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Overview of Proposition 98 Budget

LEGISLATIVE ANALYST'S OFFICE

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Subcommittee No. 1 on Education Finance

Hon. Carol Liu, Chair





Governor Proposes to Keep Proposition 98 Funding Roughly Flat Year Over Year

Proposition 98 Funding					
<i>(Dollars in Millions)</i>					
	2009-10 Final	2010-11 Revised	2011-12 Proposed	Change From 2010-11	
				Amount	Percent
K-12 Education					
General Fund	\$31,732	\$32,239	\$32,401	\$162	0.5%
Local property tax revenue	12,328	11,557	11,406	-152	-1.3
Subtotals	(\$44,060)	(\$43,796)	(\$43,807)	(\$11)	(—)
California Community Colleges					
General Fund	\$3,721	\$3,885	\$3,542	-\$343	-8.8%
Local property tax revenue	2,000	1,892	1,873	-19	-1.0
Subtotals	(\$5,721)	(\$5,777)	(\$5,415)	(\$361)	(-\$6.3%)
Other Agencies					
	\$93	\$85	\$78	-\$7	-8.7%
Totals, Proposition 98					
General Fund	\$49,874	\$49,658	\$49,300	-\$358	-0.7%
Local property tax revenue	\$35,546	\$36,209	\$36,021	-\$188	-0.5%
	14,327	13,449	13,279	-170	-1.3

- ☑ The Governor's plan reduces total Proposition 98 funding by \$358 million (less than 1 percent) from 2010-11 to 2011-12.
- ☑ K-12 funding changes negligibly.
- ☑ Funding for the California Community Colleges (CCC) reduced by \$361 million (6.3 percent).
- ☑ Funds a 0.22 percent increase in K-12 average daily attendance.
- ☑ Provides no K-14 cost-of-living adjustments (1.67 percent).



Governor’s Proposition 98 Package Has Three Main Components

Major Proposition 98 Spending Changes	
<i>2011-12 (In Millions)</i>	
Proposed Changes	Amount
Backfill prior-year one-time K-14 actions	\$2,167
Fund K-12 revenue limit cost increases	470
Make various other K-14 adjustments	96
Fund ongoing K-14 mandates	90
Fund Emergency Repair Program	43
Defer K-12 revenue limit payments	-2,064
Eliminate Special Disabilities Adjustment	-74
Make technical reduction to Economic Impact Aid	-54
Phase out Department of Juvenile Facilities funding	-9
Restore CalWORKs Stage 3 child care veto	256
Reduce Child Care Subsidies by 35 Percent	-577
Reduce child care income eligibility ceiling to 60 percent of SMI	-79
Eliminate child care eligibility for 11- and 12-year olds	-59
Reflect Stage 2 child care savings from CalWORKs reforms	-34
Reduce CCC Apportionments	-400
Defer CCC Apportionment Payments	-129
Total Changes	-\$358

SMI = state median income.

- Relies heavily on K-14 payment deferrals—\$2.1 billion in K-12 payments and \$129 million in CCC payments. Deferrals reflect a form of borrowing that uses next year’s money to pay for this year’s program.
- Reduces child care subsidies by 35 percent. Assumes same number of child care slots and that families pay higher rates to make up for the loss in state funding.
- Reduces CCC apportionments by \$400 million. (This reduction is offset by \$110 million in new fee revenue resulting from increasing the per unit fee from \$26 to \$36.) The Governor does not specify how colleges would accommodate the cut.



Big Proposition 98 Issues for Legislature

- Assume new tax package? Develop contingency plan?
- Adopt same level of cuts for child care, community colleges, and school districts? Distribute cuts differently?
- Rely on deferrals? Rely as heavily on deferrals?



Governor’s Proposition 98 Package Assumes Adoption of Tax Package

General Fund Tax Proposals Increase Proposition 98 Funding			
<i>(In Billions)</i>			
	2010-11	2011-12	Two-Year Totals
General Fund Revenue Proposals			
Extend the 0.25 percent point personal income tax surcharge for five years	\$1.2	\$2.1	\$3.3
Extend reduction in dependent exemption credit for five years	0.7	1.2	2.0
Make single sales factor mandatory for multistate firms	0.5	0.9	1.4
Repeal enterprise zone tax credits	0.3	0.6	0.9
Other	0.4	0.1	0.5
Totals	\$3.2	\$4.9	\$8.1
Proposition 98 Effect	—	\$2.0	\$2.0
Revenues Remaining for Noneducation Purposes	\$3.2	3.0	6.1

- Assumes personal income tax rate increases are extended five years.
- Together with other General Fund revenue proposals generates \$8.1 billion in additional revenue (\$3.2 billion in 2010-11 and \$4.9 billion in 2011-12).
- Tax package has no effect on the Proposition 98 minimum guarantee in 2010-11 due to the suspension of Proposition 98.
- Increases Proposition 98 minimum guarantee by \$2 billion in 2011-12 (about 40 percent of additional budget-year revenue would go to K-14 education).
- State could face one of two risks when rate increases expire: (1) a cliff effect for education funding or (2) a crowding-out effect on rest of state budget.



K-12 Programmatic Funding Down From 2007-08 Level

K-12 Programmatic Funding^a					
<i>(Dollars in Millions Unless Otherwise Specified)</i>					
	2007-08 Final	2008-09 Final	2009-10 Final	2010-11 Revised	2011-12 Proposed
Programmatic Funding					
K-12 ongoing funding ^b	\$48,883	\$43,215	\$40,717	\$42,945	\$43,131
New payment deferrals	—	2,904	1,679	1,719	2,063
Settle-up payments	—	1,101	—	267	—
Public Transportation Account	99	619	—	—	—
Freed-up restricted reserves ^c	—	1,100	1,100	—	—
ARRA funding ^c	—	1,192	3,575	1,192	—
Federal education jobs funding ^c	—	—	—	421	781
Totals	\$48,982	\$50,130	\$47,070	\$46,544	\$45,975
Per-Pupil Programmatic Funding					
K-12 attendance	5,947,758	5,957,111	5,933,761	5,951,826	5,964,800
K-12 Per-Pupil Funding (in dollars)	\$8,235	\$8,415	\$7,933	\$7,820	\$7,708
Percent Change From 2007-08	—	2.2%	-3.7%	-5.0%	-6.4%
^a Excludes federal funds not associated with stimulus package, lottery, and various other local funding sources. ^b Includes ongoing Proposition 98 funding, Proposition 98 accounting adjustments, and funding for the Quality Education Investment Act. ^c Reflects LAO estimates of funds spent in each year.					

- ☑ K-12 per-pupil programmatic funding in 2010-11 is 5 percent lower than 2007-08 level.
- ☑ Under the Governor's 2011-12 proposal, programmatic funding would be 6.4 percent lower than the 2007-08 level.



CCC Programmatic Funding Also Down From 2007-08 Level

California Community College (CCC) Programmatic Funding^a				
<i>(Dollars in Millions Unless Otherwise Specified)</i>				
	2007-08 Final	2008-09 Final	2009-10 Final	2010-11 Revised
Programmatic Funding				
CCC ongoing funding ^b	\$6,164	\$5,995	\$5,721	\$5,845
New payment deferrals	—	340	163	129
Settle-up payments	—	—	—	32
ARRA funding	—	—	35	4
Student fees	291	303	353	350
One-time backfills ^c	69	—	5	—
Other ^d	179	158	172	178
Totals	\$6,703	\$6,796	\$6,449	\$6,538
Per-FTES Programmatic Funding				
CCC funded enrollment	1,169,606	1,205,741	1,161,806	1,187,482
CCC Per-FTES Funding (in dollars)	\$5,731	\$5,636	\$5,551	\$5,506
Percent Change From 2007-08	—	-1.7%	-3.1%	-3.9%
^a Excludes federal funds not associated with stimulus package and various local funding sources. ^b Includes ongoing Proposition 98 funding and funding from the Quality Educational Investment Act. ^c Various funds designated to partially backfill local property tax shortfalls in 2007-08 and 2009-10. ^d Includes lottery and funds for the statewide Chancellor's Office. ARRA = American Recovery and Reinvestment Act and FTES = full-time equivalent student.				

- ☑ Budgeted CCC per-student programmatic funding in 2010-11 is 3.9 percent lower than 2007-08 level, slightly less than the K-12 reduction.

- ☑ In 2011-12, the per-student funding amount is highly sensitive to assumptions about CCC enrollment.
 - Under the Governor's assumption that enrollment *grows* by 1.9 percent, per-student funding would be down 10.2 percent from the 2007-08 level.

 - Assuming the Chancellor's Office request to *reduce* enrollment in 2011-12 by 60,000 students from the 2010-11 level, per student funding would be down 3.6 percent from the 2007-08 level.



Child Care and Development Programmatic Funding Would Be Down Furthest From 2007-08 Level

Child Care and Development Programmatic Funding					
<i>(In Millions)</i>					
	2007-08 Final	2008-09 Final	2009-10 Final	2010-11 Revised	2011-12 Proposed
CalWORKs Stage 2 and 3 child care	\$953	\$923	\$897	\$633	\$455
Non-CalWORKs child care	1,088	1,109	1,118	1,102	653
Preschool	422	429	439	439	438
Support programs	106	106	109	100	76
Totals	\$2,569	\$2,567	\$2,563	\$2,274	\$1,622
Percent Change From 2007-08	—	-0.1%	-0.2%	-11.5%	-36.9%

Note: Includes funding from all sources. Does not include CalWORKs Stage 1.

- Child Care and Development (CCD) programmatic funding was virtually flat from 2007-08 through 2009-10.
- The CCD programmatic funding in 2010-11 was down almost 12 percent from 2007-08—largely as a result of the CalWORKs Stage 3 veto.
- Under the Governor’s 2011-12 proposal, funding would be down 37 percent from the 2007-08 level—reflecting a much deeper cut relative to K-12 education and CCC.



State Has Relied Heavily on K-14 Deferrals Over Last Few Years

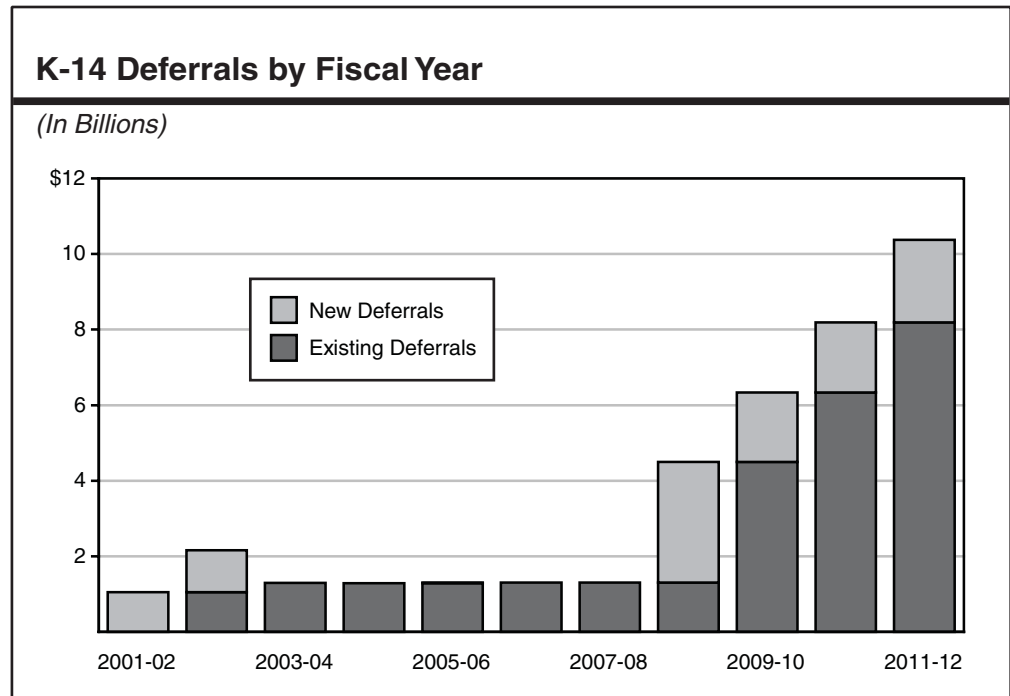
Inter-Year Deferrals of Proposition 98 Payments

(In Millions)

Deferrals	Amount
Existing as of 2007-08	
Shift some K-12 revenue limit and categorical payments from June to July	\$1,103
Shift some CCC apportionment payments from June to July	200
Subtotal	(\$1,303)
Enacted in February 2009 Budget (to begin in 2008-09)	
Retire Home-to-School Transportation deferral	-\$53
Shift some K-12 revenue limit and categorical payments from February to July	2,000
Shift K-3 Class Size Reduction payment from February to July	570
Increase size of existing K-12 deferral from June/to/July	334
Shift portions of CCC apportionments from January-April to July	340
Subtotal	(\$3,191)
Enacted in July 2009 Budget (to begin in 2009-10)	
Shift portion of K-12 revenue limit payments from May to August	\$1,000
Shift portion of K-12 revenue limit payments from April to August	679
Increase size of existing CCC apportionment deferral from April-May to July	163
Subtotal	(\$1,842)
Enacted in October 2010 Budget Package (to begin in 2010-11)	
Increase size of existing K-12 June-to-July deferral	\$500
Increase size of existing K-12 May-to-August deferral	800
Increase size of existing K-12 April-to-August deferral	420
Increase size of existing CCC apportionment deferral from January-June to July	129
Subtotal	(\$1,849)
Proposed in Governor's January Budget (to begin in 2011-12)	
Increase size of existing K-12 revenue limit deferral (likely to October)	\$2,064
Increase size of existing CCC apportionment deferral from January-May (likely to October)	129
Subtotal	(\$2,193)
Total Inter-Year Deferrals	\$10,378
K-12 Education	\$9,417
CCC	961
Share of Proposition 98 Program Paid Late	21%
K-12 Education (excluding child care)	21%
CCC	17



Deferrals Allow State to Achieve One-Time Savings Without Cutting Programs



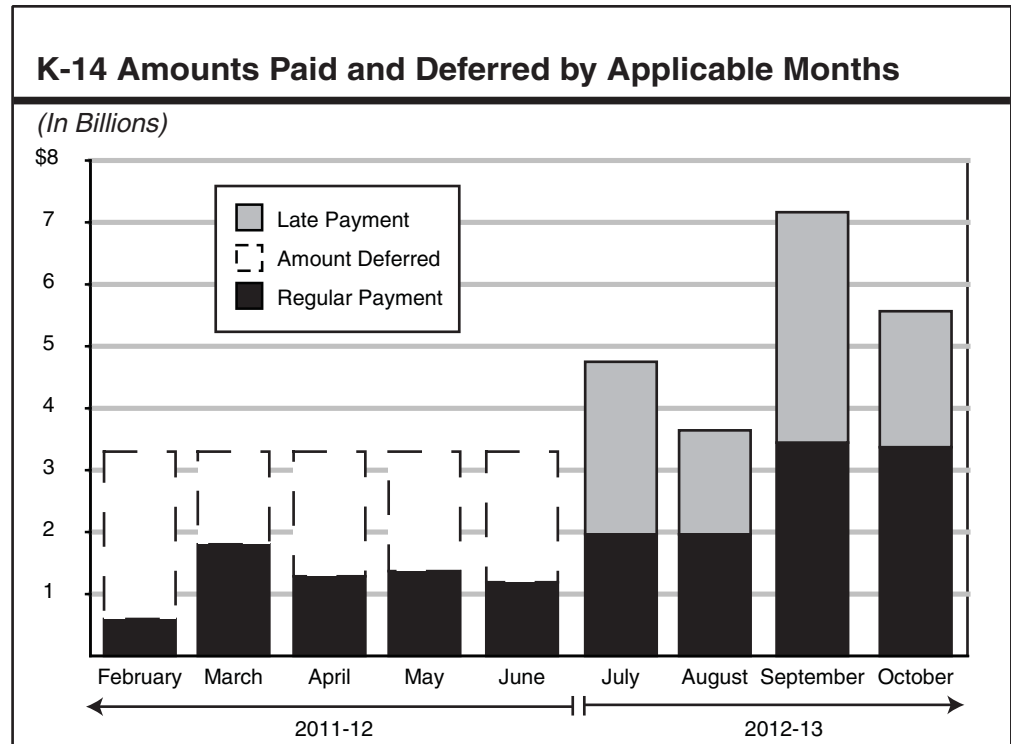
- Initially, state relied on deferrals to achieve midyear budget solution.
 - The 2001-02, 2002-03, and 2008-09 deferrals were all the result of midyear actions.
 - Deferrals allowed a higher programmatic level to be sustained—essentially borrowing funds from the next fiscal year to cover current-year programmatic costs.

- In 2009-10 and 2010-11, the state included deferrals in its *initial* budget act plans—authorizing a programmatic level it could not afford in those years.

- The Governor also builds deferrals into his initial budget plan—essentially budgeting a programmatic level it cannot afford in 2011-12 (even assuming the tax package is adopted).



Almost Two-Thirds of February-June State Payments Would Be Made in Next Fiscal Year



- Deferrals result in districts receiving state funding after they already have had to pay program costs.
- To cover their costs prior to state payment, districts borrow internally from their special funds and/or externally from their county office of education, county treasurer, and/or the market (using Temporary Revenue Anticipation Notes, or TRANs).
- State deferring large portions of February-June payments.
- First deferrals stretched a few days (meaning schools were almost immediately repaid) whereas some deferrals now span more than half a year.



Deferrals: The Trade-offs



Advantages of Deferrals:

- Reduces the need for cuts.
- Provides way to get through what might otherwise be the worst fiscal year for schools since 2007-08 (largely due to the expiration of federal American Recovery and Reinvestment Act funding).



Disadvantages of Deferrals:

- Authorizes spending that the state cannot afford.
- Requires districts to borrow to support program.
- Fosters questionable borrowing practices, with districts in some cases using one short-term loan to cover costs associated with a second short-term loan.
- Relies on questionable accounting practices, with districts attributing funds potentially coming as late as October to the prior fiscal year.
- Places districts in financially risky positions. If districts cannot front the cash to cover costs or make comparable reductions, they become insolvent and require emergency state loans.



To Borrow or Not to Borrow?



To Borrow. Legislature could adopt the Governor's \$2.2 billion deferral.

- Programmatic K-12 spending would be down 6.4 percent from 2007-08 level.
- 21 percent of K-12 Proposition 98 program would be paid late.



Not to Borrow. Legislature could reject the \$2.2 billion deferral.

- Programmatic K-12 spending would be down 11 percent from 2007-08 level.
- 13 percent of K-12 Proposition 98 program would be paid late.
- Proposition 98 support would be a little higher than the 2009-10 level and a little lower than the 2010-11 May Revision level, upon which most districts budgeted in the current year.



Governor's Redevelopment Proposal— Issues Involving School Districts

- Current System.** Redevelopment agencies (RDAs) receive about \$5 billion in local property tax revenues and pass through about \$1.2 billion to local governments. School districts receive nearly 25 percent of the local share, or almost \$300 million. Of the school district amount, about \$40 million offsets state Proposition 98 costs.

- Governor's Proposal.** The Governor proposes to eliminate RDAs.

 - In 2011-12, assumes school districts would be largely unaffected.
 - In 2012-13, assumes school districts would begin receiving roughly \$1 billion in additional revenues—none of which would count for Proposition 98 purposes.
 - The decision regarding how funds would be distributed among school districts appears to be still under development.

- Issues for Legislative Consideration**

 - Should school districts receive additional local property tax revenues?
 - Should the funds offset/not offset state Proposition 98 costs?
 - Should the funds be available for any educational purpose?
 - How should the funds be distributed to school districts?
 - Given some districts could benefit significantly more than other districts by the redistribution of RDA funds, will school equity issues be exacerbated, legal action taken against the state?



Governor's Realignment Proposal— K-12 Issues

- Juvenile Justice.** The Governor's realignment proposal includes the three-year phase out of the Division of Juvenile Justice (DJJ). The Governor reduces Proposition 98 support for DJJ by \$8.7 million in 2011-12 to recognize year-one savings.

- AB 3632 Mental Health.** The Governor would maintain county-based responsibility for providing mental health services to special education students, but fund with \$99 million Proposition 63 funds in 2011-12 and realignment funds thereafter.

- Issues for Legislative Consideration**
 - How will eliminating DJJ affect county court schools?
 - Would the Governor's proposed funding for AB 3632 be sufficient to maintain required services?
 - Should the Legislature consider funding school districts directly for students' mental health needs given federal mandate and accountability for student outcomes reside with schools?