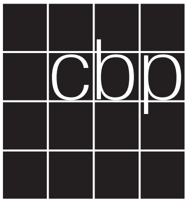


CALIFORNIA BUDGET PROJECT

budget brief

MARCH 2009

WHAT WOULD PROPOSITION 1A MEAN FOR CALIFORNIA'S FUTURE?

Proposition 1A of 2009 would require the state to make annual contributions to a budget reserve until the balance in the reserve reaches 12.5 percent of General Fund revenues, impose limits on the use of the reserve in "bad budget" years, and limit the state's ability to spend existing revenues. Proposition 1A was placed on the ballot by the Legislature as part of negotiations over measures aimed at addressing the 2008-09 budget shortfall and the 2009-10 budget. Proposition 1A replaced another constitutional amendment (SCA 30 of 2008), placed on the ballot by the Legislature in September 2008.[1]

What Would Proposition 1A Do?

Proposition 1A would modify the maximum size of, and the annual contribution into, the state's budget reserve; impose new conditions on the use of the reserve; allocate a portion of the reserve for certain purposes; and restrict the use of "unanticipated revenues" for specified purposes. If Proposition 1A is approved by the voters, the temporary tax increases included in the 2009 budget agreement would be extended and governors would gain the unilateral authority to make mid-year reductions in state spending.[2] Specifically, Proposition 1A:

- Renames the state's budget reserve the Budget Stabilization Fund (BSF) and creates two new accounts, the Supplemental Budget Stabilization Account (SBSA) and the Supplemental Education Payment Account (SEPA). The SEPA would only be created if Proposition 1B is also approved by the voters in May.
- Requires the state to deposit an amount equal to 3 percent of estimated General Fund revenues in the BSF beginning in September 2008 and annually thereafter until the balance in the BSF equals 12.5 percent of General Fund revenues as estimated in the Budget Bill for each fiscal year. Under current law, the state is required to add money to the BSF until the balance reaches the greater of $8 billion or 5 percent of General Fund revenues.
- Transfers half of the annual contribution – an amount equal to 1.5 percent of General Fund revenues – from the BSF to the SEPA or the SBSA. Transfers to the SEPA would be allocated for purposes subject to the Proposition 98 guarantee until such payments total $9.3 billion. If Proposition 1B is not approved by the voters, or after all SEPA payments have been made, an amount equal to 1.5 percent of General Fund revenues would be transferred to the SBSA each year. Funds in the SBSA could only be used for one-time infrastructure or other capital outlay expenditures and to repay state General Obligation or other bond debt.
- Limits the conditions under which transfers to the BSF can be suspended beginning July 1, 2011. As of that date, transfers could only be suspended in years when General Fund revenues and available balances are less than prior year's expenditures adjusted for population, as defined, and the Consumer Price Index (CPI). However, transfers to the SEPA could not be suspended under any circumstances. Under current law, transfers to the BSF can be suspended by an executive order issued by the governor.
- Requires "unanticipated revenues" as determined by one of two formulas to be transferred to the BSF based on a calculation made on or before May 29, 2011 and each year thereafter. Proposition 1A defines unanticipated revenues as the lesser of:
    - The difference between estimated General Fund revenues for a given fiscal year and an amount determined "by extrapolating from the trend

line derived by a linear regression" of the prior 10 years' General Fund revenues (the "revenue forecast amount"); or
    - The difference between estimated General Fund revenues, transfers, and available balances and the prior year's estimated spending adjusted for population and inflation using the CPI.
- Excludes changes in tax revenues attributable to policy change – tax increases or decreases – from the calculation of the revenue forecast amount unless and until the policy change has been in effect for the 10-year period covered in the linear forecast. This exclusion would adjust the revenue forecast amount to allow amounts raised by legislated tax increases to be spent in years when the unanticipated revenue calculation is based on historic revenue trends. It would also reduce the revenue forecast amount to reflect any reduction in state taxes.
- Excludes the proceeds of the deficit financing bonds authorized by Proposition 57 of 2004 from the calculation of the revenue forecast amount. This would reduce revenues received in years in which the state received proceeds from the sale of the bonds.
- Restricts the use of "unanticipated revenues" to satisfaction of any unfunded obligation under the Proposition 98 school funding guarantee, including any maintenance factor obligation, for the current fiscal year.[3] Any remaining amounts could only be used to satisfy prior years' Proposition 98 obligations, be transferred to the BSF to bring the balance up to the 12.5 percent of General Fund revenue target, be used to repay amounts owed as a result of suspension of Propositions 1A of 2004 or 2006, or repay outstanding General Obligation bond debt.[4] Any remaining amounts could be transferred to the BSF, spent for one-time infrastructure or capital outlay purposes, used to repay outstanding bond debt, rebated to taxpayers, or appropriated for unfunded nonpension benefit costs for state retirees.
- Limits the use of funds transferred to the BSF as follows:
    - Half of the annual transfer, excluding amounts deposited in the SEPA, up to a maximum of $5.0 billion would be used to make supplemental payments on outstanding deficit financing bonds authorized by Proposition 57 of 2004.
    - To address budget shortfalls; however, the amount that could be transferred to the General Fund would be limited to the difference between General Fund revenues, transfers, and balances available in a fiscal year and the prior year's expenditures adjusted for the change in population and the CPI. Funds in the BSF could not be used to support "baseline" budget obligations to the extent these obligations exceed the expenditure forecast amount.
    - To respond to certain emergencies declared by the governor.
    - Once the balance in the BSF reaches 12.5 percent of General Fund revenues, any excess could only be used for specified purposes including bond debt service, payment of amounts owed to transportation funds and local governments, other one-time purposes, nonpension state retiree benefit costs, or rebates to taxpayers.
- Defines change in population as the percentage change in the state's population multiplied by the share of the prior year's budget spent on purposes other than K-14 education and the percentage change in average daily attendance for K-14 education multiplied by the share of the prior year's budget spent on K-14 education.
- States that transfers to the BSF, SBSA, and SEPA shall be considered General Fund revenues for all purposes defined in the Constitution. This provision means that amounts transferred to these funds and accounts would count toward, for example, calculation of the Proposition 98 guarantee and the State Appropriations Limit.
- Would extend the length of temporary tax increases approved as part of the February 2009 budget agreement. Specifically, the one cent increase in the sales tax rate would be extended for one year, from July 1, 2011 to June 30, 2012; the 0.50 percentage point increase in the Vehicle License Fee (VLF) rate would be extended for two years, from July 1, 2011 to June 30, 2013; and the 0.25 percentage point increase in state personal income tax rates and the reduction in the size of the dependent tax credit would be extended for two years, to 2011 and 2012.

Where Are We Now?

California has had a limit on state and local government appropriations since 1979. Article XIIIB of the state Constitution limits appropriations from the proceeds of taxes. In brief, the State Appropriations Limit (SAL) is the prior year's limit adjusted for the change in population and inflation measured as the change in per capita personal income.[5] Prior to 1990, the SAL was adjusted for inflation using the CPI. In addition to changing the inflation factor used to calculate the SAL, Proposition 111 of 1990 excluded appropriations for debt service and capital outlay from the spending limit.

How Does Proposition 1B Relate to Proposition 1A?

A second proposed constitutional amendment, Proposition 1B, is tied to the passage of Proposition 1A. Proposition 1B was also placed on the ballot by the Legislature as part of the February budget agreement. Proposition 1B establishes a mechanism for increasing funding subject to the Proposition 98 guarantee in future years to make up for the reductions in the 2007-08 and 2008-09 budgets. Proposition 1B would only take effect if the voters also approve Proposition 1A.

Proposition 1B responds to a technical, and unresolved, issue related to the calculation of the Proposition 98 school funding guarantee.[6] The Governor's Proposed Budget assumes that the minimum required 2008-09 funding level for education would be determined by Proposition 98's "test 1." The Governor then asserts that under "test 1," no maintenance factor obligation is created and the state would not be required to restore funding to the level at which it would have been if 2008-09 funding had been determined on Proposition 98's "test 2."[7] Education advocates and some analysts argue that the Governor's interpretation of Proposition 98 is in error and that a maintenance factor should be created in 2008-09. While the dollar difference between the guarantee calculated under "test 1" and "test 3" is small, the difference of interpretation has a major impact on future years' school funding.

Proposition 1B, along with Proposition 1A, would sidestep this controversy by creating the Supplemental Education Payment Account (SEPA), linked to the Budget Stabilization Fund (BSF), that would be used to restore the Proposition 98 "base" by allocating half of the amount contributed to the BSF each year – an amount equal to 1.5 percent of General Fund revenues – to Proposition 98-supported programs beginning in 2011-12. This allocation would continue until $9.3 billion in payments, which would count toward the Proposition 98 guarantee for purposes of calculating subsequent years' guarantees, are made.

What Does Proposition 1B Do?

If the voters approve both Proposition 1A and Proposition 1B, Proposition 1B would:

- Allocate 1.5 percent of estimated General Fund revenues to the SEPA each year beginning on October 1, 2011 until a total of $9.3 billion of payments have been made.
- State that contributions to the SEPA are in lieu of any maintenance factor obligation that otherwise may apply as a result of the level of funding provided under Proposition 98 in 2007-08 and 2008-09.
- Count any payments made from the SEPA toward the calculation of subsequent years' Proposition 98 school funding guarantee.
- Allocate up to $200 million of each year's SEPA payment to certain school districts that receive relatively low "revenue limit" allocations from the state.[8] Payments to these districts are generally referred to as "equalization" payments.
- Allocate the remainder of the annual contribution to school and community college districts. Payments to K-12 education would be based on school districts' per pupil "revenue limits."

What Impact Would Proposition 1B Have on the Budget?

The impact of Proposition 1B on the budget depends on the interpretation of Proposition 98 and, in particular, resolution of the question of whether "test 1" or "test 3" should apply in 2008-09 and whether or not a maintenance factor obligation is created in 2008-09. Passage of Proposition 1B would likely avert further controversy over, or resolution of, this issue by providing future payments in an amount similar to what would be owed had a maintenance factor obligation been created. If a maintenance factor is, in fact, created by the 2008-09 funding level, the balance of the outstanding obligation for 2007-08 and 2008-09 would be equal to $9.3 billion.[9]

Absent resolution of the question of which of Proposition 98's tests should apply in 2008-09 and whether a maintenance factor obligation is created in "test 1" years where "test 1" is below "test 2," the impact of Proposition 1B on the state budget is unclear. Proposition 1B either increases the state's school funding obligation or provides payments similar to those that would be required under current law. The Legislative Analyst's Office (LAO) notes that Proposition 1B "could postpone maintenance factor payments that otherwise would have been made" in 2009-10 and 2010-11, but that under alternative interpretations, no savings would occur.[10] Similarly, the LAO notes that the long-term impact of payments mandated by Proposition 1B is "subject to considerable uncertainty…however, costs for K-14 education likely would be higher than under current law – potentially by billions of dollars each year."

California also has a budget reserve, the Budget Stabilization Account (BSA) that was established by Proposition 58 of 2004. Proposition 58 requires an amount equal to 3 percent of estimated General Fund revenues to be transferred to the BSA, up to the greater of 5 percent of estimated revenues for the year or $8 billion. Proposition 58 allowed transfers to the BSA to be suspended or reduced by the governor by executive order and allowed the Legislature to transfer funds from the BSA to the General Fund by statute.

The Context for This Measure

Proposition 1A would not address California's existing structural shortfall – the gap between revenues and expenditures – that exists in all but the best budget years. The state's two long-term budget forecasts, issued by the Legislative Analyst's Office (LAO) and the Department of Finance, both identify an ongoing gap between revenues and expenditures. Moreover, the Department of Finance's forecast projects a significant ongoing gap even taking into account the continuation of the spending reductions outlined by the Governor in his proposed 2009-10 budget.

The revenue forecast amount established by Proposition 1A, which limits spending from the state's existing tax base, would be significantly below the Governor's "baseline" spending forecast, a forecast that assumes that the cuts proposed by the Governor in his New Year's Eve budget release continue.[11] For example, in 2010-11, the first year when the Director of Finance would be required to calculate whether the state has received "unanticipated revenues," the revenue cap would be an estimated $16 billion lower than the Governor's "baseline" spending estimate for the same year. The gap would widen in 2011-12 and 2012-13 to $17 billion and $21 billion, respectively.[12]

By basing the new cap on a level of revenues that is insufficient to pay for the current level of programs and services, Proposition 1A would limit the state's ability to restore reductions made during the current downturn out of existing revenues. Had Proposition 1A been in effect during the late 1990s, for example, it would have diverted "unanticipated" revenues from the General Fund in 1995-96 and 1996-97, years when the "expenditure forecast" amount, the test used to trigger the shift of monies out of the General Fund, was below the LAO's 1995 "current services" forecast for the same fiscal year.

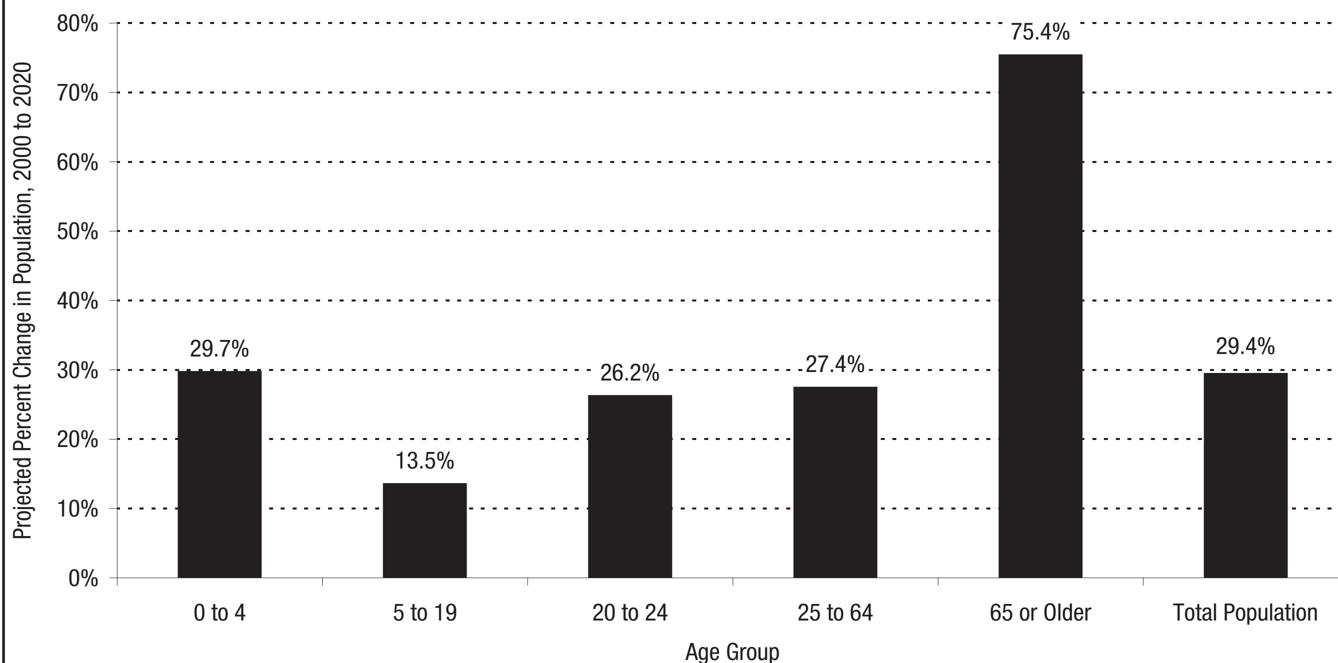
How Will Reserve Contributions Be Funded?

Proposition 1A would limit the state's ability to suspend the 3 percent annual transfer from the General Fund into the BSF. Currently contributions can be suspended by an executive order of the governor. Beginning in 2011-12, contributions could only be suspended in years when estimated revenues are below the prior year's expenditures adjusted for population and the CPI and contributions to the SEPA could not be suspended under any circumstances.[13] Based on the Governor's most recent baseline budget forecast, the 3 percent transfer to the BSF would equal $3.144 billion in 2011-12. Assuming that the portion that would remain in the BSF is suspended, the 1.5 percent transfer to the SEPA would equal $1.572 billion.

Because Proposition 1A leaves other constitutional earmarks and mandates intact, the 3 percent transfer to the BSA would compete with spending that is outside of the Proposition 98 guarantee and not mandated by other contractual or constitutional requirements in years when revenues are less than the amount needed to support a workload budget. In 2011-12, for example, the 3 percent transfer would equal 4.6 percent of spending for purposes outside of the Proposition 98 guarantee and exclusive of the transfer required by Proposition 42 of 2002. The 1.5 percent transfer to the SEPA, which could not be suspended, would equal 2.3 percent of spending – $1.6 billion – for purposes other than Proposition 98 and Proposition 42. In other words, Proposition 1A would require reductions of $3.1 billion to satisfy the required 3 percent transfer to the BSF. If the portion of the transfer dedicated to the BSF could be suspended, reductions of $1.6 billion would be needed to fulfill the required SEPA transfer. The amount of the 3 percent transfer is approximately equal to the 2011-12 workload budget for the California State University system.[14]

Proposition 1A Would Prevent Use of the Reserve to Fund "Baseline" Spending

Proposition 1A limits the amount that can be used from the reserve in "bad budget" years to the difference between anticipated revenues and prior year's spending adjusted for population growth and the CPI. It does not allow the reserve to be used to support a "current services" or "baseline" budget, even if sufficient funds would be available in the reserve to do so.[15] The discrepancy arises from the fact that the CPI – the inflation measure used by Proposition 1A – is designed to measure changes in the cost of goods purchased by households, not governments. Thus, the CPI does not accurately measure the year-to-year increase in the cost of delivering the same level of public services. Specifically, the CPI does not take into account the fact that government spends a larger share of its budget on items – such as health care – for which costs have risen faster than the rate of inflation. Between 1990 and 2007, for example, national per capita health care expenditures more than doubled, rising by 164 percent, while the CPI for California, which measures inflation in households' purchases, rose by just 61 percent.



The disparity between the amount of a gap that could be filled under Proposition 1A and the amount needed to support a baseline budget is further magnified by the fact that the population measure used – enrollment in K-14 education for the part of the budget spent on programs covered by the Proposition 98 guarantee and the change in the total population for the remainder of the budget – does not accurately capture demand for public services. For example, the Department of Finance projects that the population of the state as a whole will increase by 29.4 percent between 2000 and 2020, while the population age 65 or older will increase by 75.4 percent. Thus, demographic factors can be expected to increase demands on the budget from the cost of programs that serve the elderly – such as SSI/SSP, IHSS, and nursing home care funded by Medi-Cal – at a rate that exceeds the growth in programs that serve the population as a whole. The Legislative Analyst, for example, projects that state costs for IHSS will increase at an average annual rate of 7.9 percent between 2008-09 and 2013-14 based on the program's current benefits and structure.[16] The same forecast projects that the state's Medi-Cal costs will rise by 6.1 percent annually, on average, over the same period. In contrast, the combined growth rate for population and the CPI averaged 4.8 percent between 1998-99 and 2007-08.

Proposition 1A Will Require Contributions Even in Years With Budget Shortfalls

Proposition 1A limits the conditions under which transfers to the BSF can be suspended. If the voters approve Proposition 1B, the 1.5 percent annual contribution to the SEPA cannot be waived until all required payments are made. The remaining 1.5 percent contribution to the BSF, along with the 1.5 percent contribution to SBSA, can only be suspended in years when estimated revenues are less than prior year's spending adjusted for population and inflation. As discussed above, in some years, this adjustment factor may not be sufficient to allow full funding of a baseline budget. To test the impact of this provision, the CBP examined how Proposition 1A would have applied had it been implemented in 1990. This analysis found that Proposition 1A would have required contributions to the reserve in a number of years where the state experienced a moderate deficit. In November 1995, for example, the Legislative Analyst's Office projected that the cost of a General Fund "current services" budget would increase by 8.6 percent from 1995-96 to 1996-97. However, in that same year, because revenues exceeded the "expenditure forecast" amount, a BSF contribution of $2.0 billion would have been required, which would have left available revenues $1.0 billion – 2.2 percent – below the amount needed to support a current services budget.

Proposition 1A also would have required both a transfer to the BSF and a shift of "unanticipated revenues" out of the General Fund in 2005-06. These shifts would have been required despite the fact that by most measures, 2005-06 was a "bad budget" year, which required $5.9 billion in "solutions" to bring the budget into balance.[17] Had Proposition 1A been in effect, $1.4 billion in additional "solutions" would have been needed to provide sufficient resources to make the mandatory 1.5 percent transfer to the BSF.[18] At the end of the year, an additional transfer of revenues out of the General Fund would have been required since estimated collections were in excess of the revenue cap.[19]

Proposition 1A Allows Adjustments for New Taxes, But Not Fees

Proposition 1A's limits on spending adjust the "revenue forecast" amount to reflect increases (or decreases) in state taxes that have been in effect for less than 10 years. The result of this adjustment is to allow the state to spend revenues from tax increases that exceed the limit that otherwise would apply in years when state spending is determined by the 10-year trend line. Proposition 1A does not, however, make a similar adjustment for changes in state fees.

The failure to provide similar treatment for fees would limit the Legislature's ability to raise fees to close a budget gap to the extent the increase raised General Fund revenues above the amount determined by the 10-year trend line.

If Proposition 1A Is Approved by the Voters, Governors Will Gain the Authority To Make Mid-Year Spending Reductions

SB 8 (Ducheny), passed as part of the recent budget agreement, gives governors the unilateral authority to cut spending if available resources decline or expenditures increase "substantially" mid-way through a budget year. This provision would only take effect if Proposition 1A is approved by the voters. The new authority would allow an appointee of the governor, the director of finance, to reduce appropriations that support the operations of the state by up to 7 percent, except for amounts appropriated for the support of the Legislature and constitutional officers, the transfer of the sales tax paid on gasoline from the General Fund to transportation, debt service, health and dental benefits for state retirees, and limited other expenditures.[20] Items appropriated pursuant to collective bargaining agreements with state employee unions also would be excluded from reductions.

SB 8 also allows the Director of Finance to suspend cost-of-living adjustments or rate increases for up to 120 days and, if the governor declares a fiscal emergency, cost-of-living adjustments would not be made until the Legislature sends the governor one or more bills addressing the emergency.[21]

SB 8 does not define the term "substantially" and would thus allow directors of finance to make significant reductions – of up to 7 percent of an appropriation – in response to a relatively modest budget shortfall. Moreover, directors would gain this authority based on estimated, rather than actual, revenue shortfalls or expenditure increases, including estimates made early in a fiscal year when forecasts may differ significantly from final collections or spending levels.

Proposition 1A Is Incompatible With Existing Constitutional Guarantees, "Earmarks," and Set-Asides

Proposition 1A would be layered on top of the state's existing and complex array of constitutional funding guarantees, funding restrictions, and revenue set-asides. In some instances, the interaction of Proposition 1A with these existing provisions could result in unintended consequences and could limit the state's ability to fund programs and services that lack constitutional protection, such as health, human services, resources, and higher education. For example:

- Proposition 1A allows "unanticipated revenues" to be used to fund an increase in the state's school spending guarantee in the year the unanticipated revenues occur, but doesn't adjust the revenue cap to take into account the ongoing cost of sustaining the higher level of education spending in future years. As a result, services outside of the Proposition 98 guarantee would be "crowded out" in future years, years when the Proposition 98 guarantee increases at a rate faster than inflation. This could occur frequently, since growth in per capita personal income, the "normal" inflation factor used to calculate the Proposition 98 guarantee, exceeded the rise in the CPI in 20 out of the 30 years between 1979 and 2007.

- Among the state's more volatile revenues are the sales taxes paid on gasoline, a portion of which is constitutionally earmarked for transportation by Proposition 42 of 2002 and Proposition 1A of 2006. These revenues, however, are first deposited in the General Fund. In years when gasoline prices rise rapidly, such as 2008, the rapid increase in revenues could generate "unanticipated revenues." Proposition 1A would require the "unanticipated revenues" to be transferred out of the General Fund and used for limited purposes, while at the same time leaving intact the requirement that all of these moneys be transferred to transportation. In essence, the interaction of Proposition 1A of 2009 with the existing transfer would be to spend the same dollars twice – requiring both transfers to transportation and a set-aside

of the portion of revenues deemed to be "unanticipated" for a limited set of purposes. The result would be a reduction in the resources available to support programs and services lacking constitutional protection.

Proposition 1A Is Based on Estimated, Not Actual, Revenues and Expenditures

Many of the calculations used in Proposition 1A are based on estimated, not actual, revenues and expenditures. The annual contribution, for example, would be 3 percent of the amount estimated in the Budget Bill for a given fiscal year, an estimate generally prepared in May for the fiscal year that begins on July 1. This would inevitably result in contributions that are larger or smaller than would be required by a calculation based on actual collections. In years when revenues fall below forecast, it could result in contributions that are much larger than 3 percent of final revenues and/or transfers being made in years when the state experiences a significant mid-year budget shortfall.

While the calculations used to determine whether there are "unanticipated revenues" are made in late May, near the end of the fiscal year, they are based on estimates made by the Director of Finance. Proposition 1A does not provide a procedure for legislative oversight or appeal of an estimate that it believes is in error. Studies show that the revenue and expenditure forecasts prepared by the Department of Finance have historically been subject to considerable errors.[22] The broad power granted by Proposition 1A could provide an incentive for directors of finance to manipulate revenue and expenditure estimates to achieve particular policy goals.

Proponents Argue

Supporters of Proposition 1A argue that it is needed to force "politicians to set aside money every year into a special 'rainy day' fund" and to put "restrictions on the amount the state can spend each year."[23]

Opponents Argue

Opponents of Proposition 1A argue that "its complex formulas and fine print will invite unintended consequences and behind the scenes manipulation" and that as a result, "the effects of Proposition 1A will be far different than its supporters promise."[24]

Conclusion

Proposition 1A would make permanent changes to the state's Constitution that would have major implications for future budgets and policymaking. When considering this measure, voters should carefully consider not only the current budget debate but, more importantly, what the proposed measure would mean for the state's ability to address future policy, demographic, and economic challenges.

Jean Ross prepared this Budget Brief. The California Budget Project (CBP) was founded in 1994 to provide Californians with a source of timely, objective, and accessible expertise on state fiscal and economic policy issues. The CBP engages in independent fiscal and policy analysis and public education with the goal of improving public policies affecting the economic and social well-being of low- and middle-income Californians. General operating support for the CBP is provided by foundation grants, individual donations, and subscriptions. Please visit the CBP's website at www.cbp.org.

ENDNOTES

1 The key change made by SCA 30 was a limitation on the use of the Budget Stabilization Fund (BSF) in "bad budget" years. This limitation restricted the amount that could be transferred from the BSF to the difference between estimated General Fund revenues and prior year's spending adjusted for population growth and the percentage change in per capita personal income. Proposition 1A modifies this restriction to limit withdrawals to the amount needed to fund prior year's spending adjusted by population and the Consumer Price Index (CPI).

2 The links between Proposition 1A and the length of the temporary tax increases and the Governor's authority to make mid-year spending reductions are contained in AB 3xxx (Evans) and SB 8xxx (Ducheny).

3 For more information on the Proposition 98 guarantee, see California Budget Project, *School Finance in California and the Proposition 98 Guarantee* (April 2006).

4 Proposition 1A of 2004 restricted the state's ability to shift property taxes among school districts and local governments. Proposition 1A of 2006 severely limits the conditions under which the state can suspend the transfer of certain sales tax revenues from the General Fund to transportation programs. The transfer required by Proposition 1A of 2006 is sometimes referred to as the Proposition 42 shift, for the ballot measure that first required that transfer.

5 For more information on the SAL, see California Budget Project, *Will the State Hit the "Gann" Limit?* (April 2000). The state last hit the SAL in 1999-00. In 2007-08, appropriations subject to the SAL were $16.9 billion below the limit.

6 For more information on Proposition 98, see California Budget Project, *School Finance in California and the Proposition 98 Guarantee* (April 2006).

7 A maintenance factor is created in years when "test 3" is used to calculate the Proposition 98 guarantee. In essence, a maintenance factor is an obligation to restore Proposition 98 funding in the future, based on a specified formula, to the level at which it would have been had "test 2" been in effect. A maintenance factor does not require the state to restore funds that schools did not receive in the intervening years; instead, it is an obligation to restore the Proposition 98 "base" to the long-term, test 2 level.

8 For a discussion of revenue limits, see California Budget Project, *How School Districts Get Their Money* (February 2009). Revenue limits provide general purpose funding to school districts, county offices of education, and community college districts.

[9] Legislative Analyst's Office, *Proposition 1B Education Finance*, downloaded from http://www.sos.ca.gov/elections/public-display-051909/1b-lao.pdf on March 16, 2009.

[10] Legislative Analyst's Office, *Proposition 1B Education* Finance, downloaded from http://www.sos.ca.gov/elections/public-display-051909/1b-lao.pdf on March 16, 2009.

[11] Department of Finance, *General Fund Projection at 2009-10 Governor's Budget* (January 2009) downloaded from http://www.dof.ca.gov/reports_and_periodicals/documents/MY_at_2009-10_GB-web.pdf on March 11, 2009. The CBP modeling subtracts $4.673 billion in 2010-11 expenditures since the recent budget agreement did not include the issuance of an equivalent amount of Revenue Anticipation Warrants in 2008-09.

[12] These estimates do not adjust for the impact of the tax cuts included as part of the 2008-09 budget agreement; however, since these cuts would reduce the revenue forecast amount, the gaps may be understated, not overstated.

[13] An amount equal to 1.5 percent of estimated revenues would be transferred to the SEPA if Proposition 1B also is approved by the voters until transfers totaling $9.3 billion are made.

[14] Legislative Analyst's Office, *California's Fiscal Outlook: LAO Projections 2008-09 Through 2013-14* (November 20, 2008), p. 26.

[15] A current services or baseline budget is the amount needed to support programs and services based on "current law" obligations adjusted for the impact of caseload and inflation specific to certain types of expenditures.

[16] Legislative Analyst's Office, *California's Fiscal Outlook 2008-09 Through 2013-14* (November 2008).

[17] Legislative Analyst's Office, *California Spending Plan 2005-06* (September 2005), p. 3. The "solutions" used to balance the budget included $4.1 billion in spending reductions, $728 million in internal fund shifts, $886 million in loans and borrowing, and $94 million from enhanced tax compliance efforts.

[18] In this hypothetical, an additional $1.4 billion in reductions would have been needed to support SEPA contributions if they had been in effect. Alternatively, if SEPA payments had not been required, the 1.5 percent contribution to the SBSA could have been used to offset debt service costs paid out of the General Fund.

[19] Preliminary modeling suggests that this additional transfer of "unanticipated revenues" would have been sufficiently large to leave the state with a General Fund deficit, rather than the surplus that actually occurred. Precise modeling is complicated by Proposition 1A's provision that allows "unanticipated revenues" to be applied toward school funding obligations that arise from an increase in the Proposition 98 guarantee during a budget year.

[20] Local assistance appropriations, which include payments to Medi-Cal providers, local governments, and schools, could not be reduced. State operations appropriations include the budgets of the California State University and University of California systems.

[21] The ability to delay or suspend cost-of-living adjustments would not apply to "revenue limit" payments to school districts and county offices of education or increases provided by collective bargaining agreements covering state employees.

[22] Sabrina Birnbaum Landreth, *Gubernatorial Spending Controls: Surviving State Revenue Shortfalls* (Goldman School of Public Policy, University of California, Berkeley: Spring 2004).

[23] "Argument in Favor of Proposition 1A," in Secretary of State's Office, *California Statewide Special Election: Tuesday May 19, 2009 Official Voter Information Guide,* downloaded from http://www.sos.ca.gov/elections/public-display-051909/official-ballot-pamphlet-public-display-051909.htm on March 11, 2009.

[24] "Argument in Favor of Proposition 1A," in Secretary of State's Office, *California Statewide Special Election: Tuesday May 19, 2009 Official Voter Information Guide,* downloaded from http://www.sos.ca.gov/elections/public-display-051909/official-ballot-pamphlet-public-display-051909.htm on March 11, 2009.