

Revised Budget Proposal Trims Health Care Spending to Address Multibillion Dollar Deficit

Last week, Gov. Newsom unveiled a revised state budget proposal, which spans 2024-25 and starts on July 1. The budget now heads to the Legislature, which has until June 15 to adopt a balanced spending plan.

State Has a Big Budget Problem. The budget deficit has swollen to \$45 billion due to revenues coming in lower than anticipated earlier in the year. To put this into perspective, the deficit is more than 20% of what the state brings in annually in general purpose revenues. What's more, the shortfall is projected to persist over the next several years unless the structural problem is addressed. This spring, the Legislature took early action to address \$17 billion of the shortfall — leaving more than \$27 billion in expenditure cuts or new revenue needed to balance the budget, as required under the state constitution.

A Mix of Proposals to Solve the Deficit. The revised budget proposal has over 200 distinct approaches to address the budget shortfall in 2024-25 and beyond, including:

- Reductions in spending – \$24 billion
- Use of reserves – \$13 billion (spread out over the next two years)
- New revenues and borrowing – \$9 billion
- Shifting funding away from general purpose revenues – \$4.6 billion
- Spending delays – \$1.9 billion

Spending reductions largely pull back new commitments made in recent years when the state had record surpluses. Rather than focusing exclusively on the current budget window (through 2024-25), the revised proposal seeks to balance next year's (2025-26) budget as well.

Health Programs Face Reductions of Roughly \$10 Billion. The May budget proposal includes major reductions to health care programs, generally related to recent *augmentations* — rather than cuts to *current* service levels — in programs such as Medi-Cal eligibility, benefit levels, or provider rates. Proposed changes include:

- **Diversion of Managed Care Organization (MCO) Tax Funding Dedicated to Providers.** The budget proposal redirects the MCO tax funding previously committed to Medi-Cal provider payment increases beginning in 2025. This saves the state \$879 million in 2024-25 and \$2.4 billion annually thereafter. If approved, it would eliminate almost \$1.5 billion in new annual funding for hospitals (including federal matching dollars).
- **MCO Tax Increase.** The May revision proposes to further increase the MCO tax and use the new funds to address the deficit, creating additional revenue of \$690 million in 2024-25, \$950 million in 2025-26, and \$1.3 billion in 2026-27. (This is on top of the MCO tax increase already enacted this year by state lawmakers and pending federal approval.) The proposed increase is based on a recalculation of the amount of federal matching revenues that are allowable under federal rules.

- **Behavioral Health Funding Cuts.** The May revision eliminates \$1.2 billion dedicated to behavioral health infrastructure programs over the next several years. These reductions are fairly evenly split between the following programs:
 - Children and Youth Behavioral Health Initiative, which aims to improve access to behavioral health services for young Californians
 - The Behavioral Health Continuum Infrastructure Program, which provides grants to hospitals and other providers to expand service capacity
 - The Behavioral Health Bridge Housing Program, which provides resources to house individuals with behavioral health needs who are homeless or at risk of homelessness obtain and retain housing

Previously, some of this funding had been proposed for delay rather than elimination. Funding from Proposition 1, the Behavioral Health Services Program and Bond Measure, approved by voters in March, is expected to backfill a portion of this eliminated funding.

- **Health Care Workforce Reductions.** The proposal eliminates \$639 million previously dedicated to health care workforce development programs. The cuts will affect programs geared toward community health workers, nurses, social workers, primary care residents, and others. Previously, much of this funding had been proposed for delay rather than elimination.
- **New Fee on Public Hospital Directed Payment Programs.** The revised budget proposes a new state fee on two directed payment programs, the Enhanced Payment Program and the Quality Incentive Pool, that certain public hospitals participate in and self-finance. Funds raised by the fee, which would be assessed on moneys put up by public hospitals that draw down federal Medicaid funding, are expected to save the state \$37 million in 2024-25 and \$74 million in 2025-26.
- **Equity and Practice Transformation Payments.** The May revision proposes to eliminate \$280 million for quality, equity, and primary care infrastructure payments — leaving only \$70 million remaining in this program.

Health Care Worker Minimum Wage Changes Expected. During a press conference on the revised budget proposal, Gov. Newsom committed statutory changes to the health care minimum wage law (SB 525) within the next few weeks. This is likely to include technical changes, such as clarifying which entities are subject to the law, and could add a “trigger” that would pause future minimum wage increases depending on state fiscal conditions. While the June 2024 minimum wage increase is likely to take effect (potentially with a one-month delay), further delays likely would not occur until 2025.