MARCH 5, 2020

Overview of Proposition 98 Budget Proposals

PRESENTED TO:

Senate Budget and Fiscal Review Subcommittee No. 1
On Education Finance
Hon. Richard D. Roth, Chair

LEGISLATIVE ANALYST'S OFFICE

Update on the 2018-19 and 2019-20 Minimum Guarantee

(In Millions)

	2018-19			2019-20		
	June 2019 Estimate	January 2020 Estimate	Change	June 2019 Estimate	January 2020 Estimate	Change
Minimum Guarantee						
General Fund	$54,445	$54,505	$61	$55,891	$56,405	$514
Local property tax	23,701	23,942	241	25,166	25,168	3
Totals	**$78,146**	**$78,448**	**$302**	**$81,056**	**$81,573**	**$517**

▶ Current- and Prior-Year Estimates of the Minimum Guarantee Revised Upward

- Relative to June 2019 estimates, the 2018-19 guarantee is up $302 million and the 2019-20 guarantee is up $517 million.
- The increases reflect upward revisions to estimates of General Fund revenue and local property tax revenue.
- The state is required to make one-time payments to "settle up" to the higher guarantee in both years.

2020-21 Guarantee Grows Under Governor's Estimates

(Dollars in Millions)

	2018-19 Revised	2019-20 Revised	2020-21 Proposed	Change From 2019-20 Amount	Change From 2019-20 Percent
Minimum Guarantee	**$78,448**	**$81,573**	**$84,048**	**$2,475**	**3.0%**
By Segment					
K-12 Education	$69,253	$71,572	$74,279	$2,707	3.8%
California Community Colleges	9,195	9,477	9,807	330	3.5
Reserve deposit (+) or withdrawal (-)	—	524	-38	-562	—
By Source					
General Fund	$54,505	$56,405	$57,573	$1,168	2.1%
Local property tax	23,942	25,168	26,475	1,307	5.2

▶ Minimum Guarantee Is $2.5 Billion Above the Revised 2019-20 Level

- Growth in state General Fund revenue and local property tax revenue each account for about half of the increase.
- The minimum guarantee is determined by "Test 1," meaning the state must provide schools a fixed share (about 40 percent) of General Fund revenue.

▶ K-12 Funding Would Be $12,619 Per Student, an Increase of $499 (4.1 Percent) Over the Revised 2019-20 Level

▶ State Constitution Requires Small Withdrawal From the Proposition 98 Reserve

- After adjusting for changes in student attendance and per capita personal income, the 2020-21 guarantee is $38 million below the 2019-20 level. The Constitution requires the state to withdraw this amount from the reserve.
- The remaining balance in the reserve would be $487 million.

Comments on Estimates of the Minimum Guarantee

▶ Estimates of General Fund Revenue Are Reasonable

- General Fund revenue typically is the most volatile factor affecting the estimate of the minimum guarantee.
- Across the three-year budget period, the Governor's revenue estimates are less than $100 million below ours (roughly 0.01 percent of total tax collections).

▶ Changes in General Fund Revenue Would Affect the Guarantee

- Though the administration's revenue estimates are reasonable based on current conditions, some signs suggest the state economy could cool in the coming months. For example, job growth has slowed and trade activity is down.
- Each dollar of higher or lower revenue would increase or reduce the minimum guarantee by about 40 cents.
- Changes in revenue also could affect the Proposition 98 Reserve. Higher revenue probably would require larger deposits. Lower revenue probably would mean larger withdrawals.

▶ Changes in Property Tax Revenue Also Would Affect the Guarantee

- The administration's estimates of property tax revenue are $671 million above ours over the three-year period.
- Some of the difference reflects additional information the administration received after we prepared our estimates. The difference between our estimates probably will decrease by May.

Overview of New Proposition 98 Spending

▶ Budget Contains $3.7 Billion in New Spending Proposals

- Slightly more than half ($2 billion) is for one-time activities.
- Remainder ($1.7 billion) is for ongoing augmentations.

▶ $3.3 Billion Allocated for K-12 Schools

- Funds a number of one-time initiatives intended to (1) improve school employee training, recruitment, and retention, or (2) address poor academic outcomes for specific student subgroups. Also funds a new special education preschool grant.
- Provides a 2.29 percent statutory cost-of-living adjustment (COLA) for the Local Control Funding Formula (LCFF) and certain other programs.

▶ $388 Million Allocated for Community Colleges

- Provides one-time funding for apprenticeships, work-based learning, and deferred maintenance, among other priorities.
- Provides a 2.29 percent COLA for apportionments and certain categorical programs. Also funds 0.5 percent enrollment growth and a few smaller ongoing augmentations.

Governor's Proposition 98 Spending Proposals

(In Millions)	
K-12 Education	
Ongoing	
COLA (2.29 percent) and attendance changes for LCFF	$1,206
COLA for select categorical programs (2.29 percent)	126
Child nutrition reimbursement rate increase	60
Other	6
Subtotal	($1,398)
One Time	
Educator Workforce Investment Grants	$350
Community school grants	300
Opportunity grants	300
Special education preschool grant	250
Grants to address school staffing shortages	193
Teacher Residency Grant Program	175
Stipends for teachers in hard-to-staff subjects/schools	100
Inclusive Early Education Expansion Program	75
Classified employees credentialing program	64
Literacy grants	53
County coordination grants	18
Computer science resources for educators	18
Refugee student services	15
Other	21
Subtotal	($1,932)
Total K-12 Education	**$3,329**
California Community Colleges	
Ongoing	
COLA for apportionments (2.29 percent)	$167
Enrollment growth (0.5 percent)	32
Apprenticeship instructional hours	28
COLA for select categorical programs	22
Immigrant legal and support services	16
California Apprenticeship Initiative	15
Other	16
Subtotal	($296)
One Time	
Funding for current-year apprenticeship costs	$20
Work-based learning initiative	20
Deferred maintenance	17
Faculty diversity fellowships	15
Other	20
Subtotal	($93)
Total California Community Colleges	**$388**
Total Spending Proposals	**$3,717**

Strengths of the Governor's K-12 Spending Proposals

▶ Relies Upon a Reasonable Mix of One-Time and Ongoing Spending

- About half of the new spending specifically attributable to 2020-21 is for one-time activities.
- One-time spending provides a cushion that reduces the likelihood of cuts to ongoing programs if the guarantee falls below projections.

▶ Identifies Some Longstanding Challenges in K-12 Education

- Achievement gaps are a persistent issue for many school districts.
- Many districts report longstanding difficulty finding, training, and retaining teachers in certain subject areas.

Concerns About the Governor's K-12 Spending Proposals

▶ Many of the One-Time Proposals Are Unlikely to Address Root Issues

- Not directly connected to the underlying problems.
- Not aligned with existing state and federal efforts.
- Few details about how funds would be spent.

▶ Budget Package Does Not Provide Much Fiscal Relief for Districts

- Districts face fiscal pressure from various sources, including rising pension costs and higher costs for serving additional students with disabilities. In addition, following several years of significant increases, school funding is now growing more slowly.
- Most districts are facing relatively tight budgets. For example, school districts' pension costs are expected to increase by $800 million to $1 billion next year—nearly as much as the funding increase associated with the LCFF COLA ($1.2 billion).

Recommendations for Overall K-12 Spending

▶ Build a Final Budget Package That Continues to Rely Upon a Mix of One-Time and Ongoing Spending

▶ Fund a Few of the Governor's One-Time Initiatives

- Fund a few of the proposals that (1) directly address underlying problems, (2) align with existing state and federal programs, and (3) have clear objectives and spending requirements. In some cases, adopt modifications to make the proposals less costly or better targeted.
- Reject the other one-time proposals, freeing-up roughly $1 billion.

▶ Use Freed-Up Funding to Provide Fiscal Relief for Districts

- We think the most promising option is to pay down district's unfunded pension liabilities. Paying down these liabilities would improve the fiscal health of the pension systems and could reduce district costs on a long-term basis.
- If interested in providing more immediate fiscal relief to districts, consider using about $300 million to smooth out projected pension rate increases in 2020-21. Though this option lacks the potential for long-term savings, it would make district budgets easier to balance next year.