Summary of the 2024-25 State Budget

Over the weekend, the governor and Legislature reached a final agreement on the 2024-25 state budget. The agreement resolves the major differences between the branches of government. Numerous budget bills will be acted on by the Legislature and signed by the governor this week to ensure the spending plan is in place by July 1. Either Senate Bill (SB) or Assembly Bill (AB) 108 will be passed to incorporate final changes to the budget. SB or AB 159 will enact budget-related statutory changes to health care programs. As is typical, certain decisions and budget-related legislation will likely follow in July and August. This weekend's agreement resolves most of the major health care-related issues relevant to hospitals and health systems.

Big Budget Problem Addressed Through a Mix of Solutions. The state had a $28 billion budget shortfall to solve this year after accounting for actions taken earlier in the year to address $17 billion of the shortfall. In addition, state policymakers projected a $30 billion deficit the following year (2025-26). State revenues for the state's main operating account — the General Fund — are around $200 billion per year, meaning that major, difficult actions were needed to solve the record-setting deficit. The budget agreement addresses the upcoming year's budget problem with a mix of:

- Spending reductions - $16 billion
- Increased revenues - $13.6 billion
- Drawdown of reserves - $6 billion
- Other solutions - $11.2 billion

The budget also aims to solve the following year's budget deficit, resulting in balanced budgets for both 2024-25 and 2025-26. Should projections of state revenues and expenditures hold, this would prevent the state from having to make a new round of spending cuts or revenue increases in next year's budget.

Increases Corporation Taxes Through the Suspension of Major Deduction and Credit - The budget suspends the net operating loss deduction and limits business tax credits to $5 million for the tax years 2024, 2025, and 2026, which is expected to increase state revenues between $10 billion and $20 billion over the next few years. This will affect many different types of businesses, including investor-owned hospitals. Implementation of these changes will begin and end one year earlier than the governor had previously proposed.

Backtracks on Last Year's Budget Agreement on the Managed Care Organization (MCO) Assessment - The governor and Legislature entered final budget negotiations in different places on the MCO assessment, with the governor having proposed a full elimination of future Medi-Cal provider reimbursement increases and the Legislature opting instead to delay them one year, from 2025 to 2026. The final agreement carves a new path and marks a retreat from the funding priorities agreed to last year:

- **Slows Implementation of Reimbursement Increases** - Rather than providing $2.6 billion in reimbursement increases starting in 2025 (accounting for state, but not matching federal Medicaid funds), the approved budget dedicates $133 million for this purpose in 2024-25, $728 million in 2025-26, and $1.2 billion in 2026-27.

- **Substantially Changes Which Providers Will Benefit** - Rather than funding the priorities agreed to last year, a new mix of providers and services would receive funding increases from the MCO assessment. For 2025, these include:
    - Abortion and family planning services
    - Emergency department physicians
    - Ground emergency transportation
    - Air ambulance
    - Community-based adult services
    - Community health workers
    - Congregate living health facilities
    - Pediatric day health centers

  Reimbursement increases would be extended to the following providers and services the following year (2026):
    - Primary care and specialist office visits, preventative services, and care management
    - Obstetric services
    - Non-specialty mental health
    - Vaccine administration
    - Optometry services
    - Federally qualified health centers and rural health clinics
    - Private duty nursing
    - Non-emergency medical transportation
    - Other evaluation and management services and procedures
- **Supports Additional Augmentations** - Starting in 2026, the agreement also provides funding to establish continuous Medi-Cal eligibility for children ages 0-5 and allocates $40 million for a workforce pool supporting labor management committees.
- **Makes MCO Assessment Spending Plan Inoperable If MCO Assessment Ballot Measure Is Approved by Voters** - The budget recognizes that in November voters will decide whether to approve a ballot measure that would direct MCO assessment dollars to be directed in ways that differ from the approved 2024-25 budget. To avoid these differences, statutory changes approved alongside the budget will make this new spending plan inoperable if the MCO assessment ballot initiative is approved this fall.
- **Approves Increase in the MCO Assessment** - In May, the governor proposed to increase the MCO assessment to bring in roughly $3 billion more in revenue over the next three years, and in addition to the "early action" MCO assessment increase enacted in March via SB 136. The final budget agreement agrees with this further increase and is included in separate budget-related legislation (AB/SB 160). Both changes will require federal approval and are not expected to substantially affect how much Californians pay in insurance premiums.

Health Care Minimum Wage (SB 525) Delay and Trigger - SB 525, signed by Gov. Newsom last year, required wage increases as early as June 1, 2024, and will reach a $25 minimum in 2026, 2027, or 2028 for the majority of California health care workers. The schedule for reaching the $25 minimum hourly wage depends on employer size and other characteristics. For example, the $25 minimum wage is required by July 2026 for large health systems with 10,000 full-time equivalent

employees or more, and not until 2033 for hospitals in rural areas and those predominantly providing care to Medi-Cal and Medicare patients.

SB 828, signed into law last month, delayed the minimum wage increases by one month from June 1 to July 1, in order to align with the state fiscal year. However, the budget agreement announced over the weekend further delays the effective date until one of two conditions are met or 12 months, whichever comes sooner. The two conditions that could "trigger" on the required SB 525 increases before July 1, 2025, include:

1) State cash receipts between July 1 and Sept. 30, 2024, exceed 3 percent greater than the total General Fund revenue projected at the time of the Budget Act (in which case the minimum wage requirements would start on Oct. 15, 2024); or

2) The Department of Health Care Services notifies the Legislature that it has initiated the data retrieval necessary to implement an increase to hospital fee program revenues in the upcoming program period effective Jan. 1, 2025, upon approval from the federal government (in which case the minimum wage requirements would start 15 days from the Department's notification to the Legislature or Jan. 1, 2025, whichever date is earlier).

Data retrieval for the hospital fee program is expected to be initiated in October. This means that, based on the budget agreement, it is likely that the health care minimum wage requirements under SB 525 will be "triggered" back on in the last quarter of this year.

The language included in the trigger does not make any reference to the content or parameters of the next hospital fee program, beyond contemplating an unspecified increase in hospital fee revenues and the resultant supplemental payments to hospitals. However, the language does indicate that the next fee program "will provide significant new revenues to hospitals." All of the work to develop the new fee program will take place as usual in negotiations with the state and federal government over the coming year.

Other Actions Affecting Health Care Programs - The budget includes various other changes to health care programs, largely as solutions to reduce the deficit. Funding for core programs (eligibility, benefits, and reimbursement) is generally maintained. Major actions include:

- **Creates New Directed Payment Program for Children's Hospitals** - The budget provides $115 million General Fund ($230 million total funding including federal Medicaid funds) annually on an ongoing basis to create a new directed payment program that will increase Medi-Cal reimbursement for children's hospitals. Budget-related statutory language allows the state to reduce this funding by the amount children's hospitals receive under the MCO assessment ballot measure (if approved by voters), but not by more than $75 million (inclusive of federal funds).
- **Establishes New Fee on Public Hospital Directed Payment Programs** - The budget creates a new fee on intergovernmental transfers made by public hospitals that participate in the Enhanced Payment Program and Quality Incentive pool. The fee is expected to raise $111 million.
- **Eliminates Behavioral Health Funding** - The budget eliminates over $1 billion in funding previously committed to the Children and Youth Behavioral Health Initiative and the

Behavioral Health Bridge Housing Program. The budget additionally reverts funding for the Behavioral Health Continuum Infrastructure Program, but this is expected to be restored with funding from Proposition 1 (2024), the Behavioral Health Service program and Bond Measure, that voters approved in March of this year.

- **Reduces Health Care Workforce Funding but Protects Existing Awards** - The budget eliminates $746 million previously dedicated to health care workforce development programs at the Department of Health Care Access and Information. However, in contrast with the governor's May budget proposal, the final budget includes $109 million to protect existing awards in the Song-Brown Program, the Health Professionals Career Opportunity Program, and the California Medicine Scholars Program.
- **Eliminates Equity and Practice Transformation Payments** - The budget eliminates remaining funding for the program, saving the state $111 million.

Defers Action on Hospital Bed Capacity - Earlier this month, the Administration released proposed statutory changes directing the state to develop a hospital capacity data solution to collect, aggregate, and display information about the availability of beds in, at minimum, general acute care hospitals, emergency departments, and behavioral health facilities. This language was not included in SB or AB 159. If these changes are to move forward, they will be included in future legislation, potentially as part of budget-related bills acted upon later this year.