values from recent home sales.

For 2016-17, General Fund revenues will grow by 5.9% (6.9 billion); the three largest taxes (income tax, sales tax, and corporate tax) will grow by 3%.

For 2016-17, General Fund spending will increase by 5.1% ($5.9 billion). General Fund spending on schools required by Prop 98 will be $770 million, and the increased state contributions to the State Teachers Retirement Fund will be $533 million. General Fund spending for Medi-Cal will grow by $2.5 billion or 14%. The largest contributor will be the $1 billion decline in revenues associated with the expiration of the MCO tax.

Overall, the LAO concludes the state is far better positioned to weather a future economic slowdown than it has been in many years.

Some details on the economy. personal incomes will grow by 6% and CPI (i.e. inflation) will grow by 2.5%. Unemployment rates will decline to 5.25%, and population growth will be 0.8%. Factors that could slow future economic growth: aging population, results of the 2016 elections, changes in monetary policy, slow downs in the growth of China, climate change and energy costs, slow downs in the Bay Area's growth in incomes, and housing prices.

Job growth is highly variable by region: the Bay Area is at the top at close to 5%; Kern is at the bottom at -0.2%. Unemployment ranges from 3-4% in the Bay Area to over 8% in Fresno and Bakersfield.

The sales tax increase under Prop 30 will expire in 2016-17 while the increase in income tax rates for high income Californians will expire in 2018. The growth in taxes from the income tax and the sales tax will slow in 2016-17, but the revenues from the corporate income tax will grow. As a result the transfers into the Budget Stabilization Account (Rainy Day Fund) will slow.

School funding ($67.8 billion in 2015-16 budget). Prop 98 governs school funding with an interlocking set of tests that include the growth in school attendance, growth in personal incomes, the growth in local property taxes, and the growth in state General Fund revenues. The growth in school attendance is negative (13,000 less in 2014-15 and 21,000 less in 2015-16); the growth in state General Fund revenues is slowed by both the expiration of Prop 30 and the stock market. So the minimum guarantee of state General Funds allocated for schools will grow by only 1.7% annually over the next four years. Local property taxes have increased (about 6%) due to rising property values and the amount dedicated to schools has also increased due to the dissolution of local redevelopment authorities. Overall, there will be an increase of $3.5 billion (5.1%)

in 2016-17 available for schools that will be divided between one-time needs and ongoing needs. Over the next four years, Prop 98 guarantees for school spending will grow by 2.9%, of which 5.6% annually will be from local property taxes and 1.7% from the state General Fund.

Health and Human Services ($31.7 billion State General Fund in 2015-16 Budget). HHS includes programs such as Medi-Cal, IHSS ($2.8 billion), DDS ($3.5 billion), TANF (CalWorks), Child Care, and SSI ($2.8 billion) among others. General Fund spending will increase from $31.7 billion in 2015-16, to $33.8 billion in 2016-17, and to $38.2 billion in 2019-20 – increases of 5% annually. Among these programs, General Fund spending on CalWorks will decline by 32% (from $588 million to $127 million), SSI will grow on average by 1.3% annually, and Medi-Cal by 7.6% annually. Enrollment in many programs is expected to decline as the job market continues to improve and minimum wages increase.

Medi-Cal. General Fund spending will grow by 14% to $20.5 billion in 2016-17. The prime contributor is the expiration of the MCO tax ($1.1 billion). Other contributors are health care inflation, the expiration of the CHIP match for children and the initiation of the state match for those newly eligible under the ACA. Enrollment growth, which has reached 12.6 million, will start to decline as counties complete redeterminations, and more people are employed and have job-based coverage. LAO projects that family enrollment will decline by 3.5% (260,000) in 2016-17 due to redeterminations and by another 50,000 in 2017-18. It expects coverage of the newly eligible (optional expansion) will peak at 3 million in 2016-17 and then decline due to redeterminations. LAO projects that capitation rates will grow by 1.5% in 2016-17, and by 4% in 2017-18. LAO also notes that plans were overpaid for the new eligibles as utilization rates were much lower than projected and these rates are being decreased. The state General Fund cost of the match for the newly eligible will be $500 million in 2016-17 growing to $1.5 billion in 2019-20. The enhanced CHIP match of 88% is expected to expire in 2017 and would add state General Fund costs of $600 million annually beginning in September 2017.

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