

COMMUNITY COLLEGE UPDATE

PUBLIC EDUCATION'S POINT OF REFERENCE FOR MAKING EDUCATED DECISIONS

An Overview of the 2024-25 Governor's Budget Proposals



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Overview of the Governor's Budget Proposals

When you expect a budget gap of \$68 billion, a budget gap of \$37.9 billion feels like a good day. While there is no debating the magnitude of unrealized revenues from 2022, Governor Gavin Newsom today framed the current budget situation as the state returning to a more normal economic environment from recent years of explosive growth. This is a key difference from the expectations set last fall by the Legislative Analyst's Office (LAO) Fiscal Outlook and the tone set today by Governor Newsom.

The good news for education: no mid-year cuts, no deferrals, no program rollbacks. The bad news for education: a barely growing Student Centered Funding Formula due to a meager cost-of-living adjustment (COLA) and no restorations of prior reductions.

California is better prepared to weather the proverbial storm due to the significant rainy day deposits made during the good years that allows the state to address this budget gap. In addition to reserve withdrawals (including the Proposition 98 Rainy Day Fund), the Governor proposes reductions, internal borrowing, funding delays, funding shifts, and non-Proposition 98 deferrals. It remains to be seen whether one-time funds successfully create a bridge to increased future revenues, or if they eventually run dry and are merely delaying cuts to align actual spending to revenues.

The Economy and Revenues

Governor Newsom assumes a continued slow-growth economy for 2024-25 and notes a possible resurgence of higher inflation and continued elevated interest rates as the biggest near-term threats to the economy. Additional risks include, but aren't limited to, geopolitical tensions, climate change impacts, and the high cost of living in California. Importantly, no recession is forecasted. The Governor's Budget assumes Gross Domestic Product growth to slow to 1.6% in 2024 and 1.2% in 2025, and California unemployment is projected to increase to 5.1% and 5.2% in 2024 and 2025, respectively. Headline inflation is projected to drop to 2.6% in 2024 and 2% in 2025.

As he did last year, the Governor began his press conference standing beside a chart showing fluctuations in capital gains revenues as a percentage of personal income, which he again likened to an electrocardiogram, or EKG. The Governor described the economic situation as a story of correction and normalization following a period of distortion, highlighting the unprecedented surpluses in revenue a couple of years ago followed by the deficits experienced in the current year and projected for the 2024-25 budget year.

The largest source of state General Fund revenues is derived from taxes on personal income, including capital gains, and relies heavily on high-income taxpayers. Personal income tax makes up 65% of pre-transfer General Fund revenue for 2022-23 and is projected to account for 74% of pre-transfer General Fund revenue in 2024-25. One percent of the state's highest income earners paid 50% of all personal income taxes in 2021, a slight increase from the prior year. According to the Governor's Budget summary, "[t]hese two related phenomena—significant reliance of the General Fund on capital gains and stock-based compensation, and on taxes paid by a small portion of the population—underscore the difficulty in forecasting personal income tax revenue" and, by extension, General Fund revenues.

Capital gains revenue as a percentage of annual General Fund revenues are projected to stabilize and make up 8.4%, 8.3%, and 8.7% of total annual General Fund revenues for 2022, 2023, and 2024, respectively. The Newsom Administration assumes a stock market that is largely consistent with Wall Street's mid-November 2023 levels.

The Governor's Budget recognizes a budget shortfall of \$44 billion over the three-year budget window (2022-23, 2023-24, and 2024-25). The Governor's Budget draws primarily on the following measures to balance against the shortfall:

- \$13.1 billion in draw down of reserves
- \$8.5 billion in funding reductions without cuts to Proposition 98 programs
- \$5.7 billion in borrowing
- \$5.1 billion in funding delays over three years
- \$3.4 billion in funding shifts from the General Fund to other funds
- \$2.1 billion in deferrals to payroll and University of California/California State University
- \$5.7 billion in withdrawals from the Public School System Stabilization Account (PSSSA)
- \$402 million in tax revenue proposals

The Governor's Budget makes significant reductions to the "Big Three" tax revenues relative to the 2023-24 Enacted Budget across the three-year budget window, for a total downward adjustment of \$42.9 billion.

Big Three Tax Revenues
(in millions)

	2022-23		2023-24		2024-25	
	2023-24 Enacted Budget	Governor's Budget	2023-24 Enacted Budget	Governor's Budget	2023-24 Enacted Budget	Governor's Budget
Personal Income Tax	\$122,769	\$101,749	\$118,161	\$113,768	\$118,903	\$114,730
Corporation Tax	\$42,091	\$37,140	\$42,081	\$36,913	\$43,369	\$38,055
Sales and Use Tax	\$33,072	\$33,186	\$33,366	\$34,643	\$34,383	\$35,123

Again, the Governor's Budget revenue estimates do not forecast a recession—even a mild one. Risks to the projected continuing slow-growth economy are noted and could lead to a recession in which case a mild recession could lead to General Fund revenue losses between \$20 billion to \$30 billion over the budget window.

Proposition 98 Minimum Guarantee and Rainy Day Fund

Proposition 98 Minimum Guarantee

Based on the Governor's revenue estimates, which account for lower-than-expected 2022 tax collections, the Proposition 98 minimum guarantee for 2022-23 and 2023-24 are reduced by \$9.1 billion and \$2.7 billion from the 2023-24 Enacted Budget levels, respectively. Further, the Governor expects state revenues to rebound from current levels, which will result in an increase in funding for K-12 and community college agencies in 2024-25, bringing the minimum guarantee to \$109.1 billion by the end of the budget window. Proposition 98 in 2024-25 includes additional funding to cover the increased K-12 costs resulting from Transitional Kindergarten expansion and the required set-aside to support arts and music programs in K-12 schools. Under the Governor's estimates, Test 1 is operative across the budget window, which means that K-14 education receives nearly 40 cents of every state General Fund dollar.

Proposition 98 Minimum Guarantee, Prior and Current Year
(In billions)

	2023-24 Enacted Budget	2024-25 Governor's Budget Adjustments	Minimum Guarantee
2022-23	\$107.4	-\$9.1	\$98.3
2023-24	\$108.3	-\$2.7	\$105.6

Proposition 98 Rainy Day Fund

Changes in state General Fund revenues have similar impacts on the state's requirement to make deposits into and withdrawals from the Proposition 98 Rainy Day Fund (or the PSSSA). The Governor's Budget proposes the following activity in the reserve account.

Proposition 98 Rainy Day Fund (In billions)				
	2021-22	2022-23	2023-24	2024-25
Deposits		\$0.3	\$0.3	\$0.8
Withdrawals			-\$3.0	-\$2.7
Fund Balance	\$8.1	\$8.4	\$5.7	\$3.8

Student Centered Funding Formula and Enrollment

The Governor's Budget estimates, and fully funds, a statutory COLA of 0.76% for the Student Centered Funding Formula (SCFF), which is lower than the LAO estimated in its November Fiscal Outlook report (1.26%). Both are significantly lower than the estimate of 3.94% from the 2023-24 Enacted Budget. While there are still two data points outstanding in order to calculate the final statutory COLA—one anticipated in a matter of weeks and the other at the end of April—time will tell whether the Administration or the LAO have a clearer crystal ball, it is very apparent that the statutory COLA will be closer to 1% than 4%.

The Governor estimates that it will cost \$69.1 million ongoing to provide SCFF the COLA. Additionally, the Governor's Budget proposal reflects withdrawals from the K-14 Rainy Day Fund in order to avoid major spending reductions. For the SCFF, the Governor's Budget proposes withdrawals from the K-14 Rainy Day Fund of \$235.9 million for 2023-24 and \$486.2 million in 2024-25.

As a reminder the 2021-22 Enacted Budget extended the SCFF hold harmless provision, by which districts earn at least their 2017-18 total computational revenue (augmented by COLA each year), through the 2024-25 fiscal year. The 2022-23 Enacted Budget extended the hold harmless protections with some modifications. Specifically, the 2022-23 Enacted Budget stipulates that a district's 2024-25 funding become its new "floor" beginning with the 2025-26 fiscal year. This means that beginning in 2025-26, districts will be funded at either their SCFF-generated amount for that year or their 2024-25 "floor" amount, whichever is greater. It is important to note that the modified hold harmless will not include adjustments to reflect COLA over time, meaning a district's hold harmless amount will not grow like it did through 2024-25. Since the 2024-25 funding will lock in districts' new hold harmless "floor," it is a crucial year for community college districts.

Additionally, Governor Newsom also proposes to provide \$29.6 million to fund 2024-25 student enrollment growth of 0.5%.

California Community College (CCC) Facilities and Deferred Maintenance Cut

The 2023-24 Enacted Budget included a net reduction of \$494.3 million deferred maintenance reduction based on reductions and appropriations from the 2021-22, 2022-23, and 2023-24 fiscal years. While the [2024-25 System Budget and Legislative Request](#) included a request for the state to restore the nearly \$500 million cut in deferred maintenance, there is nothing in the Governor's Budget summary that indicates that those dollars will be restored. With the budget situation being what it is, it is very unlikely that those dollars will be restored in the final Enacted Budget.

Proposition 51 (2016) authorized \$2 billion in state General Obligation bonds to support the improvement and construction of community college facilities. The Governor's Budget summary indicates that over 98% of these bonds have been committed to addressing nearly 100 critical infrastructure projects. Governor Newsom is only proposing funding for one project in 2024-25. He is proposing to use \$29.3 million in Proposition 51 dollars for the e Siskiyou Joint Community College District, College of the Siskiyous: Remodel Theater and McCloud Hall project.

Despite the lack of facilities dollars included in the State Budget proposal, Governor Newsom said that his Administration expects to enter into negotiations with the Legislature on their education facilities bond proposals to reach agreement on a bond proposal to be considered in the November 2024 election (see "[Statewide Facilities Bond Bills Pending in the Legislature](#)" in the June 2023 Community College Update article for more specifics about the two bond bills). Lawmakers have until Thursday, June 27, 2024, to qualify a statewide school facilities bond for the November 5, 2024, General Election ballot.

Other CCC Apportionments and Categorical Programs

Other community college programs that are funded outside of the SCFF that would also receive the 0.76% COLA under the Governor's Budget proposal are: Adult Education, Extended Opportunity Programs and Services, Disabled Students Programs and Services, Apprenticeship, CalWORKs Student Services, Mandates Block Grant and reimbursements, Cooperative Agencies Resources for Education, and the childcare tax bailout. The Governor's Budget assumes \$9.3 million ongoing to cover the COLA for the above programs.

The Governor is also proposing a one-time investment of \$60 million to expand nursing programs and Bachelor of Science in Nursing partnerships to develop, educate, and maintain the next generation of registered nurses through the community college system, subject to future statutory changes. We will get more information about this proposal when trailer bill language is released in a few weeks.

Student Housing

The 2023-24 Enacted Budget shifted the funding sources for all Higher Education Student Housing Grant Program projects from the state General Fund to local lease revenue bonds issued by colleges. This change applied to the 12 prior community college projects originally funded by \$547 million (non-Proposition 98) in the 2022-23 Enacted Budget, the seven new community college housing projects authorized in the 2023-24 Enacted Budget, and any future housing projects.

After the CCC field expressed issues about this shift, lawmakers approved intent language in the higher education budget clean up trailer bill for “a statewide lease revenue bond or other statewide financing or fiscal approach be developed and included to support California community college affordable student housing projects.”

The Governor’s Budget proposal says that the Administration remains committed to a statewide lease revenue bond approach. While we thought that proposal might be considered for early action, it is not fully fleshed out and won’t be released for consideration until the May Revision.

The 2023-24 Enacted Budget provided about \$61.5 million in ongoing (non-Proposition 98) funding for annual rental subsidies for affordable student housing. The Governor’s Budget proposal redirects these funds to instead support CCC affordable student housing programs that do not fit within the lease revenue approach referenced above. The specifics of this shift will be shared in upcoming trailer bill language.

To address the projected budget shortfall, the Governor also proposes suspending funding for the California Student Housing Revolving Loan Fund Program, which includes pulling back \$300 million one-time (non-Proposition 98) previously intended to be appropriated for the program for each year from 2024-25 to 2028-29, and reverting \$194 million of \$200 million one-time (non-Proposition 98) that was appropriated in 2023-24, which is the amount estimated to be net of the program’s expected operational costs.

Master Plan on Career Education

On August 31, 2023, Governor Gavin Newsom signed [Executive Order N-11-23](#), launching the development of a new Master Plan on Career Education (Master Plan) that will look to adequately prepare students for the workforce of tomorrow. The Executive Order (EO) requires specified state agencies to develop and submit the proposed Master Plan to the Governor’s Office by October 1, 2024.

The first phase in the development of the Master Plan is for the Governor’s Office to convene interagency teams at both the state level (under the [Governor’s Council for Career Education](#)) and at the regional level (as part of the [K-16 Regional Collaboratives](#)) that will drive results on the tens of billions in workforce investments made in the first four years of the Newsom Administration. The second phase is to engage in a 13-month planning process to investigate how existing policies, investments, and structures can be improved, culminating in the Governor’s Master Plan scheduled for publication in the winter of 2024. The three goals of the plan are to ensure that all Californians are:

1. On-ramped into well-paying, purposeful careers.
2. Empowered to build real-life skills.
3. Able to access and afford a quality education throughout life.

While the Governor's State Budget proposal does not offer any new information on the Master Plan, it does clarify that the Governor intends to pursue the timeline stipulated in the EO despite the state's challenging budget circumstances.

Minimum Wage

Governor Newsom does not make any changes to the already enacted California state minimum wage of \$16.00 an hour or to Assembly Bill 1228 (Holden, Statutes of 2023) which raises the minimum wage for fast food workers to \$20.00 an hour, effective April 1, 2024. The proposed Governor's Budget does include an annual budgetary "trigger" which could delay the effective date of Senate Bill 525 (Durazo, Statutes of 2023) which was written to increase the minimum wage for health care workers to \$25.00 an hour effective June 1, 2024.

Retirement Systems

Governor Newsom does not propose additional funding for the California State Teachers' Retirement System (CalSTRS) or the California Public Employees' Retirement System (CalPERS) employer contribution rate relief for community colleges. Based on current assumptions, CalPERS employer contributions would increase from 26.68% to 27.80% in 2024-25, while CalSTRS employer contribution rates are expected to remain the same from the prior year at 19.10%.

The Rest of Higher Education

In order to address the projected budget shortfall, the Governor proposes to defer the planned University of California (UC) 2024-25 Compact investment of \$227.8 million and the planned investment of \$31 million to offset revenue reductions associated with the replacement of 902 nonresident undergraduate students in 2024-25. The Governor argues that these deferrals would largely maintain ongoing UC General Fund at 2023-24 levels, while enabling the UC to use interim financing structures or other internal borrowing to support UC spending at the planned 2024-25 Compact level and at the level necessary to offset revenue reductions associated with the replacement of 902 nonresident undergraduate students enrolled in 2024-25.

The Governor takes a similar approach with the California State University (CSU). In order to address the projected budget shortfall, the Governor proposes to defer the planned 2024-25 Compact investment of \$240.2 million to 2025-26. This deferral would largely maintain ongoing CSU General Fund at 2023-24 levels, while enabling the CSU to use interim financing structures or other internal borrowing to support CSU

spending at the planned 2024-25 Compact level. The Governor argues that this approach will enable the CSU to continue its efforts to meet the Compact goals to expand student access, equity, and affordability, and to create pathways to high-demand career opportunities.

K-12 Education Proposals

The Governor's Budget also proposes applying the 0.76% COLA to the K-12 Local Control Funding Formula (LCFF) and categorical programs. Of the proposed \$5.7 billion PSSSA withdrawals across the current and budget year, the Administration is proposing to allocate \$5.0 billion for purposes of supporting the LCFF—approximately \$2.8 billion for 2023-24 and another \$2.2 billion for 2024-25.

The Governor's Budget also includes a series of instructional continuity proposals aimed at offsetting student absences and mitigating learning loss. These proposals include:

- Expanding the allowable days and times of day used for the purpose of recovering attendance both for the purpose of apportionment and chronic absentee mitigation,
- Requiring local educational agencies (LEAs) to offer remote instruction during emergencies, including instruction through enrollment at a neighboring LEA, and
- Encouraging hybrid or remote learning opportunities for students who are unable to attend school

Regarding facilities, the Newsom Administration proposes to further delay the planned \$550 million California Preschool, Transitional Kindergarten and Full-Day Kindergarten Facilities Grant Program investment to 2025-26 and to reduce a planned 2024-25 investment for the School Facility Program from \$875 million to \$375 million.

Closing

The education world had been expecting the worst since the release of the LAO's economic forecast this past fall, leaving many to let out a sigh of relief at the Governor's Budget release—although a skeptical one. The Governor's Budget benefits from historic rainy day funds to address spending levels that ultimately did not align with the level of revenues generated in 2022-23. For education, these one-time dollars sustain programs that were created or grew significantly during exceptional economic times and lead the community to wonder how they will be sustained after 2024-25.

While not facing mid-year cuts, deferrals, or unfunded COLAs, with the combination of a COLA below 1% and little else, the sigh of relief may be short lived.