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Special Session Overview of Proposition 98 Budget

LEGISLATIVE ANALYST'S OFFICE

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Senate Budget and Fiscal Review

Subcommittee No. 1 on Education

Hon. Gloria Romero, Chair





Huge Budget Problem

LAO Projection of General Fund Condition If No Corrective Actions Are Taken

*2007-08 Through 2009-10
(In Millions)*

	2007-08	2008-09	2009-10
Prior-year fund balance	\$4,777	\$3,786	-\$7,501
Revenues and transfers	102,649	93,248	86,835
Total resources available	\$107,426	\$97,034	\$79,334
Expenditures	\$103,640	\$104,535	\$106,293
Ending fund balance	\$3,786	-\$7,501	-\$26,959
Encumbrances	885	885	885
Reserve	\$2,901	-\$8,386	-\$27,844
Budget Stabilization Account	—	—	—
Special Fund for Economic Uncertainties	\$2,901	—	—

- ☑ We project a budget shortfall of \$28 billion across 2008-09 and 2009-10.
- ☑ The bulk of the budget shortfall is due to a decline in revenues (down roughly \$25 billion compared to *2008-09 Budget Act* assumptions).
- ☑ For every \$1 drop in these revenues, the Proposition 98 minimum guarantee in 2008-09 drops by roughly \$0.50.



Update on Property Tax Revenues for Schools

Comparison of Property Tax Estimates			
<i>(In Millions)</i>			
	2007-08	2008-09	2009-10
Governor's proposal ^a	\$15,023	\$16,143	\$16,107
LAO estimate	14,631	15,683	15,520
Difference	-\$392	-\$460	-\$587
^a Does not update property tax estimates. Based on 2008-09 Budget Act assumptions.			

- ☒ School district property tax estimates have dropped by about \$1.4 billion across the three years.
- ☒ Drops in property tax revenues going to schools results in higher General Fund costs for Proposition 98.



Governor's Plan—Revenue Increases

Governor's Special Session Revenue Proposals			
(In Millions)			
	2008-09		2009-10
	November	December	
Revenue Increases ^a			
Increase sales tax by 1.5 cents for three years ^b	\$3,540	\$2,628	\$6,643
Expand sales tax to some services	357	273	1,156
Impose oil severance tax	530	354	1,202
Raise alcohol tax by a nickel a drink	293	195	585
Totals	\$4,720	\$3,450	\$9,586
^a Scoring reflects administration's estimates.			
^b Sales tax revenues are the net benefit to the General Fund, after accounting for higher spending required under Proposition 42.			

- ☒ In his November package, the Governor proposed raising \$4.7 billion in new revenue for 2008-09.
- ☒ These revenue solutions have eroded by \$1.3 billion due later effective start dates.
- ☒ Governor assumes new tax increases would generate full-year benefit of \$9.6 billion in 2009-10.
- ☒ Under most scenarios, for every dollar of new revenue raised, the Proposition 98 minimum guarantee is raised by roughly \$0.50.



Governor's Plan—\$2.5 Billion Midyear Reduction for K-14 Education

Governor Proposes \$2.5 Billion Midyear Reduction in Proposition 98 Funding

*2008-09
(Dollars in Millions)*

	Budget Act	Special Session	Difference	Percent
K-12 education	\$51,620	\$49,453	-\$2,168	-4.2%
California Community Colleges	6,359	6,027	-332	-5.2
Other	106	106	—	—
Totals	\$58,086	\$55,586	-\$2,500	-4.3%



K-12 spending reduced by \$2.2 billion, or slightly more than 4 percent.



California Community College (CCC) spending reduced by \$332 million, or slightly more than 5 percent.



Governor's Plan—Reduction Applied to General Purpose Funding

- ☒ The *2008-09 Budget Act* provided a 0.68 percent cost-of-living adjustment (COLA) to K-12 revenue limits and CCC apportionments. Governor's plan rescinds funding for this COLA (\$284 million).
- ☒ Also cuts base K-12 revenue limits/CCC apportionments by a total of \$2.1 billion (reflects base reduction of about 5 percent).
- ☒ Achieves a small amount of additional savings by identifying current-year funds likely to go unused and unappropriating them (\$132 million).



Governor's Plan—Fiscal Flexibility

- ☒ Allows transfers of current-year funds from categorical programs to revenue limits (not to exceed total revenue limit reduction).
- ☒ Allows transfers from prior-year categorical ending balances to revenue limits (not to exceed total revenue limit reduction).
- ☒ Reduces reserve requirement for economic uncertainties by one-half.
- ☒ Reduces requirement for deposits into routine maintenance account from 3 percent to 2 percent.
- ☒ Suspends local deferred maintenance matches.



LAO Alternative—Principles for Building Proposition 98 Budget

- ☒ Make midyear reductions that lower costs rather than shift burden.
- ☒ Use settle-up to forego deeper midyear cuts.
- ☒ Make budget-year cuts now, give schools time to plan.
- ☒ Eliminate programs that are poorly structured, create poor incentives, are duplicative of other programs, and/or have fulfilled original purpose.



LAO Alternative—Summary of Proposition 98 Recommendations

Recommend Set of Targeted Education Changes ^a		
<i>(In Millions)</i>		
	2008-09	2009-10
Rescind 2008-09 COLA (0.68 percent)	\$284	\$284
Foregone growth ^b	—	81
Savings from current/prior years ^c	216	—
K-12 program suspensions	400	915
K-12 program eliminations	—	500
Increase California Community College (CCC) credit fee	40	120
Reduce funding rate for certain CCC enrichment courses	60	200
Total Reductions	\$1,000	\$2,100
^a All amounts reflect reductions from funding levels assumed at the time the <i>2008-09 Budget Act</i> was adopted. ^b Assumes no growth in overall Proposition 98 funding for 2009-10. ^c Reflects one-time savings from lower-than-expected program expenditures. Assumes roughly one-half will materialize from child care programs, with the other one-half coming from K-14 programs.		



LAO Alternative—Specific Proposition 98 Recommendations

LAO Proposition 98 Alternative				
(In Millions)				
Program		Action	2008-09	2009-10
Statewide Issues:				
K-14 COLA	Withdraw 0.68 percent COLA for K-12 revenue limits, county office of education revenue limits, and CCC apportionments.		\$284	\$284
Estimated Growth in Minimum Guarantee	Foregone growth in 2009-10 guarantee.		—	81
Subtotals			(\$284)	(\$365)
Scoop Current/Prior-Year Savings:				
Non-CalWORKs child care	Reduce current-year General Fund spending. Savings due to revised estimate of 2008-09 expenditures.		\$55	—
CalWORKs Stages 2 and 3	Reduce current-year General Fund spending. Savings due to revised 2008-09 caseload estimate.		42	—
Excess federal funds for child care	Increase federal authority and reduce current-year General Fund spending. (Additional federal funds available due to lower-than-anticipated expenditures.)		19	—
Unspent K-12 funds from current/prior years	Combination of reducing current-year General Fund spending and redirecting prior-year funding, both due to lower-than-expected expenditures.		90	—
Unspent CCC funds from current/prior years	Combination of reducing current-year General Fund spending and redirecting prior-year funding, both due to lower-than-expected expenditures.		10	—
Subtotals			(\$216)	(—)
K-12 Program Eliminations/Reductions:				
High Priority Schools Grant Program	As of July 1, 2009, eliminate because of substantial overlap with federal improvement program.		—	\$114
Year-Round Schools Operational Grants	As of July 1, 2009, eliminate because year-round schools are largely being phased out at local level.		—	97
Physical Education Teacher Incentive Grants	As of July 1, 2009, eliminate because poorly structured.		—	42
School Safety Competitive Grants	As of July 1, 2009, eliminate because of substantial overlap with a larger, less restrictive school safety program.		—	18
Ninth Grade Class Size Reduction	As of July 1, 2009, eliminate because other funds are available for class size reduction in grade 9 and is much more targeted. Research findings are lackluster on effect of class size reduction on student performance.		—	96
Continued				



LAO Alternative—Specific Proposition 98 Recommendations *(Continued)*

Program	Action	2008-09	2009-10
K-12 Program Eliminations/Reductions:			
Community-Based English Tutoring	As of July 1, 2009, eliminate because program does not serve K-12 students. Other opportunities exist for adults to take English language classes.	—	50
Pupil Retention Block Grant	As of July 1, 2009, eliminate block grant but fund continuation high schools separately. Since block grant was created, a new supplemental instruction program (\$73 million) and a new counseling program (\$200 million) have been created.	—	62
Adult education	Achieve one-time savings by scooping excess growth provided from 2004-05 through 2008-09. Change growth formula moving forward.	—	45
Subtotals		(—)	(\$524)
K-12 Program Suspensions:			
Professional Development Block Grant	Suspend for one year, beginning July 1, 2009.	—	\$273
Math and Reading Professional Development	Suspend funding, beginning January 1, 2009.	\$28	57
Peer Assistance and Review	Suspend funding, beginning January 1, 2009.	15	30
Certificated Staff Mentoring	Suspend funding, beginning in January 1, 2009.	6	12
National Board	Honor existing grants only. Make no new awards.	2	3
Principal Training	Fund only existing participants and new principals in 2009-10.	1	2
Bilingual Teacher Training	Suspend funding, beginning July 1, 2009.	—	2
Instructional Materials Block Grant	Move required math purchases from 2009-10 to 2010-11. Move required reading/language arts purchases from 2010-11 to 2011-12. Retain some funding for replacement, consumables, and classroom supplies.	140	235
Deferred maintenance	As of July 1, 2009, eliminate because it sets up poor local incentives. It predates the School Facility Program, which has better incentive for school districts to maintain facilities (a required 3 percent set-aside).	208	277
Subtotals		(\$400)	(\$891)
CCC Fee Increases/Funding Rate Reductions:			
CCC personal enrichment courses	As of January 1, 2009, reduce funding for certain credit-bearing physical education courses (for example pilates, racquetball, golf) to noncredit rate. As of July 1, 2009, extend rate reduction to certain enrichment courses (for example ballroom dancing, drawing, photography).	\$60	\$200
CCC fees	As of January 1, 2009, increase fee for credit courses to \$26 per unit (from \$20). Effective fall 2009, increase fee to \$30 per unit.	40	120
Subtotals		(\$100)	(\$320)
Totals		\$1,000	\$2,100
Two-Year Total		\$3,100	



Senate Bill 8xxxx—Summary of Proposition 98 Actions

- ☒ ***Makes \$2.5 Billion in Midyear Proposition 98 Cuts.*** Eliminates/reduces funding for lower priority programs as well as programs that are poorly structured, create poor incentives, or are duplicative.
- ☒ ***Provides Certain Types of Fiscal Flexibility.*** Suspends deferred maintenance match, lowers required routine maintenance deposits, allows transfers from categorical ending balances.
- ☒ ***Uses Settle-Up as Solution.*** Uses about \$500 million in outstanding Proposition 98 settle-up obligations to further reduce Proposition 98 spending in 2008-09.



Senate Bill 8xxxx— Specific Proposition 98 Actions

Senate Bill 8xxxx, Committee on Budget and Fiscal Review		
2008-09 (Dollars in Millions)		
Program	Reduction	Comments
K-12 Education		
K-12 COLA	\$244	Eliminate COLA. (Budget act provided partial COLA of 0.68 percent.)
High Priority Schools Grant Program	114	Eliminate funding.
Math and Reading Professional Development Program	57	Eliminate funding.
Administrator Training	5	Eliminate funding.
Adult education	45	Reduce funding.
Education technology	18	Eliminate funding.
K-12 High Speed Network	2	Reduce funding.
Deferred maintenance	277	Eliminate funding.
Instructional materials	418	Eliminate funding.
Peer Assistance and Review Program	30	Eliminate funding.
National Board Certification	6	Eliminate funding.
Charter School Categorical Block Grant	23	Reduce funding to conform to categorical reductions.
School safety programs	99	Eliminate funding for program but retain funding for school safety plans.
Pupil Retention Block Grant	62	Eliminate funding for block grant but retain funding for Continuation High Schools.
Teacher Credentialing Block Grant	36	Reduce funding for second-year teachers but retain full funding for first-year teachers.
Professional Development Block Grant	273	Eliminate funding.
School and Library Improvement Block Grant	230	Reduce funding.
School Safety Competitive Grant	18	Eliminate funding.
P.E. Teacher Incentive Grants	42	Eliminate funding. New program.
Arts and Music	110	Eliminate funding. New program.
Certificated Staff Mentoring	12	Eliminate funding. New program.
Oral Health Assessments	4	Eliminate funding. New program.
Alternative Certification (Intern) Program	7	Reduce funding.
Paraprofessional Teacher Training Program	1	Reduce funding.
Emergency Repair Program	100	Eliminate funding.
Unspent current/prior-year funds	96	Achieves General Fund savings.
Non-CalWORKS child care	55	Achieves General Fund savings.
CalWORKS Stage 2	20	Achieves General Fund savings.
Additional federal child care funds	19	Achieves General Fund savings.
Subtotal K-12	(\$2,423)	
California Community Colleges (CCC)		
CCC COLA	\$40	Eliminate COLA. (Budget act provided partial COLA of 0.68 percent.)
Physical plant and instructional support	27	Eliminate funding.
Career technical education	20	Reduce funding.
Mandates	4	Eliminate funding.
Puente Program reappropriate/savings	1	Achieves General Fund savings.
Unspent current/prior-year funds	2	Achieves General Fund savings.
Subtotal Community Colleges	(\$95)	
Grand Total	\$2,518	



Other Options

- ☒ ***Cut Option.*** Absent any new revenue, the Proposition 98 minimum guarantee in 2008-09 would be \$54 billion. Getting down to this lower level would require \$4.1 billion in midyear Proposition 98 cuts.
- ☒ ***Even Deeper Cut Option.*** Statute requires a supplemental payment be provided to K-14 education in certain years, including 2008-09. Although it has never been done, this supplement can be waived. If the supplement was not provided in 2008-09, the Proposition 98 minimum guarantee in 2008-09 would be \$52.8 billion. This would require \$5.3 billion in midyear cuts.
- ☒ ***Revenue Option.*** If the entire budget shortfall were to be addressed with new revenues, then the Proposition 98 spending level could remain at \$58.1 billion, with no midyear cuts needed.



Potential Consequences of Not Acting Now

- ☒ Increase likelihood of needing to make even deeper cuts—both in midyear and budget year.
- ☒ Increase likelihood school districts cannot achieve midyear savings in response to midyear cuts and must dip into reserves. Near-term result is more school districts in financially precarious positions.
- ☒ Increase likelihood of needing to suspend the Proposition 98 minimum guarantee in 2009-10.