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California's years of fiscal prudence enabled it to respond quickly to protect lives during the COVID-19 Pandemic, while making significant investments to support greater opportunity for all Californians. This included expanding paid family leave, establishing a Young Child Tax Credit, launching universal transitional kindergarten, expanding afterschool and summer programs, and providing universal no-cost school meals. It also included streamlining pathways from K-12 to higher education to connect degrees to careers and expanded financial aid to keep college costs down. In addition, California expanded health care subsidies for the middle-class and access to Medi-Cal for young adults and seniors, regardless of immigration status. The state also continued to expand and improve its emergency preparedness and response capacity, while dealing with extreme weather and record wildfires.

The state's continuing economic growth provides opportunities to build on these efforts and provide a strong foundation for California's future. The Governor's Budget supports the safety and health of all Californians—including continued support for the state's science-based approach to the COVID-19 Pandemic—and builds on California's innovation and entrepreneurial spirit to address climate change and build a more inclusive economic future.

The state now has a projected surplus of \$45.7 billion, which includes \$20.6 billion in General Fund for discretionary purposes, \$16.1 billion in additional Proposition 98 for K-14 education, and \$9 billion in reserve deposits and supplemental pension payments.

OVERALL BUDGET STRUCTURE

The state's budget resilience is stronger than ever: the result of building reserves, eliminating budgetary debt, reducing retirement liabilities, and focusing on one-time spending over ongoing investments to maintain structurally balanced budgets over the long term. These efforts enabled the state to protect programs during the COVID-19 Recession while responding immediately to combat the pandemic. The Budget allocates 86 percent of the discretionary surplus to one-time investments, and is projected to be structurally balanced in 2025-26, the last year in the multi-year forecast.

The Budget reflects \$34.6 billion in budgetary reserves. These reserves include: \$20.9 billion in the Proposition 2 Budget Stabilization Account (Rainy Day Fund) for fiscal emergencies; \$9.7 billion in the Public School System Stabilization Account; \$900 million in the Safety Net Reserve; and \$3.1 billion in the state's operating reserve. The Rainy Day Fund is now at its constitutional maximum (10 percent of General Fund revenues) requiring \$2.4 billion to be dedicated for infrastructure investments in 2022-23.

The Budget accelerates the paydown of state retirement liabilities as required by Proposition 2, with \$3.9 billion in additional payments in 2022-23 and nearly \$8.4 billion projected to be paid over the next three years.

The Budget projects the State Appropriations Limit or "Gann Limit" will likely be exceeded in the 2020-21 and 2021-22 fiscal years. Any funds above this limit are constitutionally required to be allocated evenly between schools and a tax refund. An updated calculation of this limit, and proposals to address it, will be included in the May Revision.

The economic forecast, finalized last November, does not consider the surge of the Omicron variant, thus the COVID-19 Pandemic remains a risk to the forecast. Strong stock market performance has generated a significant increase of volatile capital gains revenue that is approaching its prior peak levels (as a share of the state's economy) in 2000 and 2007. A stock market reversal could lead to a substantial decrease in revenues. Given the state's history of boom and bust cycles, additional deposits into the state's reserves would further prepare the state for future economic slowdowns. However, deposits into the reserves count towards the State Appropriations Limit. Therefore, any additional deposits would have to be carefully balanced against other spending priorities.

COVID-19 PANDEMIC

As the pandemic approaches two years, the state continues its science- and data-driven fight against COVID-19. California continues efforts to increase vaccination rates and expand testing to help slow the spread of the virus. To continue these efforts, the Administration is requesting early action to allocate an additional \$1.4 billion required to continue these efforts for the remainder of the fiscal year. The Budget also reflects \$1.3 billion for 2022-23 to continue COVID-19 efforts. This funding will support continued vaccine distribution and administration, including booster shots, and statewide testing, to keep Californians safe and the economy moving forward. The state also continues to support statewide hospital and medical surge efforts, precautionary measures in state institutions, contact tracing, and efforts to protect public health at the border.

To permanently expand the state's ability to protect public health and address social determinants of health, the Budget includes \$300 million General Fund for the Department of Public Health and local health jurisdictions. The Budget also includes major ongoing investments to modernize public health data systems that have been critical during the COVID-19 Pandemic.

EDUCATION AND PARENTS AGENDA

The Budget includes total funding of \$119 billion for K-12 education. K-12 per-pupil funding totals \$15,261 Proposition 98 General Fund—its highest level ever—and \$20,855 per pupil when accounting for all funding sources.

Last year's budget made major investments to benefit all parents, especially those with young children, with the centerpiece being launching universal transitional Kindergarten to all four-year-olds. The Budget includes \$1 billion Proposition 98 General Fund to begin the first year of this program, increasing access to at least 56,000 children and reducing student-to-adult ratios, with full implementation planned by 2025-26. With this change, schools are encouraged to use State Preschool programs to provide wraparound care for income-eligible students so they may have a full day of developmentally appropriate care and education. The Budget also includes nearly \$309 million total funds to focus the State Preschool program to better serve dual language learners and students with disabilities.

Parents' lives were upended by the COVID-19 Pandemic. The Budget recognizes the critical need for child care to support working parents by adding an additional 36,000

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slots on top of 110,000 slots added in the 2021 Budget Act, with the goal of adding 200,000 slots by 2025-26.

The 2021 Budget Act made a \$1.8 billion Proposition 98 General Fund down payment to expand after-school and summer programs to extend learning opportunities and address learning gaps caused by the pandemic. This investment helped provide families the opportunity for a 9-hour day filled with developmentally appropriate academics and enrichment, including six weeks during the summer. The Budget continues these opportunities with an additional \$3.4 billion Proposition 98 General Fund ongoing to support access to expanded-day, full-year instruction and enrichment for all elementary school students, with a focus on local educational agencies with the highest concentrations of low-income students, English language learners, and youth in foster care. Linked to this expansion is an additional \$937 million Proposition 98 General Fund to support integrating arts and music into enrichment programs.

The Young Child Tax Credit, established in 2019, provides a \$1,000 refundable tax credit to low-income earners with a child age 5 or younger. The Budget expands this tax credit to families that file returns without income, allowing more families to benefit, and proposes to index the credit to inflation, which will prevent the erosion of its value.

HIGHER EDUCATION

The Budget proposes multi-year compacts with the University of California (UC) and California State University (CSU), and a multi-year roadmap for the California Community Colleges (CCCs). These include an expectation of ongoing base augmentations for the UC and the CSU to aid the systems in achieving goals that include expanding access for California students, reducing total cost of attendance through timely degree completion, and closing equity gaps. Building on earlier efforts to better connect students to careers and strengthen occupational pathways that improve student economic mobility, the compacts will also center around better aligning curricula and student learning objectives to the state's workforce needs. The Administration is also establishing an overarching goal of achieving 70 percent postsecondary degree and certificate attainment among working-aged Californians by 2030, a recommendation of the Governor's Council on Post-Secondary Education.

Following the landmark expansion of the financial aid entitlement to all CCC students, the Budget further supports efforts to reduce the overall cost of attendance by continuing a second year of funding to support the construction of affordable student housing and a second year of funding for learning-aligned employment, and

supporting the first year of a revamped Middle Class Scholarship that will help reduce the total cost of college for more California families.

EXPANDING OPPORTUNITY AND STRENGTHENING CALIFORNIA'S FUTURE

California is uniquely positioned to confront climate change while simultaneously investing in expanding opportunity and strengthening California's future. The Budget focuses new investments in the continued growth of the state's economy and opportunity for all Californians, and positions the state as a global leader in innovation and solutions to both mitigate and adapt to the changing climate.

California is home to industries that have fundamentally altered the way the world lives and communicates. This leadership will be furthered by encouraging the development of climate solutions that prepare and protect communities, create jobs, and fuel economic growth.

ECONOMIC GROWTH AND JOB CREATION

The Budget restores business tax credits, including research and development credits and net operating losses that were limited during the COVID-19 Recession, and proposes an additional \$250 million per year for three years for qualified companies headquartered in California that are investing in research to mitigate climate change.

The Budget also includes a new tax credit for those that opt in to develop green energy technologies—totaling \$100 million per year for three years. So Californians can share more broadly in the gains from these innovations, these new credits will be structured so that when the business becomes profitable, a share of the profits will be repaid to the state. The state also plans to develop naturally occurring resources of lithium—a critical component of advanced battery technology—to improve the state's ability to store renewable energy while creating high-paying jobs and generating benefits for surrounding communities and all Californians.

The Budget also proposes direct investments in climate-related research and development at the UC, including \$185 million for applied research, regional networks of climate-focused technology incubators, and workforce development and training hubs. These investments will support the next generation of inventions and innovations to address climate change.

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In addition to the federal Infrastructure Investment and Jobs Act (IIJA) of 2021, which will deliver billions of dollars for infrastructure to California, the Budget makes an historic state investment of over \$20 billion in infrastructure-related investments to prepare and protect California communities from climate change. These investments will further facilitate economic growth and create thousands of jobs.

STRENGTHENING SMALL BUSINESS

California small businesses are drivers of economic growth—creating two-thirds of the state's new jobs during the recovery. Last year's budget created the nation's largest small business relief program—providing billions in needed relief to thousands of small businesses, and the Budget proposes approximately \$500 million in additional tax relief over several years through state conformity for qualified California recipients of federal relief grants in significantly impacted industries. To further encourage small business creation, the Budget waives initial filing fees for new businesses. In addition, the Budget permanently expands programs that provide technical assistance and access to capital to spur business creation in underserved communities. The Budget also includes \$150 million one-time General Fund to support small businesses previously waitlisted in prior rounds of the state's Small Business COVID-19 Relief Grant Program.

The Budget also allocates \$3 billion General Fund over the next two years to reduce the Unemployment Insurance Trust Fund debt owed to the federal government. Over the long-term, this will reduce costs to the state and benefit employers by reducing debts accumulated during the pandemic.

EXPANDING WORKFORCE TRAINING AND OPPORTUNITY

So more Californians can participate in California's economic growth, the Budget includes a multipronged strategy to train workers for jobs critical to California's economic growth and to meet growing demands for teachers and health care workers.

These investments start in the K-12 school system with \$1.5 billion Proposition 98 General Fund to support the development of college and career pathways focused on education, health care, technology, and climate-related fields. Promoting pathways that allow students to move seamlessly from high school to college to career will improve the number of students who pursue and achieve post-secondary education and training. These funds will focus on creating local partnerships that bring

together school systems, higher education institutions, and employers to develop integrated pathways to college and careers in these high-demand fields.

In addition, the Budget invests \$1.7 billion to expand the state's health and human services workforce, including training strategies to increase the state's workforce of nurses, social workers, emergency medical technicians, behavioral health care providers, and community health care workers.

Building upon last year's multi-billion dollar investment in teacher preparation, retention, and training, the Budget waives certain teacher examination fees and encourages the development of new integrated teacher preparation programs to address the state's shortage of qualified teachers.

CLIMATE CHANGE AND WORKFORCE

The Budget includes multiple workforce investments with a focus on climate change, including \$35 million General Fund for the UC to create regional workforce development and training hubs focused on climate change; \$30 million General Fund over two years to the CCC to train, develop, and certify forestry professionals; and \$60 million General Fund over three years for the California Workforce Development Board's Low Carbon Economy Workforce grant program to support workforce development programs that align with strategies in the state's Climate Change Scoping Plan.

Last year, \$600 million was allocated to the Community Economic Resilience Fund for regional strategies that support economic and workforce transitions caused by the COVID-19 Pandemic, climate change, and other factors. The Budget complements this effort with \$450 million General Fund over three years starting in 2023-24 to support local governments as local economies adjust, \$215 million General Fund over two years to support an oil and gas well capping initiative to improve the safety of communities while providing high-quality jobs, and \$50 million General Fund to establish a fund for displaced oil and gas workers as the state continues to phase out oil production.

ADDRESSING CLIMATE CHANGE

Building on last year's historic \$15 billion in climate investments, the Budget integrates climate, equity, and economic opportunity across the state's budget—including housing, health, and education—to mobilize a coordinated state response to the climate crisis.

WILDFIRES

California experienced 4 of the 20 largest wildfires in its history in 2021. Last year, the state expanded firefighting capacity and invested \$1.5 billion to significantly increase the state's ability to prevent wildfires. The Budget proposes an additional \$1.2 billion over two years to continue investments in forest health and fire prevention, including a major new reforestation effort. The Budget also makes a major investment to expand firefighting efforts, including new dedicated aircraft and hand crews, as well as \$400 million to address the effects of the recent prolonged wildfire seasons on CAL FIRE firefighters.

DROUGHT

Despite recent rain, dry conditions may extend to a third consecutive year, requiring the state to prioritize State Water Project allocations for health and safety needs and to maintain salinity control in the Bay-Delta to protect endangered species. Building upon last year's three-year, \$5.2 billion allocation to support drought response and long-term water sustainability, the Budget includes an additional \$750 million General Fund to address immediate drought response needs, including \$250 million set aside as a contingency. These investments will expand support for critical drinking water emergencies and mitigate drought damage to fish and wildlife, and the investments will also support small farmers and ranchers and water systems facing a loss of water supply.

TRANSPORTATION

The IIJA will deliver more than \$10 billion of new formula-based transportation funding to California over the next five years and billions of dollars in additional funding from new competitive grants. This measure could also provide billions in additional funds for clean drinking water, clean energy, toxic cleanup, broadband, and other infrastructure investments.

The Budget includes an additional \$9.1 billion (\$4.9 billion General Fund and \$4.2 billion Proposition 1A bond funds) to support the continued development of a first-in-the-nation, electrified high-speed rail system in California, regional transit and rail projects, bicycle and pedestrian projects, and climate adaptation projects, with a particular focus on aligning the state's transportation system with its climate goals. The Budget also includes \$1.2 billion General Fund for improvements to the state's goods

movement infrastructure, including improving data interconnectivity to reduce congestion and increase supply chain efficiency, thereby reducing harmful emissions from this critical sector.

The Budget adds an additional \$6.1 billion (General Fund, Proposition 98 General Fund, federal funds, and Greenhouse Gas Reduction Fund) over five years, which builds on last year's unprecedented zero-emission package, for a total of \$10 billion to advance California's climate and transportation goals. These funds are focused on supporting zero-emission vehicles and charging infrastructure in low-income communities across the state, including funding for community-based projects. The Budget also invests significantly in replacing heavy-duty trucks and buses with zero-emission vehicles, given their disproportionate impact on low-income communities and communities near California's ports, as well as green school transportation to reduce harmful emissions from aging diesel-fueled bus fleets and reduce ongoing school transportation costs.

ENERGY

The Budget makes investments to meet the state's clean energy goals with \$2 billion General Fund over two years to provide incentives for long-duration-storage projects, renewable hydrogen, and industrial decarbonization, including in the food processing sector. The Budget also includes funding for decarbonization and electrification of existing buildings in disadvantaged communities, as well as infrastructure improvements to facilitate the development of offshore wind energy production.

HOUSING

Since 2019, California has invested significant funding for affordable housing development throughout the state, and has enacted laws to hold local jurisdictions accountable for meeting their regional housing needs. The Budget builds upon the \$10.3 billion housing investment made last year with a focus on aligning housing goals and climate goals.

The Budget proposes an additional \$1.5 billion over two years to accelerate the development of affordable housing. The focus of the majority of these investments is on development in and near downtowns throughout the state. Building housing near jobs, schools and other amenities reduces commutes and greenhouse gas emissions.

IMPROVING HEALTH CARE AFFORDABILITY

California has advanced multiple measures in recent years to improve health care affordability—expanding Covered California premium subsidies for the middle class, increasing access to Medi-Cal for children, young adults, and older adults regardless of immigration status, providing greater coverage for preventative services, and taking actions to reduce prescription drug costs. The 2021 Budget Act also included \$1.4 billion to transform California's behavioral health system for children and youth.

The Budget will make California the first state to realize the goal of universal access to health coverage for all Californians by closing a key gap in preventative coverage for individuals ages 26 to 49, regardless of immigration status. The Budget also continues progress in improving health care affordability and proposes \$30 million to create the Office of Health Care Affordability, charged with increasing the transparency of pricing, developing specific cost targets for different sectors of the health care industry, and imposing financial consequences for entities failing to meet these targets.

The Budget continues efforts to improve preventative care for families with children and includes \$400 million (General Fund and federal funds) for provider payments focused on closing equity gaps for children's preventative care measures, maternity care, depression screenings, and follow up behavioral health emergency visits. The Budget also includes \$53.2 million (General Fund and federal funds) to reduce premiums for children, pregnant women, and working disabled adults in Medi-Cal.

Finally, while other states seek to limit a woman's ability to receive reproductive care, the Budget expands access to reproductive healthcare services, and invests to improve clinical infrastructure and expand the workforce in reproductive healthcare services—continuing California's commitment to a woman's right to choose.

HOMELESSNESS

The state has invested billions of dollars in recent years to provide funding to local governments for critical housing supports and homelessness services, marked by last year's three-year, \$12 billion allocation. The state has also invested in new housing through Homekey—an effort started during the COVID-19 Pandemic that has acquired and converted a variety of building and housing types—including hotels, motels, and commercial buildings—to house individuals and families experiencing homelessness. This effort was also expanded last year to include the development of a behavioral health continuum of housing and community care facilities.

The Budget proposes an additional \$2 billion General Fund over two years to continue the state's efforts to address homelessness by investing in behavioral health housing and encampment cleanup grants. These investments are intended to serve as a bridge to other related efforts such as Homekey and California Advancing and Innovating Medi-Cal (CalAIM), which will redesign Medi-Cal to better serve Californians, including individuals experiencing homelessness and provide long-term care.

CRIME

Personal safety is one of the most basic needs—and expectations—of all Californians. The Budget provides \$285 million General Fund over three years for grants to bolster local law enforcement response to organized retail theft crime, as well as to assist local prosecutors in holding perpetrators accountable. The Budget expands the California Highway Patrol's retail theft task force and also includes \$18 million General Fund over three years for the Attorney General to prosecute organized retail theft crimes, and \$5 million ongoing General Fund for the Attorney General to continue leading anti-crime task forces throughout the state.

In addition, the Budget makes one-time General Fund investments of \$25 million to provide matching grants for local government gun buyback programs, \$20 million to support small businesses victimized by retail theft, and \$20 million for a drug interdiction program at the California-Mexico border.

LOOKING AHEAD

While California's economy is much improved from this time a year ago, considerable risks remain, including a potential stock market decline that could affect higher-income households that contribute substantially to state revenues. A strong reserve was critical to the state's response to the COVID-19 Pandemic and the resulting recession, and reserves will remain critical to balancing the budget in the event of an economic downturn. If current budgetary conditions continue, expenditures are expected to be near or exceed the State Appropriations Limit—and increased deposits into the reserves are not currently exempt from this limit. If the state's expenditures exceed the limit, tax refunds and supplemental school payments are required.

In addition to strengthening reserves, it is essential that one-time revenues be used for one-time expenditures in order to maintain fiscal stability. Maintaining a balanced

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budget over the long-term will minimize disruptions to core programs such as education and health care when revenues decline.