Santa Clara County Office of Education CBO Meeting

State Budget Outlook and Hot Topics

Presented by:
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Topics for Today

- The Recovery in the Stock Market
- State Revenues and the May Revision Outlook
- California State Teachers' Retirement System (CalSTRS) Unfunded Liability
- State Minimum Wage

Stock Market Decline and Recovery

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- In February we reported on the sharp decline in the Dow Jones and other market averages
  - At that time the Dow was off 1,500 points, or about 8.5%, since mid-December when the Department of Finance (DOF) staff built the Governor's Budget; most of this decline took place in the first few weeks of January
  - We noted the significant implications that a drop in the stock market could have on state General Fund revenues
    - General Fund revenues are dominated by the personal income tax
    - The top 1% earners pay about half of the income tax
    - High-income earners receive much of their income from capital gains

Stock Market Rebound

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- As of early April, the Dow Jones is trading around 17,700, fully recovering from the drop in January
- For now, this key barometer of General Fund revenues is no longer signaling a downward revision for 2016-17
  - The January Governor's Budget forecast for capital gains revenues of $13 billion should remain largely unchanged at the May Revision
- HOWEVER, the stock market is volatile and another significant drop should not be ruled out
  - Monitor this key state revenue indicator as we move toward May

Economic News

- On the broader front, the national and California economies continue to expand
  - No forecasts of a recession
  - The U.S. unemployment rate is down to 4.9%; the California rate is down to 5.7%
    - California has outpaced the U.S. in job creation for the last four years
- Federal Reserve chair Janet Yellen testified to Congress that short term interest rate hikes could threaten the recovery, given global economic weakness
  - Two, rather than four, rate hikes are now anticipated during the year

State Revenues

- General Fund revenues since the release of the January Governor's Budget are now running slightly ahead of the forecast
  - Through February, year-to-date revenues are up $442 million
    - The strong February collections of $636 million above forecast more than eliminated shortfalls in December and January
- The May Revision is on track to reinforce the January forecast
  - At this point, there are no significant developments that would signal a significant upward or downward revision

CalSTRS Unfunded Liability

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- Earlier this year, the Legislative Analyst's Office (LAO) posted a series of blogs drawing attention to administrative actions at CalSTRS that have significant implications for school employers
- The LAO found that the methodology that CalSTRS was using to allocate the unfunded liability reduced the burden on the state and increased the burden on school employers
  - The CalSTRS methodology was dubbed an "alternate universe" calculation
    - Investment gains were credited to the state
    - Higher benefit costs were assigned to the employers
- The net result is that the calculated employer liability increased from $47 billion to $58 billion, while the state's share dropped from $20 billion to $15 billion

Implications for School District Employers

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- The LAO concludes that the administrative actions of CalSTRS not reflect the principle of shared responsibility that was envisioned during the development of the legislation to hike contribution rates
  - The CalSTRS administrative actions reduce transparency and over time will make it more difficult to correct
- While employer contribution rates are fixed in law through 2020-21, thereafter the employer rate will be subject to marginal increases or decreases to reflect what is needed to exhaust the unfunded liability by 2046
  - If left unchanged, these administrative actions could result in higher employer contribution rates

Minimum Wage Hike

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- The Governor and Legislature increased the state minimum wage to $15 per hour by 2022 with the enactment of Senate Bill (SB) 3 (Chapter 4, Statutes of 2016) by Senator Mark Leno (D-San Francisco)
  - Commencing on January 1, 2017, the minimum wage will increase from $10 to $10.50 per hour for employers with 26 or more employees
  - On January 1, 2018, the minimum wage will increase to $11 per hour, with annual $1 per hour increases until reaching $15 per hour in 2022
    - From that point forward, the minimum wage will be indexed for inflation
    - Employers with 25 or fewer employees are given an additional year for implementation
- The Governor can suspend the scheduled increase under certain economic and State Budget conditions

Minimum Wage Hike

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- Economic conditions for suspension:
  - Job growth for the previous three- and six-month periods are negative and
  - Sales tax receipts for the preceding 12 months are negative
- Budget conditions for suspension:
  - General Fund in a deficit in the current year or in either of the following two fiscal years
    - ◊ Deficit is defined as a negative balance exceeding 1% of General Fund revenues
- Suspension is limited to two times

Minimum Wage and California CPI

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- In 1973, the state minimum wage was $1.65 per hour
  - Over this period, the average annual increase in the minimum wage has been 4.3%
  - At full implementation to $15 per hour, the average annual increase in the minimum wage will be 4.6%
  - The California Consumer Price Index (CPI) over the period 1973 through 2015 is 4.3%
- The increase in the minimum wage along with CalSTRS and California Public Employees' Retirement System (CalPERS) rate hikes will put pressure on local education agency budgets through this decade

Legislative Hot Topics

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- In addition to SB 799, several bills were introduced this year to address the school district reserve cap
  - SB 1249 (Bates, R-Laguna Niguel) would repeal the current law regarding the school district reserve cap; the bill does not repeal the additional reporting requirements around school district reserves
  - Assembly Bill (AB) 2689 (Gray, D-Merced) would delete the numerical cap of two or three times the minimum reserve level for school districts and would instead replace those numbers with blanks
    - This author introduced the same legislation last year, which was not heard in committee

Legislative Hot Topics

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- About a dozen bills were introduced this year with the intent to help address the current teacher and substitute teacher shortage:
  - AB 2122 (McCarty, D-Sacramento) would establish the California Classified School Employee Teacher Credentialing Program to recruit and financially support classified school employees to enroll in a teacher training program
  - AB 2336 (Olsen, R-Modesto) would, until January 1, 2022, require the California Commission on Teacher Credentialing to issue “Emergency Special Education Substitute Teaching Permits”, authorizing the holder to serve as a special education substitute teacher for up to 40 days for any one teacher during a school year
  - AB 2401 (O’Donnell, D-Long Beach) would reestablish the Beginning Teacher Support and Assessment (BTSA) System, including appropriating an unspecified amount to provide grants for BTSA participants

Legislative Hot Topics

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- Introduced ahead of a ruling on the *Vergara v. California* lawsuit, Assembly Member Susan Bonilla (D-Concord) would tackle some of the laws being challenged through AB 934
  - Among its numerous provisions, AB 934 would allow a school board to require a certificated employee to continue to be classified as a “probationary” employee for a third or fourth year under certain conditions
  - The bill would also change the order for terminating certificated employees:
    1. Probationary employees who received below satisfactory reviews.
    2. Permanent employees without satisfactory reviews.
    3. Probationary employees with satisfactory reviews.
    4. Permanent employees with satisfactory reviews.
  - With the inevitable opposition of the California Teachers Association, this bill has a slim chance for success

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Thank you!


100%
80%
50%
Success
Vision
Process
Action
Plan
Analysis
Implement
Development