California State Assembly

Assembly Budget Agenda

Assembly Budget Subcommittee No. 3 on Education Finance

Assemblymember David Alvarez, Chair

Tuesday, February 10, 2026

9:00a.m. – State Capitol, Room 447

Items To Be Heard

Item	Description	Page
6100	**California Department of Education** **Proposition 98: All Agencies**	**2**
Issues	1. Proposition 98 and Guarantee Estimates 2. Public School System Stabilization Account 3. Education Funding Deferrals	2 13 17

Items To Be Heard

Proposition 98: All Agencies

Issue 1: Proposition 98 Guarantee

This issue will cover the Proposition 98 guarantee, as projected in the Governor's Budget, for the 2024-25, 2025-26, and 2026-27 Budget years. This issue will also cover the Governor's Budget proposals impacting the guarantee calculation, including Maintenance Factor payments and balance, rebenching, and Proposition 98 settle-up.

Panel

- Alex Shoap, Department of Finance (DOF)
- Kenneth Kapphahn, Legislative Analyst's Office (LAO)

Background

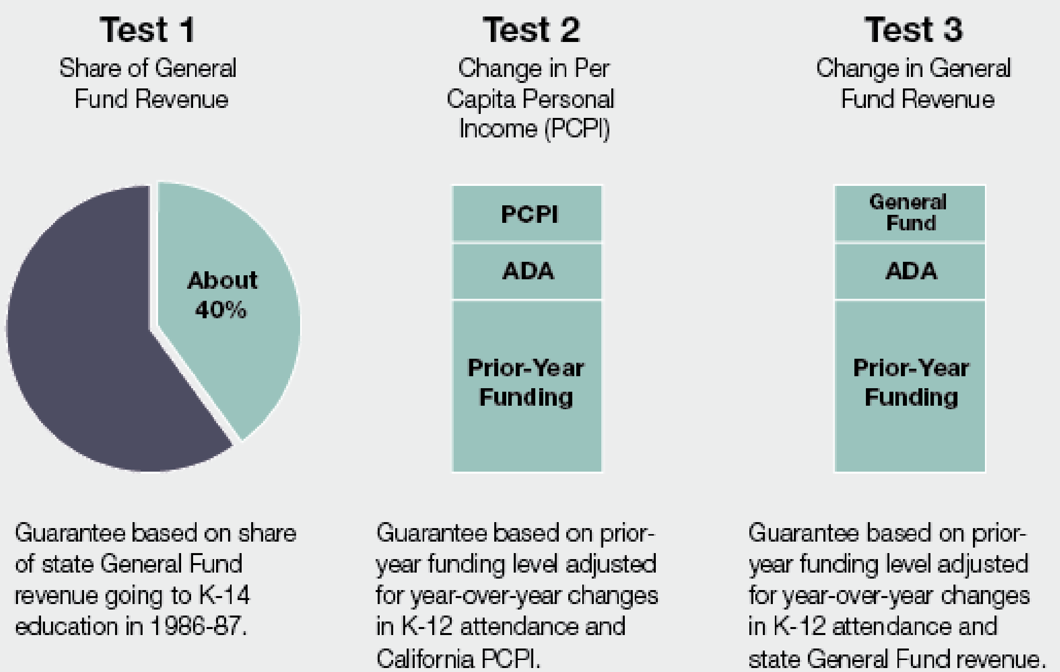
The State Constitution was amended by California voters, through Proposition 98 in 1988, to create a minimum "guarantee" for public school and community college funding. Proposition 98 provides TK-14 schools and colleges with a guaranteed funding source that grows each year with the economy and the number of students. The guarantee consists of state General Fund and local property tax revenue.

The Constitution sets forth three main "tests" for calculating the Proposition 98 minimum guarantee. Each test takes into account certain inputs, including General Fund revenue, per capita personal income, and student attendance (LAO, Figure 1, on the next page). Test 1 links school funding to a minimum share of General Fund revenue, whereas Test 2 and Test 3 build upon the amount of funding provided the previous year. The Constitution sets forth rules for comparing the tests, with one of the tests becoming operative and used for calculating the minimum guarantee that year.

Although the state can provide more funding than required, it usually funds at or near the guarantee. With a two-thirds vote of each house of the Legislature, the state can suspend the guarantee and provide less funding than the formulas require that year.

Figure 1

Three Proposition 98 Tests



ADA = average daily attendance.

The state makes an initial estimate of the guarantee when it enacts the annual budget, but this estimate typically changes as the state updates the relevant Proposition 98 inputs.

When the guarantee exceeds the initial budget estimate and appropriation, the state must schedule an additional appropriation to "settle up" for the difference. If the guarantee drops, the state can reduce spending to the lower guarantee. After making these revisions, the state finalizes its calculation of the guarantee through an annual statutory process called "certification." Certification involves the publication of the underlying Proposition 98 inputs and a period of public review. The most recently certified year is 2023-24. The process of 2024-25 certification will begin in May of 2026.

Figure 6

Typical Schedule for Updating Proposition 98 Estimates and Paying Settle Up

Budget-Year Estimates (Before the Year Begins)

- Legislature adopts June budget with initial estimates of the guarantee.
- Budget appropriates funding to meet the estimated guarantee.

Current-Year Revisions (as the Year Ends)

- Legislature adopts revised estimate of the guarantee in June.
- Settle up paid if guarantee rises.
- Spending reduced if guarantee drops.

Spending revised up or down

Prior-Year Revisions (One Year After the Year Ends)

- Legislature adopts final estimate of the guarantee in June.
- Settle up paid if guarantee rises.
- Certification process begins with public review and comment period.

Upward spending adjustments only

Certification (Two Years After the Year Ends)

- State certifies final Proposition 98 calculations.
- Legal challenge period (90 days).
- Director of the Department of Finance provides a schedule for paying any settle-up obligation that the state did not previously address.

No further spending adjustments

Calculations and Appropriations Are Final

LAO

2023-24 Proposition 98 Guarantee Suspension

Suspension and Maintenance Factor. The Legislature, with a two-thirds vote, can suspend the Proposition 98 minimum guarantee for a fiscal year. Under a suspension, the Legislature can appropriate K-14 funding at whatever level it chooses, but creates "maintenance factor" obligations for the out-years.

The state creates maintenance factor when Test 3 is operative or the Legislature suspends the guarantee. The maintenance factor obligation equals the difference between the actual level of funding provided and the higher Test 1 or Test 2 level. Moving forward, the state adjusts the obligation annually for changes in student attendance and per capita personal income. In future years, the Constitution requires the state to make maintenance factor payments when General Fund revenue is growing faster than per capita personal income. The size of these payments increases in tandem with faster revenue growth. These payments add to the guarantee in the future and accelerate school funding increases until the obligation is paid down.

2022-23 Budget Act Shortfall. In March 2023, the state delayed the deadline for various personal income and corporation tax payments to conform with delays in federal tax deadlines. When the state finally received these payments in November 2023, they showed that revenues for 2022-23 were far below the previous estimate. These lower revenues eventually reduced the Proposition 98 guarantee that year by $9.8 billion—an unprecedented drop for a fiscal year that was already over. This drop led to a debate about whether the state should reduce school and community college funding to the lower guarantee or maintain funding at the higher level it originally approved. A major consideration was that significant changes to 2022-23 would have led to corresponding changes in the Proposition 98 guarantee in 2023-24 and 2024-25.

The final budget agreement involved funding schools above the revised guarantee in 2022-23, suspending the guarantee in 2023-24, withdrawing funds from the Proposition 98 "Rainy Day Fund," and shifting payments across fiscal years.

Suspension of the Proposition 98 Guarantee in 2023-24. Under the previously enacted budget, the Proposition 98 guarantee would have required the state to provide $106.8 billion in funding in 2023-24. The state determined it could not afford to fund schools and community colleges at this level and suspended the guarantee that year.

Trailer bill legislation set the funding level for 2023-24 at $98.5 billion. By suspending the guarantee, the state automatically created an obligation—known as maintenance factor—equal to the $8.3 billion difference between the suspended funding level and the guarantee. Use of the Prop 98 Rainy Day Fund ensured actual school funding in 2023-24 was not reduced during this Suspension.

Rebenching the Proposition 98 Guarantee & Transitional Kindergarten

Modifications to the Proposition 98 guarantee calculations, beyond the constitutional Prop 98 inputs under either of the three "tests," are commonly known as a "rebench." The state constitution is silent on whether the Proposition 98 minimum guarantee can be adjusted to account for policy changes, but a rebench has been adopted in prior years to prevent certain state actions from having unintended consequences on the Proposition 98 minimum guarantee. In prior rebench budget actions, the state adjusted the total Guarantee for the single fiscal year value of the shift, thereby ensuring that it achieved an associated dollar–for–dollar impact. For example, the removal of child care programs from the Proposition 98 calculation resulted in a $1.1 billion reduction in the guarantee, and the shift of responsibility for student mental health services from counties to school districts resulted in a $222 million increase in the guarantee.

The 2021-22 Budget agreement included shared Administrative and Legislative intent to rebench the Proposition 98 guarantee to accommodate the growth of average daily attendance (ADA) for Universal Transitional Kindergarten (UTK). This agreement and statutory timeline would add new UTK enrollment and ADA in Budget years 2022-23, 2023-24, 2024-25, and 2025-26. The intent is that the Proposition 98 guarantee would be rebenched in each year of statutory UTK eligibility growth, to reflect the actual costs of the new grade's ADA. The intent of the agreement is to create adequate room inside the guarantee in each year TK enrollment is required to expand in statute, and then adjust for actual attendance impacts.

"The Split" for School and Community Colleges

The state divides Proposition 98 funding between schools and community colleges using an uncodified methodology known as "the split." The methodology involves allocating approximately 89 percent of the available funding to schools and approximately 11 percent to community colleges, with certain expenditures excluded from these percentages.

The 2025-26 Budget established a new exclusion to "the split", beginning in 2025-26, for the costs associated with the recent expansion of TK. Compared with the previous methodology, this modification shifted $233 million in ongoing Proposition 98 funding from community colleges to schools, as of the enacted Budget.

Governor's 2026-27 Budget

Guarantee Estimates

The Governor's January Budget estimates a total Proposition 98 funding level of $123.8 billion in 2024-25, $121.4 billion for the 2025-26 Current Year, and $125.5 billion in the 2026-27 Budget Year. This represents a total of $14.9 billion in estimated available funding over the three-year budget window, compared to the 2025-26 Budget Act (LAO Figure below).

Compared with the 2025-2026 Budget enactment, the administration's estimate of the minimum guarantee is up $6.9 billion (6 percent) in 2025-26 and remains in Test 1.

Compared with the June 2025 budget estimate, the administration's estimate of the minimum guarantee is up $3.9 billion (3.2 percent) in the 2024-25 Prior Year.

Proposition 98 Key Inputs and Outcomes Under Governor's Budget

Dollars in Millions

	2024-25	2025-26	2026-27
Minimum Guarantee			
General Fund	$91,197	$87,473	$89,877
Local property tax	32,636	33,947	35,604
Totals	**$123,833**	**$121,420**	**$125,480**
Change From Prior Year			
General Fund	$24,182	-$3,724	$2,404
Percent change	36.1%	-4.1%	2.7%
Local property tax	$1,166	$1,311	$1,656
Percent change	3.7%	4.0%	4.9%
Total guarantee	$25,349	-$2,413	$4,061
Percent change	25.7%	-1.9%	3.3%
General Fund Tax Revenue[a]	$213,420	$222,181	$228,467
Growth Rates			
K-12 average daily attendance	-0.4%	0.6%	-0.3%[b]
Per capita personal income (Test 2)	3.6	6.4	4.4
Per capita General Fund (Test 3)[c]	11.4	4.1	3.3
Maintenance Factor			
Amount created (+) or paid (-)	-$7,768	—	—
Total outstanding[d]	523	$560	$585
Proposition 98 Reserve			
Deposit (+) or withdrawal (-)	$3,845	$664	-$407
Cumulative balance	3,845	4,509	4,102
Operative Test	1	1	1

[a] Excludes nontax revenues and transfers, which do not affect the calculation of the guarantee.

[b] This decline is deemed to be zero for the purpose of calculating the guarantee. As set forth in the State Constitution, an attendance decline does not reduce the guarantee unless attendance has declined in the two previous years.

[c] As set forth in the State Constitution, reflects change in per capita General Fund plus 0.5 percent.

[d] Includes adjustments to the previous year's maintenance factor for growth in per capita personal income and K-12 attendance as required by the State Constitution.

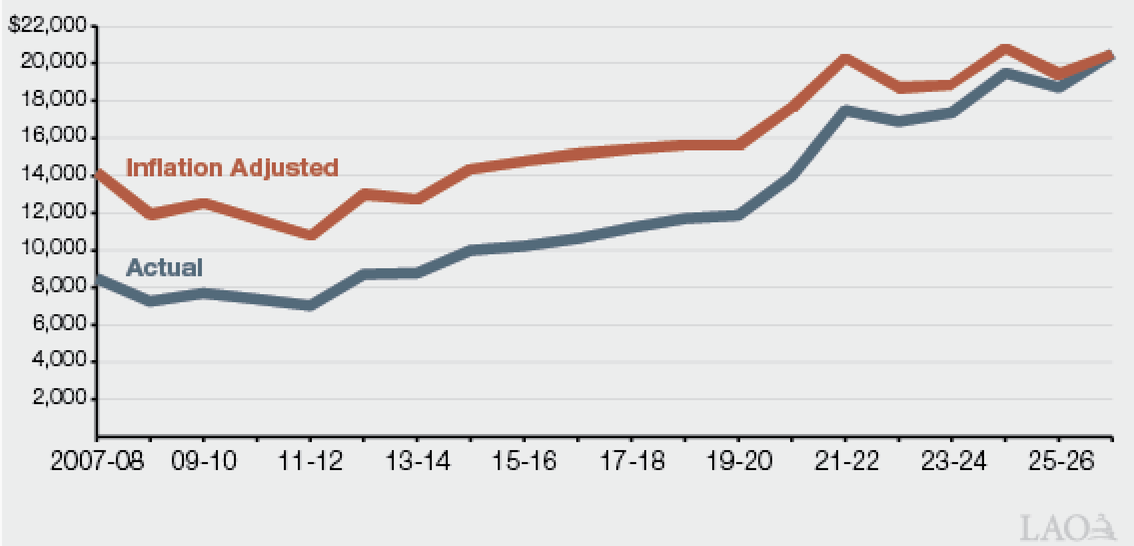
Source: LAO

Under the Governor's budget, total Proposition 98 funding for schools would be $20,427 per student in 2026-27, an increase of $1,887 (10.1 percent) per student over the 2025-26 Budget Act. Total Proposition 98 funding would increase $10.9 billion (9.5 percent) over the enacted 2025-26 level.

Figure 8

Proposition 98 Funding Per Student Is Volatile but Growing

Through 2026-27 Under Governor's Budget



According to the LAO, the 2026-27 per pupil funding level is actually $300 lower than the 2024-25 level, when adjusted for inflation, as seen in the graph above.

Universal Transitional Kindergarten Rebench

The January Budget estimates $121.4 billion for Proposition 98 funding for 2025-26, which includes an $190 million reduction to the rebench of the guarantee to reflect the final year of Universal Transitional Kindergarten enrollment growth. According to DOF, this reflects the approximately 139,000 additional children eligible for and attending UTK in the final implementation year.

The January Budget estimates $123.8 billion for Proposition 98 funding for 2024-25, which includes an $80.4 million reduction to the rebench of the guarantee to reflect actual school year attendance, with 5,900 fewer students than the prior estimate.

The actual 2025-26 ADA in TK will impact the final rebench amount, which is estimated in the January Budget at a total of $2 billion, over the four years of UTK rollout.

Maintenance Factor Payments

The 2023-24 Proposition 98 suspension created a maintenance factor obligation of $8.3 billion.

The increase in the Prior Year guarantee increases the 2024-25 Maintenance Factor payment to a total of $7.8 billion, compared to $2.3 billion from the June 2025 estimate.

DOF projects a $584.6 million maintenance factor remainder at the end of the Budget Year, and does not estimate payments in 2025-26 or 2026-27.

Settle-Up Proposal

In the January Budget, total proposed spending on schools and community colleges in 2025-26 is approximately $5.6 billion less than the DOF revised estimate of the Proposition 98 guarantee.

The difference between the Governor’s Prop 98 estimate and proposed total spending would create a $5.6 billion settle-up obligation the state would need to pay in the future if general fund revenues remain consistent with the January projections. The administration indicates the state would address the “settle-up” pursuant to statute, after the state makes its final revenue estimate for 2025-26, recalculates the guarantee, and determines the amount actually owed to schools. According to the administration, the delay is intended to mitigate the risk that the guarantee drops, as experienced during the uncertainties of the 2022-23 Budget Act.

The 2025-26 Budget Act adopted the Governor’s settle-up proposal for the 2024-25 Proposition 98 guarantee, but earmarked $1.9 billion in estimated Prop 98 funds for future appropriations, once the guarantee was certified. The Budget trailer bill specified legislative intent that the unappropriated funds be uses to reduce ongoing deficits and protect core program funding, and required the January Budget to utilize the funds for ongoing school and community college growth costs, and to reduce funding deferrals.

The January Budget maintains this Budget agreement and proposes to appropriate the estimated $1.9 Billion 2024-25 settle-up to eliminate the education deferrals. The Governor’s Budget estimates an additional $2 Billion in 2024-25 settle-up, and proposes appropriations to meet the higher requirement as part of the 2026-27 Budget Act.

“The Split”

The January Budget increases Community College spending in 2024-25, one-time, by $391 million above the traditional 11% split for community colleges as a total share of Proposition 98 spending.

LAO Comments

Recommendations

Alternative Approach Makes Difficult Decisions Now but Reduces Future Budget Challenges. We recommend an alternative to the Governor's proposal that would continue to mitigate short-term forecasting risk while also reducing future state costs and better protecting school and community college programs from future downturns. This approach entails additional solutions affecting the non-Proposition 98 side of the budget this year. Some details of this alternative will depend on the state's updated revenue estimates in May. The Legislature could adopt the alternative under a range of potential revenue scenarios, but for illustrative purposes, we describe its effects using the Governor's budget as the baseline.

Fully Fund the Estimate of the Guarantee. We recommend the Legislature allocate enough funding to cover the full cost of the guarantee based on the revenue estimates it adopts. Relative to the Governor's budget, the state would need to set aside an additional $5.6 billion. Adopting this approach would recognize the full cost of the state's school funding obligations this year and avoid creating new settle-up obligations

Deposit Some of the Additional Funding Into the Proposition 98 Reserve. Whereas we recommend setting aside additional funding to meet the guarantee, we do not recommend a corresponding increase in school and community college spending this year. Instead, we recommend (1) making a larger deposit into the Proposition 98 Reserve, and (2) adopting trailer legislation that automatically reduces the deposit if the 2025-26 guarantee declines relative to May estimates. The savings from any reductions in the deposit would help the state balance the budget. Like the Governor's proposal, this approach would allow the state to avoid inadvertently exceeding the guarantee if revenues fall short of projections, thereby mitigating the state's short-term forecasting risk. We recommend that the Legislature make a total deposit of at least $3.5 billion in 2025-26. This deposit would provide a buffer to address the likely range of reductions to the 2025-26 guarantee relative to the state's May estimate. The Governor's budget already contains $644 million in Proposition 98 Reserve deposits for 2025-26, so implementing this recommendation would involve an additional deposit of $2.9 billion.

Use Remaining Funds to Build Additional Resiliency for School Programs. If the state makes an additional $2.9 billion deposit in 2025-26, it would have $2.7 billion remaining for other one-time school and community college priorities (relative to the Governor's budget). We recommend using this funding to build additional resiliency for school programs. One option is to deposit all the remaining funds into the Proposition 98 Reserve, bringing the total balance to $9.7 billion. At this level, the reserve likely would be large enough to protect school and community college programs from the initial effects of a significant downturn. Another option is to provide advance payments to districts toward their 2027-28 funding allotments, consistent with an approach we outlined in our November 2025 report, The 2026-27 Budget: Fiscal Outlook for Schools and Community Colleges. This approach would help protect district cash flow by reducing the state's reliance on deferrals to manage future downturns. A third option is to provide additional funding for district pension costs. The state could structure this payment to reduce pension costs over time or to provide short-term relief if costs rise above a specified threshold. This approach would build resiliency by reducing future pressure on district budgets.

Adopt Solutions That Address the State's Underlying Budget Problem. Setting aside enough funding to cover the guarantee means adopting a commensurate level of budget solutions for the non-Proposition 98 side of the budget this year. (Using the Governor's budget as a baseline, the state would need $5.6 billion in additional solutions.) As we explained in The 2026-27 Budget: Overview of the Governor's Budget, we recommend the Legislature adopt a plan to shrink multiyear deficits that includes spending reductions, revenue increases, or a combination of both. (General Fund tax increases would increase the state's constitutional requirements further, eroding some of the benefit to the budget's bottom line.) These additional solutions would entail difficult decisions amidst an already tight budget. Nevertheless, taking this proactive approach would avoid an even more difficult budget situation next year and begin to address the state's structural deficit.

Consider Repealing Prohibition on Prior-Year Spending Reductions. Repealing the law on prior-year spending reductions would mitigate some of the risk motivating the Governor's settle-up proposal. It would also reduce pressure to use funding maneuvers, spending exclusions, settle-up delays, or similar actions that complicate state budgeting and make school funding less predictable. If the Legislature wanted to implement the recommendation in a way that protected local district budgets, it could replace the law with a less strict alternative. Specifically, it could allow reductions through state-level accounting adjustments while still prohibiting reductions that require districts to return previous funding.

Staff Comments

The current year and Budget Year Proposition 98 funding estimates and relevant proposals will be considered as part of the Final Budget guarantee estimate, and so no action will be recommended until after the May Revision.

Balancing Volatile Revenues & Stable School Funding. Due to the volatile nature of state revenue growth, significant one-time Prop 98 funding has become a common budget opportunity. Unfortunately, one-time funding can be treated as a short-term investment for the state and local LEAs, and can create cliffs in funding for ongoing priorities.

In light of the large, projected, one-time funds available for Prop 98 purposes, how could one-time funds create ongoing-like pathways to sustainability and coherence with local LEA goals?

With the magnitude of the January Budget's settle-up proposal, what are the ongoing-like priorities for the Legislature to identify, for this investment?

Suggested Questions:

1. What is the best policy to address the “new normal” of large one-time surplus revenues, year over year?

2. What are the right metrics of volatility, inside the Prop 98 calculation, to consider for the proposed settle-up size?

3. Why is the Current Year settle-up amount significantly larger than the Prior Year?

4. Why is the total amount unappropriated, and not a voluntary and conditional contribution to the PSSSA?

5. Does DOF have priorities in mind for the $5.6 billion settle-up, if those funds materialize?

6. The settle-up proposal addresses volatility inside the Current Year. What proposals address volatility inside the Budget Year estimates? Are they sufficient in size?

7. What proposals would DOF reduce or eliminate in the Budget Year, if revenues are lower at May Revision? Or are there other ways to prevent LEAs from Budgeting from the January proposals, as occurred in recent past?

8. What is the Administration’s intent on “the split,” if community college enrollment growth outpaces the split moving beyond 2024-25?

9. Are we artificially restraining ongoing actual growth in the guarantee being used for ongoing priorities at the local level? What is the actual ongoing growth between 2023-24 revenues, 2024-25 revenues, and 2025-26 projected revenues, under the revised collections and guarantee estimates?

Staff Recommendation: Hold Open.

Issue 2: Public School System Stabilization Account Overview & Proposals

This issue will cover the Public School System Stabilization Account (PSSSA) contributions and withdrawals in the January Budget.

Panel

- Alex Shoap, Department of Finance
- Kenneth Kapphahn, Legislative Analyst's Office

Background

Proposition 2 (2014) established the PSSSA or “Prop 98 Rainy Day Fund”, a constitutional reserve account within Proposition 98. The purpose of this reserve is to set aside some Proposition 98 funding in relatively strong fiscal times to mitigate funding reductions during economic downturns. Prop 98 Rainy Day Fund can grow to a maximum of 10% of the Proposition 98 guarantee in the Budget Year. A deposit to the PSSSA was first triggered in the 2019-20 budget. Withdrawals are attributed to the Prop 98 guarantee in the deposit year.

The 2021-22 budget plan triggered a statutory cap on school district reserves in the 2022-23 fiscal year. The local cap applies the year after the balance in the Prop 98 Rainy Day Fund exceeds 3 percent of the Proposition 98 funding allocated to TK-12 schools. The cap prohibits medium and large districts—those with more than 2,500 students—from holding general purpose reserves that exceed 10 percent of their annual expenditures. Districts can respond to the cap by designating their reserves for specific purposes, seeking exemptions from their county offices of education (COEs), or spending down their reserves. When the local reserve cap went into effect in 2022-23, the LAO estimated that approximately 265 LEAs statewide would be impacted, and that districts held a total of $21 billion in reserves.

Under the enacted 2023-24 Budget, the state deposited a total of $7.5 billion into this Prop 98 Rainy Day Fund across the 2021-22 through 2023-24 period—an increase of $1.3 billion compared with the estimates made in June 2022. These deposits brought the total balance in the Prop 98 Rainy Day Fund to $10.8 billion in 2023-24—10 percent of the Proposition 98 guarantee, the maximum amount allowed.

The Constitution provides two Prop 98 Rainy Day Fund withdrawal options. The first requires the state to withdraw funds from the Fund if the guarantee is below the prior-year funding level, as adjusted for student attendance and inflation. The amount withdrawn equals the difference between the prior-year adjusted level and the actual guarantee, up to the full balance in the Prop 98 Rainy Day Fund. If the Governor declares a budget emergency, the Legislature may withdraw any amount from the reserve or suspend required deposits. Unlike other state reserve accounts, the Prop 98 Rainy Day Fund is available only to supplement the funding schools and community colleges receive under Proposition 98.

2024-25 and 2025-26 Budget Acts

The suspension of the Prop 98 guarantee in 2023-24 set a minimum guarantee funding level for schools below the appropriated 2022-23 level. This lower 2023-24 funding level triggered the Prop 98 Rainy Day Fund required withdrawal threshold, and the state withdrew the entire balance of $8.4 billion. The 2023-24 adjusted budget allocated $7.6 billion of this amount for schools and $788 million for community colleges. For both segments, these withdrawals prevented an actual reduction in state funding.

The 2024-25 Budget Act made a new discretionary Prop 98 Rainy Day Fund deposit of $1.1 billion. This deposit was not mandatory under revenue assumptions, but was designed to count toward any deposit that became necessary under the final reserve calculation for 2024-25. This discretionary deposit for 2024-25 was revised in the 2025-26 Budget Act to a mandatory deposit of $455 million. The 2025-26 Budget Year and enacted Budget estimated a mandatory $455 million withdrawal, reducing the total Rainy Day Fund balance to zero.

Governor’s 2026-27 Budget

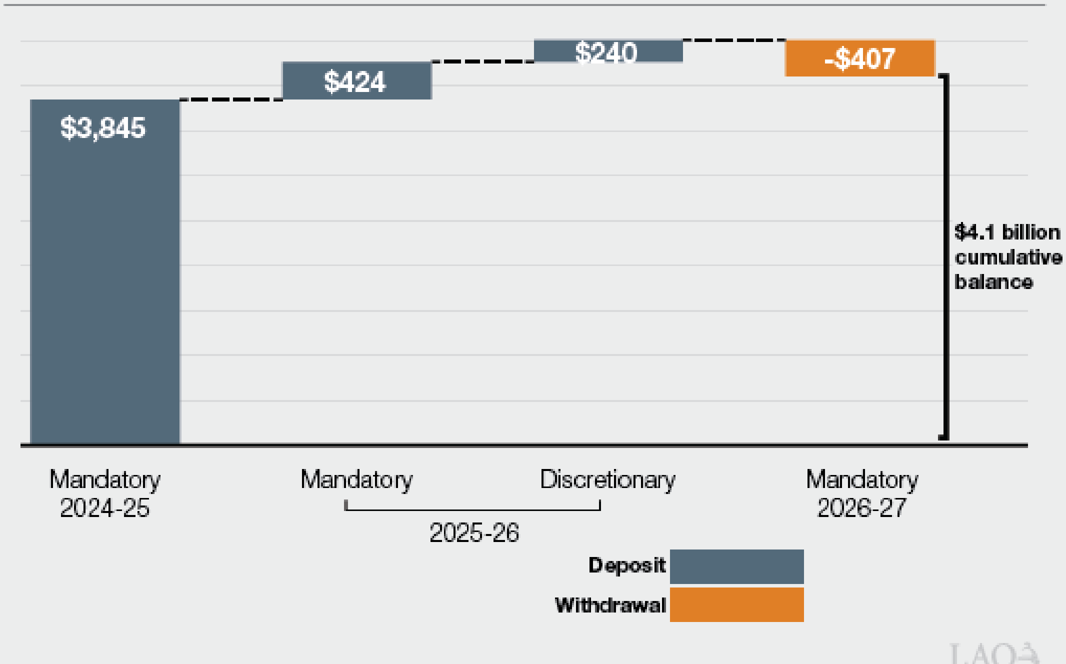
The January Budget estimates the state must make Prop 98 Rainy Day Fund deposits of $3.8 billion in 2024-25 and $424.3 million in 2025-26, under the requirements of Prop 2. Additionally, the proposal includes a new discretionary deposit of $240 million in the 2025-26 fiscal year. Under the same estimates, the state would make a mandatory withdrawal of $407 million in 2026-27.

These deposits and withdrawal would bring projected Proposition 98 “Rainy Day” fund, the Public School System Stabilization Account, to a total of $4.1 billion through the Budget year. This total is approximately 3.3 percent of the 2026-27 Proposition 98 guarantee total estimate.

Figure 4

Proposition 98 Reserve Balance Would Grow to $4.1 Billion

(In Millions)



According to DOF, this level of funding triggers the statutory 10% cap on local school district reserves beginning in the Budget Year. This Prop 98 Rainy Day Fund calculation assumes the $5.6 billion "settle-up" that is unallocated in the 2025-26 January Budget spending proposals, is part of the guarantee calculation.

LAO Comments

Deposit Some of the Additional Funding Into the Proposition 98 Reserve. Whereas we recommend setting aside additional funding to meet the guarantee, we do not recommend a corresponding increase in school and community college spending this year. Instead, we recommend (1) making a larger deposit into the Proposition 98 Reserve, and (2) adopting trailer legislation that automatically reduces the deposit if the 2025-26 guarantee declines relative to May estimates. The savings from any reductions in the deposit would help the state balance the budget. Like the Governor's proposal, this approach would allow the state to avoid inadvertently exceeding the guarantee if revenues fall short of projections, thereby mitigating the state's short-term forecasting risk. We recommend that the Legislature make a total deposit of at least

$3.5 billion in 2025-26. This deposit would provide a buffer to address the likely range of reductions to the 2025-26 guarantee relative to the state's May estimate. The Governor's budget already contains $644 million in Proposition 98 Reserve deposits for 2025-26, so implementing this recommendation would involve an additional deposit of $2.9 billion.

Staff Comments

Suggested Questions:

1. Could a larger discretionary PSSSA contribution, that is contingent on actual final revenues, be a prudent way to protect against possible over-spending in the Current Year?

2. Should one-time voluntary contributions to the PSSSA be considered for the Budget Year, considering the risk of economic conditions changing? Should this be a regular consideration in years of dramatic growth and/or volatility?

3. For the LAO: what metrics should the Legislature consider for when a voluntary contribution is prudent? And at what size?

4. Does the DOF have a definition for withdrawal parameters, for the proposed discretionary PSSSA deposit?

Staff Recommendation: Hold Open.

Issue 3: Education Funding Deferrals

This issue will cover prior state Budget deferrals to local education agencies' Proposition 98 funding, and repayment of these deferrals, as proposed in the Governor's Budget, for the 2025-26 and 2026-27 Budget years.

Panel

- Alex Shoap, Department of Finance
- Kenneth Kapphahn, Legislative Analyst's Office

Background

A Prop 98 payment "deferral" is a budgetary tool that allows the state to delay or defer payments to schools and community colleges from month to month within a single fiscal year, or across fiscal years to align school and community college funding to the Prop 98 guarantee availability each fiscal year, and to address cash availability. The purpose of a deferral is to postpone a planned payment to schools, based on funding availability, in lieu of a reduction to appropriated funding overall.

The 2025-26 Budget Act reduced spending in 2025-26 by deferring $2.3 billion in payments to 2026-27. Of this amount, $1.9 billion pertains to schools, where the state would shift a portion of the June 2026 payment to July 2026. The law exempts school districts and charter schools that can demonstrate the delay would make them unable to meet their financial obligations. The remaining $408 million in deferrals pertains to community colleges, where the state would move payments from May and June 2026 to July 2026. These deferrals free up funding for additional one-time and ongoing spending that would otherwise exceed the Proposition 98 guarantee in 2025-26.

Governor's 2026-27 Budget

The Governor's budget provides $2.3 billion to eliminate the school and community college deferrals and restores the regular payment schedules beginning in 2026-27.

LAO Comments

Eliminating Deferrals Is Prudent. Conceptually, deferrals are similar to borrowing from future Proposition 98 funds. The Governor's proposal to eliminate them would align the ongoing costs of school programs with the ongoing funding needed to support them. This realignment would ease pressure on future budgets, improve cash flow for districts, and simplify state and school accounting.

Staff Comments

Suggested Questions:

1. Is fully paying off the deferral the Administration's first priority for new fund availability? In not, which new ongoing proposals rank higher for the Administration in the January Budget?

2. The need to create a deferral in the 2025-26 Budget Act was caused by a decrease in available revenues at the May Revision: what architecture in the January Budget would prevent this dynamic, if the 2026 May Revision forecast is lower than January Budget for Proposition 98?

Staff Recommendation: Hold Open.

This agenda and other publications are available on the Assembly Budget Committee's website at: Sub 3 Hearing Agendas | California State Assembly. You may contact the Committee at (916) 319-2099. This agenda was prepared by Erin Gabel.