The 2021-22 Budget:

The Governor's Suspension Proposal

JANUARY 2021

Background

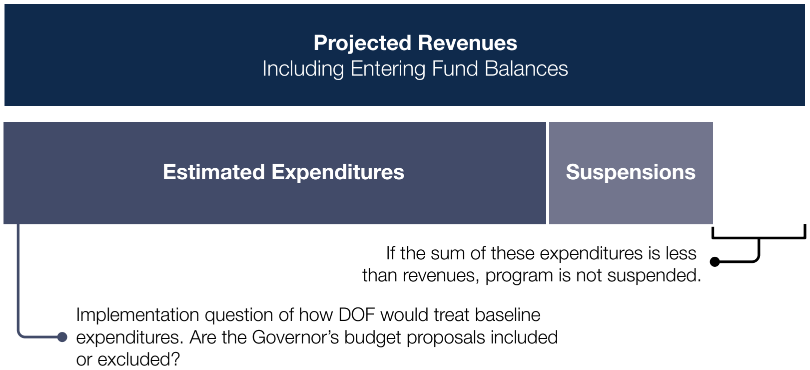
The 2019-20 Budget Made Several Programs' Costs or Augmentations Subject to Suspension. In the 2019-20 May Revision, the administration anticipated an operating deficit would emerge—absent further actions—under its multiyear projections. In response, the final budget act made some program spending amounts subject to potential suspension. Under this budget bill language, if certain conditions persisted, these program costs would be suspended—resulting in General Fund savings—on December 31, 2021. This language was included in both the 2019-20 and 2020-21 budget acts.

How the Suspensions Work. Current law empowers the Department of Finance (DOF) to administer the suspension calculation. The formula is shown in **Figure 1**. Under the formula, DOF compares estimates of General Fund revenues to General Fund expenditures—without suspensions—in 2021-22 and 2022-23. If DOF determines projected revenues *will* exceed expenditures, then the programs' ongoing expenses continue on an ongoing basis. If not, expenditures across nearly a dozen different programs are automatically suspended (with no explicit provision for reinstatement). For the purposes of the calculation, we understand DOF would *include* the entering fund balance (the carry-in from the previous year's budget) in revenues.

How Are Governor's Budget Proposals Treated in the Calculation? A key question for the implementation of the language under current law is whether DOF should include or exclude the Governor's budget proposals from General Fund expenditures in the calculation. If they are *included* in expenditures, it would mean higher expenditures and lower entering fund balances in 2021-22 and 2022-23. If they are *excluded* from expenditures, the opposite would be true. The suspensions are much more likely to be operative if the Governor's budget proposals are included in the calculation.

Figure 1

How the Suspension Calculation Works



DOF = Department of Finance.

Governor's Proposal

Under Current Law, Programs Would No Longer Be Subject to Suspension… Under current law, the suspension calculation would occur once: at the 2021 May Revision. If, at that time, DOF finds revenues exceed expenditures for both 2021-22 and 2022-23, the suspensions would not become operative and the costs would continue on an ongoing basis. Because the state has a significant windfall in 2021-22, as long as Governor's proposals are *excluded* from expenditures in the calculation, then DOF would find that revenues are sufficient to fund expenditures including the suspensions. As a result, spending on those programs would continue.

…But Governor Proposes Maintaining Suspension Calculation. Rather than executing the suspension calculation this May, the Governor's budget proposes a new suspension calculation in 2022. Specifically, the Governor proposes that the Legislature enact new suspension language that would give DOF the authority to make this calculation again at the time of the May Revision in 2022. In this case, the calculation would apply to 2022-23 and 2023-24. Suspensions would occur, under the Governor's proposal, on December 31, 2022 if revenues were not sufficient to cover expenditures.

Spending Subject to Suspension

Figure 2 shows the list of program items that would be subject to suspension under the Governor's budget and how this list compares to those enacted in the 2019-20 and 2020-21 Budget acts.

Figure 2

Programs or Augmentations Subject to Suspension and Proposed in Governor's Budget

Program	Funding Subject to Suspension	2019 Budget Act	2020 Budget Act	2021 Governor's Budget
Medi-Cal	Use of Proposition 56 revenues for provider payment increases	X	X	X
IHSS	Continued restoration of 7 percent service hour reduction	X	X	X
DDS/DOR	Supplemental provider payment increases	X	X	X
Medi-Cal	Extension of coverage for postpartum mental health	X	X	X
Medi-Cal	Restoration of optional benefits	X	X	X
DDS	Non-enforcement of uniform holiday schedule policy	X	X	X
Child welfare	Funding for Family Urgent Response System	X	X	X
Senior nutrition	Augmentation for Senior Nutrition Program	X	X	X
UC and CSU	Student financial aid during the summer term	X	X	X
Aging	Aging and Disability Resource Connections	X	X	X
Child welfare	Emergency Child Care Bridge program supplement	X	X	X
Child welfare	Public health nursing early intervention pilot program in Los Angeles County	X	X	X
HCD	All Transitional Housing Program grants to counties for former foster youth	X	X	X
Child welfare	Foster Family Agency social worker rate increase	X	X	X
DPH	STD prevention	X		
DPH	HIV prevention and control	X		
DPH	Hepatitis C virus prevention and control	X		
Medi-Cal	Expansion of screening and intervention to drugs other than alcohol[a]	X	X	

[a] This benefit is now federally required.

IHSS = In-Home Supportive Services; DDS = Department of Developmental Services; DOR = Department of Rehabilitation; HCD = California Department of Housing and Community Development; DPH = Department of Public Health; and STD = sexually transmitted disease.

Some Suspension Items Provide Direct Funding for Core Government Services. A number of the suspension amounts, especially those with larger dollar amounts, provide direct funding for longstanding or core government services. For example, some major items that are subject to suspension are:

- ***Using Proposition 56 (2016) Funding for Provider Payment Increases in Medi-Cal.*** Recent budgets have used funding from Proposition 56, which established a higher tax on tobacco products, to increase provider payments in Medi-Cal. If the suspensions went into effect, most of these payment increases would cease. Proposition 56 would instead cover cost growth in Medi-Cal, providing General Fund savings. (Under current law, these payment increases are subject to suspension on July 1, 2021 rather than December 31, 2021.)
- ***Restoration of In-Home Supportive Services (IHSS) Service Hours.*** During the last recession, the state reduced IHSS service hours, but the Legislature reversed this reduction in every year since 2015-16. If the current law suspensions went into effect, the state would reinstate a 7 percent reduction to service hours. The nearby box describes some potential legal challenges that could arise if this occurred.
- ***Supplemental Rate Increases for Developmental Services Providers.*** The 2019-20 and 2020-21 budgets enacted supplemental rate increases for certain developmental services providers. If the current law suspensions went into effect, the state would return to rates provided before these supplemental increases took effect.

Other Items Provide Funding for Newer State Programs. Not all suspensions directly fund longstanding government programs. For example, the funding for California State University and University of California summer financial aid and some child welfare programs, like the family urgent response system and Los Angeles County public health nurse pilot, were created in recent years.

Legal Risks Associated With In-Home Supportive Services (IHSS) Reduction Proposals

Proposals to reduce or eliminate IHSS services generally are vulnerable to litigation asserting that the change violates federal Medicaid rules and/or puts recipients at risk of institutional placement, which could violate the United States Americans with Disabilities Act (ADA). In the past, courts have issued temporary injunctions preventing the state from making reductions to Medicaid personal care services programs, including IHSS, due to possible violation of federal Medicaid and ADA rules. It is possible that future state proposals to eliminate or reduce IHSS services could face the similar legal challenges.

Multiyear Savings of Governor's Proposal

State Faces Multiyear Operating Deficit Under Governor's Budget. An operating deficit occurs when baseline expenditure growth outpaces anticipated revenue growth. Both our office and the administration anticipate an operating deficit is quite likely to emerge in the coming years. In our November *Fiscal Outlook*, we found the state faces large and growing multiyear operating deficits over the outlook period. Under its own revenue forecast, assuming the suspensions were operative, the administration estimates operating deficits would grow from $7.6 billion in 2022-23 to $11.3 billion in 2024-25.

Rejecting Governor's Proposal Would Result in Higher State Costs. If the Legislature rejected the Governor's proposal to maintain the suspensions, without taking any other actions, the size of the operating deficit would increase by $1.3 billion in 2022-23. Figure 3 shows the costs of rejecting the Governor's proposal in 2022-23 and 2023-24.

Figure 3

General Fund Cost of Rejecting Governor's Proposal

(In Millions)

Program	Funding Subject to Suspension	2022-23	2023-24
Medi-Cal	Use of Proposition 56 revenues for provider payment increases	$760	$840
IHSS	Continued restoration of 7 percent service hour reduction	243	540
DDS/DOR	Supplemental provider payment increases	139	284
Medi-Cal	Extension of coverage for post-partum mental health	29	57
Medi-Cal	Restoration of optional benefits	23	47
DDS	Nonenforcement of uniform holiday schedule policy	20	41
Child welfare	Funding for Family Urgent Response System	15	30
Senior nutrition	Augmentation for Senior Nutrition Program	9	18
UC and CSU	Student financial aid during the summer term	5	10
Aging	Aging and Disability Resource Connections	5	10
Child welfare	Emergency Child Care Bridge program supplement	5	10
Child welfare	Public health nursing early intervention pilot program in LA County	4	8
HCD	All Transitional Housing Program grants to counties for former foster youth	4	8
Child welfare	Foster Family Agency social worker rate increase	3	7
		$1,263	**$1,909**

IHSS = In-Home Supportive Services; DDS = Department of Developmental Services; DOR = Department of Rehabilitation; and HCD = California Department of Housing and Community Development.

Comments

Maintaining Suspensions Treats Ongoing Programs as Temporary. The suspension language treats policies that are fundamentally ongoing in nature as temporary. For example, health and developmental services-related spending amounts subject to suspension generally support core programmatic funding intended to improve consumer access to an entitlement program. Some reductions—such as the IHSS 7 percent service hour reduction—also could present legal risks in addition to being a reduction to a core service. Treating ongoing program costs as temporary fundamentally understates the true ongoing cost of the state's policy commitments.

Suspending Core Government Services Poses Programmatic Issues. Many of the suspension items, particularly the larger ones, are related to core government services. The suspension language creates uncertainty in these programs, which can pose problems for providers and recipients of these services. The potential suspension of supplemental rate increases for developmental services providers makes staffing and planning more difficult. For example, hiring permanent staff to work directly with program consumers is more challenging when the funding is uncertain. Similarly, retaining staff may be more difficult if a provider cannot assure employees that any pay increase will remain intact. More staff turnover means less stability for consumers. In some cases, this uncertainty can work against the Legislature's objectives for the spending.

Suspensions Were Not Originally Proposed as an Annual Calculation. The suspension language enacted into law in 2019-20 was framed as a one-time determination made in May 2021. By proposing a new suspension calculation, however, the administration appears to intend to make this calculation ongoing. This is not consistent with our understanding of what the Legislature envisioned.

Recommendations

Recommend Legislature Reject Suspension Language... We recommend the Legislature reject the Governor's proposal to create new budget bill suspension language. Considering that most of the costs of the suspension items directly fund core state services, including those costs in multiyear fiscal projections is appropriate. Given the state's multiyear deficits, however, the state likely will need to make changes to its budget within the next few years. As it stands, the state probably cannot afford existing programs, avoid the suspensions, and fund the Governor's proposals over the next few years. The Governor's proposal to include new suspension language simply papers over a portion of a larger structural problem.

...But Evaluate the Merits of Some Suspension Items. Some of the suspension items are recently created programs. As part of the broader effort to address the ongoing budget problem, evaluating whether these newer programs are achieving their intended goals would be worthwhile. To this end, the Legislature could take a look at reporting and oversight to ensure programmatic design aligns with its policy objectives and that the programs are resulting in the intended outcomes.

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This report was prepared by Ann Hollingshead, and reviewed by Carolyn Chu. The Legislative Analyst's Office (LAO) is a nonpartisan office that provides fiscal and policy information and advice to the Legislature.