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Proposition 98 Overview

LEGISLATIVE ANALYST'S OFFICE

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Proposition 98 Input Factors



Several Factors Affect the Proposition 98 Requirement:

- Prior-year Proposition 98 funding level.
- General Fund tax revenues (per capita).
- Personal income (per capita).
- Local property tax revenues.
- K-12 average daily attendance.
- State population.



The Legislature can affect the budget-year Proposition 98 requirement by (1) changing current-year Proposition 98 funding and (2) increasing General Fund revenues.



The Legislature has little direct control over the other Proposition 98 factors.



Proposition 98 “Tests”



Each Year, the Proposition 98 Funding Level Is Determined by One of Three Formulas (Tests).

- **Test 1:** Roughly 40 percent of General Fund revenues must be dedicated to Proposition 98. This minimum requirement must be met each year.
- **Test 2:** The Proposition 98 requirement is determined by growth in the economy (as measured by per capita personal income) and K-12 attendance. Applies in years when state General Fund growth is relatively healthy and formula yields more than under Test 1.
- **Test 3:** The Proposition 98 requirement is determined by per capita growth in General Fund revenues and K-12 attendance. Applies in years when the General Fund grows more slowly than the economy and formula yields more than under Test 1.



State Can Also Provide More or Less Than the Applicable Formula Requires.

- Providing more increases the base moving forward.
- Providing less requires suspending the minimum guarantee.



In Years When the State Provides Less Than Test 2—Through Test 3 or Suspension—“Maintenance Factor” Is Created.

- Whenever maintenance factor is created, the Constitution requires the state to provide accelerated growth in Proposition 98 funding in future years (until the “long-term Test 2” is reached).



Proposition 98: History of the Operable Tests

| | Applicable Test | Growth Factors per Capita | |
|----------------------|-----------------|---------------------------|----------------|
| | | Personal Income | General Fund |
| 1988-89 | 1 | 3.9% | — ^a |
| 1989-90 | 2 | 5.0 | — ^a |
| 1990-91 | 3 | 4.2 | -4.0% |
| 1991-92 | 2 | 4.1 | 8.0 |
| 1992-93 | 3 | -0.6 | -4.4 |
| 1993-94 | 3 | 2.7 | -3.4 |
| 1994-95 | 2 | 0.7 | 6.6 |
| 1995-96 | 2 | 3.4 | 8.0 |
| 1996-97 | 2 | 4.7 | 5.5 |
| 1997-98 | 2 | 4.7 | 10.7 |
| 1998-99 | 2 | 4.2 | 6.5 |
| 1999-00 | 2 | 4.5 | 18.4 |
| 2000-01 | 2 | 4.9 | 6.9 |
| 2001-02 | 3 | 7.8 | -18.7 |
| 2002-03 | 2 | -1.3 | 0.9 |
| 2003-04 | 2 | 2.3 | 6.0 |
| 2004-05 | Suspended | 3.3 | 12.4 |
| 2005-06 | 2 | 5.3 | 12.1 |
| 2006-07 | 3 | 4.0 | 1.9 |
| 2007-08 ^b | 3 | 4.4 | -0.8 |

^a Test 3 was added to Proposition 98 in 1990 by Proposition 111. Thus, per capita General Fund revenues were not part of the calculation in these years.

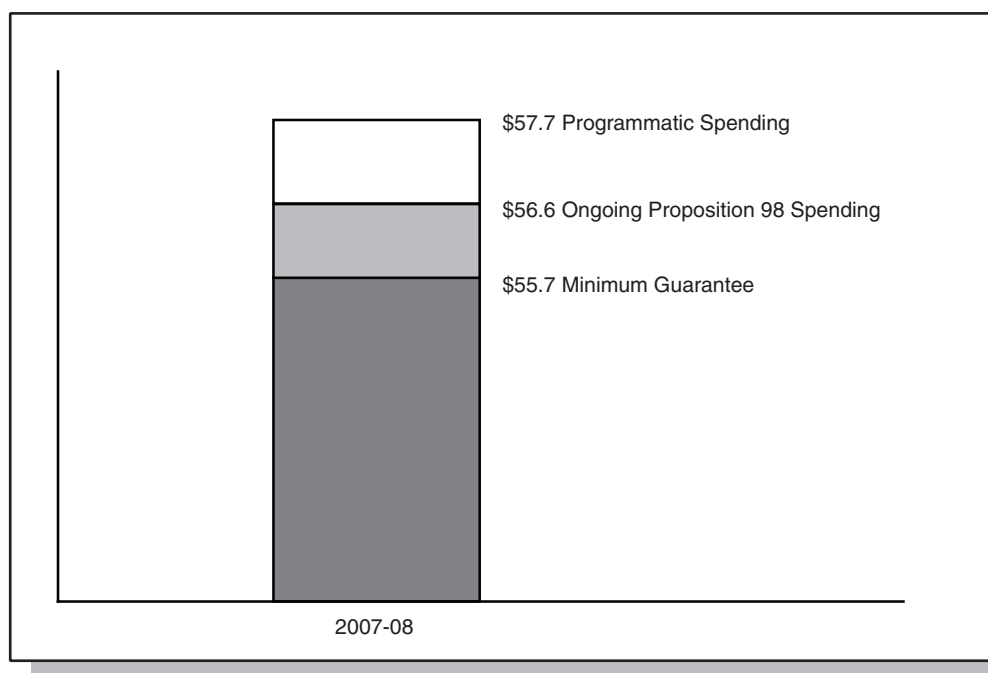
^b Based on LAO underlying forecast, absent any additional revenues.

- ☒ Test 1 has been operable only once during the last 20 years.
- ☒ Test 2 has been operable 12 of the last 20 years.
- ☒ Test 3 has been operable 6 of the last 20 years.
- ☒ Proposition 98 has been suspended only once since its inception.



Current-Year Proposition 98 Issues

2007-08 (In Billions)



- ☑ The state is spending about \$1.1 billion in one-time monies to support ongoing program in 2007-08.
- ☑ The special session Proposition 98 spending level is almost \$900 million higher than the estimated minimum guarantee for 2007-08.
- ☑ Reducing ongoing Proposition 98 spending for 2007-08 reduces the minimum guarantee for 2008-09 by roughly the same amount.
- ☑ We have identified ways to reduce ongoing spending to the minimum guarantee without affecting schools' current operations.



Budget-Year Proposition 98 Ongoing Funding

2008-09 (In Billions)

| | Governor | Assembly | Senate | LAO |
|--------------------------------|----------|----------|--------|--------|
| Ongoing Proposition 98 funding | \$56.8 | \$59.1 | \$59.8 | \$57.8 |
| New General Fund tax revenues | \$2.1 | \$6.8 | \$11.5 | \$3.6 |
| Applicable test | 3 | 2 | 2 | 3 |

- ☒ Governor's plan includes \$1 billion in across-the-board cuts for almost all K-14 programs. It does not fund a cost-of-living adjustment (COLA).
- ☒ Assembly and Senate plans do not cut programs. They also provide partial COLA increases (Assembly: 1.65 percent, Senate: 3.67 percent).
- ☒ The LAO plan contains targeted reductions for 7 programs (totaling \$337 million). It does not fund a COLA.



Interaction Between New Revenues and Proposition 98

| Incremental Increase in Revenues | Applicable Test | Share of New Revenues That Go to Proposition 98 |
|---|-----------------|---|
| \$0-\$5.3 billion | Test 3 | Roughly 50 percent of every new dollar. |
| \$5.3 billion to \$6.4 billion | Test 2 | No additional effect. |
| \$6.4 billion to \$8.9 billion | Test 2 | Roughly 50 percent of every new dollar. |
| \$8.9 billion to \$15.2 billion | Test 2 | No additional effect. |
| \$15.2 billion and above | Test 1 | Roughly 40 percent of every dollar. |
| Note: Baseline reflects 2008-09 revenue projection using LAO forecast (assumes no revenue other than what would be generated under current-law tax policy). | | |

- ☒ For the first roughly \$9 billion in new revenue, about half of every dollar goes to K-14 education (with the exception of the \$5.3 billion to \$6.4 billion range—within this range, there is no additional effect on Proposition 98).
- ☒ Within the \$9 billion to \$15 billion range, there is no additional effect on Proposition 98. This is because the long-term Test 2 level is reached, with all maintenance factor paid off.



One-Time Funding for K-14 Education

(In Millions)

| | Governor | Assembly | Senate | LAO |
|---|------------------|------------------|------------------|--------------------------|
| One-Time Proposition 98 Funding | | | | |
| Child care (ongoing) | \$324 | — | \$355 | \$63 |
| Mandates | — | \$334 | — | — |
| Other one-time purposes | 186 | 175 | 176 | 153 |
| Totals | \$509 | \$509 | \$531 | \$216^a |
| Other One-Time Funding | | | | |
| Public Transportation Account | — | — | — | \$589 |
| Quality Education Investment Act | \$450 | \$450 | \$450 | — |
| Settle-up payment | 150 ^b | 550 ^b | 150 ^b | — ^c |
| ^a The LAO plan recognizes \$521 million in one-time Proposition 98 funding but uses \$305 million as current-year solution. ^b Current law designates \$150 million settle-up payment for mandates. ^c The LAO plan prepays 2008-09 settle-up obligation as part of current-year solution. | | | | |



More than \$500 million in one-time Proposition 98 funding is available to support K-14 programs.

- Assembly uses no one-time funding for child care whereas Senate uses \$355 million. (Houses provide same total level of funding for child care.)
- Assembly uses \$334 million in one-time Proposition 98 funding for mandates. Senate uses no one-time Proposition 98 funding for mandates.



Assembly and Senate both make statutorily scheduled settle-up payment for 2008-09 (\$150 million). Current law designates this payment for mandates.



Assembly also makes accelerated settle-up payment in 2008-09 (\$400 million).