

**TO:** Marin County Superintendents  
**FROM:** Terena Mares, Deputy Superintendent  
**SUBJECT:** Legislative Analyst’s Annual Fiscal Outlook

**DATE:** November 26, 2014

On November 19, the Legislative Analyst (LAO) issued his annual independent assessment of California’s economy and demographics entitled "California's Fiscal Outlook". This LAO “November Forecast” provides revised projections of General Fund revenues and expenditures for the five-year period: 2015-16 through 2019-20.

**OVERVIEW**

Citing strong growth in stock, real estate and labor markets, the LAO is now projecting \$2.055 billion in higher general fund revenue in the current and prior year. In addition, higher-than-expected local property tax collections will generate \$374 million of increased revenue that will provide relief to the state general fund during this same time period.

In the budget year (2015-16), the LAO now estimates that California’s slow economic recovery will continue and that General Fund revenues will increase from \$107.4 billion in 2014-15 to \$111.4 billion in 2015-16 (see Figures 1 and 4 below). The LAO attributes most of this revenue growth to \$2.7 billion in higher personal income tax revenues, \$1.2 billion in increased sales tax collections, and \$893 million in higher corporate tax revenues. It is worth noting, however, that this LAO revenue forecast for 2015-16 is \$2.4 billion lower than the projection made one year ago in the November, 2013 Fiscal Outlook.

**Figure 1**  
**LAO General Fund Condition Under Main Scenario<sup>a</sup>**

*(In Millions)*

	2013-14	2014-15	2015-16
Prior-year fund balance	\$2,186	\$3,680	\$836
Revenues and transfers	102,277	107,442	111,397
Expenditures	100,783	110,286	110,638
Difference between revenues and expenditures	\$1,494	-\$2,843	\$760
Ending fund balance	\$3,680	\$836	\$1,596
Encumbrances	-955	-955	-955
SFEU balance	2,725	-119	641
<b>Reserves</b>			
SFEU balance	\$2,725	-\$119	\$641
Pre-Proposition 2 BSA balance	—	1,606	1,606
Proposition 2 BSA balance	—	—	1,974
<b>Total Reserves</b>	<b>\$2,725</b>	<b>\$1,488</b>	<b>\$4,222</b>

<sup>a</sup> Includes Education Protection Account created by Proposition 30 (2012).  
SFEU = Special Fund for Economic Uncertainties (the General Fund’s traditional budget reserve) and  
BSA = Budget Stabilization Account.

Figure 4

**LAO Revenue Outlook (Main Economic Scenario)**

*General Fund and Education Protection Account Combined (Dollars in Millions)*

	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
Personal income tax	\$66,667	\$72,201	\$74,932	\$78,011	\$81,521	\$83,055	\$84,054
Sales and use tax	22,251	23,420	24,653	25,433	26,029	27,238	28,418
Corporation tax	8,519	9,482	10,375	10,287	10,240	10,562	11,163
Subtotals, "Big Three" taxes	\$97,437	\$105,103	\$109,960	\$113,732	\$117,790	\$120,855	\$123,635
Percent change from prior year	—	7.9%	4.6%	3.4%	3.6%	2.6%	2.3%
Insurance tax	\$2,371	\$2,435	\$2,512	\$2,593	\$2,687	\$2,771	\$2,854
Other revenues	2,093	2,050	2,018	1,909	1,940	1,935	1,928
Transfers to Pre-Proposition 2 BSA	—	-1,606	—	—	—	—	—
Transfers to Proposition 2 BSA	—	—	-1,974	-1,288	-1,122	-940	-963
Transfers and loans	376	-540	-1,118	-926	-208	-288	-5
<b>Totals, Revenues and Transfers<sup>a</sup></b>	<b>\$102,277</b>	<b>\$107,442</b>	<b>\$111,397</b>	<b>\$116,020</b>	<b>\$121,087</b>	<b>\$124,335</b>	<b>\$127,449</b>
Percent change from prior year	—	5.1%	3.7%	4.2%	4.4%	2.7%	2.5%

<sup>a</sup> Totals reflect transfers out of the General Fund to the Budget Stabilization Account (BSA). As such, this is not directly comparable to revenue displays in prior LAO publications.

**K-14 EDUCATION / PROPOSITION 98 SUMMARY**

As a result of continuing strength in California’s fiscal outlook, the elimination of all but \$992 million in K-14 cross-year deferrals and the state’s debt repayment obligations under Proposition 98, the LAO is now forecasting that the Governor’s January 2015-16 budget will be able to:

- End all remaining cross-year deferrals, and
- Provide in excess of \$8 billion in one-time and ongoing funds to schools and community colleges.

Specifically, the LAO is now estimating that the current year minimum funding guarantee for K-14 schools (Proposition 98) will be \$63.2 billion or **\$2.35 billion** higher than the enacted 2014-15 Budget (Figure 3). The LAO is also projecting that local property tax collections will increase by \$259 million. Accordingly, the amount of additional GF expenditures required to meet the revised, 2014-15 Proposition 98 guarantee is only \$2.1 billion.

Figure 3

**Updating Estimates of 2013-14 and 2014-15 Minimum Guarantees**

*(Dollars in Millions)*

	2013-14			2014-15		
	2014-15 Budget Plan	November LAO Estimates	Change	2014-15 Budget Plan	November LAO Estimates	Change
<b>Minimum Guarantee</b>						
General Fund	\$42,731	\$42,794	\$63	\$44,462	\$46,548	\$2,086
Local property tax	15,571	15,686	114	16,397	16,656	259
<b>Totals</b>	<b>\$58,302</b>	<b>\$58,479</b>	<b>\$177</b>	<b>\$60,859</b>	<b>\$63,204</b>	<b>\$2,345</b>
<b>Operative Test</b>	3	3	—	1	1	—
<b>K-12 ADA</b>	5,982,431	5,992,567	10,136	5,975,558	5,985,682	10,124
<b>New Maintenance Factor:</b>						
Created	\$458	\$381	-\$77	—	—	—
Paid	—	—	—	\$2,583	\$3,843	\$1,260

ADA – average daily attendance.

In 2015-16, the LAO is projecting that the K-14 (Proposition 98) spending level will be \$65.810 billion or \$2.6 billion higher than the updated current-year level. Significantly, because the bulk of cross-year

K-14 deferrals were eliminated in the current year, the LAO forecasts that \$6.4 billion will be available for new K-14 spending in 2015-16 under the Proposition 98 guarantee.

The LAO also provided estimates for K-14 education revenue throughout the forecast period (see Figure 6 below). The LAO projects annual increases in the minimum guarantee of \$2 to \$3 billion from 2016-17 through 2019-20. In 2018–19 and 2019–20, slightly more modest annual growth in the minimum guarantee is projected as the temporary personal income revenues enacted by Proposition 30 phase out.

**Figure 6**

**Proposition 98 Outlook**

<i>LAO Main Scenario (Dollars in Billions)</i>						
	2014-15	2015-16	2016-17	2017-18	2018-19	2019-20
<b>Minimum Guarantee</b>						
General Fund	\$46.5	\$46.4	\$47.6	\$48.7	\$49.4	\$49.9
Local property tax	16.7	19.4	20.5	21.9	23.3	24.6
<b>Totals</b>	<b>\$63.2</b>	<b>\$65.8</b>	<b>\$68.1</b>	<b>\$70.6</b>	<b>\$72.7</b>	<b>\$74.5</b>
<b>Change In Guarantee From Prior Year</b>						
Amount	\$4.7	\$2.6	\$2.3	\$2.5	\$2.1	\$1.8
Percent change	8.1%	4.1%	3.4%	3.7%	2.9%	2.5%
<b>Change In General Fund From Prior Year</b>						
Amount	\$3.8	-\$0.1	\$1.1	\$1.2	\$0.6	\$0.6
Percent change	8.8%	-0.3%	2.4%	2.4%	1.3%	1.1%
<b>Change In Local Property Tax From Prior Year</b>						
Amount	\$1.0	\$2.7	\$1.1	\$1.4	\$1.4	\$1.3
Percent change	6.2%	16.4%	5.8%	6.7%	6.5%	5.4%
<b>Maintenance Factor Created/Paid (+/-)</b>	<b>-3.8</b>	<b>—</b>	<b>—</b>	<b>0.8</b>	<b>1.6</b>	<b>1.7</b>
<b>Key Factors</b>						
Proposition 98 "Test"	1	2	3	3	3	3
K-12 average daily attendance	-0.1%	-0.4%	-0.5%	-0.4%	-0.4%	-0.3%
Per capita personal income (Test 2)	-0.2	4.1	4.0	5.4	5.6	5.1
Per capita General Fund (Test 3)	7.4	4.4	3.4	3.6	2.6	2.2
K-14 cost-of-living adjustment	0.9	1.6	2.1	2.4	2.7	2.9
Assessed property values	6.1	5.5	5.3	6.2	6.4	5.8
<b>Public School Stabilization Account Deposit?</b>	<b>—</b>	<b>No</b>	<b>No</b>	<b>No</b>	<b>No</b>	<b>No</b>

The November LAO Fiscal Outlook is significant to school district budget planning as it represents the first revenue projection adjustment since the enactment of the current budget and serves as a possible preview of the Governor’s January budget. For the third consecutive year it affirms continued strength in California’s economy, robust growth in education spending and underscores the validity of revenue projections (contained in the FCMAT/BASC LCFF Calculator). While some of the increases – particularly the amount of spending owed to schools under the Proposition 98 guarantee – are even more positive than expected, the LAO clearly acknowledges that there is significant upside risk on revenues if the stock market performs well in the coming months. While the Governor’s January budget will likely contain lower budget-year revenue projections than the LAO Forecast, school district leaders can safely expect strong short-term increases in K-14 (Proposition 98) and LCFF gap funding levels above the current 2014-15 budget.

***CalSTRS Rate Increases Also Phasing in Over Period*** - Based upon legislation adopted in 2014 that is designed to address outstanding CalSTRS' liabilities, school and community college districts' contribution rates are set to increase beginning in 2014–15 and every year thereafter of the forecast period. In 2014–15, the rate increase is 0.63 percent (for a total district contribution rate of 8.88 percent). By the last year of the forecast period, the total cumulative rate increase is 9.88 percent (for a total district contribution rate of 18.13 percent). CalSTRS estimates that districts' contribution costs will be \$3.1 billion higher in 2019–20 compared to 2014–15. Under the LAO's main scenario, the minimum guarantee in 2019–20 is \$11.3 billion higher than 2014–15. So, approximately 30 percent of all new funding will have to go to paying STRS obligations.

***No Deposit Into Public School System Stabilization Account (PSSSA) Projected*** - Proposition 2, approved by voters in November 2014, created a new reserve—the PSSSA. Proposition 2 is connected with a recently enacted state law that triggers a reduction in school district reserve levels the year after the state makes a deposit into the PSSSA. Under the LAO's main revenue scenario the state would not make a deposit into the PSSSA. This is primarily because of the Proposition 98 maintenance factor that has yet to be repaid. The cap on school district reserve levels therefore would not be triggered at any time during the forecast period.