

MAY 16, 2024

The 2024-25 Budget: Proposition 98 and K-12 Funding in the May Revision



LEGISLATIVE ANALYST'S OFFICE

Changes to Proposition 98 Guarantee Since January

Estimates Revised Down \$3.7 Billion Over the Three-Year Budget Period

- Most of the reduction in the guarantee is attributable to 2023-24. The guarantee is slightly lower in 2022-23 and essentially unchanged in 2024-25.
- The reductions in 2022-23 and 2023-24 reflect lower General Fund revenue estimates.
- Higher property tax estimates over the period offset some of the drops associated with lower General Fund revenue.

Comparing Estimates of the Proposition 98 Guarantee

(In Millions)

	2022-23	2023-24	2024-25	Three-Year Totals
Governor's Budget				
General Fund	\$68,563	\$74,633	\$76,894	\$220,091
Local property tax	29,742	30,953	32,185	92,881
Totals	\$98,306	\$105,586	\$109,080	\$312,972
May Revision				
General Fund	\$67,753	\$71,500	\$76,606	\$215,859
Local property tax	29,774	31,072	32,524	93,369
Totals	\$97,527	\$102,572	\$109,129	\$309,228
Change From Governor's Budget				
General Fund	-\$811	-\$3,133	-\$288	-\$4,232
Local property tax	32	119	338	489
Totals	-\$779	-\$3,015	\$50	-\$3,744



Overview of K-12 Spending Package

Aligns Overall K-12 Spending Level With Lower Estimates of Proposition 98 Guarantee

- The May Revision includes several actions to mitigate the effects of lower Proposition 98 spending on schools. The primary actions are (1) reserve withdrawals, (2) cost shifts, and (3) repurposing of unspent/unused funds.
- Local school programs generally would not be reduced by these actions.

Commits to Additional Spending in Three Main Areas

- **Cost-of-Living Adjustment (COLA).** The May Revision provides an additional \$260 million to cover a higher 1.07 percent COLA for the Local Control Funding Formula and various categorical programs (up from 0.76 percent in the Governor’s budget).
- **Universal School Meals.** Relative to the Governor’s budget, the May Revision provides an additional \$111 million across 2023-24 and 2024-25 related to higher estimates of meals served through the universal school meals program.
- **Zero-Emission School Buses.** The May Revision provides an additional \$395 million for zero-emission school buses on top of the \$500 million in the Governor’s budget.

Withdraws Remaining Balance in the Proposition 98 Reserve

- The Governor’s budget proposed withdrawing \$5.7 billion from the reserve for schools and community colleges and leaving nearly \$3.9 billion for future use.
- The May Revision would draw down the entire balance by the end of 2024-25.



Overview of K-12 Spending Package

(Continued)

Relies on Larger Proposition 98 Funding Maneuver

- The Governor’s budget proposed “accruing” \$7.1 billion in prior-year payments to schools to future years (without changing any previously disbursed funds). These costs would be attributed to the non-Proposition 98 side of the budget.
- The May Revision retains this funding maneuver and accrues an additional \$666 million to future years, bringing the total to nearly \$7.8 billion. (Including community colleges, the total amount accrued is \$8.8 billion.)

Reverts Additional Unspent/Unallocated Funds

- The Governor’s budget obtained \$482 million in one-time savings from repurposing unspent or unallocated funds. Most of this amount consisted of State Preschool funds that exceeded the cost of existing rates and slots.
- The May Revision repurposes an additional \$327 million in unspent or unallocated funds for total savings of \$809 million. Most of this increase is associated with unallocated funds in the Inclusive Early Education Expansion Program.



LAO Comments

School Funding Decisions Unfolding Amidst Significant Budget Shortfall

- Under the May Revision, General Fund revenues from the state's three largest taxes are \$10.5 billion below the estimates in the Governor's budget over the 2022-23 through 2024-25 period.
- If the state does not reduce school funding to the Proposition 98 minimum level, the state would face more difficult decisions elsewhere in the budget.

Estimates of the Proposition 98 Guarantee Are Plausible but Probably Somewhat High

- Compared with the May Revision, our May estimates of General Fund tax revenue are \$8.6 billion lower across 2023-24 and 2024-25. (We have no differences in 2022-23.)
- Under this lower revenue assumption, the guarantee would be about \$3.3 billion lower across the two years (holding other factors constant).

Revised Funding Maneuver Involves the Same Downsides as the January Proposal

- The maneuver establishes a new type of internal obligation, creates pressure for similar cost shifts in the future, and reduces budget transparency.
- Under the May Revision, the maneuver would increase state costs by nearly \$1.8 billion per year over the next five years (up from \$1.6 billion under the Governor's budget).
- Rejecting the maneuver and addressing the drop in 2022-23 in other ways would allow the state to avoid these significant downsides.



LAO Comments

(Continued)

The May Revision Creates a Future Shortfall for School Programs

- The May Revision would avoid immediate reductions to school programs but creates a shortfall in the future by using \$2.3 billion in one-time funds to pay for ongoing programs in 2024-25.
 - Entering 2025-26, these one-time funds expire but the ongoing costs of these programs continue.
 - The state would need to address this \$2.3 billion shortfall before funding COLA or other priorities emerging next year.
- The state would have fewer tools to address future budget shortfalls.
 - The May Revision exhausts the balance in the Proposition 98 Reserve.
 - The state will have much less ability to pull back unspent funds because a significant portion of these funds will be committed in the coming year.

Governor's Spending Proposals Seem Unaffordable

- The state historically has tried to contain spending during tight times. During the Great Recession, for example, the state (1) avoided new commitments, (2) suspended the annual COLA, and (3) reduced funding for categorical programs.
- The May Revision takes the opposite approach and proposes additional spending of more than \$2.1 billion—an increase of about \$760 million compared with the Governor's budget.
- Rejecting some or all of this new spending would help the state accommodate the drop in the Proposition 98 guarantee without shifting costs into the future.



LAO Comments

(Continued)

The Legislature Has Options to Obtain Additional One-Time or Ongoing Savings

- Some of the actions we recommend the Legislature consider include:
 - Rescinding various unallocated grants that represent lower priorities.
 - Reforming certain ongoing programs and add-ons to be less costly.
 - Making temporary reductions to school funding and mitigating them by freeing up restricted reserves held at the local level.
- These actions potentially involve difficult decisions now, but offer several advantages relative to the May Revision:
 - They would allow the state to reduce its reliance on reserve withdrawals and/or the funding maneuver.
 - They would ease some of the future budget pressure on core school priorities (and potentially other state programs).
 - They would set up better choices next year by aligning school spending with available funding.

