Santa Clara County Office of Education Countywide CBO Meeting

Beyond the 2015-16 Governor's Budget

Presented by:
Robert D. Miyashiro, Vice President

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School Services of California INC.

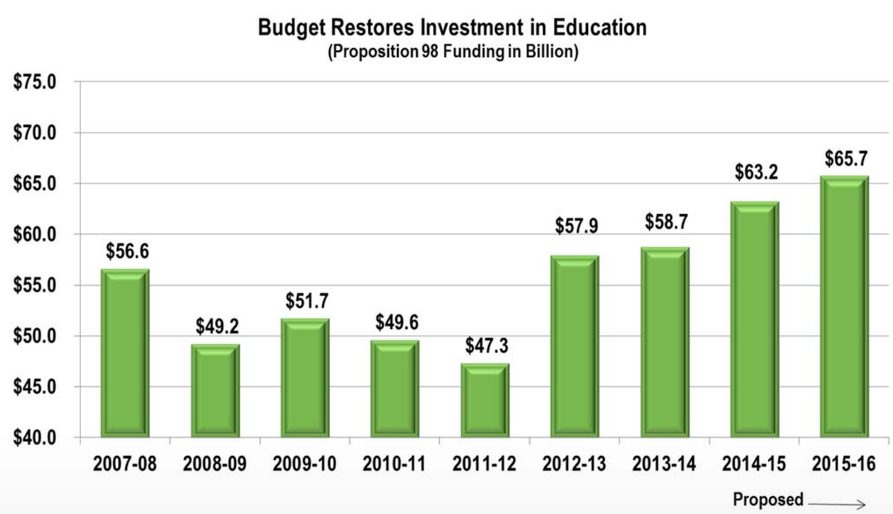
Themes for 2015-16 Governor's Budget 1

- Positive economic growth fuels public education spending
- Proposition 98 continues to receive most of the new money
- Funding is tight for the non-Proposition 98 side of the State Budget
- Governor stays the course on the Local Control Funding Formula (LCFF) and the Local Control and Accountability Plan (LCAP)
- State makes a firm commitment to Adult Education and Career Technical Education (CTE)
- The Wall of Debt continues to come down and is replaced with the Rainy Day Fund

Economic Growth Continues

- Both national and state economies continue to improve
  - Economic activity is up
  - Stronger job growth
  - Real estate prices continue to climb
  - The stock market hits new highs
    - Generates high levels of capital gain potential
- Big upside potential
  - Lower oil prices

Impact of Revenues on Proposition 98

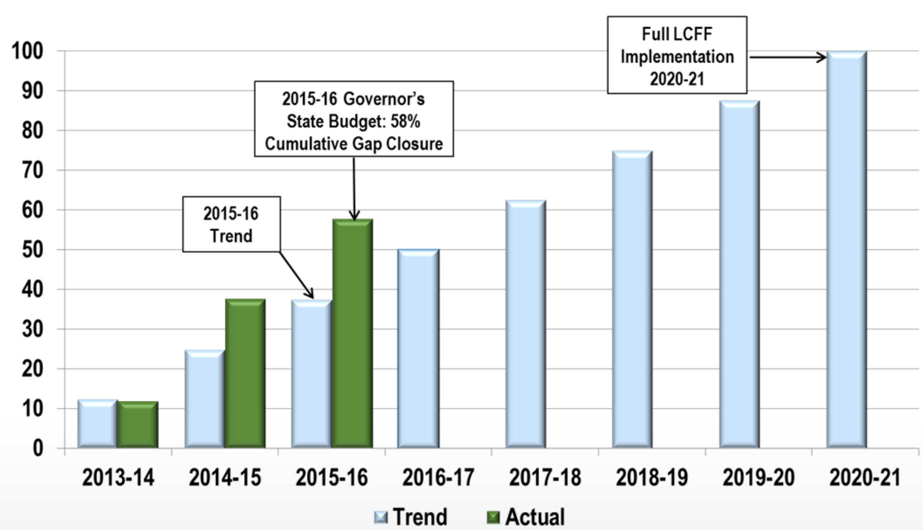


Source: Governor's State Budget Summary, page 6

2015-16 Local Control Funding Formula

- Budget proposes $4 billion for continued implementation of the LCFF
- Provides a statutory cost-of-living adjustment of 1.58% on LCFF target grants – not relevant to actual increases for individual school districts
- New funding is estimated to close the gap between 2014-15 funding levels and LCFF full implementation targets by 32.19%
- When combined with 2013-14 and 2014-15 LCFF funding, implementation progress would cover almost 58% of the gap in just three years
- 2014-15 LCFF growth provides *an average* increase in per-pupil funding of 8.7%, or $675 per average daily attendance (ADA)
  - Individual local educational agencies (LEA) experiences will vary

Progress Toward LCFF Implementation



Wall of Debt Replaced by Rainy Day Fund

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- Four years ago, then-newly elected Governor Brown declared war on the "Wall of Debt"
  - Multiple Governors have used debt to mitigate cuts, but even after economic conditions improved, the debt remained
  - Remarkably, the combination of better fiscal practices, improved economics, and Proposition 30 funding has allowed Governor Brown to reduce debt while building programs
- The move from the "Wall of Debt" to the creation of a Rainy Day Fund marks a major change in the state's approach to preparing for the next recession
- One downer is that Proposition 2, which dedicates funding for rebuilding the State Budget, came with a terrible limitation on the ability of local school boards to determine appropriate levels of reserves
  - The Governor has now opened the door to readdressing that issue

Recent Developments on the Local Cap

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- Since enactment of the current-year State Budget in June 2014, a number of triggering conditions are closer to being met:
  - Maintenance Factor – estimated at $6.6 billion with a five-year horizon before it would be fully paid
    - The Governor's State Budget shows that $1.9 billion will remain at the end of 2015-16
    - A significant revenue gain in April could fully pay the maintenance factor in the current year
  - Test 1 Funding – this has been considered unlikely, since funding under Proposition 98 has been determined in most years by Test 2 or Test 3
    - In the current year, Proposition 98 is based on Test 1
    - Strong property tax growth in 2015-16 could trigger Test 1 again

Trigger for Reserve Cap May Occur Soon

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- Full funding for enrollment growth and cost-of-living adjustment (COLA)
  - This condition is easily met because statewide K-12 enrollment has been either flat or declining and projected COLAs are expected to be below 2.6% through 2017-18
- Capital gains revenues must exceed 8% of state General Fund revenues
  - The Governor's State Budget projects this condition will be met
    - Capital gains are projected to reach 11.0% in 2014 and 9.4% in 2015
  - Historically, capital gains exceeded 8% of state General Fund revenues in six of the last ten years
- Conclusion: The cap on school district reserves could be triggered sooner than we think; therefore, this provision *must be* repealed before it becomes operative

Reserve Cap Trigger Conditions

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Reserve Cap Trigger	2014-15	2015-16	2016-17
Maintenance Factor	*Possible*	*Possible*	Probable
Test 1 Funding	Met	Probable	*Possible*
Enrollment and Growth	Met	Probable	Probable
Capital Gains	Met	Probable	*Possible*

"Unfunded" Proposals and Initiatives

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- Cost Pressures: The Governor's Budget doesn't address some of the cost pressures that school districts now face as a result of state actions – most notably retirement system rate increases
- The employer contribution costs for both California State Teachers' Retirement System (CalSTRS) and California State Public Employees' Retirement System (CalPERS) are projected to double over the next several years
  - CalSTRS – From 8.25% in 2013-14 to 19.1% in 2020-21
  - CalPERS – From 11.442% in 2013-14 to 20.4% in 2020-21
- School Facilities: The Governor's Budget Summary includes a discussion of principles, but no proposal, to spark a discussion about a radically different role for the state in supporting school construction and modernization

The "Promise" of a Return to 2007-08 Purchasing Power

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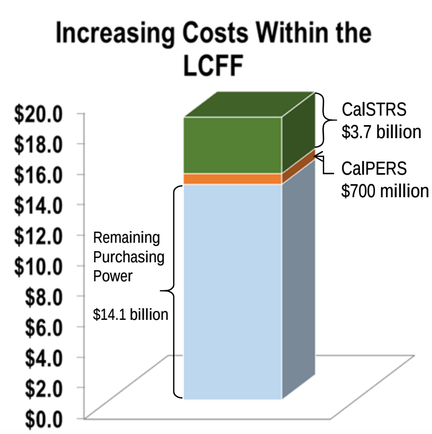
- When promoting the LCFF, the Governor promised a return to 2007-08 purchasing power
  - A modest goal, but a high water mark for California education funding
- It will take an estimated $18.5 billion to reach that goal
- Increasing costs such as CalSTRS and CalPERS erode that promise and make it difficult for districts to achieve the goals of the LCFF



May Revision Outlook

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- Upside potential for additional tax revenues
  - Expanding economy and low oil prices
  - Capital gains from stock transactions
- Remaining maintenance factor means most of the gain will come to K-14 education
  - Creates a political problem in the Legislature
    - Other General Fund programs will gain little
  - The Governor has been successful in getting his Budget priorities
- Both current-year and budget-year Proposition 98 spending should rise by billions of dollars

Longer Term Proposition 98 and LCFF Outlook

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- Total Proposition 98 revenue growth will slow after the maintenance factor is paid off
  - Revenue growth will likely follow increases in per capita personal income
    - The Test 2 factor has averaged 3.8% since 1995
  - The expiration of Proposition 30 revenues will slow Proposition 98 and LCFF growth
    - The Department of Finance's projected $976 million for gap closure in 2018-19 will not cover inflation
      - ◊ A 2.7% COLA would cost an estimated $1.2 billion

Adequacy will be a Major Challenge

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- Making the case that California schools are underfunded relative to the rest of the states is a major challenge
  - Proposition 98 – in the near term – provides major funding increases
- Other states are investing in education as well
- Proposition 98 will likely have to be amended in order to achieve real progress in advancing California's standing among the states

Questions?

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Notes

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Thank you

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