



To: CHEAC General Membership

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RE: Governor's 2018-19 May Revision

This morning, Governor Brown unveiled his final [May Revision](#) to his 2018-19 state budget proposal. On a lighter note, the press conference began with a brief visit from California's First Lady Ann Gust Brown as she introduced the newest member of their team and Deputy First Dog, Cali.

Even more noteworthy is the tribute to Nancy McFadden included in the budget summary. Nancy served as Governor Brown's Chief of Staff and sadly lost her battle with cancer this past March at the age of 59.

Despite the roughly \$8.8 billion increase in the budget surplus since the January budget proposal, Governor Brown expressed his continued concern that California was nearing its longest stretch of economic recovery since 1991. He further highlighted that revenues included in the May Revision were predictions of what is to come but have not been realized yet. He proudly noted California's significant investments in both health care and K-14 education surpassing any other state.

Governor Brown's May Revision continues fill the rainy-day fund to the constitutional target of \$13.5 billion by dedicating an additional payment of \$3.5 billion. According to the Administration, the May Revision also dedicates surplus revenues to one-time funding for three core areas: homelessness (\$359 million), mental health (\$312 million) and infrastructure (\$2 billion).

Highlights of interest to local health departments are summarized below.

340B Drug Pricing Program. The Governor's May Revision maintains the repeal of the 340B Drug Pricing Program under Medi-Cal, beginning in July 1, 2019. The May Revision includes a savings estimate of \$16.6 million annual General Fund savings beginning in 2020-21; however, it does not offer any details regarding how that amount was determined. The proposal faced scrutiny in the Legislature and continues to be opposed by a large coalition that includes CHEAC. Our coalition letter can be found [here](#).

AB 85 1991 Realignment Diversions. The Governor's May Revision estimates that \$688.8 million and \$773.2 million will be diverted from counties to the state in FY 2017-18 and FY 2018-19, respectively. This reflects an increased diverted amount of \$242.7 million for FY 2018-19 compared to the Governor's January budget proposal.

The May Revision does not include updated true-up calculations from FY 2015-16 final redirection. Recall, the Governor's January budget proposal estimated a net true-up of \$208 million for FY 2015-16, which included roughly \$23.2 million owed to counties and \$231.1 million owed to the State. We anticipate updated FY 2015-16 final redirection amounts to be included in the final budget package.

Recall, after the passage of the Affordable Care Act (ACA) and Medi-Cal expansion, the State anticipated lower indigent care expenditures for counties since more individuals would qualify for coverage through Medi-Cal or Covered California. Based on this assumption, AB 85 (Chapter 24, Statutes of 2013) was enacted, diverting health realignment dollars from counties to the State. The State diverted either: 1) 60 percent of health realignment funding received in a given year; or 2) a specified amount of health realignment funding based on a formula that took into account county revenues and expenditures.

Redirection amounts are estimated in the Governor's January budget proposal and updated in the May Revision. AB 85 also included a true-up mechanism two years after the close of the fiscal year. This mechanism determines what the actual county diversion should have been based on updated county data.

AB 85 county-by-county numbers are available [here](#).

Mental Health Investments. Acknowledging the challenges facing the mental health system with the prevalence of individuals with co-occurring substance use disorder issues, homelessness and those interacting with the criminal justice system, Governor Brown included the following proposals for investments to mental health in the May Revision:

- *No Place Like Home (NPLH)* – Places the NPLH program on the November 2018 ballot. Recall in 2016 the Legislature passed the NPLH program which proposes to use a portion of Mental Health Services Act (Proposition 63) funding, to finance \$2 billion in bond funding for permanent supportive housing units for chronically homeless individuals with severe mental illness. Challenges to the legality of the NPLH program have caused delays in implementation and the Administration proposes placing it on the statewide ballot for voter validation.

- *Children's Mental Health Mandate Repayment* – Proposes a repayment of roughly \$254 million plus interest for repealed mandates related to county services to emotionally disturbed children related to AB 3632. This reflects costs incurred between 2004-2011.
- *Homeless Mentally Ill Outreach and Treatment* – Proposes a one-time augmentation of \$50 million for DHCS to provide counties with targeted funding for multi-disciplinary teams for intensive outreach, treatment and related services.
- *Graduate Medical Education* – Provides a one-time General Fund increase of \$55 million to support graduate medical education programs serving health professional shortage areas or medically underserved rural areas.
- *Oversight and Planning* – Proposes \$6.7 million for additional staffing at the Department of Health Care Services for the oversight of county mental health programs and Mental Health Service Act expenditures and planning efforts for systems and data improvement.

Mental Health Services Federal Audit Repayment. The May Revision includes proposal for the Department of Health Care Services to repay the \$180.7 million federal disallowance stemming from a recent U.S. Department of Health and Human Services, Office of the Inspector General audit. Counties will be expected to repay the State back over the next four years as determined by the State and counties.

Homelessness. With the rising number of homeless individuals, the Governor's May Revision provides roughly \$47.3 million General Fund in 2018-19 and \$63.7 million in 2019-20 to support the following county programs aimed at preventing homelessness:

- *CalWORKs Housing Support Program* – Provides a \$24.2 million increase to help CalWORKs families secure permanent housing.
- *CalWORKs Homeless Assistance Program* – Increases the daily payment rate from \$65 to \$85 per day for temporary assistance to families who are homeless or are facing imminent eviction. Provides an \$8.1 million in FY 2018-19 and \$15.3 million in 2019-20.
- *Home Safe Pilot Program* – Provides \$15 million, one-time funding to pilot housing-related supports to seniors experiencing homelessness or at risk of homelessness. Funding is available over a three-year period.

Poverty. The May Revision highlights continued investments to counter the impacts of poverty, citing \$21 billion in new annual funding for poverty focused programs since 2012. The May Revision provides continued funding for: Medi-Cal expansion, restoration of Medi-Cal benefits, including dental, the repeal of the maximum family grant rule, and increased child care and early education provider rates.

In-Home Supportive Services (IHSS). Based on updated revenue projections and projected 1991 Realignment revenues, the Administration projects no net fiscal impact to counties through FY 2019-20. Recall, in January 2017, the Administration deemed the Coordinated Care Initiative (CCI) to no longer be cost-effective and as a result terminated the CCI in FY 2017-18. The major impact to counties was the discontinuation of the 3.5% cap on the county's share of IHSS costs. Through negotiations between counties and the Administration, a new structure was put into place to mitigate the county impact (see [CHEAC's June 2017 Budget Memo](#) pages 1-2).

Though a five-year deal, counties are focused on year three (FY 2019-20), where at the time of the deal and from the county perspective, the impact to counties was expected to be unmanageable. The Administration's projection of no net fiscal impact to counties may indicate a reluctance to reopening the five-year deal.

Medi-Cal Shortfall. The May Revision projects a current year Medi-Cal shortfall of roughly \$830 million General Fund, which is an increase of \$286 million from January. The Administration is proposing trailer bill language to increase the General Fund loan that can be used for the Medi-Cal shortfall, from \$1 billion to \$2 billion. The Administration indicates significant growth in the Medi-Cal budget since 2003, in addition to the cash accounting system for Medi-Cal and the increase in retroactive managed care rate adjustments, has led to an increased need for a General Fund loan in the event of a shortfall.

Children's Health Insurance Program (CHIP). Governor Brown's May Revision includes a combined two-year General Fund savings of \$898.1 million in 2017-18 and 2018-19 as a result of federal CHIP reauthorization and an enhanced federal match rate.

Recall, at the time of the January budget proposal, Congress had just passed in late December a short-term reauthorization of CHIP that extended the federal cost sharing ratio at an enhanced 88 percent federal match through March 2018. Due to timing constraints of the Governor's budget development process, the proposed budget did not include December's short-term reauthorization and instead assumed a non-enhanced federal match rate of 65 percent through FY 2018-19.

Through two additional actions by Congress in January and February 2018, CHIP was ultimately reauthorized for 10 years and included the enhanced 88 percent federal match through September 30, 2019. The enhanced federal match rate will incrementally decrease over time beginning in 2019-20 to the historic cost sharing ratio of 65 percent federal funds and 35 percent state funds. In future years, costs to California's General Fund will increase as this federal share decreases.

Tobacco Tax Initiative – Proposition 56. Tobacco tax revenues included in the May Revision increased slightly compared to the Governor's January budget proposal. Proposition 56, which was passed by voters in 2016 and took effect in April 2017, raised the tax on cigarettes by \$2.00

per pack. Revenues raised backfill Proposition 99, Proposition 10, the Breast Cancer Fund, and state and local governments. New revenues are directed toward Medi-Cal provider payments and program growth, law enforcement, physician training, dental programs, research, and existing tobacco prevention and control activities.

After accounting for backfill, net Proposition 56 revenues total \$1.3 billion, reflecting an increase of \$32 million from the Governor's January budget proposal. An additional \$55.3 million is included in the May Revision to support new Medi-Cal program growth in 2018-19. \$629.9 million is also forecasted for supplemental Medi-Cal provider payments and rate increases, which is \$51.6 million lower than what was included in the Governor's January budget proposal.

Despite provider claims coming in lower than expected based on year-to-date expenditures from 2017-18, the May Revision includes \$163 million for physician payments and \$70 million for dental payments for 2018-19. Work continues between the Brown Administration, the Legislature, and stakeholders to develop a supplemental provider payment framework that will be submitted to the federal government for approval by September 2018.

Cannabis. With the creation of the Medical Marijuana Regulation and Safety Act in 2015 and the passage of Proposition 64, the Adult Use of Marijuana Act, California has been busy implementing a new statewide regulatory system for both the medicinal use and adult use of cannabis. Proposition 64 included new excise taxes on the cultivation and retail sale of cannabis with revenues generated directed to the Cannabis Tax Fund.

In keeping with the Governor's January budget proposal, the May Revision continues to fund ongoing state-level cannabis regulatory activities. As we noted in our [January budget memo](#), the Administration continues to underscore that the amount and timing of revenues generated by cannabis taxes remains uncertain given a variety of factors including local regulatory activity and cannabis price and consumption changes. The May Revision slightly increases the Administration's current year budget cannabis revenue amount from \$175 million to \$185 million; however, they also decrease their FY 2018-19 cannabis revenue estimate from \$643 million down to \$630 million.

For FY 2018-19, the Administration, following the Proposition 64 specified tiered allocation of resources from the Cannabis Tax Fund, will use initial state-level cannabis tax revenues to repay \$120 million in state General Fund loans for their initial regulatory and administrative costs for implementing the proposition. Funding will also be directed to the following agencies for ongoing state-level licensing and enforcement activities:

- California Department of Food & Agriculture - \$28.3 million
- California Department of Public Health - \$10.6 million
- California Department of Consumer Affairs - \$33.9 million
- California Department of Finance - \$440,000

- General Fund loan of up to \$59 million to the Cannabis Control Fund to provide sufficient cash for FY 2018-19.

Additional resources will be directed to various other state entities for the purposes of tax collection, business filings, and hearings and appeals.

The May Revision also includes \$10 million in funding for the Community Reinvestments Grants program. Recall this pot of money is directed to local health departments and community-based organizations to support substance use disorder treatment, job placement, legal services, and other cannabis use related programs. For more detailed information on how Prop 64 funding distributions flow, please see [CHEAC's memo](#) from earlier this year.

Cannabis research is funded with \$2 million directed to the UC San Diego Center for Medicinal Cannabis Research to study the efficacy and adverse effects of cannabis and \$10 million to a public university or universities to research and evaluate the implementation and effects of Prop. 64. The California Highway Patrol would also receive \$3 million to establish and adopt protocols to determine whether a driver is operating a vehicle while impaired.

Similar to the Governor's January Budget, the Administration notes that based on estimated cannabis revenues, the remaining programs outlined in Prop. 64 will not receive funding until FY 2019-20 and that the level of funding for those programs will be based on revenues collected in 2018-19.

Finally, the May Revision includes \$14 million from the Cannabis Tax Fund to create four investigative teams and one interdiction team to combat large-scale illegal cannabis activities.

Hepatitis C. The Governor's May Revision details two new Hepatitis C proposals:

- *Hepatitis C Inmate Treatment* – \$105.8 million General Fund annually for three years will be dedicated to expanding Hepatitis C treatment to all infected state prison inmates. The May Revision notes that approximately 22,000 inmates are currently infected with Hepatitis C and approximately 2,300 inmates will be treated in the current year with existing resources at a cost of around \$60 million. The funding augmentation included in the May Revision is the result of a new procedure being implemented by the court-appointed Federal Receiver overseeing inmate medical care that provides treatment to all inmates at any stage of Hepatitis C. According to the U.S. Centers for Disease Control and Prevention (CDC), Hepatitis C is closely associated with the nationwide opioid epidemic and is responsible for more deaths in the U.S. than any other infectious disease.
- *Hepatitis C Treatment Clinical Guidelines* – \$70.4 million (\$21.8 million General Fund) is slated to be used to authorize Medi-Cal treatment for Hepatitis C patients ages 13 years

and older regardless of liver fibrosis stage or comorbidity (except for patients with a life expectancy of less than 12 months). Medi-Cal currently limits treatment for patients with stage two or above liver fibrosis or any patient with a qualifying comorbid condition.

Wildfire Response and Recovery. The Governor's January Budget included \$419 million for various wildfire recovery, response, and preparation activities, and the May Revision includes significant further investments. In addition, the federal government provided \$4.4 billion in supplemental disaster-related funding to support the state's recovery efforts in February as part of the federal budget deal. Funding for these purposes includes:

- Increased funding out of the State Emergency Telephone Number Account (SETNA) of \$15 million (up from \$11.5 million in the January Budget) to modernize the state's 911 system.
- \$14.4 million in federal funds to assist schools impacted during the state's declared emergencies.
- \$2.8 million General Fund and \$8.4 million in federal funds to address increased workload related to disaster recovery activities.
- \$353,000 General Fund and \$325,000 in other funds for the Office of Emergency Services (OES) to manage and train local agencies on the use of the Situational Awareness and Collaboration Tool to assist with coordinating evacuations, warnings, and shelters in the field.
- \$3.2 million in federal funds to handle increased hazard mitigation activities statewide.
- \$3.4 million General Fund to OES to provide regional and on-site support for planning, response and mitigation capabilities in the event of a hazardous materials release.
- \$1.3 million from the CA Integrated Waste Management Fund for CalRecycle to lead a disaster response and recovery team to become subject matter experts for disaster recovery and debris removal. The Team would also support local agency requests for technical assistance and to assist with disaster response and debris removal plans.
- \$49.5 million General Fund in one-time funds to increase the amount of funding available through the CA Disaster Assistance Act including to reimburse local government costs associated with certain emergency response activities.
- \$32.8 million General Fund to backfill the property tax revenue losses that cities, counties and special districts will incur in FY 2017-18 and 2018-19 due to the 2017 wildfires and Southern California mudslides.

Budget Links:

Governor's 2018-19 May Revision:

<http://www.ebudget.ca.gov/>

DHCS 2018-19 May Revision Highlights:

http://www.dhcs.ca.gov/Documents/Budget_Highlights/FY2018-19-MR-Highlights-051118.pdf

Next Steps. The Legislature will begin to hear items related to the Governor's May Revision next week and will take action on all items previously held open in the coming weeks. Conference Committees will also meet upon Budget Subcommittees concluding their business to reconcile issues where the Senate and Assembly Actions do not align. The Constitutional deadline for the Legislature to pass the budget is June 15.

Questions. For questions on the items highlighted above or other budget-related inquiries, please feel free to contact the CHEAC office at (916) 327-7540.