



Economic Development Analysis Governor's May Revise to FY 2023-2024 Budget

May Revise Proposes Funding Delays, Reductions, Swaps, and Bonds as State Deficit Deepens; Economic Development Proposals Retained and Augmented

The May Revise the Governor presented reflected what everyone expected; state revenues continued to decline from January projections, increasing the deficit from \$22.5 to \$31.5 billion. However, that's the rosy scenario, given that deficit estimates are based on the hope that there is no recession, belief that the federal debt limit dispute will be resolved, and anticipation that \$42 billion will be collected in October from taxpayers in disaster-affected counties. Should such an optimistic outlook not occur, state budget woes would become much deeper. Yet, at least for now, programs that CALED members care the most about remain untouched, and a few are even augmented. A copy of the May Revise can be found here: <https://ebudget.ca.gov/budget/2023-24MR/#/BudgetSummary>

The Governor's plan builds off his initial January budget and proposes a combination of funding shifts, reductions, delays, and bonds to close the gaps. He said the state's budget challenges derived from its volatile income tax structure that relies heavily on the fortunes of a narrow group of high-income earners. He also maintained that it was not prudent for the state to dip into its reserves, nor was he open to tax increases being proposed by legislators. Some of the major features of the Governor's proposed solutions include:

- Shifting \$1.1 billion in proposed spending on climate issues to a Climate Bond.
- Shifting Prop. 63 mental health funds, currently allocated to counties, to help offset \$500 million in General Fund expenditures and support a Behavioral Health Bond, that would also fund housing and substance abuse needs.
- Renewing the Managed Care Organization (MCO) tax (\$19.4 billion over three years) levied on health care organizations that helps pull down federal funding for MediCal.
- Delaying allocation of \$345 million to a foreclosure assistance program.
- Shifting \$635 million in proposed zero emission vehicle expenditures to the Greenhouse Gas Fund.
- Paying interest on bonds to support over \$1 billion in UC/CSU construction projects rather than the General Fund.
- Recovering over \$629 million in unexpended funding from various programs, and allocating \$495 million in safety net reserve funds to backfill program obligations.

LAO Estimates Deeper Budget Problem: The Legislative Analyst's Office issued brief initial commentary on the May Revise, including that the budget condition was \$6.2 billion larger than the Administration estimates, and the state faced \$15 billion operating deficits in each of the next two fiscal years. To better prepare for the downturn, they also urged legislators to pull back on \$11 billion in one-time or temporary spending included in the FY 23-24 budget. A copy of the LAO's comments on the budget can be found here: <https://www.lao.ca.gov/Publications/Report/4769>

Governor's Positive Comments on Economic Development: During his press conference, the Governor recognized the vital role of economic development, entrepreneurs, and small businesses in California's Economy. To view his presentation on this topic it begins at the 35.50-minute mark and goes through 41.20. <https://www.youtube.com/watch?v=ZbEZKZzZmNw>

Economic Development Programs and Other New Proposals:

The May Revise continues to support the proposals in the Governor's January Budget that many CALED members are tracking, including:



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- **CERF:** Continues to fund the Community Economic Resilience Fund (CERF) program at \$600 million.
- **Broadband:** Continues to fund broadband investments, with no additional proposed delays or deferrals other than as proposed in the Governor's January budget.
- **Workforce:** Continues to fund the various workforce investment programs, as proposed in January, while also restoring \$30 million for workforce training for women in the construction sector, and another \$49.8 million for public health workforce training.
- **Film Tax Credit:** Continues to extend the existing film and television tax credit by five years at \$330 million annually.
- **Semiconductor Manufacturing:** Continues to offer additional incentives for semiconductor manufacturing, including \$120 million in targeted California Competes Grants, and removing geographic limitations associated with the existing New Employment Credit.

Permitting/Procurement Reform Package Announced: As part of his press conference, the Governor announced his plan to unveil a permitting and procurement reform package aimed at accelerating "shovel ready" infrastructure projects (clean energy, roads, bridges, public transit, water storage and conveyance, and faster internet), funded by over \$180 billion in federal and state funds over the next decade. The proposals, which may affect housing as well, are projected to cut timelines by three years, save hundreds of millions, and reduce paperwork by hundreds of thousands of pages. The Governor revealed the contents of this proposed 11-bill package on Friday, May 19. A link to his announcement and related documents can be found here:

<https://www.gov.ca.gov/2023/05/19/governor-newsom-unveils-new-proposals-to-build-californias-clean-future-faster/>

In addition, the May Revise proposes the following additions, reductions, and changes:

- **Office of Small Business Advocate:**
 - Allocates \$23.5 million federal funds, to be spent over five years, for the Office of the Small Business Advocate to provide technical assistance to small businesses, including businesses owned by socially- and economically-disadvantaged individuals, applying for State Small Business Credit Initiative capital programs.
 - Makes other statutory changes to extend the sunset date on several programs administered by the Office of the Small Business Advocate to allow additional time for grant awards and program closeout activities.
- **Restores Funding to IBank Climate Catalyst Fund:** Restores \$25 million (out of a proposed \$41 million proposed reduction in the January budget) to the Climate Catalyst Fund which offers funding to innovative climate-smart agricultural, forestry, clean energy, and other advanced technologies and projects. This restoration means \$33 million is available for this program.
- **Shifts Rural County Funding to City of Fresno:** Reallocates \$250 million to the City of Fresno, out of \$300 million originally proposed in the Governor's Budget to be allocated to small counties with high rates of unemployment and poverty. The reallocated funds would be used to support the City of Fresno's Public Infrastructure Plan to invest in the downtown area. This plan includes projects to build parking structures, develop green space, improve walkability, and for water infrastructure.
- **Augments Funding to Combat Local Flooding:** Reflecting California's fickle climate, the May Revise proposes to shift \$125 million from drought to flood relief, reduces funds set aside to combat salinity (due to low river flows) in the Delta by \$24.5 million, reduces by \$25 million a



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program that helps limit agricultural groundwater pumping near drought-stricken communities, and instead allocates:

- \$75 million to support local flood control projects.
- \$25 million for potential flood-related disaster relief.
- \$40 million for San Joaquin Floodplain Restoration.
- ***Agricultural Small Business Relief:*** Allocates \$25 million one-time General Fund (for a total of \$100 million) to the California Small Agricultural Business Drought Relief Grant Program to provide direct assistance to eligible agricultural businesses affected by recent storms.
- ***Reductions & Fee Increases Affecting Recreational Boating:*** Communities with recreational boating should be aware of the May Revise proposal to decrease local funding for boat launch facilities by \$6 million, and funding to combat invasive aquatic species by \$5.3 million, while also quadrupling annual boating registration fees from \$10 to \$40. Funding to assist local boating law enforcement and safety will remain funded at \$11.5 million annually.
- ***Reductions to Cannabis Tax Program Funding:*** The May Revise estimates \$567.4 (a decrease of \$102 million from initial estimates in the Governor's budget) will be available from cannabis tax revenues for education, environmental protection, and public safety programs:
 - \$340.4 million for education, prevention, and treatment of youth substance use disorders and school retention.
 - \$113.5 million for clean-up, remediation, and enforcement of environmental impacts created by illegal cannabis cultivation.
 - \$113.5 for public safety-related activities.
- ***Staffing-Up Program to Monitor Oil Refiner Profits:*** The May Revise allocates \$5.9 million for 14 positions at the California Energy Commission to begin collecting data and monitoring petroleum supply chain and pricing, and establish and enforce a maximum gross refining profit margin for refiners, as a result of SB X1-2 (Skinner) being enacted in March 2023.
- ***Offers No New Assistance (Yet) For Transit:*** Despite intense lobbying from transit agencies for state funding to help offset major declines in operational revenues due to decreased ridership, the May Revise contains no proposed additional funding, but states that the Administration "welcomes discussions" with the Legislature on potential near- and long-term solutions.
- ***Small Business COVID Relief:*** Reduces \$50 million in funding that was previously allocated to the California Small Business COVID-19 Relief Grant Program, given that there will be an additional amount remaining after all grants have been awarded.
- ***Reducing Positions at OPR:*** The May Revision proposes to reduce requested new staffing positions at the Governor's Office of Planning and Research (OPR) from 26 to 16, while also establishing a new information technology unit. The Administration will continue to evaluate existing positions within OPR and make further modifications over the next year.

Bond Proposals in May Revise

During his presentation the Governor highlighted his work with the Legislature on two bond proposals, which would, in part, offset state General Fund commitments:

- ***A Behavioral Health Bond,*** of an unknown amount, which would include proposed changes to the Mental Health Services Act, Prop. 63 of 2004. The Mental Health Services Act (MHSA) currently generates approximately \$3 billion annually that is allocated to counties to support various mental health programs. The Governor is proposing to authorize funding for increasing behavioral-related housing by 6,000 units, including housing for homeless veterans, and assisting those with substance abuse. In a related move, the Governor is also proposing to swap \$500 million in MHSA funds to backfill a proposed General Fund deferral of \$250 million to the



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Behavioral Health Bridge Housing Program, along with an additional \$250 million in budgetary savings.

- ***A Climate Resilience Bond***, of an unknown amount, which would include a swap-out from the General Fund to the bond of \$1.1 billion of funds dedicated to various climate resilience programs. The Governor said that the bond would also “allow us do even more in this space than was proposed in January.” With this statement, it appears that the bond could also propose to offset some or all of the \$6 billion in proposed reductions to these programs listed in the Governor’s January budget, which reduced (from \$54 to \$48 billion) the commitments made to these programs. Proposed funding to be shifted to the bond includes:
 - Water Recycling—\$270 million
 - Salton Sea Restoration—\$169 million
 - Community Resilience Centers—\$160 million
 - Transformative Climate Communities—\$100 million
 - Regional Resilience Program—\$100 million
 - Urban Greening—\$100 million
 - Statewide Parks Program—\$86.6 million
 - Sustainable Groundwater Management Act Implementation—\$60 million
 - Dam Safety and Flood Management—\$50 million
 - Multi-Benefit Land Repurposing—\$20 million

While shifting state General Fund commitments to bonds may be an attempt to maintain momentum on various priorities during a deficit, the additional interest costs are significant. The May Revise states: “When the state borrows to pay for infrastructure, roughly one out of every two dollars spent on infrastructure investments pays long-term interest costs, rather than construction costs.”

The Governor did not discuss two other bond-related items:

- ***A School Bond*** mentioned in the infrastructure section of the May Revise: “Given the ongoing need to construct and/or renovate educational facilities, the Legislature and Administration will need to engage in a conversation regarding the potential placement of a general obligation bond supporting the construction and/or modernization of education facilities on a future ballot for consideration by the voters.”
- ***A Housing Bond*** given that there are two major proposed housing bonds pending in the Legislature, AB 1657 (Wicks) for \$10 billion, and SB 834 (Portantino) for \$25 billion. Housing advocates and local governments cite inadequate funding as the key barrier to affordable housing.

Housing and Homelessness

Understanding that housing is a critical factor related to a comprehensive economic development strategy, here is additional information regarding both housing and homelessness. While the May Revise offered several minor funding adjustments -- a proposed funding swap to a homeless program, and a new deferral and reversion to existing housing programs -- the focus of the Governor’s comments at his press conference was on holding local agencies accountable to demonstrate results using the funds that have been, and are proposed to be, allocated.

- ***Continued Focus on Local Government Accountability***: “Accountability, accountability, it’s all about accountability, and that extends to housing affordability...” he said, promising that details would be revealed in a budget trailer bill. During his presentation, and in responses to questions from the press, he praised the work of HCD’s Housing Accountability Unit and the Attorney General, insisted that 2.5 million units was a “legally binding” requirement, promised more



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lawsuits against local governments would soon be filed, and declared that it was time to “clean up these damn encampments.” He dismissed press questions about local government requests for ongoing homeless funding and stated no Governor has focused or spent more in an effort to address the problem.

- **State Lowers Housing Need Projections to 148K:** While not addressed in the press conference or in the policy sections, information included in the Economic Outlook portion of the May Revise reveals that the state has reduced its projected housing needs stating: “As California population growth slows and projections of future growth decreases, California is now estimated to need around 148,000 housing units permitted annually (down from the Department of Housing and Community Development’s 2018 estimate of 180,000) to keep pace with projected population growth.” The May Revise also projects current housing production for 2023 at 109,000 units which will climb to 129,000 units annually by 2026.
- **Homelessness:** The May Revise maintains homeless funding allocations levels proposed in the Governor’s Budget for the following programs:
 - \$400 million for a third round of encampment resolution grants.
 - \$1 billion for a fifth round of Homeless Housing, Assistance, and Prevention (HHAP) grants. The Administration maintains its intent to focus HHAP funds on highest priority needs, especially reducing unsheltered homelessness, and pursue statutory changes to prioritize spending on activities such as encampment resolution, Homekey operating sustainability, and Community Assistance, Recovery, and Empowerment (CARE) Act housing supports.

Related language in the May Revise states that the Administration is continuing to engage the Legislature in discussions about enhancing local accountability around homeless services and enhancing regional coordination on homelessness strategies.

- **Controversial Funding Swap:** The May Revise proposes a funding swap that may be controversial with counties. It proposes to shift \$500 million one-time from the Mental Health Services Fund (funds which are allocated to counties from Prop. 63 for mental health services) in 2023-24, in lieu of a General Fund allocation, to the Behavioral Health Bridge Housing Program. This program is managed by the Department of Health Care Services (DHCS), and offers support to homeless individuals through various “bridge” housing settings, including tiny homes, interim housing, rental assistance models, and assisted living settings. When questioned about this proposal by the press, the Governor offered a series of arguments supporting the use of these mental health funds for housing, including stating “housing is foundational...look what’s happening on the streets, look at the crisis...I have zero interest in the status quo ante....” He further noted “change is uncomfortable, and change has its enemies...we are not interested in failing more efficiently any longer.”
- **Housing Funding: January Reductions and Deferrals:** In January, the Governor proposed various reductions to previously approved housing funding totaling \$600 million. These reductions are subject to potential restoration based upon a 2024 budgetary trigger as follows:
 - \$200 million (out of a total of \$500 million) approved for the Dream for All homeownership assistance program for FY 23-24 at the California Housing Finance Agency.
 - \$100 million (out of a total of \$350 million) allocated in the FY 2022-23 Budget to the CalHome program, which provides local agencies and nonprofits grants to assist low- and very-low-income first-time homebuyers with housing assistance, counseling, and technical assistance.
 - \$50 million allocated to the California Housing Finance Agency for an Accessory Dwelling Unit program.



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- \$250 million to seismically retrofit “soft story” multifamily housing, where the first floor of the structure, due to garages and other features, is vulnerable to collapse.
- **Housing Funding: May Reductions and Deferrals:** In the May Revise, the Governor proposed the following additional deferral and reductions:
 - Defer \$345 million, out of an original \$500 million included in the 2021 Budget Act, for the Foreclosure Intervention Housing Prevention Program, which provides funds to various non-profit organizations to acquire foreclosed property and operate as affordable housing. The May Revise proposed to defer the allocation of these funds over four fiscal years: \$50 million in 2023-24, \$100 million in 2024-25, \$100 million in 2025-26, and \$95 million in 2026-27.
 - Reduce \$17.5 million in unexpended funding from a \$25 million allocation in the 2000 Budget Act for the Downtown Rebound Program, which provides funding for adaptive reuse of commercial and industrial structures to residential housing.
- **LAO Overview on Housing and Homeless Funding:** For a recap on all housing and homeless related funding allocated by the state in recent years, including the housing and homeless funding proposed in the Governor's January Budget, see this recent summary prepared by the Office of Legislative Analyst:
<https://www.lao.ca.gov/handouts/socservices/2023/State-Housing-Spending-022823.pdf>

Next Steps: Now that the May Revise has been released, legislative deliberations will accelerate. The Constitutional deadline for the Legislature to send the Governor a budget is June 15, which the Governor must sign by July 1. Debates over cuts will be more challenging than dispersing enormous surpluses. As mentioned at the outset, the LAO has opined that the May Revise underestimates the budget problem by \$6.2 billion, and the Governor has rejected Legislative proposals to increase various taxes or heavily tap state reserves. Many uncertainties also exist with state revenues, which will not be fully known until October when filers from disaster-impacted counties submit their returns. Local agencies should expect additional adjustments during FY 23-24 to whatever initial budget the Governor signs in July. CALED will monitor developments and update members as necessary.

CONTACT:

The California Association for Local Economic Development (CALED) is the voice of economic development practitioners and stakeholders in California. With over 800 members, CALED is one of the largest economic development associations in the country. We believe that through partnership and collaboration with local economic developers, the state of California can leverage the energy of California's economic development network to create positive impacts that benefit our businesses and residents while growing the economy.

<http://caled.org> or (916) 448-8252