



## LEGISLATIVE REPORT #257

### Governor Brown Releases Budget with Surplus / Forgives Retroactive Medi-Cal 10% Cut

**January 9, 2014:** This morning, Governor Brown released his proposed 2014-2015 budget. Due to an improved economy, along with a windfall of capital gains revenue, and continued revenue from Proposition 30 the Governor's proposed budget included a surplus of nearly \$2 billion (Resources of \$108.7 billion versus Expenditures of \$106.8 billion). Some of this surplus would go into the State's "rainy day" fund and some would be used to payback existing debt.

The main highlight for physicians is the Governor's proposed forgiveness of the retroactive 10% cut to Medi-Cal reimbursement rates. This is a big win as the Administration was set to demand payment on Medi-Cal claims for the 10% reduction going back to June of 2011.

The Governor was in particularly good mood this morning as he released his budget. With revenues up and signs the economy continues to stabilize Governor Brown has ambitious plans for the next few years to further clean up the budget deficits which accumulated over the years.

The Governor proposed a more aggressive payment schedule to pay down budgetary debt from past years. Recent state budgets have reduced this debt from \$34.7 billion to \$24.9 billion. During the press conference discussing his budget, Governor Brown expects to have all this debt paid off by the 2017-2018 budget year.

This debt does not include other long term obligations such as retirement-related unfunded liabilities which are estimated to be as much as \$218 billion. The Governor was asked if he intended to address these obligations in this budget and he responded he was not prepared to tackle this issue at this time although he left the door open to solutions proposed by the Legislature.

The Governor continues to preach pragmatism with the recent influxes of revenue. He pointed out capital gains were \$4 billion higher than in previous years and should not be expected to continue at the same high levels. He also pointed out the temporary taxes in Proposition 30 which he believes should truly be temporary (1/4 cent sales tax increase through 2016 and income tax increase through 2018). He views these funds as opportunities to reduce existing debt and avoid getting the State into another fiscal calamity when the next inevitable economic downturn occurs.

The Governor also announced his intention to place an initiative on the ballot to further bolster the State's "rainy day" fund. The initiative would do the following:

- \* When capital gains revenues rise to more than 6.5 percent of General Fund tax revenues those additional funds would be deposited into the rainy day fund.
- \* Doubling the maximum size of the Rainy Day Fund from 5 percent to 10 percent of revenues.
- \* Allowing supplemental payments to the Wall of Debt or other long-term liabilities in lieu of a year's deposit.
- \* Limiting the maximum amount that could be withdrawn in the first year of a recession to half of the fund's balance. This will ensure that the state does not overly rely on the fund at the start of a downturn.
- \* Creating a Proposition 98 reserve, whereby spikes in funding would instead be saved for future years of decline. This would smooth school spending to prevent the damage caused by cuts. The reserve would make no changes to the guaranteed level of funding dedicated to schools under Proposition 98.

Overall, General Fund spending in the proposed budget will grow by approximately 8.5 percent from the current budget year, driven largely by increases in education funding and debt repayment. To provide some context, state budget expenditures previously peaked in 2007-08 with spending of about \$103 billion. Thus, the budget year is the first year in which expenditures will be at or above the level of seven years ago.

Spending in healthcare is proposed to increase by \$460 million or roughly 2% of the healthcare budget. Much of the increase is due to the Medi-Cal expansion which California will be implementing this year.