

Democratic Budget Proposal

by Adonai Mack, Legislative Advocate

August 17, 2010

After returning from their summer break, the Democratic leaders, Senator Steinberg and Speaker Perez released their latest budget proposal to close the state's budget shortfall. Consequently, the Joint Legislative Budget Conference Committee closed out the remaining open items on the state budget. This sets the stage for a possible floor vote next week. Of course, the governor and the leadership of the Republican Caucus denounced the proposal as soon as the ink dried.

The Democratic proposal includes a combination of program cuts (\$8.3 billion), additional revenue, a suspension of Proposition 98 and a modest reserve. Below the chart shows a breakdown for the solutions designed in the Democratic proposal.

A summary of the Conference Committee's solutions, by category, is shown below. Starting Problem (per May Revision)	-\$17.9 billion
Solutions:	
Expenditure Reductions	\$8.3 billion
Federal Funds	4.1 billion
Additional Revenues	2.4 billion
➤ <i>LAO update revenue forecast</i>	<i>(1.4 billion)</i>
➤ <i>Corporate tax break delays, Oil severance tax, tax reform package</i>	<i>(4.5 billion)</i>
➤ <i>Tax enforcement measures</i>	<i>(0.2 billion)</i>
➤ <i>Adjustment: Prop. 98</i>	<i>(-3.2 billion)</i>
➤ <i>Adjustment: Revenues dedicated to Public Safety restructuring</i>	<i>(-0.5 billion)</i>
Alternative Funding	1.0 billion
Fund Shifts, Other	2.7 billion
Total Solutions	\$18.5 billion
Reserve	\$535 million

Education Budget

The education budget presented by the Democratic caucus is a mixed bag of euphoria and disappointment. The education budget provides \$52 billion which is \$3 billion more than the governor's budget proposal that funds Proposition 98 with \$49 billion. This funding level would restore all proposed cuts in the May Revision including the \$1.5 billion reduction to revenue limits, the \$1.4 billion elimination of child care, or the \$230 million associated with a negative cost of living adjustment (COLA). Further, the proposal also includes an additional \$1.3 billion to \$4 billion of one-time funding to payoff past mandate claims.

However, the proposal simultaneously suspends the Proposition 98 minimum guarantee. A suspension of Proposition 98 allows the Legislature to fund non- Proposition 98 programs while funding education above the governor’s proposal. Democratic leadership argues that a suspension eliminates any ambiguity over the creation of a maintenance factor or any attempts to manipulate the Proposition 98 guarantee.

Through the Budget Conference Committee, the Legislature closed several items to finish up their work thereby giving the budget some meat. These items include the following:

❖ **State Mandates** – Provides an additional \$1.3 billion to \$4 billion of one-time money to schools to pay off past mandate claims and court-ordered settlements. In an attempt to handle several ongoing issues with state mandates, the Conference Committee adopted several changes that will determine how mandates are addressed. State mandates were approached by addressing past mandated costs, examining the existing mandates and attempting to reform or eliminate some mandates. In order to address past mandated cost claims, the budget would establish a statewide local school district Joint Powers Authority (JPA) to enable school districts to accelerate the mandate funds. This JPA concept is based on the successful JPA used by local governments last year to accelerate the \$2 billion in Prop 1A suspension repayments. This would be accomplished by establishing a Joint Power Authority (JPA) that would allow school districts and local districts to opt-in to get immediate repayment of their mandate obligations this year. Under the proposal:

- School districts and local governments would assign their annual mandate payments to the JPA.
- The JPA would then pledge to sell securities to outside investors with the proceeds of the sale going immediately to participating school districts and local governments.
- The state would make its annual payments for past mandates which would be sufficient to pay-off principal and interest on the securities.

The specifics as to how successful this JPA proposal will be or the impact on Proposition 98 are unclear. However, local government has used a similar proposal to ensure that local government would receive their resources. Local governments have used the JPA model to successfully receive resources from the Vehicle License Fee shift and the Prop 1A shift in the past. ACSA will continue to monitor the budget language associated with this proposal to ensure it protects education funding.

❖ **Mandate Reform** – The budget also includes a suspension of several mandates and modifies others. Further, the budget includes direction that a working group is formed to examine additional reforms. It is unclear what the specific changes are for those mandates that are modified or cleaned up. At this time, the language changing these mandates is not complete. The following is the list of suspended, modified or technical cleaned up mandates. Those not listed will continue per current law.

- Suspended – Pupil Residency Verification and Appeals (K-12)
Scoliosis Screening (K-12)
Physical Performance Tests (K-12)
Removal of Chemicals (K-12)
Financial and Compliance Audits (K-12)
Pupil Promotion and Retention (suspend three required activities) (K-12)
Student Accountability Report Card (suspend three required activities) (K-12)
Law Enforcement Jurisdiction Agreements (CCC)
Integrated Waste Management (CCC)

- Modified – Truancy Notification
Truancy Habitual Truants
Collective Bargaining Mandate
- Technical – Teacher Incentive Program
Physical Education Reports

- ❖ **Special Disability Adjustment (SDA)** – The Conference Committee voted to continue with the existing SDA formula in 2009-10 and 2010-11, but to repeal it by July 1, 2011. In an effort to move this issue along quicker, a bill authored by Assemblyman Block, AB 184 was amended to include this extension. AB 184 was passed by the Senate Education Committee and the Senate Appropriations Committee last week. It is expected to move through the legislative process quickly for an expected signature by the governor. The conference committee also appropriated \$300,000 to the California Department of Education in order to contract for a study that includes several items:
 1. A summary of the extent to which the incidence of severe disabilities are evenly or unevenly distributed across the state;
 2. A determination of whether any observed differences in incidence have significant effect on the relative costs to SELPAs for providing special education services;
 3. Suggested methods for adjusting the state’s funding formula that do not create inappropriate fiscal incentives for identifying students as needing special education.
- ❖ **Education Technology (EETT) Grants:** The Committee approved a compromise that would provide \$5 million in funding for the current competitive grants and would set aside \$30 million for a new competitive grant program aimed at high school students based on college and career readiness.
- ❖ **Court School funding** – The Committee voted to hold county court schools harmless from 2010-11 revenue limit reductions proposed by the governor. Further, the budget proposal provides approximately \$3 million in Economic Impact Aid funding to county court schools beginning in 2010-11, but ensures that students in county courts schools receive the required instructional minutes.
- ❖ **AB 3632 Mental Health Funding** – The Conference Committee rejected the governor’s proposal to eliminate the state mandate on counties to provide special education mental health related services pursuant to AB 3632 in 2010-11. They also approved reduction of \$52 million from the General Fund (GF) to the Department of Mental Health for payment of AB 3632 mandate claims in 2010-11. In an effort to pay prior year mandates, the Committee included \$133 million in GF monies for the Commission on State Mandates to pay claims. The Committee appropriated \$3 million in one-time federal special education (IDEA) funds so that the CDE can contract for statewide technical assistance to SELPAs regarding best practices in mental health related service delivery for students with disabilities beginning in 2010-11. The Committee also approved the establishment of a work group to study if and how this mandate might be shifted to schools in the future.
- ❖ **Child Care:** The Committee rejected the governor’s cuts to child care, but also acted to take from local reserves all funding in excess of 5 percent of the local LEAs child care funding, or \$2,000, whichever is less, based upon local reserves reported in the 2009-10 budget year. They also approved language that would henceforth limit child care program reserves to no more than 5 percent or \$2,000, whichever is less. The Committee also directed the state Department of Education to commence investigation of potential local over-payments and fraud in all state and federally funded child care programs.

Tax Proposal

The proposed tax reform attempts to increase those taxes that are federally deductible taxes while also reducing the state sales tax. The tax proposal increases the State Personal Income Tax (PIT) by 1 percent except for the highest tax bracket. It is believed that this would flatten the tax structure thereby reducing the reliance on the top income bracket and reduce personal income tax volatility. The proposal would also increase the Vehicle License Fee (VLF) by .5 percent and dedicate those resources to public safety. Both the PIT and the VLF are tax deductible for federal purposes. Alternatively, the State Sales Tax would be decreased by 2.5 percent by 2011-12 (1.75 percent in 2010-11 and .75 percent in 2011-12).

The other tax changes include delaying for two years the start of new corporate business tax breaks scheduled to take effect in 2010-11 and creating an oil severance tax for California. These changes would generate \$4.5 billion additional revenues.

ACSA Analysis

On its surface the Democratic proposal sounds like a great compromise. And that is exactly what it should have been, a compromise. However, the Democratic leadership seems to be negotiating against themselves. If you will recall the first iteration of the Assembly Jobs Budget included an education budget of \$54 billion. Now the budget contains a funding level of \$52 billion and a suspension of the minimum guarantee. Without any pressure from the governor or the Republican Caucus, the Democrats have already started to make concessions. If ACSA was certain that this proposal would be the final budget, we would consider supporting this proposal in full. Unfortunately, this proposal has yet to gain support from the governor or the Republican Caucus. As soon as the ink was dry on the Democratic proposal, the governor and the Republican Caucus denounced the plan because of the revenue package which is instrumental in balancing the proposal. It is unclear if any members of the Republican Caucus will vote for the tax plan proposed in the budget.

In addition, there are some components of the budget plan that are significantly underdeveloped so far. For example, it is unclear if the JPA plan for state mandates will truly be effective for education. ACSA has spoken to representatives from local government who are experienced with implementing the JPA model and they feel confident that this could be effective. However, the interplay between education funding and governance often leads to different outcomes than those experienced in other areas of the state budget.

It is still likely that the Legislature will attempt to vote on a budget in the coming weeks, but less likely that it will pass the first time around. With session ending at the end of the month and an important November election looming, the pressure to pass the state budget will continue to increase. While many believe that the budget impasse could last well into the fall months, many others believe that it is just as likely that a budget could be completed simultaneously with the end of the legislative session.