

## **Governor Unveils May Revision Changes to 2015-16 State Budget**

Earlier this morning, Governor Brown released his “May Revision” to the 2015-16 Budget, including his adjusted proposals for public education. The Governor now projects an additional \$6.7 billion in state revenues above January estimates, with K-14 schools receiving \$5.5 billion of this new state general fund revenue. Moreover; with local property tax collection estimates also increasing, total K-14 spending will increase by over \$6 billion from the Governor’s January estimates.

The May Revision to the Budget clearly shows that the state’s economy has picked up and that revenues have surged beyond expectations. However, the Governor continues to stress that the state’s finances remain somewhat precarious with the possibility of future deficits. As a result, the May Revision continues to focus on the key elements of the January Budget — carrying out the Local Control Funding Formula, federal health care reform, public safety realignment, the Water Action Plan, and the Cap and Trade expenditure plan and maintains fiscal restraint and prudence. However, because of the Proposition 98’s formula, there is significant new revenue for K-14 schools.

### **General Fund and Proposition 98 Revenue Adjustments**

The Governor’s revised budget now estimates General Fund (GF) revenues will be \$6.7 billion higher over the three-year forecast period (2013-14, 2014-15, and 2015-16). The specific revenue estimate changes include:

- \$1.05 billion in increased GF revenue in 2013-14.
- \$3.265 billion in increased GF revenue in the current year (2014-15).
- \$2.287 billion in increased GF revenue in the budget year (2015-16).

Unlike last year’s May Revision, when the combination of higher current year revenue and lower budget year revenue produced an actual decrease in Proposition 98 Maintenance Factor obligations and projected spending in 2014-15, the Governor now estimates Proposition 98 spending to increase in 2015-16 to \$68.4 billion. This is an increase of \$2.7 billion from January.

The extraordinary increase in GF revenue over three years, combined with higher local property tax collections produces a \$6.1 billion upward adjustment in Proposition 98 spending in the May Revision, as follows:

- \$240 million in increased K-14 spending in 2013-14.
- \$3.1 billion in increased K-14 spending in the current year (2014-15).
- \$2.7 billion in increased K-14 spending in the budget year (2015-16).

While much of the new education spending proposed by the Governor will be in one-time investments, K-12 schools receive \$2.4 billion in additional ongoing spending—including an additional \$2.1 billion in 2015-16 LCFF gap funding for school districts and charters.

### **Long Term Economic Forecast**

The Governor’s May Revision continues to project slow growth over the next five years; acknowledging that the “economic forecast has improved somewhat since the Governor’s January Budget”. General Fund revenues are \$6.7 billion higher over these years. The May Revision (Figure REV-01) compares the revenue forecasts, by source, in the Governor’s Budget and the May Revision. Total May Revision revenue, including transfers, is projected to be \$111.3 billion in 2014-15 and \$115 billion in 2015-16.

Figure REV-01  
2015-16 May Revision  
General Fund Revenue Forecast  
(Dollars in Millions)

| Source   | Governor's<br>Budget | May<br>Revision  | Change         |             |
|--|----------------------|------------------|----------------|-------------|
| <b>Fiscal 13-14: Final</b>                       |                      |                  |                |             |
| Personal Income Tax                              | \$66,560             | \$67,025         | \$466          | 0.7%        |
| Sales and Use Tax                                | 22,263               | 22,263           | 0              | 0.0%        |
| Corporation Tax                                  | 8,858                | 9,093            | 234            | 2.6%        |
| Insurance Tax                                    | 2,363                | 2,363            | 0              | 0.0%        |
| Alcoholic Beverage                               | 354                  | 354              | 0              | 0.0%        |
| Cigarette  | 86                   | 86               | 0              | 0.0%        |
| Other Revenues                                   | 1,813                | 1,814            | 0              | 0.0%        |
| <b>Subtotal</b>                                  | <b>\$102,298</b>     | <b>\$102,998</b> | <b>\$700</b>   | <b>0.7%</b> |
| Transfers  | 376                  | 376              | 0              | 0.0%        |
| <b>Total</b>                                     | <b>\$102,675</b>     | <b>\$103,375</b> | <b>\$700</b>   | <b>0.7%</b> |
| <b>Fiscal 14-15</b>                              |                      |                  |                |             |
| Personal Income Tax                              | \$71,099             | \$75,384         | \$3,686        | 5.1%        |
| Sales and Use Tax                                | 23,438               | 23,684           | 246            | 1.0%        |
| Corporation Tax                                  | 9,618                | 9,809            | 191            | 2.0%        |
| Insurance Tax                                    | 2,490                | 2,486            | -4             | -0.2%       |
| Alcoholic Beverage                               | 367                  | 353              | -14            | -3.7%       |
| Cigarette  | 84                   | 84               | 0              | 0.0%        |
| Other Revenues                                   | 1,954                | 1,556            | -398           | -20.4%      |
| College Access Transfer                          | 600                  | 4                | -596           |             |
| <b>Subtotal</b>                                  | <b>\$110,250</b>     | <b>\$113,361</b> | <b>\$3,110</b> |             |
| Other Transfers <sup>(1)</sup>                   | -2,208               | -2,054           | 154            | -7.0%       |
| <b>Total</b>                                     | <b>\$108,042</b>     | <b>\$111,307</b> | <b>\$3,265</b> | <b>3.0%</b> |
| <b>Fiscal 15-16</b>                              |                      |                  |                |             |
| Personal Income Tax                              | \$75,213             | \$77,700         | \$2,487        | 3.3%        |
| Sales and Use Tax                                | 25,166               | 25,240           | 74             | 0.3%        |
| Corporation Tax                                  | 10,173               | 10,342           | 168            | 1.7%        |
| Insurance Tax                                    | 2,531                | 2,556            | 26             | 1.0%        |
| Alcoholic Beverage                               | 374                  | 360              | -14            | -3.7%       |
| Cigarette  | 82                   | 82               | 0              | 0.0%        |
| Other Revenues                                   | 1,594                | 1,652            | 59             | 3.7%        |
| College Access Transfer                          | 350                  | 100              | -250           |             |
| <b>Subtotal</b>                                  | <b>\$115,482</b>     | <b>\$118,031</b> | <b>\$2,549</b> | <b>2.2%</b> |
| Other Transfers <sup>(1)</sup>                   | -2,102               | -2,999           | -897           | 42.7%       |
| <b>Total</b>                                     | <b>\$113,380</b>     | <b>\$115,033</b> | <b>\$1,653</b> | <b>1.5%</b> |
| <b>Three-Year Total (including BSA transfer)</b> |                      |                  | <b>\$5,617</b> |             |

Note: Numbers may not add due to rounding.

<sup>(1)</sup> Includes transfers to Budget Stabilization Account for 2014-15 and 2015-16.

The administration points to the improved economic forecast, along with strong current year cash collection through April to justify the significant projected increase in revenue.. The May Revision reports that cash tax receipts are up about \$3.2 billion over the forecast through the end of April. Cash data through April suggest that personal income tax receipts are up about \$2.7 billion, corporation tax receipts are up almost \$250 million, and sales and use tax (sales tax) receipts are up \$230 million. The Governor's revenue forecast for the three open revenue years (2013-14, 2014-15 and 2015-16) includes the following changes:

- Personal income taxes are higher by \$466 million in 2013-14, \$3.3 billion in 2014-15, and \$2.3 billion in 2015-16 due to strong withholding growth, as well as growth in capital gains and partnership income.
- Sales tax receipts are higher by \$246 million in 2014-15 and \$74 million in 2015-16. Much of the current-year revenue gain is attributable to lower utilization of the recent manufacturing sales tax exemption in the first two quarters of 2014-15.
- Corporation taxes are higher by \$234 million in 2013-14, \$60 million in 2014-15, and \$100 million in 2015-16 due to strong cash trends.

The May Revision economic forecast sees steady growth over the next four years. The projected average growth rate in U.S. real gross domestic product over the next four years is 2.6%. While the forecast does not project a recession, the Governor notes that the current expansion has already exceeded the average post-war expansion by over a year.

May Revision figure REV-02 below shows the forecast for the largest three General Fund revenues from 2013-14 through 2018-19. Total General Fund revenue from these sources is expected to grow from \$98.4 billion in 2013-14 to \$123.5 billion in 2018-19. The average year-over-year growth rate over this period is 4.8%

Figure REV-02  
Long-Term Revenue Forecast - Three Largest Sources  
(General Fund Revenue - Dollars in Billions)

|                     | 2013-14       | 2014-15        | 2015-16        | 2016-17        | 2017-18        | 2018-19        | Average<br>Year-Over-Year<br>Growth |
|---------------------|---------------|----------------|----------------|----------------|----------------|----------------|-------------------------------------|
| Personal Income Tax | \$67.0        | \$75.4         | \$77.7         | \$81.7         | \$84.7         | \$84.2         | 4.7%                                |
| Sales and Use Tax   | \$22.3        | \$23.7         | \$25.2         | \$25.8         | \$25.9         | \$27.1         | 4.0%                                |
| Corporation Tax     | \$9.1         | \$9.8          | \$10.3         | \$11.1         | \$11.7         | \$12.2         | 6.1%                                |
| <b>Total</b>        | <b>\$98.4</b> | <b>\$108.9</b> | <b>\$113.3</b> | <b>\$118.5</b> | <b>\$122.2</b> | <b>\$123.5</b> | <b>4.8%</b>                         |
| Growth              | 6.1%          | 10.7%          | 4.0%           | 4.6%           | 3.2%           | 1.0%           |                                     |

Note: Numbers may not add due to rounding.

### K-12 Budget Adjustments

**Mandate Payments: Common Core and Other Local Priorities** — The January Budget proposed \$1.1 billion in discretionary one-time Proposition 98 mandate repayments for school districts, charter schools, and county offices of education. The May Revision expands on the January proposal by proposing an additional \$2.4 billion in Proposition 98 resources for a total of \$3.5 billion in one-time funding. The Governor identifies investments in professional development, teacher induction to beginning teachers, and instructional materials and technology as likely expenditures that LEAs will make with these funds. All of the funds provided will offset any applicable mandate reimbursement claims for these entities, which builds off the approach in the 2014 Budget Act where one-time funding was provided for both general purpose activities and mandates reimbursement.

From these funds, the Governor earmarks \$40 million for county offices of education (\$20 million per year in 2015-16 and 2016-17) to assist schools in meeting new LCAP responsibilities required under the accountability structure of the LCFF. The May Revision underscores that these discretionary, mandate reimbursements are intended as a “two-year investment” to substantially reduce the outstanding mandates debt owed to local educational agencies, consistent with the Administration’s goal to pay down debt.

**Local Control Funding Formula** — The May Revision significantly increases funding for the formula by providing an additional \$2.1 billion in LCFF gap funding to school districts and charters — building upon the \$4 billion provided in the January Budget. This \$6.1 billion increases funding from 32.1 to 53% of the remaining LCFF gap in 2015-16.

**Career Technical Education** — The January Budget proposed \$250 million in one-time Proposition 98 funding in each of the next three years to support a transitional Career Technical Education (CTE) Incentive Grant Program. School districts, county offices of education, and charter schools receiving funding from the program would be required to provide a dollar-for-dollar match each year. The May

Revision proposes an additional \$150 million in 2015-16 for the first year of this transition program, an additional \$50 million in 2016-17, and a reduction of \$50 million in 2017-18. This adjusted schedule of funding will better allow schools to transition to entirely using their own discretionary funds by 2018-19.

The May Revision also proposes a series of other changes to the Administration's January proposal on CTE, including:

- Increases the minimum local-to-state funding match requirement to 1.5:1 in 2016-17 and 2:1 in 2017-18, to assist local educational agencies' transition in supporting CTE with their Local Control Funding Formula apportionments and other existing resources after this program expires.
- Eliminates Career Pathways Trust from the list of allowable sources of local matching funds.
- Directs CDE and the State Board of Education to give funding priority to applicants administering programs located in rural districts or regions with high student dropout rates.

**Quality Education Investment Act Transition Funding** – The May Revision provides an increase of \$4.6 million one-time Proposition 98 General Fund to provide half of the final apportionment of Quality Education Investment Act (QEIA) funding to selected school districts in 2015-16 that do not qualify for concentration grant funding under the Local Control Funding Formula. This funding will help ease the transition off QEIA funding for districts with isolated concentrations of English learners and students who qualify for free or reduced-priced meals.

**Simon Wiesenthal Center** — The May Revision includes an increase of \$2 million Proposition 98 General Fund for the Los Angeles County Office of Education to contract with the Simon Wiesenthal Center to support the Museum of Tolerance's "Tools for Tolerance" training programs. These funds allow the center to partner with schools throughout the state to advance anti-bias education, inclusion, and equity through professional development programs.

**Local Property Tax Adjustments** — A decrease of \$123.3 million Proposition 98 General Fund in 2014-15 for school districts, special education local plan areas, and county offices of education as a result of higher offsetting property tax revenues. A decrease of \$224 million Proposition 98 General Fund in 2015-16 for school districts, special education local plan areas, and county offices of education as a result of higher offsetting property tax revenues.

**Average Daily Attendance** — The May Revision provides an increase of \$94.4 million in 2014-15 and an increase of \$173.5 million in 2015-16 for school districts, charter schools, and county offices of education under the Local Control Funding Formula as a result of an increase in 2013-14 average daily attendance (ADA), which drives projections of ADA in both 2014-15 and 2015-16.

**Proposition 39** — The California Clean Energy Jobs Act was approved by voters in 2012, and increases state corporate tax revenues. For 2013-14 through 2017-18, the measure requires half of the increased revenues, up to \$550 million per year, to be used to support energy efficiency projects. The May Revision decreases the amount of energy efficiency funds available to K-12 schools in 2015-16 by \$6.7 million to \$313.4 million to reflect reduced revenue estimates.

**Categorical Program Growth** — The May Revision includes a decrease of \$18.4 million Proposition 98 General Fund for selected categorical programs, based on updated estimates of projected ADA growth.

**Cost-of-Living Adjustments** — A decrease of \$22.1 million Proposition 98 General Fund to selected categorical programs for 2015-16 to reflect a change in the cost-of-living factor from 1.58 percent at the Governor’s Budget to 1.02 percent at the May Revision.

**K-12 Mandated Programs Block Grant** — The May Revision includes an increase of \$1.2 million Proposition 98 General Fund to reflect greater school district participation in the mandates block grant. This additional funding is required to maintain statutory block grant funding rates assuming 100-percent program participation.

### **Special Education**

The Governor’s May Revision acknowledges the work of the California Statewide Special Education Taskforce which was formed to examine the state of special education in California to analyze and consider best practices within the state and nation, and ultimately propose recommendations for improving the system.

In response to these recommendations, the Governor’s May Revision proposes \$60.1 million Proposition 98 General Fund (\$50.1 million ongoing and \$10 million one-time) in 2015-16 to implement selected program changes recommended by the taskforce, and make targeted investments that improve service delivery and outcomes for disabled students, with a particular emphasis on early education.

The \$60.1 million will be expended in the following way:

- **\$30 million to increase Opportunities for Infants and Toddlers to Receive Early Interventions** — The proposed funding will augment the Early Education Program for Infants and Toddlers with Exceptional Needs, which identifies and provides early interventions for infants from birth to age two with special needs. Participation in the current program is limited to local educational agencies that have historically received state funding for this program. This investment will allow for new participation in the program, and provide an opportunity for the state to reassess the outdated funding model.
- **\$12.1 million to increase Opportunities for Children with Exceptional Needs in State Preschool** — The proposed funding will be used to provide access to an additional 2,500 children in State Preschool. Priority for this funding is for children with exceptional needs.
- **\$6 million increase to the State Preschool Program to Improve Outcomes for Children with Exceptional Needs who participate in State Preschool** — The May Revision proposes to increase State Preschool reimbursement rates by 1 percent (at a cost of \$6 million Prop 98) to reflect these changes. The May Revision would also require the State Preschool programs to: (1) provide parents with information about accessing local resources for the screening and treatment of developmental disabilities, and (2) within existing professional development requirements, provide teachers with training on behavioral strategies and targeted interventions to improve kindergarten readiness.
- **\$10 million to establish Statewide Resources to Encourage and Assist Local Educational Agencies in Aligning Systems of Learning and Behavioral Supports** — The May Revision proposes a one-time investment of \$10 million Prop 98 General Fund dollars to provide technical assistance and build statewide resources to assist local educational agencies interested in implementing school-wide, data-driven systems of support and intervention. School-wide tiered systems provide scientifically based practices and interventions that are proportional to a

student's needs. Research indicates that schools that have implemented tiered systems are more successful at improving disabled student outcomes.

- **\$1.7 million to increase Dispute Resolution Resources** — The May Revision proposes an increase of \$1.7 million federal Individuals with Disabilities Education Act state-level activity funds to expand the current Alternative Dispute Resolution Grant Program to all Special Education Local Plan Areas in the state. On a limited scale, this program has proven successful in resolving special education disputes at the local level.
- **\$500,000 to increase State Systemic Improvement Plan Resources** — The May Revision proposes an increase of \$500,000 federal Individuals with Disabilities Education Act state-level activity funds to develop resources and provide technical assistance to local educational agencies for implementation of the federally required State Systemic Improvement Plan for students with disabilities.

### **Adult Education**

The May Revision maintains the \$500 million in Proposition 98 General Fund from the January budget to establish the Adult Education Block Grant program to provide funds for adult education to school districts and community colleges. The May Revision strengthens this proposal, and is consistent with a number of recommendations that the education community had suggested. The adjustments to the proposed adult ed program include:

**Eliminate Allocation Boards within Each Consortium** — Each consortium will be required to create rules and procedures regarding how it will make decisions, based on state guidelines that require consortia to seek and respond to input on proposed decisions from interested stakeholders and to make decisions publicly.

**Require More Robust, but Less Frequent, Planning** — Each consortium will develop a comprehensive plan for adult education in its region at least once every three years, with annual updates.

**Provide Greater Funding Certainty** — The Superintendent of Public Instruction and the Chancellor of the California Community Colleges will certify maintenance of effort levels by July 30, and will determine the allocation of any remaining block grant funds to consortia by October 30. Beginning in 2016, the Superintendent and Chancellor will provide preliminary allocations to consortia shortly following the release of each Governor's Budget, and final allocations, along with preliminary projections for two future years, shortly after each Budget is enacted. At the consortia level, allocations to districts will be at least equal to their distribution from the previous year, with limited exceptions. Further, use of a local fiscal administrator is no longer required.

**Integrate Adult Education Programs and Funding Streams** — The Superintendent and Chancellor will, by January 31, 2016, develop and submit a plan to distribute Workforce Innovation and Opportunity Act Title II and Perkins funding using the consortia structure in future years. School districts, county offices of education, and community college districts that receive other specified state funds or federal funds for adult education must be participating members of an adult education consortium.

### **Child Care & State Preschool**

The May Revision increases funding for both subsidized child care and for the State Preschool

Program. The significant adjustments include:

**CalWORKs Stage 2** — An increase of \$46.8 million non-Proposition 98 General Fund, to reflect an increase in the number of new Stage 2 beneficiaries and an increase in the cost of providing care. Total base cost for Stage 2 is \$395.4 million.

**CalWORKs Stage 3** — An increase of \$2 million non-Proposition 98 General Fund to reflect minor adjustments in caseload and the cost of providing care. Total base for Stage 3 is \$265.5 million.

**Capped Non-CalWORKs Programs** — A net decrease of \$7.2 million (\$3.1 million Proposition 98 General Fund and \$4.1 million non-Proposition 98 General Fund) to reflect a change in the cost-of-living adjustment from 1.58 percent at the Governor's Budget to 1.02 percent at the May Revision, and a net decrease of \$2.5 million (\$1.1 million Proposition 98 General Fund and \$1.4 million non-Proposition 98 General Fund) to reflect a change in the population of 0-4 year-old children.

**Child Care and Development Funds** — A net increase of \$17.7 million federal funds in 2015-16 to reflect an increase in ongoing base federal funds of \$9 million, an additional \$5.5 million in one-time general-purpose funds from 2014-15, and an additional \$3.2 million in one-time quality funds from 2014-15. In addition, the May Revision identifies basic priorities for possible mid-year federal Child Care and Development Block Grant funding adjustments, and establishes the Infant and Toddler Quality Rating and Improvement System Block Grant with anticipated federal quality funds available beginning October 1, 2016.

**State Preschool** — An increase of \$13.5 million Proposition 98 General Fund to reflect 2,500 part-day State Preschool slots as described in the Special Education section, as well as various technical adjustments including an adjustment in the cost of living and a change in the population of 0-4 year-old children.

**Early Head Start/Child Care Partnership Grant** — An increase of \$2.4 million federal funds to provide Early Head Start services to an additional 260 infants and toddlers in 11 northern counties.

### **Commission on Teacher Credentialing**

**Increases in Fees** - The Commission on Teacher Credentialing (CTC) sets the State's standards for educator preparation for the K-12 public schools of California. The CTC is a special fee agency, with teacher credential fees providing approximately 85 percent of its revenue base; the remainder is provided by examination fees paid by educators and accreditation fees paid by educator preparation programs.

According to the Governor, over the past five years, the number of candidates enrolled in and completing educator preparation programs and applying for credentials has declined, resulting in a decrease in the CTC's revenue base and the Commission's non-discretionary operating costs have continued to increase. The May Revision includes \$4.5 million to address these costs. However, in an effort to address the structural pressures on the CTC's budget, the May Revision proposes to increase the teacher credential fee to \$100 for initial and renewal credentials. Current credential fees are \$70.

**Teacher misconduct** - The Administration is looking at streamlining functions and create workload efficiencies at the Commission. The Governor proposes to begin this effort with a focus on the Commission's responsibility to monitor educator misconduct through the existing district reporting

process. The administration states that often the evidentiary files of district-reported cases of teacher misconduct are incomplete and lack basic information, which increases processing time and costs.

The minimum required information is currently specified in regulations; the Governor is proposing to place these requirements in statute in an effort to emphasize the basic information needed in a district report of teacher misconduct. The Administration also proposes to provide the CTC with jurisdiction to investigate a Superintendent or charter school administrator who fails to report educator misconduct.

### **What Happens Now?**

With both legislative leaders indicating in statements on the budget that the Governor's spending priorities were generally consistent with their own, there is no reason to think that a final budget agreement will not be reached prior to the June 15 constitutional deadline. However, both legislative leaders did reference the need to invest in additional child care and other services for our poorest citizens. As we had indicated in recent communications, the fact that there is so much new revenue indicates that there will likely be efforts by the legislature to create new program funding or to significantly expand funding for child care and preschool beyond the levels proposed by the Governor in the May Revise. This will no doubt create some friction given that the Governor will want to ensure that this budget does not create problems in future years due to declining revenues. We will continue to monitor the final budget discussions and keep you informed of any changes or concerns that arise. In the end, however, the vast majority of the K-14 budget set out by the Governor in this May Revision will ultimately be approved by the legislature.