California State Assembly

Agenda

Assembly Budget Subcommittee No. 7
on Accountability and Oversight

Assemblymember Gregg Hart, Chair

Wednesday, April 23, 2025

9:00 AM – State Capitol, Room 126

Items To Be Heard

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Issue 1: Update on Federal Funding in California

The Subcommittee held a hearing on Federal Funds in California on February 10, 2025. At that hearing, the Subcommittee announced the intention to revisit the topic again before the May Revision. This agenda item explores three facets of federal funding.

Background:

Franchise Tax Board

The Franchise Tax Board (FTB) is one of the state's two major tax collection agencies. The FTB's primary responsibility is to administer corporation tax programs and - with the assistance of the Employment Development Department - California's personal income tax. As the steward of the state's largest revenue stream, FTB's operations are critical to our protecting our General Fund. In 2025-26, the state is expected to collect over $133 billion in Personal Income Taxes and $37 billion in corporation taxes.

The Franchise Tax Board income tax filing works in tandem with federal Internal Revenue Services (IRS) filing, as taxpayers with income tax liability to the State will almost certainly to have a federal liability as well.

The Trump Administration has reduced IRS staff, especially for staff in compliance work, such as audits. The administration initially proposed eliminating 7,000 positions, although that reduction was halted by court orders. According to *the New York Times*, approximately 20,000 IRS employees have accepted the "buyout" offer to leave the administration. In addition, the Treasury Department reported to the Office of Personnel Management that it expects to cut half of its enforcement personnel in the coming year. Currently, the IRS prioritizes compliance audits on households and businesses earing above $400,000 annually, a continuation of the Biden-era policy.

Additionally, on April 7, 2025, the IRS and the Bureau of Immigration and Customs Enforcement entered into an agreement to share tax information from undocumented taxpayers for nontax criminal enforcement. This action is expected to reduce the filing of taxes by individuals with individual taxpayer identification numbers (ITINs) for both state and federal income taxes.

University of California

With a portfolio of universities, research labs and facilities, as well as some of California's largest health care groups, the UC system has unique and extensive exposure to uncertainty in federal funds. With over $15.9 billion in federal funds received in 2022-23, UC has been vigilantly at the front lines of engaging and tracking various threats to federal revenues.

Department of Finance Federal Fund Update.

At the February 10 hearing, the Subcommittee asked the Department of Finance (DOF) to report on any update on federal funds. Finance submitted an update to the committee on April 1, which outlined the impact of the March 15, 2025 Continuing Resolution which extended federal funding through September 30, 2025, mostly at the previous level. This Continuing Resolution increased defense spending by $6 billion while decreasing domestic discretionary spending by $13 billion through eliminating congressional Community Direct Funding ("earmarks") and making other smaller shifts in funding between various appropriations. Of this amount, approximately $939.5 million in reductions are expected to impact projects in the State of California.

Panel

- Roger Lackey, Franchise Tax Board
- Katherine Newman, University of California
- Mary Halterman, Department of Finance

Staff Comments

When the Subcommittee first heard this issue in February, there was uncertainty about federal funding stemming both from executive action the Trump Administration could take to halt funds previously appropriated by Congress, and congressional action to change the budget itself to reduce or change federal appropriations going forward. Despite the passage of time, neither of these two threats to California's funding have become much clearer.

The Trump Administration has attempted to halt spending and rescind grant awards of existing funding to programs that directly go to the state or are adjacent to state programs. These include funding for libraries, disaster preparedness, food banks, and public health investments. At this point, courts have intervened to forestall such actions, so the funding remains flowing as the courts consider the federal government's action. However, if the courts do ultimately side with the Trump Administration, the President has stated that funding for schools, disaster relief, universities, transportation, and other programs will be contingent on the state changing various policies, including elections, transgender rights, diversity, immigration, water policy, and climate rules. The courts may decide when and how the Trump Administration can impose new requirements or contingencies on federal appropriations to pursue policy objectives or may leave the state with a tangle of directions that could continue the uncertainty going forward.

Congress clearly has the power to change the terms of appropriation, rescind previously appropriated funds, or eliminate funding for programs. So far, the Congressional budget process has moved forward with a resolution that largely reflects the vision of the Trump Administration, with massive spending cuts, particularly from Medicaid, that would be devastating for the State.

However, the political challenges associated with passing the March Continuing Resolution and subsequent public outcry over proposed spending cuts suggest that Congress may need to compromise to find the support to pass the budget by October 1^{st}.

On the Revenue side, the Trump Administration has not formally adopted a new policy or priorities for the IRS, but reports in the *New York Times* and *the Wall Street Journal* cite reduced corporate tax audits and reduced compliance focus overall from existing staff. In the reporting tax experts express concern that the reductions in IRS staff will diminish the high level of voluntary compliance that American taxpayers typically exhibit.

Staff Recommendation: This item is presented for informational purposes

Issue 2: AB 218 Impacts on Local Governments

This item will explore the challenges local governments face in managing liabilities that arise for the enactment of AB 218 and subsequent legal settlements.

AB 218 (Chapter 861, Statutes of 2019) eliminated many claim prerequisites and increased or effectively eliminated the statute of limitation periods for claims of childhood sexual assault against public entities, including local educational agencies and municipal governments.

AB 218, The Child Victims Act, renamed childhood sexual abuse to childhood sexual assault and expanded its definition. Further, it increased public agencies' liability exposure by doing the following:

1) Extending the statute of limitation periods for claims of childhood sexual assault.
2) Permanently eliminating the Government Tort Claims Act's presentation requirements for claims involving childhood sexual assault.
3) Reviving certain claims for which the statute of limitations period had otherwise expired, if brought by December 31, 2022.

The legislation retroactively increased the time limit for beginning an action to recover damages suffered as a result of childhood sexual assault to 22 years from the date the plaintiff attains the age of majority (i.e., 40 years of age) instead of the previous eight years (i.e., 26 years of age), or within five years of the date the plaintiff discovers or reasonably should have discovered that the psychological injury or illness occurring after the age of majority was caused by sexual assault, whichever is later.

Commonly referred to as a revival statute, the legislation made it possible for victims of childhood sexual assault to seek recovery for damages after the previous statute of limitations had expired. The revival provisions allowed claims for damages to be commenced up to December 31, 2022, for victims over the age of 40. However, victims younger than age 40 before January 1, 2023, or those with repressed memory of the assault, may continue to commence claims up to age 40 or within five years of discovery, as provided. This essentially provides a 14-year window for claims to continue to be filed until victims turn 40 years old and sets no age limit for those who discover psychological injury or illness later.

FCMAT Analysis of the Impact of AB 218

The Financial Crisis and Management Assistance Team (FCMAT) prepared a report to the Legislature on January 31, 2025 outlining the impacts of AB 218 on school districts:

Even with missing details, we can conclude that the fiscal impact is and will continue to be significant and will affect programs and services. The best estimate of the dollar value of claims *brought to date because of AB 218 is $2-$3 billion for local educational agencies. Other local public agencies' costs will exceed that value by a multiplier, with one county government alone estimating their claim value at $3 billion. The dollar estimate increases further for total childhood sexual assault claims when considering claims outside of the time frame covered by AB 218. The fiscal impact is not limited to local educational and public agencies with claims but affects all public agencies, because it includes increased insurance premiums and special assessments based on the joint and several liability of current and past members of public entity risk pools.*

Additionally, FCMAT notes that the impact of AB 218 will also impact insurance coverage for all local governments given the interconnected nature of such policies:

The insurance market for public agencies is perilously unstable. In the worst case, the market could deteriorate to a point where there is not enough insurance available, and public agencies could end up competing with each other for the limited coverage still being offered.

The FCMAT report outlined options that could be considered to assist local educational agencies in managing this liability without having to resort to full insolvency.

Los Angeles County Settlement

On April 4, the County of Los Angeles proposed settling 6,800 claims, dating back to 1959, relating to AB 218 for a total of $4 billion. According to the county, the majority of the claims date from the 1980s, 1990s and 2000s and are alleged to have happened at Probation Department facilities and at the MacLaren Children's Center, which was permanently closed in 2003.

The county intends to seek a judgement bond, in addition to using reserve funds and expenditure reductions to finance the settlements. It foresees repayment of the bond taking until the 2050-51 fiscal year.

Panel

- Michael Fine, FCMAT
- Fesia Davenport, County of Los Angeles

Staff Comments

The impacts of AB 218 were anticipated, but the state and local governments failed to consider options to manage the liability. When AB 218 was passed in 2020, the Assembly Floor analysis did foresee the challenges being faced by local governments. According to fiscal section of that analysis, the bill was expected to have:

Unknown, potentially-major out-year costs to local entities and school districts to the extent litigation is successfully brought outside the current statute of limitations and/or the entities are liable for damages. If payouts are large enough, this measure could lead to cost pressures to the state to stabilize a local jurisdiction or district. Additionally, to the extent an extended statute of limitations affects liability insurance premiums, school district could experience unknown, potentially-significant costs related to procuring liability insurance, apart from any specific claims. (Local funds)

The Subcommittee may wish to consider if there are options the state can put forward to help local governments manage and repay the expected liabilities in a manner that also works for victims. In addition, the Subcommittee may wish to explore the possibility of widespread local government bankruptcies or insolvencies due to these liabilities stacking on top of other challenges faced by local governments.

The Subcommittee may also wish to ask both panelists to provide context of other fiscal challenges and liabilities faced by local governments, and to help articulate how the additional AB 218 liability will impact future decisions and investments.

Staff Recommendation: This item is presented for informational purposes.