March 30, 2016

LEGISLATIVE ANALYST'S OFFICE

LAO 75 YEARS OF SERVICE

Budget Reserves and Debt Repayments Under Proposition 2

Presented to:
Senate Budget Subcommittee No. 4
On State Administration and General Government
Hon. Richard D. Roth, Chair

March 30, 2016

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Legislature's Options for Building Additional Reserves

	Description	Limitations on Use of Funds	Limitations on Reserve Levels
Budget Stabilization Account (BSA) (Governor's Proposal)	State's mandatory "rainy-day" reserve, governed by the rules of Proposition 2 (2014).	Governor must declare a budget emergency before Legislature can reduce required deposit or make withdrawal from BSA. Administration proposes that these rules apply to additional deposits.	Constitutional deposits continue until BSA has reached maximum size—10 percent of General Fund taxes.
Special Fund for Economic Uncertainties (SFEU) (Traditional Reserve)	State's traditional discretionary reserve. Essentially General Fund ending balance.	No limitations.	If balances in SFEU reach a certain threshold (around $4 or $5 billion), the state's sales tax rate would automatically decline by one-quarter cent for one calendar year. This would reduce reserves by about $1.5 billion during each year the trigger is in place.
New Reserve Fund (LAO Alternative)	Legislature would create a new reserve fund and determine the rules that apply to its use.	Legislature may set limitations, as desired.	No limitations.
Prepay 2017-18 Bond Debt Service (LAO Alternative)	Legislature would use some amount to prepay 2017-18 bond debt service, freeing up a like amount in 2017-18 budget that it could use for any purpose.	No significant limitations.	Limited by total amount of outstanding debt service.

Note: A budget emergency can only occur upon declaration of the Governor and majority votes of both houses of the Legislature. The Governor may call a budget emergency if (1) estimated resources in the upcoming fiscal year are insufficient to keep spending at an adjusted level of the prior three budgets or (2) in response to a natural disaster.

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Legislature's Options for Paying Down Eligible Debts Under Proposition 2

Dollars in Billions

	Eligible Amount	Interest Rate	Who Benefits?	Plan in Place to Address?
Budgetary Liabilities				
Special fund loans to General Fund	$4.0	0.9%	Special fund fee payers.	No[a]
Proposition 98 settle up	1.2	—	School and community college districts.	No[a]
Unfunded Liabilities—Pensions[b]				
School and community college employees	81.5	7.5	School and community college districts.	Yes
State and CSU employees	43.3	7.5	State General Fund taxpayers.	Yes
UC employees	12.1	7.3	UC, state General Fund taxpayers, and/or future students.	Yes
Judges	3.4	4.3	State General Fund taxpayers.	No
Unfunded Liabilities—Retiree Health				
State and CSU employees	74.1	4.3	State General Fund taxpayers.	No
UC employees	17.3	4.5	UC, state General Fund taxpayers, and/or future students.	No

[a] The state does not customarily develop a plan to address a budgetary liability.
[b] Over the long run, retirement programs grow at a rate similar to the assumed rate or return on investment, holding other factors constant.