

INTRODUCTION

As California enters 2021, the state's health and economy are threatened by the highest infection rate of the COVID-19 Pandemic. However, with increasing distribution of vaccines, California is poised to begin an equitable and broad-based recovery. The state has benefited from years of fiscal prudence—enabling investments to position the state for this recovery. The Governor's Budget includes a \$14 billion investment—including early action beginning this month—to provide immediate relief for individuals and small businesses disproportionately impacted by the pandemic, the safe reopening of schools and for extended learning time, and investment in strategies for creating quality jobs.

The Budget also continues the Governor's sustained focus on expanding opportunity with investments for Californians from early childhood to college—including expanded transitional kindergarten programs and more funding for the University of California, California State University and California Community Colleges.

The Budget makes new proposals to address the affordability of health care and housing, and supports the increase in the state's minimum wage to \$14 per hour. The Budget includes significant new strategies to reduce the impacts of climate change, with focused investments to support the state's zero-emission vehicle goals and an additional \$1 billion to address a comprehensive wildfire and forest resilience strategy.

Finally, the Budget promotes effective government with additional investments to improve the state's ability to respond rapidly to emergencies and continues the critical

work to improve government efficiency and bring government services into the digital age.

The Budget continues to reflect the principle that maintaining a balanced budget and strong budget resiliency is a necessary predicate for expanding programs, especially given the increased uncertainty caused by the COVID-19 Pandemic.

OVERALL BUDGET STRUCTURE

The state entered the COVID-19 Recession on a strong fiscal foundation after years of building reserves, paying down debt, and a focus on maintaining structurally balanced budgets over the long term. This enabled the state to protect programs during the Recession while responding immediately to combat the pandemic.

The Budget reflects \$34 billion in budget resiliency—budgetary reserves and discretionary surplus—that will advance progress toward a broad-based and equitable recovery. Of this amount, the reserves include: \$15.6 billion in the Proposition 2 Budget Stabilization Account (Rainy Day Fund) for fiscal emergencies; \$450 million in the Safety Net Reserve; \$3 billion in the Public School System Stabilization Account; and an estimated \$2.9 billion in the state's operating reserve.

The Budget continues progress in paying down the state's retirement liabilities and reflects \$3 billion in additional payments required by Proposition 2 in 2021-22 and nearly \$6.5 billion over the next three years. In addition, the improved revenue picture allows the state to delay \$2 billion in scheduled program suspensions for one year.

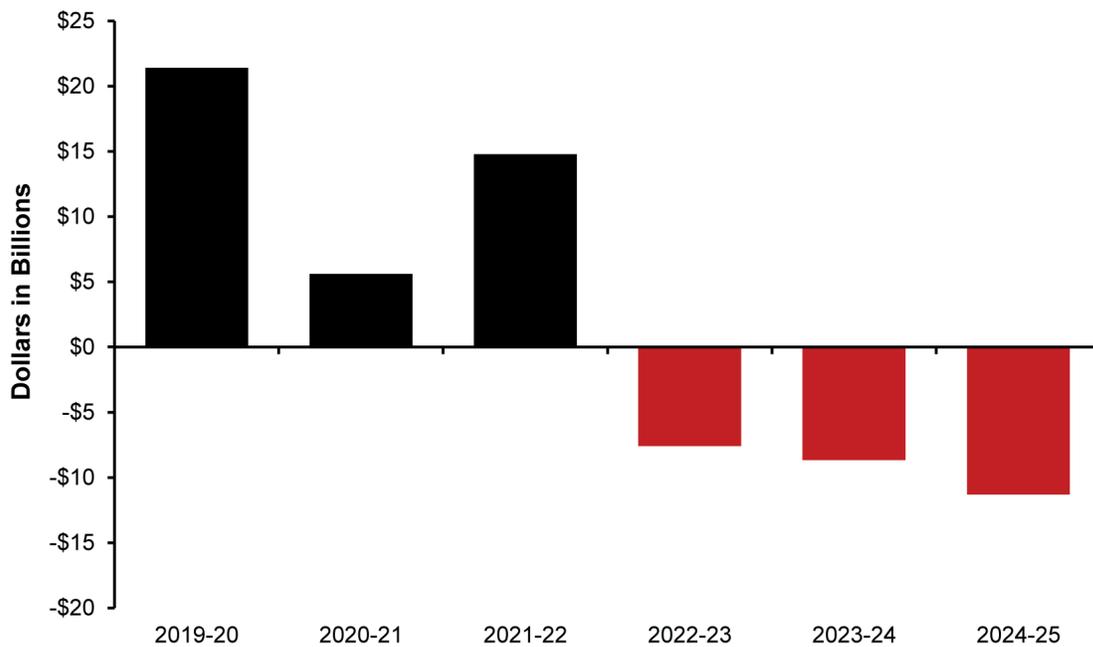
Since the 2020 Budget Act, the economic outlook and revenue forecast have improved. However, risks to the forecast remain higher than usual, and economic inequality has intensified since the pandemic began. In December, over 4 million Californians were still receiving some form of unemployment benefits, and only about half of the jobs lost from the start of the pandemic had been recovered. The Budget forecast was finalized before the provision of critical federal relief in the Coronavirus Response and Relief Supplemental Appropriations Act, and the forecast will be updated in May to reflect the positive impacts of this Act. Further federal relief is critical to help people and businesses struggling to survive and recover from the pandemic.

Budget resiliency will be critical to protect programs in the future, as expenditures are projected to grow faster than revenues, with a structural deficit of \$7.6 billion projected for 2022-23 that is forecast to grow to over \$11 billion by 2024-25.

This will also constrain the state's ability to undertake expanded ongoing commitments.

Finally, initial estimates project that Proposition 4, the State Appropriations Limit or "Gann Limit," will be exceeded for just the second time since its passage in 1979. The limit is currently projected to be exceeded by \$102 million. Any funds above this limit are constitutionally required to be allocated evenly between schools and a tax refund. An updated calculation of this limit will be included in the May Revision.

Budget Projects Surplus, But Future Shortfalls Projected ^{1/}



^{1/} Budget shortfalls or surplus, measured by the annual Governor's Budget.

IMMEDIATE ACTIONS

In December, the state approved two vaccines for distribution and is expediting their equitable distribution. As the state continues to respond to the COVID-19 Pandemic, the Budget supports expanding hospital capacity, testing, contact tracing, and securing needed personal protective equipment. The state also continues efforts to support the health care workforce and vulnerable populations, including individuals experiencing homelessness, farmworkers, and seniors.

IMMEDIATE RELIEF TO INDIVIDUALS AND SMALL BUSINESSES

In recognition of the disproportionate impact the COVID-19 Pandemic has had on low-income Californians and small businesses, the Budget proposes \$3 billion of pandemic relief for immediate action in January. This package includes:

- \$2.4 billion for the Golden State Stimulus—a \$600 state payment to low-income workers who were eligible to receive the earned income tax credit in 2019.
- An additional \$575 million for grants to small businesses and small non-profit cultural institutions disproportionately impacted by the pandemic, bringing total relief this year for small businesses to over \$1 billion.
- Immediate and targeted fee relief for impacted industries, including restaurants and personal services.

The federal COVID-19 relief bill approved in late December extends unemployment benefits by 11 weeks and adds \$300 to weekly payments, provides one-time \$600 payments to individuals, and includes support for small business, local transit, and schools. (The Potential Estimates for California: Coronavirus Response and Relief Supplemental Appropriations Act figure summarizes the major provisions of the federal COVID-19 relief bill.) This relief package will provide needed support in the first few months of 2021 to households hardest hit by the pandemic. However, more federal relief is needed, as the economic impacts of the pandemic are projected to extend beyond the first quarter of 2021.

SAFE REOPENING OF SCHOOLS AND ADDRESSING PANDEMIC IMPACTS ON STUDENTS

The vast majority of California's K-12 and higher education students have shifted to distance learning since March 2020. While school districts and teachers have done a tremendous amount to improve the quality of education from the first emergency programs, continued distance learning poses challenges to student achievement and well-being—especially for the youngest students and those in special education.

The Budget proposes immediate action in January to provide \$2 billion for the safe reopening of schools beginning in February, with a priority for returning the youngest children (transitional kindergarten through 2nd grade) and those with the greatest needs first, then returning other grade levels to in-person instruction through the spring. These payments to school districts will be structured to extend only to those districts that are already open or make plans to return students to campus for safe in-person instruction. This will accompany guidance from the California Department of Public

**Potential Estimates for California
Coronavirus Response and Relief Supplemental Appropriations Act**

(Dollars in Billions)

Cost Areas	Available Nationwide	California Estimate
Individuals and Families	\$326.4	\$42.4
Unemployment Insurance Benefits	\$120.0	\$20.0
Economic Impact Payments (\$600 per person)	\$166.0	\$18.3
Food Assistance	\$13.0	\$1.3
Rental and Utility Assistance	\$25.0	\$2.6
Funeral/Burial Assistance	\$2.4	\$0.2
Test, Trace, Vaccinate	\$54.1	\$2.2
Testing and Contact Tracing	\$19.5	\$1.8
Testing in Rural and Underserved Communities	\$2.8	TBD
Vaccine Development	\$19.7	-
Vaccine Manufacturing and Distribution	\$8.8	\$0.4
Strategic National Stockpile (PPE)	\$3.3	-
Health/Mental Health	\$10.3	\$0.7
Provider Relief	\$3.0	\$0.2
Increase Medicare Provider Payments	\$3.0	TBD
Mental Health and Substance Use Disorders	\$4.3	\$0.5
Business and Transportation Support	\$408.1	\$50.1
Small Business Support/Paycheck Protection (excluding airlines)	\$310.0	\$45.2
Live Venues	\$15.0	TBD
Child Care/Head Start	\$10.3	\$1.0
Agriculture (Farmers, Ranchers)	\$13.0	\$0.6
Loans to Underserved Communities	\$15.0	TBD
Airlines (Paycheck Protection) and Airport Improvements	\$18.0	\$0.4
Transit/Bus/Amtrak	\$17.0	\$2.0
State Highways	\$9.8	\$0.9
Education	\$81.1	\$10.1
Primary and Secondary	\$54.3	\$6.8
Governor's Emergency Education Relief (GEER) Funds	\$1.3	\$0.2
GEER - Private Schools	\$2.8	\$0.2
Higher Education	\$22.7	\$2.9
Broadband/Telehealth	\$7.0	TBD
Totals	\$887.0	\$105.5

Health on safety measures, including testing schedules for students, teachers and staff, as well as a revised framework for state technical assistance, transparency and enforcement.

The Budget also includes \$4.6 billion Proposition 98 General Fund for extending learning time, including summer school programs and other strategies to address the

pandemic's impacts on student learning. To provide time to plan for these interventions, the Budget proposes early action by the Legislature this spring to approve these funds.

EDUCATION, JOBS AND ECONOMIC RECOVERY

The K-12 and higher education systems are critical to positioning the state for sustained recovery and growth, and the Budget prioritizes funding for these systems. To accelerate job creation and an equitable recovery, the Budget includes targeted short-term business incentives, including micro-grants for entrepreneurship in underserved communities.

K-14 EDUCATION

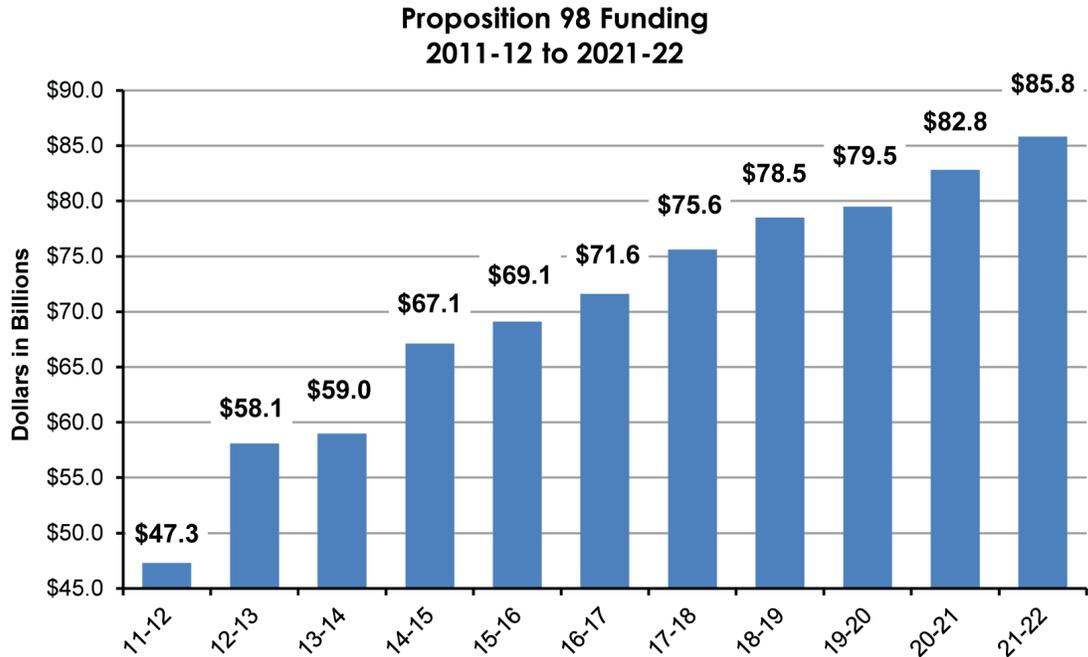
Under Proposition 98, the Budget's improved revenue estimate results in not only significantly more funding for schools, but also the highest funding level ever at \$85.8 billion. The 2020 Budget Act included a supplemental payment in addition to the Guarantee because of a projected anomaly in the school funding formula. Even though this anomaly no longer exists, the Budget continues to commit \$2.3 billion General Fund one-time in recognition of the additional costs schools face as they respond to the pandemic.

The Budget directs a significant portion of additional funding to paying down nearly two-thirds of the deferrals implemented last year and provides a 3.84-percent cost-of-living adjustment to the Local Control Funding Formula. The significant growth in capital gains and overall General Fund revenue growth also triggers deposits of roughly \$3 billion into the Public School System Stabilization Account, resulting in a statutory cap of 10 percent on local school district reserves in 2022-23.

ADDRESSING STUDENT MENTAL HEALTH

The Budget recognizes the toll the COVID-19 Pandemic has taken on mental health—especially students'—and proposes \$400 million in one-time funding to implement an incentive plan through Medi-Cal managed care plans, in partnership with county behavioral health departments, to increase the number of students receiving preventative and early intervention behavioral health services by schools.

The Budget also includes \$265 million one-time Proposition 98 General Fund to develop a range of community school models that holistically address the needs of children, \$50 million one-time Proposition 98 General Fund to create statewide resources and provide professional development on social emotional learning and trauma-informed



practices, and \$25 million one-time Mental Health Services Fund to fund partnership grants between county behavioral health departments and school districts.

EARLY EDUCATION AND CHILD CARE

Since 2019, the state has invested approximately \$400 million ongoing to expand early education and child care. The COVID-19 Pandemic has disrupted the child care system and federal funding has been critical to reducing long-term losses in this system. The Budget focuses on avoiding further loss in this system and builds on the recommendations made in the Master Plan for Early Learning and Care. It expands high-quality transitional kindergarten programs for all four-year-olds by allocating \$250 million one-time Proposition 98 General Fund in incentive funds for districts that expand these programs. The Budget also includes \$200 million one-time General Fund for transitional kindergarten and kindergarten facilities and \$50 million one-time Proposition 98 General Fund for professional development focused on preparing teachers for early childhood programs.

The Administration has already begun the collective bargaining process with representatives of child care providers to negotiate a memorandum of understanding that governs the payments made to these providers. The Budget also reflects \$44 million ongoing Cannabis Funds for 4,500 more child care vouchers, including \$21.5 million in 2020-21.

HIGHER EDUCATION AND WORKFORCE

California's higher education system continues to be exceptional, and more must be done to provide opportunities for underrepresented student groups and to reverse the significant pandemic-related decline in enrollment experienced in the community college system.

The Budget proposes early action for community college funding to provide emergency financial assistance and to re-engage students who have left higher education during the pandemic. The Budget also includes additional student supports for all three of the state's higher education systems for the coming year.

The Budget proposes a total of \$786 million General Fund for the University of California and the California State University with an expectation that they focus on measurable goals to address equity gaps, further maintain online educational opportunities, and expand dual admissions and other innovative strategies that reduce time to degree completion. The Budget also assumes resident tuition and fees remain flat in 2021-22.

The pandemic will likely have a permanent impact on the types of available jobs and the skills needed by employers. Workforce retraining, especially for those now unemployed, is a high priority in the Budget, which proposes for early action \$25 million one-time General Fund to immediately expand existing High Roads Training Program apprenticeship programs that will result in thousands of new jobs and training for new careers. The Budget also includes additional funding for the California Apprenticeship Initiative work-based learning opportunities through the community colleges.

The Budget proposes \$250 million one-time General Fund to support workforce development and better linkages between higher education and gainful employment. This will focus on communities that have been systematically excluded from opportunities to build skills and create wealth.

ACCELERATING ECONOMIC RECOVERY AND JOB CREATION

Advancing an equitable and broad-based recovery is a focus of the Budget as unemployment levels remain high and economic inequality has been exacerbated by the pandemic. This effort builds on actions taken in 2020 to support small businesses, including the elimination of the first year of the minimum franchise tax, expansion of small business loan guarantees, and creation of a new Main Street hiring tax credit. The Budget includes the following to accelerate economic recovery and job creation:

- \$777.5 million for a California Jobs Initiative to provide incentives targeted at accelerating investment and job creation;
- \$353 million for workforce development;
- \$1.5 billion for the infrastructure and incentives to implement the state's zero-emission vehicle goals;
- \$500 million for infill infrastructure to accelerate housing development;
- \$385 million for targeted investments to build a more sustainable agricultural industry; and
- \$300 million for deferred maintenance and greening of state infrastructure.

The Budget proposes early action on a portion of these incentives in the spring to accelerate recovery before the 2021-22 fiscal year begins in July.

The Governor's Future of Work Commission was established to develop recommendations to California leaders to support inclusive, long-term economic growth and prosperity for all Californians. The Commission plans to issue a report this month that will focus on the impact of technology on the workforce, job quality, wages and working conditions, worker safety nets, and workforce training.

ADDRESSING HEALTH CARE AFFORDABILITY AND AGING

The COVID-19 Pandemic has accentuated the need for health care for all. While responding to the COVID-19 Pandemic, the state continues to work on long-term plans to reduce the costs of health care by lowering prescription drug costs; the Budget includes the creation of a new Office of Health Care Affordability. The Office will increase quality and cost transparency, develop cost targets, and evaluate consequences for entities that fail to meet the targets.

During the pandemic, Covered California has extended enrollment periods to encourage individuals to enroll who may have lost their jobs and employer-based insurance due to the pandemic. The Budget also creates the Office of Medicare Innovation and Integration to support long-term care innovation in commercial Medicare Advantage Plans to leverage and integrate models under Medi-Cal, such as the Home and Community Based Services Waiver.

The Budget proposes to implement the California Advancing and Innovating Medi-Cal (CalAIM) initiative to reduce variation and complexity in the state's Medi-Cal program,

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manage member risk and need, and improve outcomes through payment reform. CalAIM will target and coordinate care for vulnerable populations with complex health needs that currently drive high-costs. The effort will include housing-related services and flexible wrap-around services so health plans may avoid costlier alternatives to hospitalization, skilled nursing facility admission, and/or discharge delay.

The Budget recognizes the extraordinary challenges older Californians and their families face during the COVID-19 Pandemic, and proposes a range of investments to increase opportunities for Californians to age well over the next decade, including developing new strategies with the federal government to leverage Medicare to provide additional long-term services and supports.

HOUSING AND HOMELESSNESS

The state continues to make progress in addressing the housing availability and affordability crisis that has been exacerbated by the COVID-19 Pandemic. In addition to the \$500 million one-time General Fund for infill infrastructure mentioned earlier in this Chapter, the Budget also proposes an additional \$500 million in low-income housing tax credits to support low-income housing development. The Administration is streamlining and reorganizing state housing programs to maximize housing production, while also continuing to support below-market rate housing.

Through Homekey—a recent effort to acquire motels for homeless housing to respond to the COVID-19 Pandemic—the state has awarded \$846 million to 51 local agencies to secure over 6,000 units of permanent housing for individuals and families who had been homeless. However, a comprehensive response to homelessness requires a continuum of supports. For too long, the state and local governments have provided only short-term mitigation strategies, and have not developed a comprehensive framework for addressing permanent solutions. The Budget includes \$1.75 billion one-time General Fund to purchase additional motels, develop short-term community mental health facilities, and purchase or preserve housing dedicated to seniors. The Budget also proposes changes to the state's Medi-Cal system to better support behavioral health and housing services that can help to prevent homelessness.

EMERGENCY RESPONSE AND PREPAREDNESS

In 2020, the state experienced catastrophic wildfires that consumed over four million acres, far more than any previous year in the state's history. The historic emergency response, while combatting the COVID-19 Pandemic at the same time, strained the

state's emergency response capabilities. The Administration is developing a spring proposal to strengthen the Governor's Office of Emergency Services' ability to respond to emergencies and support recovery efforts, especially in vulnerable communities.

Building on significant investments in the state's firefighting capabilities, the Budget adds \$143 million General Fund to support 30 new fire crews, and also includes \$48 million to continue phasing in Black Hawk helicopters and large air tankers.

CLIMATE CHANGE ACTION

As mentioned earlier in this Chapter, the Budget proposes a \$1.5 billion comprehensive strategy to achieve the state's zero-emission vehicle goals by 2035 and 2045, including securitizing up to \$1 billion to accelerate the pace and scale of the infrastructure needed to support zero-emission vehicles.

The Budget proposes an additional \$1 billion to support a coordinated forest health and fire prevention strategy that maximizes technology and science-based approaches to protect state forestlands. The Budget proposes \$323 million for early action in the spring to start these forest health and fire prevention projects before the next fire season.

The Budget includes strategic investments for the Department of Fish and Wildlife to enhance its ability to protect the state's unique biodiversity in the face of climate change, and to support California's agriculture industry as it addresses continued challenges while also producing nutritious food and advancing the state's climate resilience objectives.

ENVIRONMENTAL JUSTICE

The Budget includes \$300 million one-time General Fund for toxic site cleanup and investigations of high-priority contaminated properties in impacted communities across the state, which will be prioritized based on public health risk criteria. Further, the Budget creates incentives to clean up and develop these sites for future housing. The Budget also proposes comprehensive governance and fiscal reform for the Department of Toxic Substances Control that will provide for the support needed in the long term to address future cleanups of orphan sites and the reduction of harmful toxic substances in the environment.

The Budget includes a multi-faceted approach to reducing harmful pesticides and supports the transition of the agricultural industry to integrated pest management and more regenerative practices.

RESULTS-ORIENTED GOVERNMENT AND DIGITAL TRANSFORMATION

The COVID-19 Pandemic has required many businesses to be flexible, creative, and innovative. As the employer of a workforce of over 250,000, the state also responded immediately by putting in place a statewide telework program and new ways to conduct state business. This shift has meant the state must also evaluate its portfolio of state leases to determine spaces that can be released and/or consolidated.

The Budget assumes a five-percent permanent reduction in state operations expenditures, challenging departments and agencies to find more efficient means to provide services to Californians.

The Budget also makes major investments to provide additional support to the California Department of Technology to bolster its ability to review and improve upon critical state information technology systems before a failure occurs. In addition, the Office of Digital Innovation continues to lead state government in the transformation of consumer-facing services.

PLANNING FOR THE FUTURE

There are considerable risks to the forecast, including more widespread bankruptcies and a fall in the stock market, which could affect higher-income workers who contribute heavily to revenues. A strong reserve has supported the state in its direct response to the COVID-19 Pandemic and protected the state's core funding responsibilities. Reserves will be critical to balancing the budget in future years along with other solutions to bring spending and revenues into alignment. For now, the state must do all that it can to avoid further hardship by continuing to fight the COVID-19 Pandemic and support the populations most impacted, while also making targeted investments to accelerate an equitable and broad-based recovery.

While the state is currently in the midst of a second and more serious wave of the COVID-19 Pandemic, vaccinations are arriving in the state and science and medicine continue to make advances in treating the virus. California will overcome this challenge as it has overcome challenges in the past. The state, its businesses and its people will recover and will emerge stronger and more resilient. The Budget allocates funding to

address the inequities exacerbated by the pandemic and to prepare the state for the future.

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