

*Happy Holidays from . . .*



# COMMUNITY COLLEGE UPDATE

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PUBLIC EDUCATION'S POINT OF REFERENCE FOR MAKING EDUCATED DECISIONS

## LAO Issues Fiscal Outlook



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The Legislative Analyst's Office (LAO)—the nonpartisan budget and policy advisor for the Legislature—issued its highly anticipated [Fiscal Outlook](#) report today. The expectation of the *Fiscal Outlook* is heightened this year due to the thrice-delayed tax filing deadline, which was shifted from April 2023 to November 2023, and the anticipation of where the dust would settle for tax collections from the 2022 calendar year.

### Overall Themes

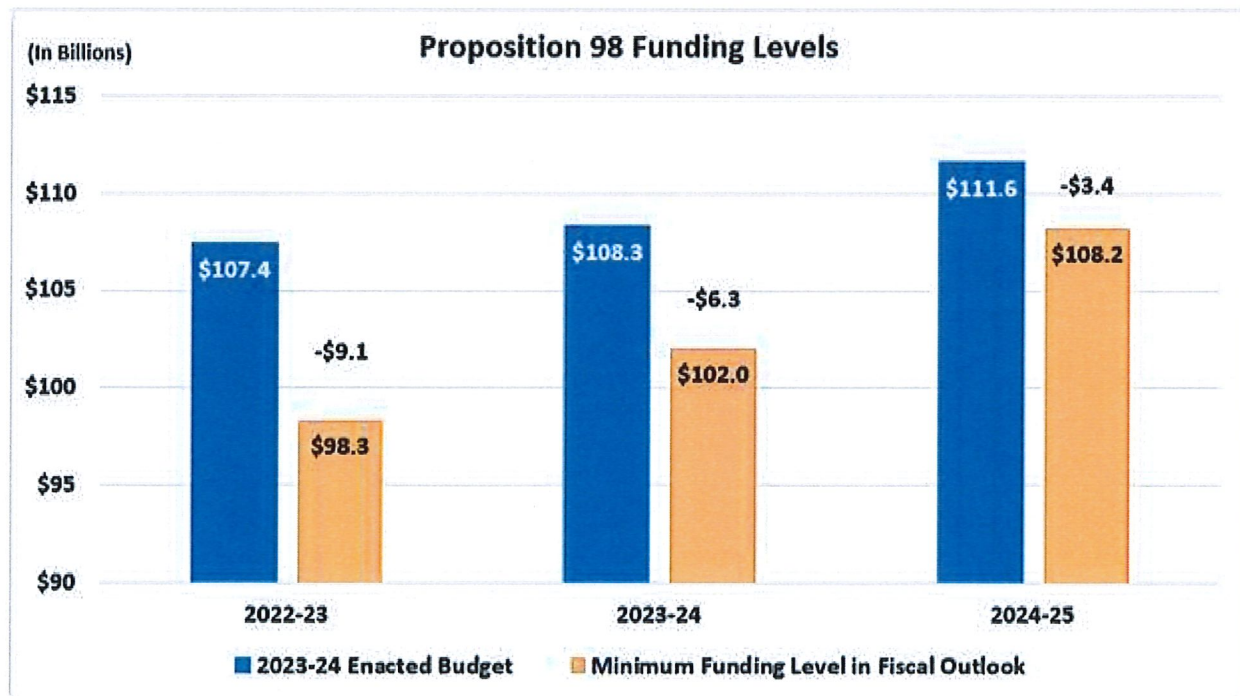
The health of California's General Fund peaked in the 2021-22 fiscal year with record revenues and reserves. However, most financial experts across the state expected that revenues would begin to taper off beginning in 2022-23 and 2023-24 relative to 2021-22. The tapering quickly turned into an exceptional shortfall, as the final estimated tax collections for 2022-23 were approximately \$26 billion less than the projection used for the 2023-24 Enacted Budget. As a result, the *Fiscal Outlook* provides three key takeaways:

- California faces a serious deficit going forward
- Unprecedented prior-year revenue shortfall
- The Legislature will need to utilize tools to address the budget problem

The *Fiscal Outlook* reports that the state’s economy entered a downturn in 2022 due to higher borrowing costs and reduced investments. This is highlighted by a decline in home sales of approximately 50%, lowered investments in startup and technology companies, and a decline of more than 80% in the number of California companies with initial public offerings. In total, the *Fiscal Outlook* estimates that the state faces a \$68 billion deficit over the three-year period covering 2022-23 to 2024-25.

### Outlook for Schools and Community College Funding

As a result of depressed tax collections in 2022 and a softening economy, the *Fiscal Outlook* projects that Proposition 98 is overcommitted by \$15.4 billion in the 2022-23 and 2023-24 fiscal years when compared against the 2023-24 Enacted Budget.



The *Fiscal Outlook* estimates that the state would need to spend \$109.3 billion to cover the cost of existing programs, adjusted for attendance and a cost-of-living adjustment—estimated to be 1.27%—in the 2024-25 fiscal year. This amount exceeds the LAO’s projected Proposition

98 funding requirement by approximately \$1.1 billion.

### **LAO Recommendations for Education**

The LAO highlights two pathways available to the Legislature as they enter 2024-25 budget negotiations. First, the Legislature could lower Proposition 98 spending down to the minimum funding levels noted in the chart above. This would require schools and community colleges to “send back” funding that has already been apportioned or is scheduled to be apportioned. Second, the Legislature could withdraw funds from the Proposition 98 reserve—the current balance is \$8.1 billion after adjustments are made to prior- and current-year deposits—to support a funding level that is greater than the minimum funding levels. The second option has ripple effects in 2024-25. Should the Legislature choose to “over-appropriate” Proposition 98 in 2022-23 and 2023-24 at the levels in the 2023-24 Enacted Budget, the projected minimum funding level in 2024-25 would increase from \$108.2 billion to \$113 billion, an amount greater than what was included in the 2023-24 Enacted Budget. However, that effect is partially blunted by the use of Proposition 98 reserves, which, from an accounting perspective, do not count as spending for the purpose of determining the minimum funding requirement in future years. Regardless of which scenario is selected, the *Fiscal Outlook* projects that the entire Proposition 98 reserve will be required to be withdrawn no later than the 2024-25 fiscal year, but the reserve could be exhausted in the current fiscal year should the Legislature choose to “over-appropriate” Proposition 98 in the prior and current fiscal years.

### **The Road Ahead**

The figures in the *Fiscal Outlook* report, while somewhat anticipated, still create an unpleasant reverberation in the state and K-14 community that will impact every corner of the state. The sobering news that 2021-22 was indeed the peak now begs the question, “How far will state revenues fall before normalizing?” Although that answer will not be known for several months, if not a year, more information about how the state will address the revenue shortfall will be available on or before January 10, 2024, when Governor Gavin Newsom unveils his priorities for the state and education as part of his 2024-25 State Budget proposal.