

LEGISLATIVE UPDATE



Week of January 5, 2026

State Issues

2026-2027 State Budget Proposal Released

Overview. In a press conference today held by Department of Finance Director, Joe Stephenshaw – and not the Governor – the Administration outlined their proposal for the 2026-2027 State Budget. You can access the budget summary document [here](#). The budget reflects \$348.9 billion total spending, with \$248.2 billion in general fund expenditure. It includes \$23 billion in total reserves. The Director noted that the state is submitting at this time a “workload” budget, which is a bit of a placeholder document, while they wait for more information on revenues and spending.

The budget includes no significant budget or policy proposals at this time. It simply reflects mandatory spending requirements and sets the stage for changes in health care directed by changes in federal policies. They intend to present a more comprehensive plan for the May Revise. While the Governor projects small deficit in 2026-2027 of \$2.9 billion, the Legislative Analyst predicts a deficit of nearly \$18 billion. The differences in these two figures will be debated during the course of the year. The Budget forecasts an estimated \$22 billion deficit in the 2027-28 fiscal year and shortfalls in the two years following.

During the press conference, Director Stephenshaw noted that the Governor is focused on protecting more vulnerable populations in the state, on keeping funding in individual’s pockets and fully supporting most programs that residents rely upon. You can find the brief statement from the Assembly Speaker and Budget Committee Chair [here](#).

Health Care Spending. Medi-Cal is the largest single program in the state budget in terms of total funds. As the State deals with how to address the deficit, the Medi-Cal program will be scrutinized and adjustments should be expected. After a decade of significant expansion of California’s Medi-Cal program, the State now faces a new fiscal and policy landscape that it must contend with. Medi-Cal costs have continued to rise, as factors like California’s fiscal situation have tightened and new federal policy will significantly cut federal funding for the program.

2025-26 Budget. The Medi-Cal budget includes \$196.7 billion (\$46.4 billion General Fund) in 2025-26 and \$222.4 billion (\$48.8 billion General Fund) in 2026-27. Medi-Cal is projected to cover approximately 14.5 million members in 2025-26 and 14 million members in 2026-27—more than one-third of the state’s population.

It includes increased Medi-Cal expenditures of approximately \$2 billion General Fund in 2025-26 compared to the 2025 Budget Act. This increase is driven primarily by federal fund claiming changes, including a one-time retroactive state-only claiming repayment and federal fund claim deferrals, as well as increased Medicare costs.

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House of Representatives H.R. 1 of 2025. The Budget reflects the following significant adjustments related to the implementation of federal requirements included in H.R. 1:

Work and Community Engagement Requirement. An estimated reduction of \$373 million in 2026-27 and \$13.1 billion by 2029-30, resulting from the new work and community engagement requirements for the Affordable Care Act adult expansion population, effective January 1, 2027. Under this federal policy, these individuals must comply with federal work or community engagement requirements as a condition of Medi-Cal eligibility unless they meet an allowable exemption or short-term exception.

Medical Assistance Percentage for Emergency Services. A cost of \$658 million General Fund in 2026-27 and \$872 million General Fund by 2029-30 due to the federal match reduction from 90 percent to 50 percent for emergency services for Affordable Care Act adult expansion population members with unsatisfactory immigration status.

Restrictions on Immigrant Eligibility. Transitions individuals impacted by the federal eligibility change for qualified non-citizens to restricted-scope Medi-Cal. Effective October 1, 2026, the federal policy will exclude individuals with certain immigration statuses from federal eligibility for full-scope Medi-Cal, which significantly reduces federal funding for this population. If the state were to provide full-scope Medi-Cal to this population, the cost is estimated to be \$786 million General Fund in 2026-27 and \$1.1 billion General Fund ongoing.

The Department of Health Care Services, in their budget summary document goes into a bit more detail on these impacts and policy changes resulting from HR 1. You can find this DHCS document [here](#).

Hospital Quality Assurance Fee (HQAF) GF Offset. The Budget assumes \$1.3 billion General Fund to support children's coverage, a decrease of approximately \$652 million General Fund. Based on the federal government's notification that California's waiver would not be approved as submitted, the Administration continues to evaluate options to modify the request for approval. Specifically, this budget assumes the new QAF 9 program will be approved at last year's QAF 8 levels, with no increase.

Managed Care Organization (MCO) Tax. \$4.5 billion in 2025-26 and \$2.5 billion in 2026-27 MCO Tax revenue to support the Medi-Cal program and \$1.6 billion across 2025-26 and 2026-27 to support increases in managed care payments relative to calendar year 2024 in certain domains. The current MCO Tax is not consistent with H.R. 1 requirement that prohibits taxing Medicaid providers at higher rates than non-Medicaid providers. Under recent federal guidance, the state will receive a transition period through June 30, 2026, which would result in a General Fund cost of approximately \$1.1 billion in 2026-27. However, the Budget assumes a transition period through December 31, 2026, as California will continue to evaluate options to receive a full transition period. Additionally, H.R. 1 and Proposition 35 requirements significantly limit the potential size of a future MCO Tax, resulting in a substantial reduction in ongoing funding to support the Medi-Cal program.

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<p>2026-2027 State Budget Proposal Released <i>(continued)</i></p>	<p>Unsatisfactory Immigration Status (UIS) Emergency Affordable Care Act (ACA) Federal Medical Assistance Percentage (FMAP) Adjustment. H.R. 1 requires a change in FMAP from 90 percent to 50 percent for emergency services for ACA Adult Expansion population members with UIS, effective October 1, 2026. This results in additional General Fund (GF) costs of \$658 million in 2026-27.</p> <p>ACA Adult Expansion Population Six-Month Redetermination. As part of H.R. 1, the Department will increase the eligibility redetermination frequency for the ACA Adult Expansion population from once per year to every six months, effective January 1, 2027. For 2026-27, this results in a cost reduction of \$463.3 million total funds (\$74.1 million GF).</p> <p>County Administration. The H.R. 1 changes Medi-Cal eligibility requirements. The Department is working with counties to evaluate needed support for county implementation. An important note, during the press conference, Director Stephenshaw noted that counties are responsible for the health care of the indigent population. How the State chooses to support and pay for the care of indigent Californians who no longer have access to health care coverage will be a major issue moving forward.</p> <p>Reduced Retroactive Medi-Cal Timeframes. As a result of H.R. 1, there is a federally mandated reduction of retroactive Medi-Cal coverage from three months to one month for the ACA Adult Expansion population and two months for all other eligible groups, effective January 1, 2027. This policy assumes implementation no sooner than January 1, 2027. Estimated savings in 2026-27 are \$23 million total funds (\$9.6 million GF).</p> <p>Community-Based Mobile Crisis Services. Existing federal law authorizes state Medicaid programs to offer “qualifying” community-based mobile crisis response with certain conditions. The budget proposes to revise the benefit to an optional benefit beginning April 1, 2027. The budget includes \$431.5 million total funds (\$50.7 million Proposition 35 funds, \$347 million federal funds, \$28.2 million 988 funds, and \$5.6 million GF) to continue this benefit across 2025-26 and 2026-27.</p> <p>MCO Tax Behavioral Health. The Budget reflects \$65 million in 2025-26 and \$95.5 million in 2026-27 MCO Tax revenue for qualifying community-based mobile crisis services, transitional rent, and behavioral health rates from the calendar year 2025 behavioral health facility throughputs domain allocation.</p> <p>DHCS also notes that the Administration will be releasing Budget Trailer Bill Language to modify policy related to these budget changes. TBL will include H.R. 1: Conforming State to Federal Law, Community-Based Mobile Crisis Intervention Services, Skilled Nursing Facility Financing Reauthorization</p> <p>Other Key Health Care Items of Note</p> <p>Federal Rural Health Transformation Program. \$233.6 million federal funds in federal fiscal year 2026 to expand access to care, strengthen the workforce, and enhance infrastructure in rural and frontier communities at the Department of Health Care Access and Information.</p> <p style="text-align: right;"><i>(more)</i></p>
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Behavioral Health Funding. A placeholder of \$150 million Behavioral Health Services Fund in lieu of General Fund for workforce and prevention programming at the Department of Health Care Access and Information and the California Department of Public Health with the specific proposal to be updated at the May Revision.

Reproductive Health Grant Program. \$60 million one-time General Fund in 2025-26 for the Department of Health Care Access and Information to provide grants to reproductive health care providers. This is in addition to \$90 million MCO Tax funds and \$56 million Abortion Access Fund in 2025-26 to support reproductive health care providers.

Menopause Services. \$3.4 million (up to \$3 million General Fund) in 2026-27 and \$391,000 Managed Care Fund ongoing, to support health care coverage for perimenopause and menopause, including enrollee access to care, provider education, and a statewide public awareness campaign.

Vocational Rehabilitation Program Capacity—\$60 million ongoing in federal funds to support increased demand for Department of Rehabilitation services provided to individuals with disabilities pursuing opportunities for employment.

Next Steps. The Legislature will begin hearings on the Governor's proposal starting with the Senate Budget Committee hearing on Wednesday, January 21 at 9:00am and the Assembly Budget Committee on the same day at 11:00am. In these hearings, the Department of Finance and the Legislative Analyst's Office provide a broad overview of the Governor's proposal and Legislators are able to ask clarifying questions. Budget Subcommittees will be set shortly thereafter.

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