

DOLLARS & DEMOCRACY:
A GUIDE TO THE

STATE BUDGET PROCESS

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Independent Analysis. Shared Prosperity.

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TABLE OF CONTENTS

04

Key Facts About California's State Budget

13

Terms and Definitions

15

The Constitutional Framework

25

What Do the Governor and the Legislature Do?

26

What Happens When?

30

Key Takeaways

32

Additional Resources

INTRODUCTION

Every year, California's governor and Legislature adopt a state budget that provides a framework and funding for critical public services and systems — from child care and health care to housing and transportation to colleges and K-12 schools.

But the state budget is about more than dollars and cents.

The budget expresses our values as well as our priorities for Californians and as a state. At its best, the budget should reflect our collective efforts to expand economic opportunities, promote well-being, and improve the lives of Californians who are denied the chance to share in our state's wealth and who deserve the dignity and support to lead thriving lives.

State budget choices have an impact on all Californians. These decisions affect the quality of our schools and health care, the cost of a college education, families' access to affordable child care and housing, the availability of services and financial support to help older adults age in place, and so much more.

Because the state budget touches so many services and our everyday lives, it is critical for Californians to understand and participate in the annual budget process to ensure that state leaders are making the strategic choices needed to allow every Californian — from different races, backgrounds, and places — to thrive and share in our state's economic and social life.

This report sheds light on the state budget and the budget process with the goal of giving Californians the tools they need to effectively engage decision makers and advocate for fair and just policy choices.

KEY FACTS ABOUT CALIFORNIA'S STATE BUDGET

THE STATE BUDGET = STATE FUNDS + FEDERAL FUNDS

Three kinds of state funds account for over half (57.6%) of California's \$455.6 billion budget for 2021-22, the fiscal year that began on July 1, 2021. Specifically:

1

The state **General Fund** accounts for revenues that are not designated for a specific purpose. Most state support for education, health and human services, and state prisons comes from the General Fund.

2

Over 500 state **special funds** account for taxes, fees, and licenses that are designated for a specific purpose.

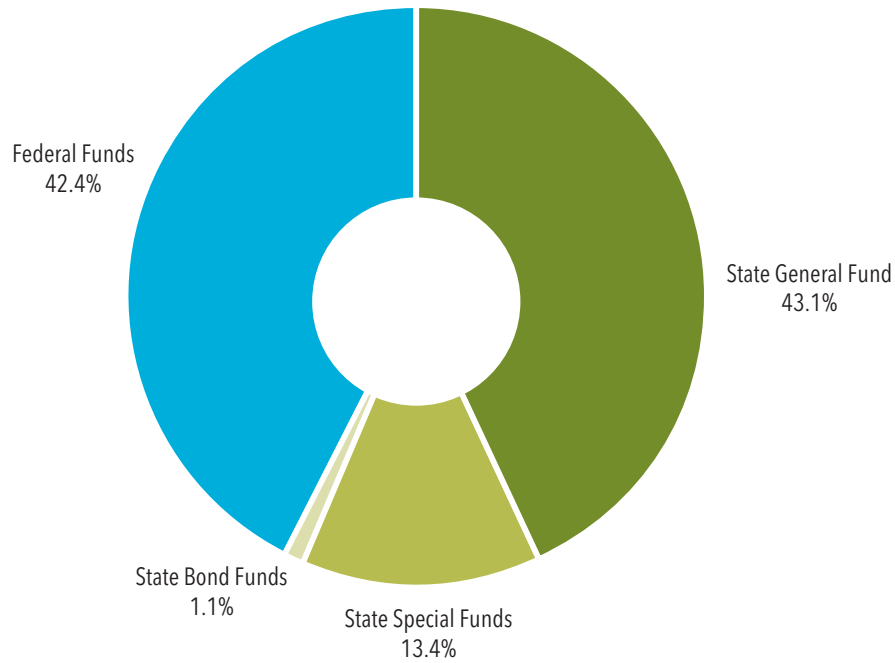
3

State **bond funds** account for the receipt and disbursement of general obligation (GO) bond proceeds.

Federal funds comprise the rest (42.4%) of the state's 2021-22 budget.

State General Fund Dollars and Federal Dollars Make Up Nearly Equal Shares of California's State Budget in 2021-22

Total Enacted 2021-22 Expenditures = \$455.6 Billion



Source: Department of Finance

THE STATE BUDGET IS A LOCAL BUDGET

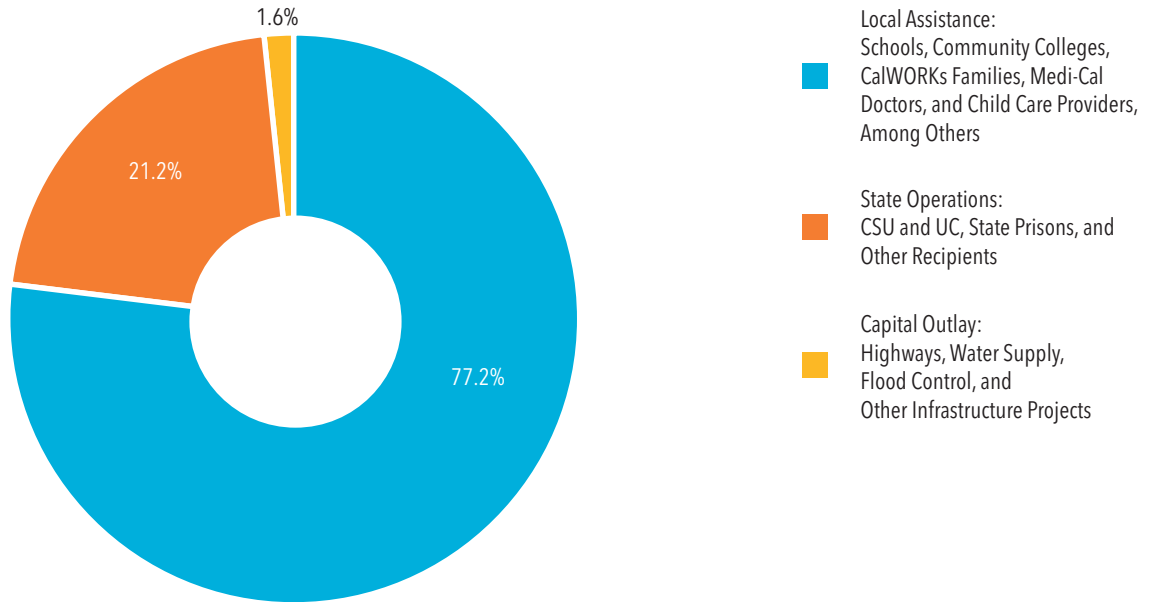


Dollars spent through the state budget go to individuals, communities, and institutions across California. Under the enacted 2021-22 state budget:

- More than three-quarters of total spending flows as “local assistance” to K-12 public schools, community colleges, families enrolled in the CalWORKs welfare-to-work program, and others.
- More than one-fifth of total spending goes to 23 California State University campuses, 10 University of California campuses, 35 state prisons, and other recipients of “state operations” dollars.
- Less than 2% of total spending flows as “capital outlay” dollars, supporting infrastructure projects across California. (Local assistance and state operations dollars also fund infrastructure.)

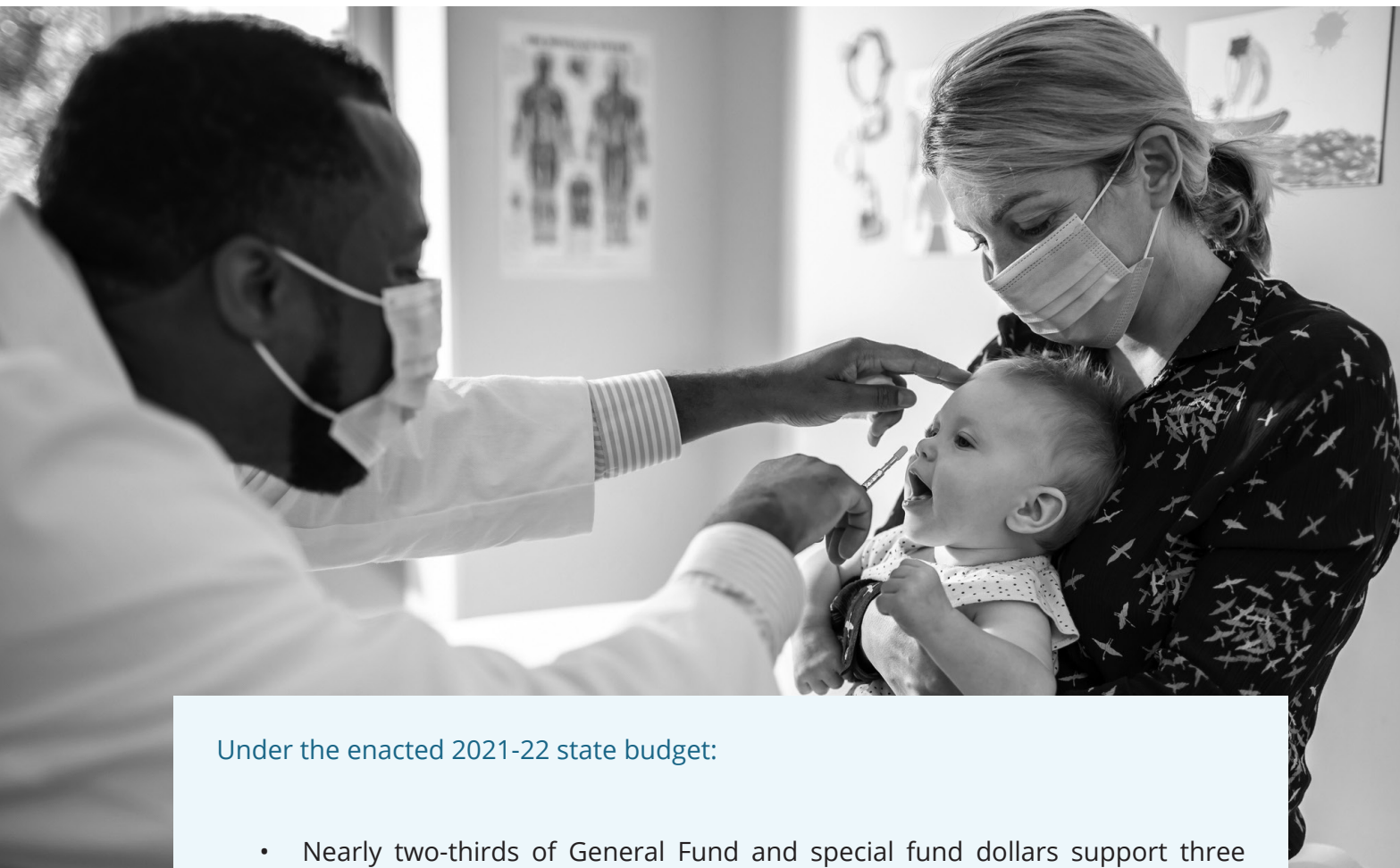
The State Budget Directs Dollars to Communities Across California Through Three Funding Categories

Total Enacted 2021-22 Expenditures = \$455.6 Billion



Note: Reflects federal funds as well as state General Fund, special fund, and bond fund dollars.
Source: Department of Finance

STATE FUNDS PRIMARILY SUPPORT HEALTH AND HUMAN SERVICES OR EDUCATION

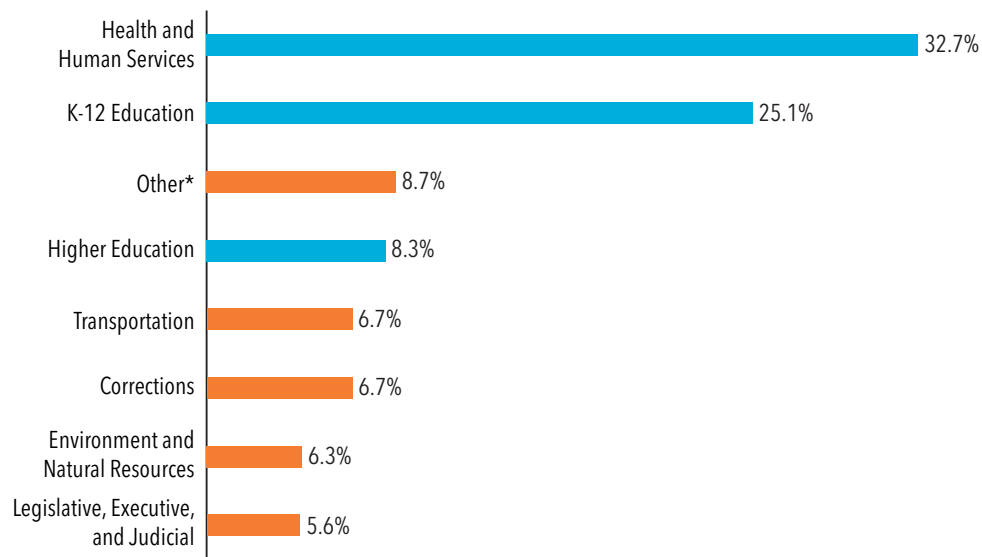


Under the enacted 2021-22 state budget:

- Nearly two-thirds of General Fund and special fund dollars support three categories of spending: health and human services (32.7%), K-12 education (25.1%), and higher education (8.3%).
- Less than 7% of General Fund and special fund dollars support corrections, primarily the state prison system.
- The balance of these dollars support other essential services (such as transportation and environmental protection) and institutions (such as the state's court system).

Nearly Two-Thirds of State Dollars Support Health and Human Services, K-12 Education, or Higher Education

Enacted 2021-22 General Fund and Special Fund Expenditures = \$257.7 Billion



* Reflects a number of budget categories, including Business, Consumer Services, and Housing; Labor and Workforce Development; Government Operations; and General Government. Percentages do not sum to 100 due to rounding.

Source: Department of Finance

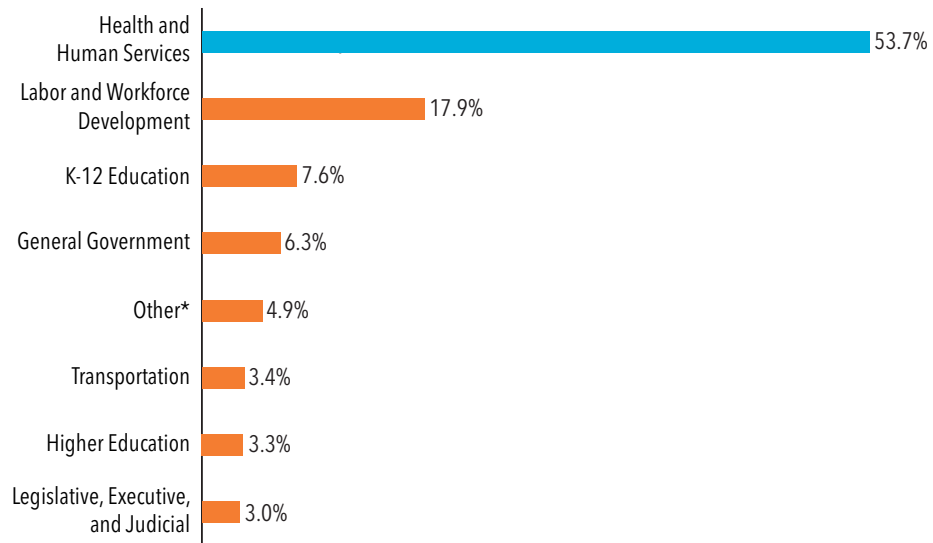
FEDERAL FUNDS PRIMARILY SUPPORT HEALTH AND HUMAN SERVICES

Under the enacted 2021-22 state budget:

- Over half of federal dollars (53.7%) support health and human services programs.
- More than 1 in 6 federal dollars (17.9%) go to labor and workforce development, primarily to fund unemployment insurance benefits for jobless workers.
- Over 7% of federal dollars support K-12 education.
- The balance of federal dollars supports other essential services, including higher education and transportation.

More Than Half of Federal Dollars Spent Through the 2021-22 State Budget Will Support Health and Human Services

Federal Funds Estimated to Be Spent Through the State Budget in 2021-22 = \$193.0 Billion



* Reflects a number of budget categories, including Business, Consumer Services, and Housing; Environmental Protection; Government Operations; and Natural Resources. Percentages do not sum to 100 due to rounding.
Source: Department of Finance

THE STATE BUDGET IS A BILL OF A DIFFERENT KIND

Bills change state law, such as by creating programs, modifying eligibility for services, or raising or lowering taxes.

- Most legislation moves through the Legislature’s policy bill process, which includes review by policy and appropriations committees.

The state budget is a bill. But unlike other bills, the “budget bill”:

- Provides authority to spend money across an array of public services and systems for a single year.
- Moves through the Legislature’s budget committees on its own timeline.
- Moves with other bills that are needed to implement the policies assumed in the budget. These bills are known as “budget-related bills” or “trailer bills.”

TERMS & DEFINITIONS

| | |
|--|---|
| Assembly Budget Committee and Senate Budget & Fiscal Review Committee | Review the governor’s budget proposals and develop each house’s version of the state budget. Most budget committee work is done through subcommittees that focus on specific policy areas. |
| Budget Act | The initial budget bill passed by the Legislature and signed into law by the governor, after any line-item vetoes. The Budget Act can be referred to by the year in which it becomes law (“Budget Act of 2021”) or by the fiscal year to which it applies (“2021-22 Budget Act”). |
| Budget Bill Jr. | The informal term to describe any budget bill that amends the Budget Act. Budget Bill Jrs. may be numbered sequentially using Roman numerals (e.g., Budget Bill Jr. I, Budget Bill Jr. II, etc.). |
| Budget-Related Bills (“Trailer Bills”) | Generally make changes to state law related to the budget bill. Trailer bills typically move in tandem with the budget bill through the Assembly and Senate budget committees. Trailer bills also may move independently of the budget bill — such as through the Legislature’s policy bill process — and still be considered part of the overall “budget package.” |
| Department of Finance (DOF) | Leads the development of the governor’s budget proposals, prepares the governor’s budget documents, testifies on behalf of the governor at legislative budget hearings, develops the governor’s economic forecasts, and performs several other functions. The DOF’s director is the governor’s chief fiscal adviser. |

| | |
|--|---|
| <p>Governor’s Budget Summary</p> | <p>Provides the governor’s economic and revenue outlook, highlights major policy initiatives in the governor’s proposed budget, and summarizes proposed state expenditures. The budget summary is released on or before January 10.</p> |
| <p>Governor’s Proposed Budget</p> | <p>Provides a detailed overview of the governor’s proposed expenditures for the upcoming fiscal year, estimated expenditures for the current fiscal year, and actual expenditures for the prior fiscal year. The proposed budget is released on or before January 10.</p> |
| <p>Legislative Analyst’s Office (LAO)</p> | <p>An independent, nonpartisan office that conducts research and analysis on state budget issues, analyzes statewide ballot measures, and provides fiscal and policy advice to the Legislature. The LAO is overseen by the Legislature’s bipartisan Joint Legislative Budget Committee.</p> |
| <p>Line-Item Veto</p> | <p>The governor’s power to reduce or eliminate specific items of appropriation while approving other portions of a bill. This power applies to any bill that contains an appropriation, including budget bills and budget-related bills. The Legislature may override a line-item veto with a two-thirds vote of each house.</p> |
| <p>May Revision</p> | <p>Released on or before May 14, the May Revision updates the governor’s economic and revenue outlook; adjusts the governor’s proposed expenditures to reflect revised estimates and assumptions; revises, supplements, or withdraws policy initiatives that were included in the governor’s proposed budget in January; and outlines adjustments to the Proposition 98 minimum funding guarantee for K-14 education.</p> |

THE CONSTITUTIONAL FRAMEWORK

THE STATE CONSTITUTION ESTABLISHES THE RULES OF THE BUDGET PROCESS

The governor and legislators craft the state's annual spending plan according to rules outlined in the state Constitution.

California voters periodically revise these rules by approving constitutional amendments that appear on the statewide ballot.

- Proposals to amend the state Constitution can be placed on the ballot through a citizens' initiative or by the Legislature.
- A constitutional amendment takes effect if approved by a simple majority of voters.

THREE KEY BUDGET DEADLINES: TWO IN THE STATE CONSTITUTION (JANUARY 10 AND JUNE 15), ONE IN STATE LAW (MAY 14)

1

The governor must propose a budget for the upcoming fiscal year on or before January 10.

- The budget must be balanced: Estimated revenues (as determined by the governor) must meet or exceed the governor's proposed spending.

2

The governor must release the May Revision on or before May 14.

3

The Legislature must pass a budget bill for the upcoming fiscal year by midnight on June 15.

- The budget bill must be balanced: Estimated General Fund revenues (as set forth in the budget bill passed by the Legislature) must meet or exceed General Fund spending.

PROPOSITION 25: SIMPLE MAJORITY VOTE FOR BUDGET BILL AND MOST BUDGET-RELATED BILLS

The budget package generally may be passed by a simple majority vote of each house of the Legislature.

- Prop. 25 of 2010 allows lawmakers to pass, by a simple majority vote, the budget bill as well as certain budget-related bills (“trailer bills”) that may take effect as soon as the governor signs them. Typically, the budget package consists entirely or primarily of such majority-vote bills.
- To qualify as a budget-related bill under Prop. 25, a bill must (1) be listed in the budget bill and (2) contain an appropriation of any amount.
- The budget package may include bills that require a two-thirds vote of each house, such as bills to raise taxes or to place constitutional amendments or general obligation bonds before the voters.

PROPOSITION 25: PENALTIES FOR A LATE BUDGET

Lawmakers face penalties if they fail to pass the budget bill on or before June 15.

- Prop. 25 requires lawmakers to permanently forfeit both their pay and their reimbursement for travel and living expenses for each day after June 15 that the budget bill is not passed and sent to the governor.
- These penalties do not apply to budget-related bills, which do not have to be passed on or before June 15.

PROPOSITION 26: SUPERMAJORITY VOTE FOR TAX INCREASES

Any tax increase requires a two-thirds vote of each house of the Legislature.

- Under the state Constitution, “any change in state statute which results in any taxpayer paying a higher tax” requires a two-thirds vote of each house.
- This standard was imposed by Prop. 26 of 2010. This measure expanded the definition of a tax increase and thus the scope of the two-thirds vote requirement, which was originally imposed by Prop. 13 of 1978.
- Prior to Prop. 26, only bills changing state taxes “for the purpose of increasing revenues” required a two-thirds vote. Bills that increased some taxes but reduced others by an equal or larger amount could be passed by a simple majority vote of each house.

PROPOSITION 26: MORE CHARGES ARE CLASSIFIED AS TAXES

Prop. 26 of 2010 also expanded the definition of a tax to include some fees.

- Prior to Prop. 26, lawmakers could create or increase fees by a simple majority vote. These majority-vote fees included regulatory fees intended to address health, environmental, or other problems caused by various products, such as alcohol, oil, or hazardous materials.
- Prop. 26 reclassified regulatory and certain other fees as taxes. As a result, a two-thirds vote of each house of the Legislature is now required for many charges that previously were considered fees and could be passed by a simple majority vote.

ADDITIONAL SUPERMAJORITY VOTE REQUIREMENTS

The state Constitution requires a two-thirds vote of each house of the Legislature in order to:

- Appropriate money from the General Fund, except for appropriations that are for public schools or that are included in the budget bill or in budget-related bills that meet the requirements of Prop. 25.
- Pass bills that take effect immediately (urgency statutes), except for the budget bill and Prop. 25 budget-related bills.
- Place constitutional amendments or general obligation bond measures before the voters.
- Override the governor's veto of a bill or an item of appropriation.

A BILL MUST BE PUBLISHED FOR AT LEAST 72 HOURS BEFORE THE LEGISLATURE CAN ACT ON IT

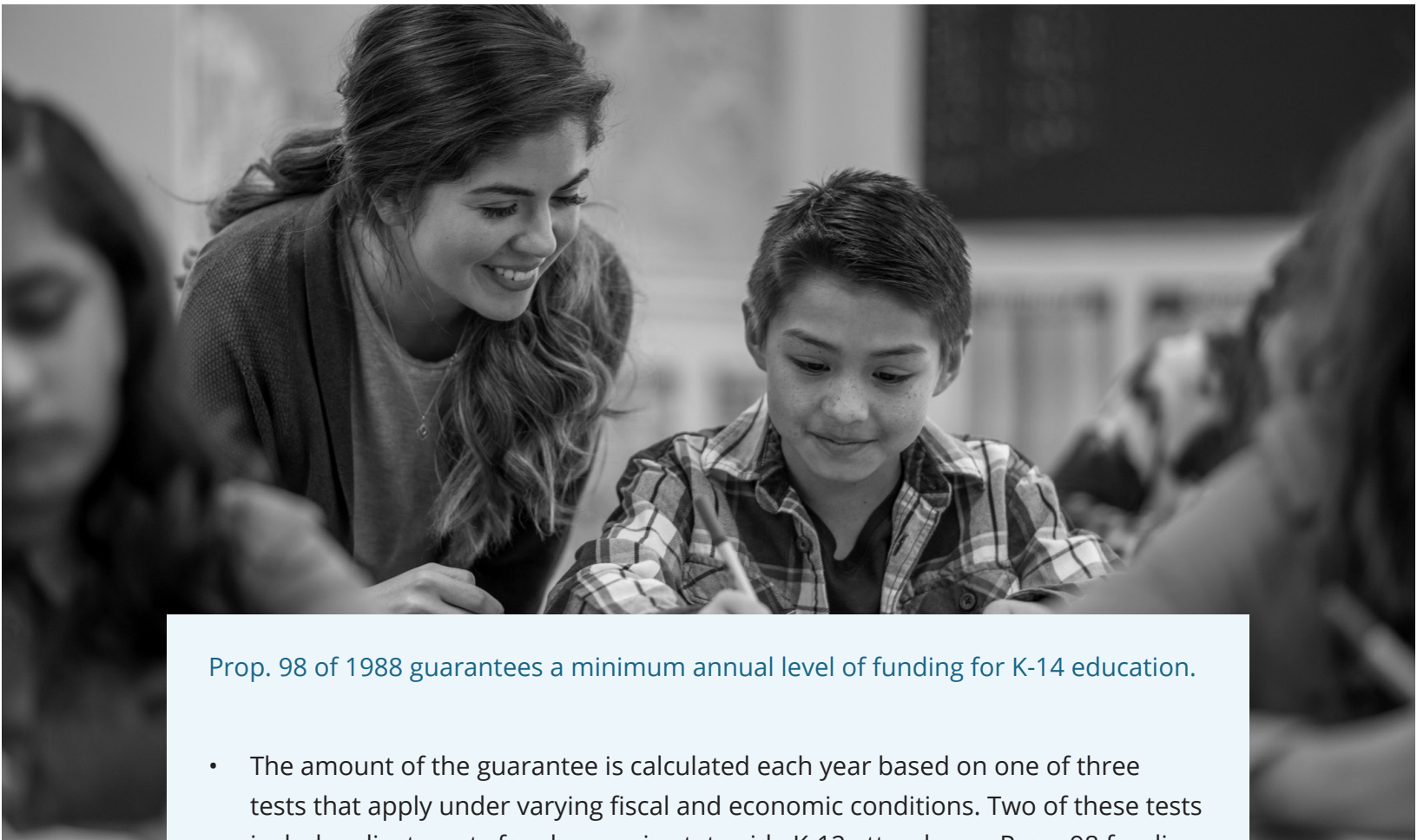
Proposition 54 of 2016 requires bills to be distributed to legislators and published on the Internet, in their final form, at least 72 hours before being passed by the Legislature.

This rule applies to all bills, including the budget bill and other legislation included in the budget package.

This mandatory review period can be waived for a bill if:

- The governor declares an emergency in response to a disaster or extreme peril, *and*
- Two-thirds of legislators in the house considering the bill vote to waive the review period.

PROPOSITION 98: A FUNDING GUARANTEE FOR K-12 SCHOOLS AND COMMUNITY COLLEGES



Prop. 98 of 1988 guarantees a minimum annual level of funding for K-14 education.

- The amount of the guarantee is calculated each year based on one of three tests that apply under varying fiscal and economic conditions. Two of these tests include adjustments for changes in statewide K-12 attendance. Prop. 98 funding comes from the state General Fund and local property tax revenues.
- The Legislature can suspend the guarantee for a single year by a two-thirds vote of each house and provide less funding. Following a suspension, the state must increase Prop. 98 funding over time to the level that it would have reached absent the suspension.
- While the Legislature can provide more funding than Prop. 98 requires, the guarantee has generally served as a maximum funding level.

PROPOSITION 2: SAVING FOR A RAINY DAY, PAYING DOWN DEBT

Prop. 2 of 2014 revised the rules that apply to the Budget Stabilization Account (BSA) — the state’s constitutional rainy day fund — and also established a new requirement to pay down state budgetary debt.

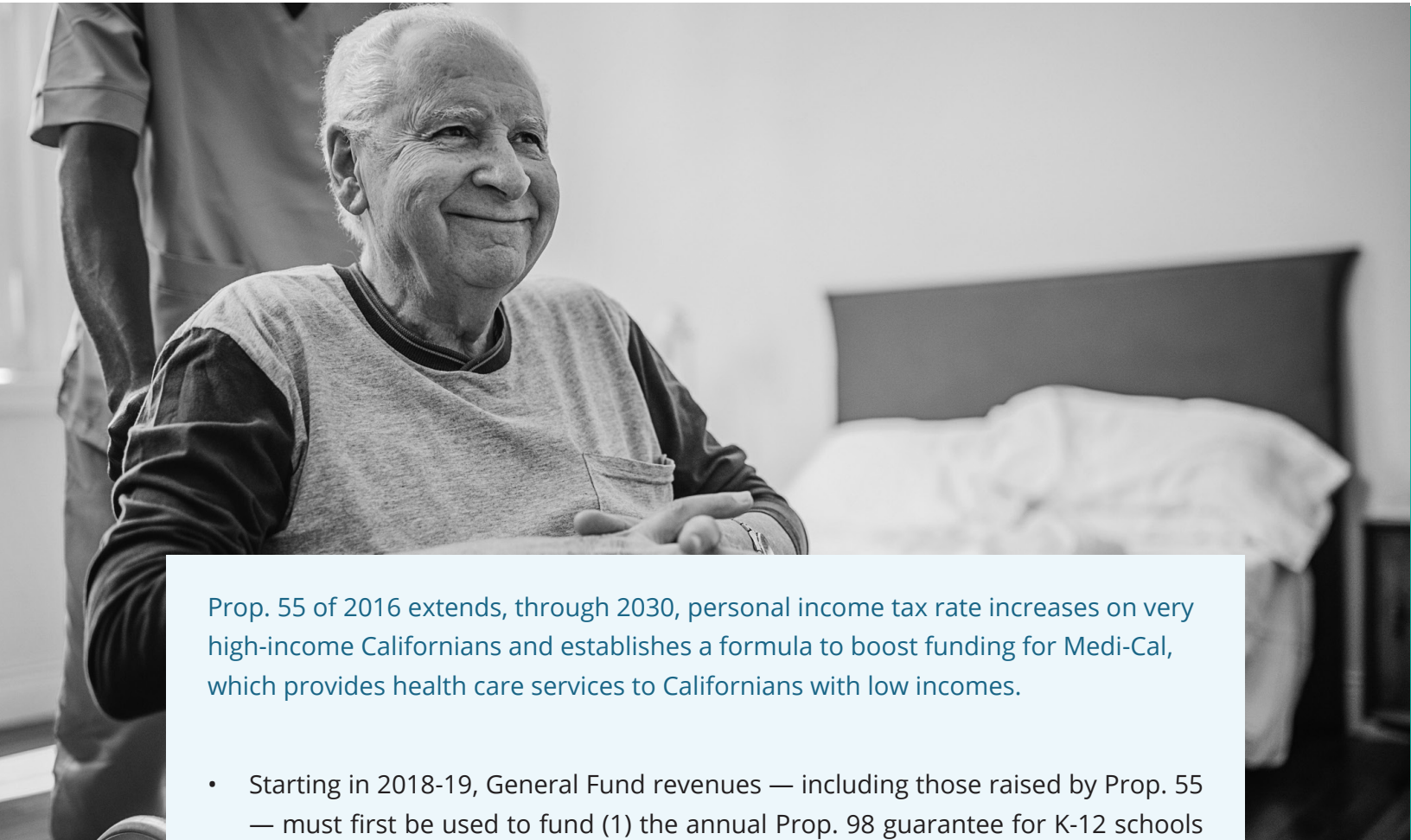
- The state is required to set aside 1.5% of General Fund revenues each year, plus additional dollars in years when tax revenues from capital gains are particularly strong.
- Until 2029-30, half of the revenues go into the BSA and the other half must be used to pay down state budgetary debt, which includes unfunded pension liabilities. Starting in 2030-31, the entire annual transfer goes into the BSA.
- State policymakers may suspend or reduce the BSA deposit and withdraw funds from the reserve, but only under limited circumstances that qualify as a “budget emergency.”

PROPOSITION 2: A BUDGET RESERVE FOR K-14 EDUCATION

Prop. 2 of 2014 also created a state budget reserve for K-12 schools and community colleges called the Public School System Stabilization Account (PSSSA).

- Deposits come from state capital gains tax revenues in years when those revenues are particularly strong.
- However, various conditions must be met before these dollars could be transferred to the PSSSA. For example, transfers could occur only in so-called “Test 1” years under Prop. 98, which have been rare.

PROPOSITION 55: POTENTIAL NEW FUNDING FOR MEDI-CAL FROM A TAX ON THE WEALTHIEST CALIFORNIANS



Prop. 55 of 2016 extends, through 2030, personal income tax rate increases on very high-income Californians and establishes a formula to boost funding for Medi-Cal, which provides health care services to Californians with low incomes.

- Starting in 2018-19, General Fund revenues — including those raised by Prop. 55 — must first be used to fund (1) the annual Prop. 98 guarantee for K-12 schools and community colleges and (2) the cost of other services that were authorized as of January 1, 2016, as adjusted for population changes, federal mandates, and other factors.
- If any Prop. 55 revenues remain after meeting these required expenditures, Medi-Cal would receive 50% of this excess, up to a maximum of \$2 billion in any fiscal year.
- Prop. 55 has not yet resulted in any additional funding for Medi-Cal.

STATE APPROPRIATIONS LIMIT (SAL): A CAP ON SPENDING

Appropriations are subject to a limit established by Prop. 4 of 1979, as modified by later initiatives. This spending cap is often called the Gann Limit.

- The SAL limits the amount of state tax proceeds that can be appropriated each year. This limit is adjusted annually for changes in population and per capita personal income.
- Some appropriations from tax proceeds do not count toward the limit, including debt service and spending that is needed to comply with court or federal mandates.
- Revenues that exceed the SAL over a two-year period are divided equally between Prop. 98 spending and taxpayer rebates. The state last exceeded the SAL in 2018-19 (but did not do so in the prior year).

STATE MANDATES: PAY FOR THEM OR SUSPEND THEM

The state is required to pay for or suspend mandates that it imposes on local governments.

- Prop. 4 of 1979 requires the state to reimburse local governments for costs related to a new program or a higher level of service that is mandated by the state.
- Prop. 1A of 2004 expanded the definition of a mandate to include the transfer of financial responsibility from the state to local governments.
- Prop. 1A also requires the state to suspend a mandate in any year in which local governments' costs are not fully reimbursed.

WHAT DO THE GOVERNOR AND THE LEGISLATURE DO?

The governor:

- Approves, modifies, or rejects spending proposals prepared by state departments and agencies through an internal process coordinated by the DOF.
- Proposes a spending plan for the state each January, which is introduced as the budget bill in the Legislature.
- Updates and revises the proposed budget each May (the “May Revision”).
- Signs or vetoes the bills included in the budget package.
- Can veto all or part of individual appropriations (line items), but cannot increase any appropriations above the level approved by the Legislature.

The Legislature:

- Approves, modifies, or rejects the governor’s proposals.
- Can add new spending or make other changes that substantially revise the governor’s proposals.
- Needs a simple majority vote of each house to pass the budget bill and Prop. 25 budget-related bills.
- Needs a two-thirds vote to pass certain other bills that may be part of the budget package, such as bills that increase taxes or propose constitutional amendments.
- Needs a two-thirds vote of each house to override the governor’s veto of a bill or an appropriation.

WHAT HAPPENS WHEN?

THE STATE BUDGET TIMELINE

The state budget process is cyclical. Decisions are made throughout the year.

Summer to Fall:

- State departments and agencies develop baseline budgets to maintain existing service levels in the upcoming fiscal year and may prepare “budget change proposals” intended to alter service levels. The DOF reviews these documents.
- Following a series of meetings within the governor’s administration, the governor makes final decisions and the DOF prepares the proposed budget for release in January.
- Independent of the governor, legislative leaders develop their budget priorities for the upcoming fiscal year.

By January 10:

- The governor releases the proposed budget for the upcoming fiscal year.

January to Mid-May:

- Budget committees and their subcommittees hold dozens of hearings to review the governor's proposals and make initial decisions.

Mid-May to June:

- The governor releases the May Revision by May 14.
- Each house of the Legislature then finalizes its version of the budget. A legislative conference committee may meet to resolve differences.

June

- Legislative leaders and the governor meet to address outstanding issues.

June 15

- The constitutional deadline for lawmakers to pass the budget bill. This deadline does not apply to budget-related bills, which can be passed at any time.
 - This deadline does not apply to budget-related bills ("trailer bills"), which can be passed at any time.

July 1

- The new fiscal year begins.
- The governor may sign the budget bill and budget-related bills — as well as issue vetoes — by this date.

July and Beyond:

- The Legislature may pass, by a simple majority vote, amendments that change the spending levels in the adopted budget bill.
- Lawmakers also may pass additional budget-related bills, thus increasing the size and scope of the original budget package.
- State departments and agencies develop baseline budgets and budget change proposals for the following fiscal year and submit them to the DOF, starting the state budget process anew.

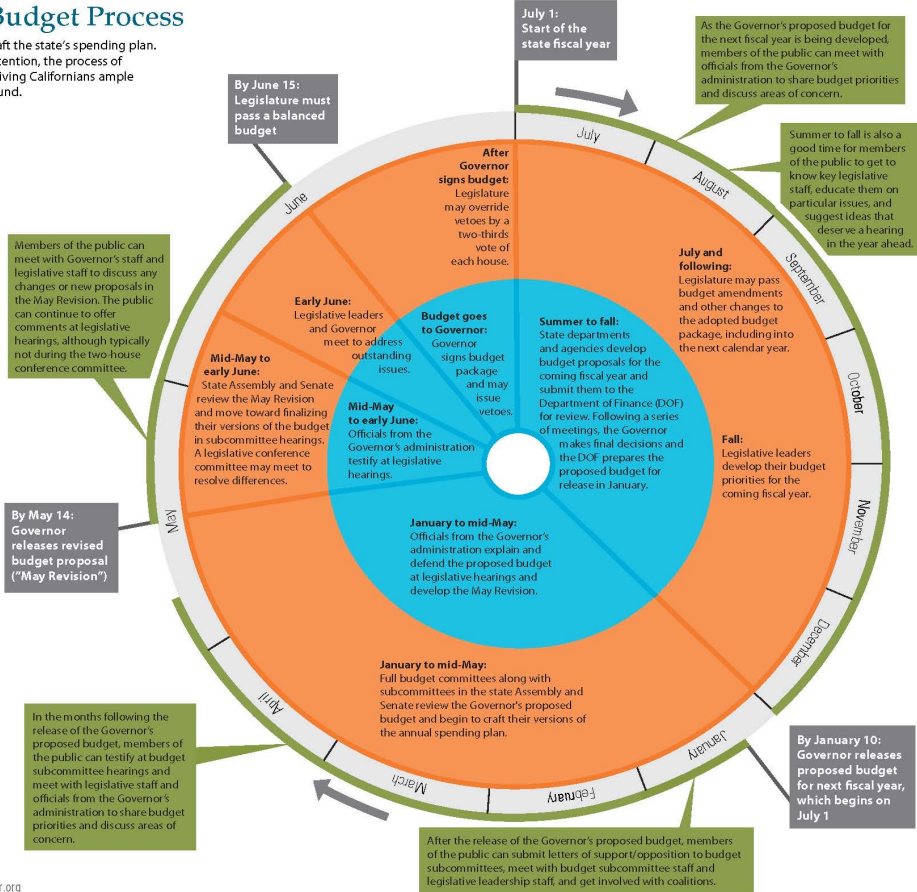
Navigating the State Budget Process

Each year the Governor and Legislature work to craft the state's spending plan. While the January-to-June period gets the most attention, the process of developing the budget is an ongoing enterprise, giving Californians ample opportunity to stay engaged and involved year-round.

The Governor
The Governor has the lead role in developing the state budget. Each year the Governor proposes a spending plan, which is introduced as the budget bill in the Legislature. The Governor can sign or veto the budget bill passed by legislators as well as other bills in the budget package that make policy changes related to the budget. The Governor can also reduce or eliminate individual appropriations using the line-item veto.

The Legislature
The Legislature – made up of the Assembly and Senate – reviews the Governor's proposed budget and crafts its own version of the spending plan. The Legislature can maintain, modify, or reject the Governor's proposals, with review occurring through each house's budget committee and related subcommittees. The Legislature must pass the budget bill, but not other bills in the budget package, by June 15. The Legislature can override a Governor's veto by a two-thirds vote of each house.

The Public
The public has various opportunities for input during the budget process. Members of the public can meet with officials from the Governor's administration and with legislators and their staffs, testify before budget committees and subcommittees, and write letters of support and opposition. Through individual engagement or as part of coalitions, members of the public can express their budget priorities and areas of concern.



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This infographic shows the year-round budget cycle, illustrating key steps in the process as well as the respective roles of the governor and the Legislature and various opportunities for public involvement. The infographic is available here: calbudgetcenter.org/stateprocess.

KEY TAKEAWAYS

THE BOTTOM LINE

1

The state spending plan is about more than dollars and cents.

- Crafting the budget provides an opportunity for Californians to express our values and priorities as a state.

2

The state Constitution establishes the rules of the budget process.

- Among other things, these rules allow lawmakers to approve spending with a simple majority vote, but require a two-thirds vote to increase taxes. Voters periodically revise the budget process by approving constitutional amendments.

3

The governor has the lead role in the budget process.

- Proposing a state budget for the upcoming fiscal year gives the governor the first word in each year's budget deliberations.
- The May Revision gives the governor another opportunity to set the budget and policy agenda for the state.
- Veto power generally gives the governor the last word.

4

The Legislature reviews and revises the governor's proposals.

- Lawmakers can alter the governor's proposals and advance their own initiatives as they craft their version of the budget prior to negotiating an agreement with the governor.

5

Budget decisions are made throughout the year.

- The public has various opportunities for input during the budget process.
- This includes writing letters of support or opposition, testifying at legislative hearings, and meeting with officials from the governor's administration as well as with legislators and their staffs.
- In short, Californians have ample opportunity to stay engaged and involved in the budget process year-round

ADDITIONAL RESOURCES

STATE BUDGET RESOURCES

- **California Budget & Policy Center:** Analyses and commentary, presentations and events, and technical assistance (www.calbudgetcenter.org).
- **Department of Finance:** The governor's budget proposals and related documents (www.dof.ca.gov).
- **Legislative Analyst's Office:** Budget and policy analyses, budget recommendations, and historical budget data (www.lao.ca.gov).
- **Legislative Counsel:** Bills and bill analyses, a free bill-tracking service, the state codes, and the state Constitution (www.leginfo.legislature.ca.gov).
- **State Assembly and Senate:** Committee agendas and other publications, floor session and committee schedules, the annual legislative calendar, and live audio streaming of legislative proceedings (www.assembly.ca.gov and www.senate.ca.gov).

The Budget Center was established in 1995 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The Budget Center engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of Californians with low and middle incomes. General operating support for the Budget Center is provided by foundation grants, subscriptions, and individual contributions. Please visit the Budget Center's website at calbudgetcenter.org.



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