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Overview of the Governor's Proposition 98 May Revision Proposal

LEGISLATIVE ANALYST'S OFFICE

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Size of Budget Shortfall Has Not Changed Much Since January



Governor identifies a budget problem of \$17.9 billion—\$1 billion less than January estimate.

- Since January, new solutions of \$2.1 billion from “gas tax swap” (\$1.4 billion) and General Fund relief for Medicare Part D (\$680 million).
- Solutions offset by \$500 million in increased costs and \$600 million in lower revenues.



Governor proposes \$19.1 billion in solutions (leaving \$1.2 billion reserve).

- \$12.2 billion in expenditure reductions (including \$4.3 billion from Proposition 98).
- \$3.4 billion in additional federal funding.
- \$2.6 billion in loans, loan extensions, transfers, and shifts.
- \$0.9 billion in additional revenues.



Overview of Governor's Proposition 98 Funding Levels

Governor's Proposition 98 Funding Proposal						
<i>(In Millions)</i>						
	2009-10			2010-11		
	January Budget	May Revision	Change	January Budget	May Revision	Change
K-12 Education						
General Fund	\$30,844	\$32,022	\$1,178	\$32,023	\$30,927	-\$1,096
Local property tax revenue	13,237	12,105	-1,133	11,950	11,529	-422
Subtotals	(\$44,082)	(\$44,127)	(\$45)	(\$43,974)	(\$42,456)	(-\$1,518)
California Community Colleges						
General Fund	\$3,722	\$3,722	—	\$3,981	\$3,991	\$9
Local property tax revenue	1,953	1,962	\$8	1,913	1,907	-6
Subtotals	(\$5,675)	(\$5,683)	(\$8)	(\$5,895)	(\$5,898)	(\$3)
Other Agencies	\$94	\$93	-\$1	\$85	\$89	\$3
Totals	\$49,851	\$49,903	\$52	\$49,954	\$48,442	-\$1,512
General Fund	\$34,660	\$35,837	\$1,177	\$36,090	\$35,007	-\$1,083
Local property tax revenue	15,191	14,066	-1,124	13,864	13,435	-428



2009-10. Minor changes to January proposal.

- \$52 million increase in total Proposition 98 spending, due primarily to increase in Public Employees' Retirement System costs.
- \$1.2 billion in increased General Fund cost, primarily due to Governor's decision to use \$877 million in one-time property tax revenues to support other parts of the budget.



2010-11. \$1.5 billion in additional reductions.

- \$1.2 billion savings from elimination of child care services (excluding state preschool programs).
- \$321 million savings by replacing ongoing Proposition 98 funding for Economic Impact Aid with one-time funds.



Governor Asserts Plan Meets Minimum Guarantee



Governor continues to assume no constitutional maintenance factor obligation exists under Proposition 98.

- Instead creates statutory obligation to make \$11.2 billion of “in-lieu” payments.



2009-10. Counts “overappropriation” toward \$11.2 billion obligation.

- Decline in General Fund revenues reduces Governor’s estimate of minimum guarantee.
- Governor proposes no associated funding reduction. Instead overappropriation (\$503 million) is counted as payment towards the \$11.2 billion statutory obligation. (Would resume subsequent payments beginning in 2011-12.)



2010-11. Depends on “rebenching” for elimination of child care.

- To rebench, the Governor no longer counts child care as a Proposition 98 expenditure and proportionally reduces the percentage of General Fund revenues required to be allocated to K-14 education under Proposition 98.
- Rebenching reduces the minimum guarantee by \$1.5 billion.
- Governor does not rebench for gas tax (thereby avoiding \$686 million in additional cost).



Changes to Revenue Limit Proposals

- ☒ Governor retains proposal to reduce revenue limits by \$1.5 billion, but no longer links proposal to reductions in noninstructional spending and contracting out. (The Governor still proposes policy language to ease contracting out restrictions.)
- ☒ Proposed \$45 million revenue limit reduction for County Offices of Education reduced to \$28 million and no longer tied to consolidation of services.
- ☒ Revenue limit reductions would be applied as a percentage reduction to base revenue limits, not a per-pupil reduction as proposed in January, but no corresponding deficit factor would be established.



Governor Now Meets K-12 MOE Requirement In 2009-10, Still Needs Waiver in 2010-11

Comparing Funding to Federally Required Maintenance-of-Effort (MOE) Level				
<i>(Dollars in Millions)</i>				
	MOE Level: 2005-06	2008-09	2009-10	2010-11
K-12 Education				
Proposition 98 General Fund	\$31,917	\$28,492	\$30,567	\$30,927
Settle-up	7	1,101	—	—
Quality Education Investment (QEIA)	—	402	—	402
Deferrals	—	2,851	1,679	—
K-12 Totals	\$31,924	\$32,846	\$32,246	\$31,329
Average Daily Attendance (ADA)	5,965,268	5,957,111	5,921,510	5,927,728
Total Per ADA (In Dollars)	\$5,352	\$5,514	\$5,446	\$5,285
Amount Above/Below MOE	—	\$966	\$556	-\$394
Institutions of Higher Education (IHEs)				
UC General Fund	\$2,839	\$2,418	\$2,596	\$3,019
CSU General Fund	2,596	2,155	2,350	2,723
Subtotals—UC/CSU	(\$5,435)	(\$4,573)	(\$4,946)	(\$5,742)
CCC				
Proposition 98 General Fund	\$3,422	\$3,918	\$3,722	\$3,990
QEIA	—	48	30	18
Deferrals	—	340	163	—
Subtotals—CCC	(\$3,422)	(\$4,306)	(\$3,915)	(\$4,008)
IHE Totals	\$8,857	\$8,879	\$8,861	\$9,750
Amount Above MOE	—	\$22	\$4	\$894



Governor removes child care funding in calculating the K-12 maintenance-of-effort (MOE) level.



In 2009-10, \$250 million early payment of K-12 Quality Education Investment Act (QEIA) funding would no longer occur (\$30 million for community college QEIA continues).



Revisiting Three Perspectives on Proposition 98 Funding



K-14 Education Contributes More General Fund Solutions.

Provides \$4.3 billion of solutions (up from \$2.4 billion in January).



Proposition 98 Funding Down Year Over Year. Reduces ongoing funding by \$1.5 billion. (The Governor's January budget kept ongoing Proposition 98 funding virtually flat.)



Programmatic Reductions Only Affect Child Care. Reduces total Proposition 98 program by \$3.3 billion (\$1.2 billion more than proposed in January).

- In per-student terms, neither K-12 or community college spending change much from January.
- Funding per child care slot reduced significantly (vast majority of slots eliminated).

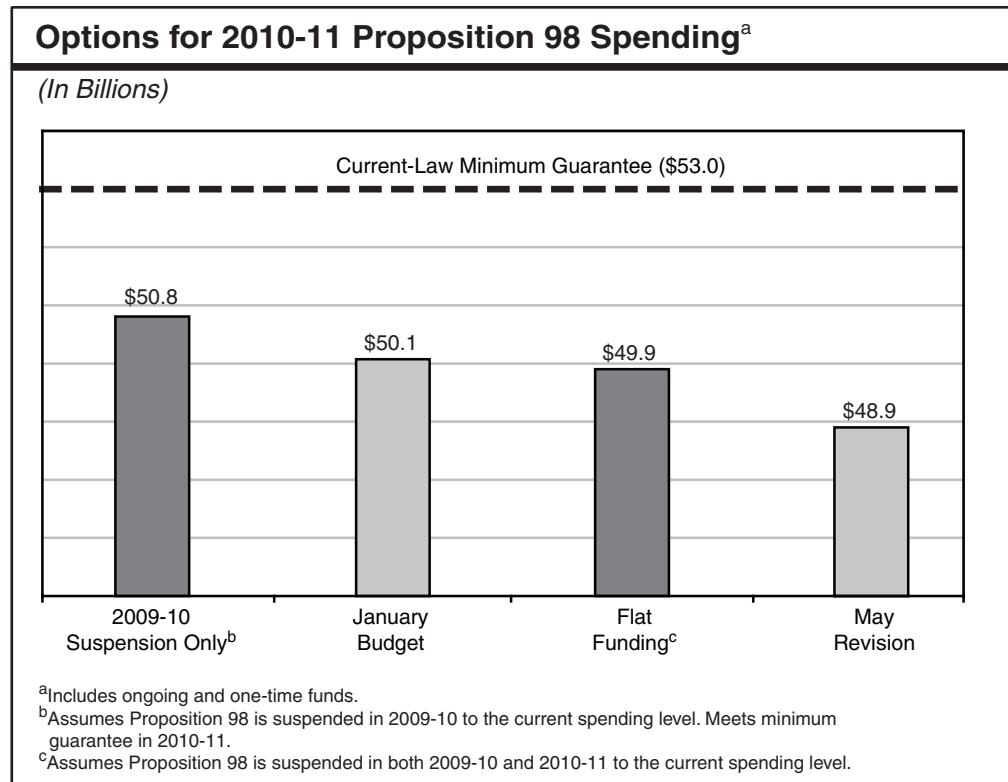


LAO Assessment of Governor's Overall Proposition 98 Funding Plan

- ☒ Governor's approach would not provide sufficient funds to meet current law Proposition 98 requirements.
 - Under current law, the state would need to provide an additional \$1.3 billion in 2009-10 and \$4.1 billion in 2010-11 compared to the Governor's May levels.
- ☒ Governor's already tenuous Proposition 98 plan becomes riskier due to rebenching for elimination of child care.
 - Does not shift functional responsibility for child care or entirely eliminate program.
 - Absent rebenching, suspension would be needed to fund at Governor's May Revision level.
 - Alternatively, minimum guarantee would be notably higher and Governor's additional May General Fund budget solution would be lost.
- ☒ Key question for the Legislature is how much the state can afford to provide K-14 education given other budget pressures.



Recommend Taking Different Approach



- ☒ Two Proposition 98 options for Legislature's consideration.
- ☒ Both options follow current law but would require suspending Proposition 98 in 2009-10 to the current spending level (same level as proposed by the Governor).



Rationale for Suspension



Proposition 98 suspension potentially could resolve maintenance factor issue in a straightforward manner moving forward.

- Signals that state recognizes a maintenance factor exists, to the benefit of K-14 education in the long run.
- Acknowledges that state cannot afford to make an immediate payment.
- Lowers minimum guarantee in 2010-11.



After suspending in 2009-10, the state in 2010-11 could:

- Fund the minimum guarantee (\$50.8 billion).
- Suspend to current spending level (\$49.9 billion).



Develop Strategy for Making Budget Reductions

- ☒ Make targeted reductions first.
- ☒ If additional savings needed, consider revenue limit and flex item reductions.
- ☒ Couple reductions with more flexibility.
- ☒ Take action to achieve non-Proposition 98 savings.
- ☒ Act now to save money later.



Recommend First Making Targeted Reductions

Targeted Proposition 98 Reduction Options		
<i>(In Millions)</i>		
Program	Recommendation	Amount ^a
Economic Impact Aid (EIA)	Require districts to use unspent EIA funds before receiving new EIA funds.	\$300
CCC physical education	Reduce base funding, and associated full-time equivalent students, for credit physical education classes by half (exemption for adaptive physical education, which is designed for persons with disabilities).	150
CCC fees ^b	Fund "overcap" enrollment using additional revenue generated by fee increase (from \$26/unit to \$40/unit).	125
Child care eligibility ceilings ^b	Reduce from 75 percent to 60 percent of state median income for both CalWORKs and non-CalWORKs programs. Of non-CalWORKs savings, redirect \$55 million to expand access to lowest income families. Results in net loss of about 4,200 CalWORKs slots and 9,000 non-CalWORKs slots.	80
Child care reimbursement rates ^b	Reduce license-exempt rates from 90 percent to 70 percent of licensed rates. Affects CalWORKs Stage 2 and 3 as well as non-CalWORKs Alternative Payment programs.	45
Year Round Schools	Eliminate program that already is being phased out. Only used by four districts.	34
Mandates ^b	Reject Governor's proposal to fund Behavioral Intervention Plans but fund 12 education mandates serving compelling statewide interests. ^c	31
Child Nutrition	Reduce per-meal reimbursement rates to 2006-07 level.	30
County offices of education (COE) ^b	Reduce general purpose revenue limit allocation by 10 percent. Redirect additional 10 percent into new regional revenue limit.	27
Charter School Facility Grants ^b	Align funding with program cost.	19
COE excess property tax	Estimate COE excess property taxes for the coming year and make a commensurate reduction to the General Fund apportionment.	15
Child care quality activities	Reduce spending on quality activities to minimum federal requirement.	7
Assessments	Reduce number of times high school exit exam is administered from seven to four.	7
Migrant child care ^b	Align funding with program need.	4
K-3 Class Size Reduction ^b	Reduce program by less than Governor (\$382 million rather than \$550 million). Specifically, reduce 2007-08 level by 20 percent (consistent with other flexed programs), then fold into K-12 flex item.	-168
Total Targeted Reductions		\$706
^a Reflects reductions from 2010-11 Governor's Budget.		
^b Reflects reduction options identified in February.		
^c Funding provided in arrears, such that 2010-11 funding covers 2008-09 costs.		



If Additional Savings Needed, Consider Revenue Limits and Flex Item Reductions

Untargeted Proposition 98 Reductions		
<i>(In Millions)</i>		
Area	Option	Amount^a
K-12 revenue limits	Reduce by some designated percentage. Amount reflects savings achieved for every 1 percent reduction.	\$310
K-12 flexed categorical programs	Reduce by some designated percentage. Amount reflects savings achieved for every 1 percent reduction. ^b	69
CCC apportionments	Reduce by some designated percentage. Amount reflects savings achieved for every 1 percent reduction.	56
Savings From Every 1 Percent Untargeted Reduction		\$435
^a Reflects reductions from the 2010-11 Governor's Budget.		
^b Assumes K-3 Class Size Reduction and Home-to-School Transportation already have been made flexible/placed in flex item.		



Couple Reductions With More Flexibility

LAO Recommendations for Providing Additional Flexibility

Recommendations	Affected Programs
Add three programs to flex item	<ul style="list-style-type: none"> • K-3 Class Size Reduction • Home-to-School Transportation • After School Safety and Education
Consolidate one program into Economic Impact Aid	<ul style="list-style-type: none"> • English Language Acquisition Program
Consolidate five Career Technical Education programs	<ul style="list-style-type: none"> • Regional Occupational Centers and Programs • Specialized secondary programs • Partnership Academies • Apprenticeship programs • Agricultural vocational education
Ease or remove state restrictions in four areas	<ul style="list-style-type: none"> • Contracting out for noninstructional services • Hiring/pay rates for substitute teachers • Quality Education Investment Act requirements^a • Certain mandated activities
Align CDE staffing levels with flex decisions	<ul style="list-style-type: none"> • Cut \$5.2 million and eliminate 70 positions

^a Would apply only to schools also subject to federal school improvement requirements.

CDE = California Department of Education



Also Opportunities to Achieve Non-Proposition 98 Savings

Non-Proposition 98 Reduction Options

(In Millions)

Program	Option	Amount ^a
Quality Education Investment Act (QEIA) ^b	Remove state requirements on schools subject to both state QEIA and federal Program Improvement requirements. Fund federal activities with federal funds. (Same level of General Fund savings would be achieved in 2011-12 and 2012-13.)	\$165.0
Child care reimbursement rates	Reduce license-exempt rates from 90 percent to 70 percent of licensed rates. Reflects CalWORKs Stage 1 savings.	35.0
California Department of Education state operations ^b	Reduce by 70 positions to align staffing with categorical program responsibilities.	5.2
Child care licensing	Fund with federal child care quality dollars. Achieves General Fund savings for licensing activities conducted by the Department of Social Services.	4.3
Total Reductions		\$210.0

^a Reflects reductions from the 2010-11 Governor's Budget.

^b Reflects reduction options identified in February.



Thinking Ahead Could Provide Significant Help in Balancing Next Year's Budget

Acting Now Can Save Money Later

(In Millions)

Program	Option	2011-12 Savings
Kindergarten	Require children to have turned five-years old prior to enrolling in kindergarten.	\$500 ^a
After School Safety and Education	Repeal Proposition 49 funding formula. Roll back to 2005-06 level.	429
Adults in Correctional Facilities	Limit the course offerings for adults in county correctional facilities to adult basic education and English as a Second Language. Payments made in arrears, so estimated savings would not materialize until 2011-12.	5
Estimated Potential 2011-12 Savings		\$934

^a Assumes \$200 million in savings is redirected to preschool for low-income students. Reflects almost a doubling of the size of the state-subsidized preschool program. (A federally subsidized preschool program, Head Start, also provides early education for low-income students.)