

PROPOSITION **TAX EXTENSION TO FUND EDUCATION AND HEALTHCARE.**
55 INITIATIVE CONSTITUTIONAL AMENDMENT.

OFFICIAL TITLE AND SUMMARY

PREPARED BY THE ATTORNEY GENERAL

55

- Extends by twelve years the temporary personal income tax increases enacted in 2012 on earnings over \$250,000 (for single filers; over \$500,000 for joint filers; over \$340,000 for heads of household).
- Allocates these tax revenues 89% to K–12 schools and 11% to California Community Colleges.
- Allocates up to \$2 billion per year in certain years for healthcare programs.
- Bars use of education revenues for administrative costs, but provides local school boards discretion to decide, in open meetings and subject to annual audit, how revenues are to be spent.
- through 2030, depending on the economy and the stock market.
- Increased funding for schools and community colleges of roughly half of the revenue raised by the measure.
- Increased funding for health care for low-income people ranging from \$0 to \$2 billion each year, depending on decisions and estimates made by the Governor’s main budget advisor.
- Increased budget reserves and debt payments ranging from \$60 million to roughly \$1.5 billion each year (in today’s dollars), depending primarily on the stock market.

SUMMARY OF LEGISLATIVE ANALYST’S ESTIMATE OF NET STATE AND LOCAL GOVERNMENT FISCAL IMPACT:

- Increased state revenues ranging from \$4 billion to \$9 billion each year (in today’s dollars) from 2019

ANALYSIS BY THE LEGISLATIVE ANALYST

BACKGROUND

State Budget

Over Half of State Budget Spent on Education. The state collects taxes and fees from people and businesses and uses these revenues to fund programs in the state budget. This year, the state plans to spend about \$122 billion from its main operating account, the General Fund. As shown in Figure 1, over half of this spending is for K–12 schools, community colleges, and the state’s public universities. About another one-quarter of this spending is for health and human services programs, the largest of which is the state’s Medi-Cal program. Most of the spending shown in the figure for “various other programs” pays for prisons, parole programs, and the courts.

Taxes

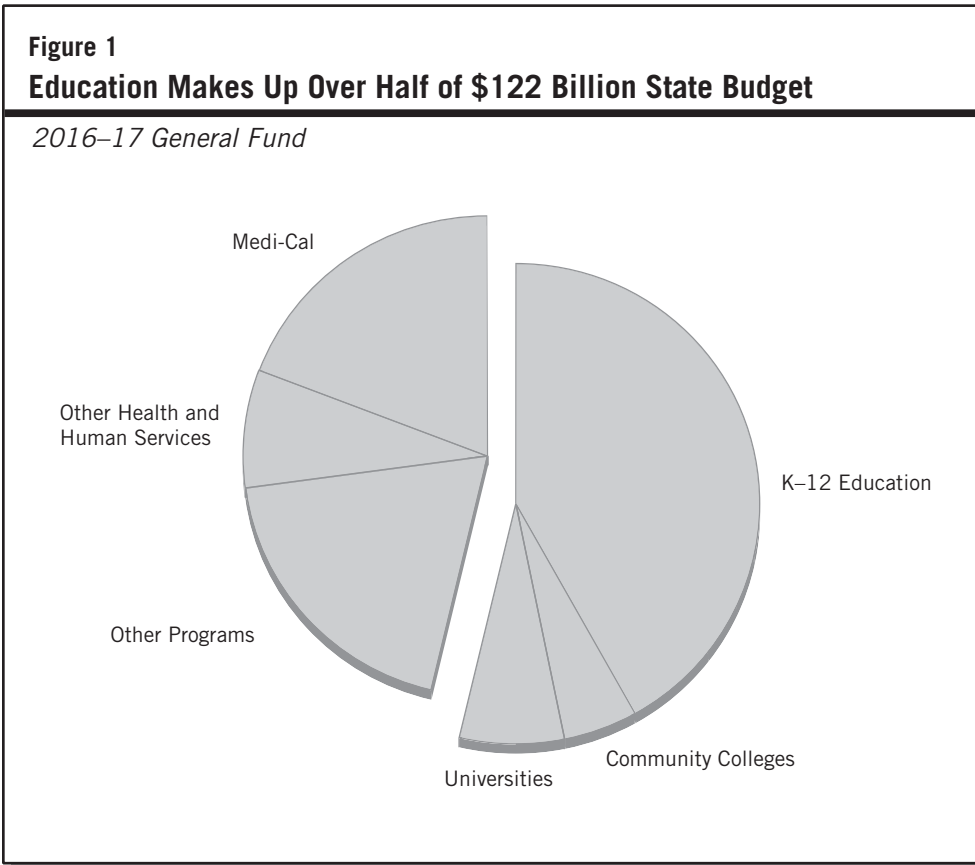
Personal Income Tax Provides Most General Fund Monies. The state’s General Fund is supported primarily by three taxes: the personal income tax, the sales tax, and the corporate income tax. (We refer to the personal income tax simply as “income tax” in this analysis.) The income tax is the most important for the state budget, as it provides about two-thirds of all General Fund revenues. The tax applies to most

forms of income—such as salaries, wages, interest income, and profits from the sales of stocks and other assets. It consists of several “marginal” tax rates, which are higher as income subject to the tax, or “taxable income,” increases. For example, in 2011 the tax on a married couple’s taxable income was 1 percent on the first \$14,632 but 9.3 percent on all taxable income over \$96,058.

Proposition 30. Proposition 30, approved by voters in November 2012, increased income tax rates on high-income taxpayers. As shown in Figure 2, depending on their income levels, high-income taxpayers pay an extra 1 percent, 2 percent, or 3 percent tax on part of their incomes. These higher rates are in effect through 2018. This year’s state budget assumes that the Proposition 30 income tax increases will raise about \$7 billion in revenue. Proposition 30 also increased the state sales tax rate by one-quarter cent from 2013 through 2016.

Education

Annual Required Spending on Education. The State Constitution requires the state to spend a minimum amount on K–12 schools and community colleges each year. This “minimum guarantee” grows over time based on growth in state tax revenues, the economy, and student attendance. This year, the state



General Fund will provide over \$50 billion toward the minimum guarantee. Local property taxes also contribute to the minimum guarantee.

Medi-Cal

Serves Low-Income People in California. The Medi-Cal program provides health care services to low-income people. These services include primary care visits, emergency room visits, surgery, and prescription drugs. The program serves over 13 million people in California—roughly one-third of the population. This year, the state will spend about \$23 billion from the General Fund on Medi-Cal. In addition, the program relies heavily on federal funding and receives some support from other state sources.

Budget Reserves and Debt Payments

“Rainy-Day” Reserves. Governments use budget reserves to save money when the economy is good. When the economy gets worse and revenues decline, governments use money that they saved to reduce the amount of spending cuts, tax increases, and other actions needed to balance their budgets.

Constitution Requires Minimum Amount Used for Debt Payments and Budget Reserves.

The Constitution requires the state to save a minimum amount each year in its rainy-day fund and spend a minimum amount each year to pay down state debts faster. The annual amounts used for debts and budget reserves depend primarily upon state tax revenues. In particular, revenues from capital gains—money people make when they sell stocks and other types of property—are an important factor in estimating how much the state must use for these purposes.

PROPOSAL

This measure (1) extends for 12 years the additional income tax rates established by Proposition 30 and (2) creates a formula to provide additional funds to the Medi-Cal program from the 2018–19 state fiscal year through 2030–31.

Taxes

Income Taxes Increased on High-Income Taxpayers. Proposition 55 extends from 2019 through 2030

ANALYSIS BY THE LEGISLATIVE ANALYST

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Figure 2
Income Tax Rates Under Proposition 30^a

Single Filer's Taxable Income ^b	Joint Filers' Taxable Income ^c	Marginal Tax Rate		
		Base Rate	Proposition 30 Increase	Total Rate
\$0 to \$8,000	\$0 to \$16,000	1.0%	—	1.0%
8,000 to 19,000	16,000 to 37,000	2.0	—	2.0
19,000 to 29,000	37,000 to 59,000	4.0	—	4.0
29,000 to 41,000	59,000 to 82,000	6.0	—	6.0
41,000 to 52,000	82,000 to 103,000	8.0	—	8.0
52,000 to 263,000	103,000 to 526,000	9.3	—	9.3
263,000 to 316,000	526,000 to 632,000	9.3	1.0%	10.3
316,000 to 526,000	632,000 to 1,053,000	9.3	2.0	11.3
Over 526,000	Over 1,053,000	9.3	3.0	12.3

^a Income brackets shown are rounded to the nearest thousands of dollars. Brackets are in effect for 2015 and are adjusted for inflation in future years.
^b Single filers include married individuals and registered domestic partners (RDPs) who file taxes separately.
^c Joint filers include married and RDP couples who file jointly, as well as qualified widows or widowers with a dependent child.

Note: Income brackets for head-of-household filers are not listed, but those filers with taxable income of \$357,981 and greater (as of 2015) also are subject to 10.3 percent, 11.3 percent, or 12.3 percent marginal tax rates under Proposition 30. Tax rates listed exclude the mental health tax rate of 1 percent for taxable income in excess of \$1 million.

the Proposition 30 income tax rate increases shown in Figure 2. These increases affect high-income taxpayers in the state. Specifically, the measure affects the roughly 1.5 percent of taxpayers with the highest incomes.

Amount of Tax Increase Depends Upon Taxable Income. The amount of increased taxes paid by high-income taxpayers would depend upon their taxable income. For example, if this measure passes, a single person with taxable income of \$300,000 would pay an extra 1 percent on their income between \$263,000 and \$300,000. This works out to a tax increase of \$370 for this person. A married couple filing a joint tax return with taxable income of \$2,000,000 also would see their taxes increased under this measure. Specifically, this couple would pay another 1 percent on their income between \$526,000 and \$632,000, an extra 2 percent on their income between \$632,000 and \$1,053,000, and an extra 3 percent on their income between \$1,053,000 and \$2,000,000. This works out to a tax increase of \$37,890 for this couple. (These examples would be somewhat different by 2019 because tax brackets would be adjusted annually for inflation.)

Does Not Extend Sales Tax Increase. Proposition 55 does not extend the one-quarter cent increase in the sales tax rate that voters approved in Proposition 30. In other words, whether or not voters pass this

measure, Proposition 30's sales tax increase will expire at the end of 2016.

Medi-Cal

Creates Formula for Medi-Cal. Proposition 55 includes a new state budget formula to provide more funding for the Medi-Cal program. The measure requires the Director of Finance, the Governor's main budget advisor, to determine each year from 2018–19 through 2030–31 whether General Fund revenues exceed (1) constitutionally required education spending and (2) the costs of government programs that were in place as of January 1, 2016. If revenues exceed these spending amounts, 50 percent of the excess (up to a maximum of \$2 billion) would be allocated to Medi-Cal. (This additional allocation could be reduced somewhat in difficult budget years.) The measure states that these Medi-Cal monies should not replace existing General Fund support for the program.

FISCAL EFFECTS

Figure 3 summarizes Proposition 55's fiscal effects. The measure's increased revenues would be used for K–12 schools and community colleges, health care services for low-income people, budget reserves, and debt payments. After satisfying these constitutional

ANALYSIS BY THE LEGISLATIVE ANALYST

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requirements, remaining amounts, if any, would be available for any state budget purpose.

Taxes

Revenue Raised by Measure Would Depend on Economy and Stock Market. The exact amount of state revenue raised by Proposition 55 would depend on several factors that are difficult to predict. A large share of high-income taxpayers’ earnings comes from capital gains. These revenues depend heavily on future stock market and other asset values, which are difficult to

to predict. It is reasonable to assume, however, that roughly half of the revenue raised by Proposition 55 would go to schools and community colleges.

Medi-Cal

May Increase Medi-Cal Funding. The formula for added Medi-Cal funding would require the Director of Finance to estimate annually revenues and spending. As noted earlier, General Fund revenues are difficult to predict. Similarly, in order to produce the spending estimates required by the measure, the Director of

Finance would have to make assumptions about how spending on programs that were in place as of January 1, 2016 would have changed over time. Additional Medi-Cal funding under the measure, therefore, would depend on decisions and estimates made by the Director of Finance. The amount of any additional Medi-Cal funding under the measure could vary significantly each year, ranging from \$0 to \$2 billion.

Figure 3

Fiscal Effects of Proposition 55

Increased income tax revenues	Between \$4 billion and \$9 billion each year (in 2016 dollars), depending upon economy and stock market.
Increased funding for schools and community colleges	Roughly half of the revenue raised by the measure.
Increased Medi-Cal funding	Between \$0 and \$2 billion each year, depending upon decisions and estimates made by the Governor’s main budget advisor.
Increased budget reserves and debt payments	Between \$60 million and roughly \$1.5 billion each year (in 2016 dollars), depending primarily upon stock market.

Budget Reserves and Debt Payments

Increases Budget Reserves and Debt Payments. As described above, Proposition 55

predict. In addition, high-income taxpayers’ earnings fluctuate with the economy. Thus, in a bad economic and stock market year, the measure might raise around \$4 billion in revenue. When the economy and stock market are good, the measure might raise around \$9 billion in annual revenue. In most years, the amount of revenue raised by the measure would be in between these amounts. (These amounts are in today’s dollars and would tend to grow over time.)

increases state tax revenues. Higher revenues increase required debt payments and budget reserve deposits. The exact amount that the state would have to use for paying down state debts and building budget reserves depends largely on capital gains revenues, which are difficult to predict. In bad stock market years, Proposition 55 could increase debt payments and budget reserves by \$60 million. In good stock market years, Proposition 55 could increase debt payments and reserve deposits by \$1.5 billion or more.

Education

Increases in Education Spending. Higher state tax revenues generally result in increased education spending. The exact amount that the state must spend on schools and community colleges in the future depends on several factors that are difficult

Visit <http://www.sos.ca.gov/measure-contributions> for a list of committees primarily formed to support or oppose this measure. Visit <http://www.fppc.ca.gov/transparency/top-contributors/nov-16-gen-v2.html> to access the committee’s top 10 contributors.

★ ARGUMENT IN FAVOR OF PROPOSITION 55 ★

55

Proposition 55 prevents billions in budget cuts without raising taxes by ensuring the wealthiest Californians continue to pay their share. 55 requires strict accountability and transparency to ensure funds get to the classroom. We can't afford to go back to the days of devastating cuts and teacher layoffs.

Fact 1: Proposition 55 does not raise anyone's taxes.

- *Does not raise taxes on anyone.* Proposition 55 maintains the current income tax rate on couples earning over \$500,000 a year.
- *Only affects the wealthiest Californians who can most afford it,* ensuring they continue to pay their share of taxes.
- *Lower sales tax.* Under Proposition 55 all Californians' sales tax are reduced.

Fact 2: Proposition 55 has strict transparency and accountability requirements to ensure education funds get to the classroom.

- *Money goes to local schools and the Legislature can't touch it.* Strict accountability requirements ensure funds designated for education go to classrooms, not to bureaucracy or administrative costs. Authorizes criminal prosecution for any misuse of money.
- *Mandatory audits and strict transparency requirements.* Local school districts must post annual accounting online to guarantee that Californians know exactly how and where funds are spent.
- *Provides local control over school funding.* Proposition 55 gives control to local school boards to determine student needs.

Fact 3: Proposition 55 prevents up to \$4 billion in cuts to schools and continues to restore funding cut during the recession.

- *Proposition 55 helps address California's looming teacher shortage.* The state needs an estimated 22,000 additional teachers next year alone. Proposition 55 gives local school districts the money they need to hire teachers and prevent overcrowded classes.
- *Proposition 55 helps restore arts and music.* Arts and

music programs faced deep cuts during the recession. Proposition 55 will help protect and restore those programs.

- *Makes college more affordable.* Proposition 55 prevents cuts to California community colleges, preventing tuition increases and helping make classes more available to California's 2.1 million community college students.
- *Expands health care access for children.* Healthier children are healthier students. Too many families can't afford basic health care, meaning children miss school or come to class sick. Proposition 55 helps kids come to school healthy and ready to learn, because all children deserve access to quality health care, not just the wealthiest Californians.

California needs to keep moving forward, we can't afford to go back to the days of devastating cuts to public schools, colleges, and health care.

30,000 teachers were laid off, class sizes grew, and the cost of community colleges doubled.

Governor Jerry Brown has said that we'll face even more cuts if Proposition 55 doesn't pass.

Proposition 55 gives Californians a clear choice: voting YES protects our schools and children from massive cuts; voting NO costs our schools up to \$4 billion a year.

California's schools are starting to come back. Passing Proposition 55 will ensure that our children won't face another round of cuts. The future of California depends on the future of our children.

Because our children and schools matter most.

Details at www.YesOn55.com

JUSTINE FISCHER, President
California State PTA

ALEX JOHNSON, Executive Director
Children's Defense Fund—California

TOM TORLAKSON, California State Superintendent of
Public Instruction

★ REBUTTAL TO ARGUMENT IN FAVOR OF PROPOSITION 55 ★

TEMPORARY SHOULD MEAN TEMPORARY

Voters supported higher income and sales taxes in 2012 because Governor Jerry Brown made the commitment that they would be temporary.

The state budget has a surplus, and these temporary taxes should go away, just like the Governor promised.

PROP. 55 WILL HURT SMALL BUSINESS AND KILL JOBS.

Prop. 55 will kill jobs, close businesses, and hurt the economy. It will raise taxes on California's small businesses, and make it even harder for them to create good-paying jobs.

WE CAN'T TRUST THE POLITICIANS AND SPECIAL INTERESTS

The politicians and special interests know California is NOT facing cuts to programs. They just want to grow government bigger by passing Prop. 55. And they are using our kids and schools to scare voters into supporting it. Don't be fooled.

SCHOOLS ARE FULLY FUNDED

Education spending has grown by \$24.6 billion since

2012—a 52% increase.

Schools are funded, and the state budget is balanced. We have a \$2.7 billion surplus and over \$9.4 billion in budget reserves.

Prop. 55's new and higher taxes aren't needed.

DON'T BE FOOLED BY SCARE TACTICS, PROP. 55 IS NOT NEEDED.

Official budget estimates by the state's non-partisan Legislative Analyst show that higher taxes are NOT needed to balance the budget and fully fund schools. California can fund education, health care and state government without new or higher taxes.

VOTE NO ON PROP. 55

JON COUPAL, President
Howard Jarvis Taxpayers Association

TOM SCOTT, State Executive Director
National Federation of Independent Business—California

TERESA CASAZZA, President
California Taxpayers Association

★ ARGUMENT AGAINST PROPOSITION 55 ★

In 2012, voters approved Proposition 30 tax increases because we were promised they'd be temporary and end in 2017.

Now special interests want to break that promise and extend these tax hikes 12 more years.

That's *not* temporary.

Here's the official title from the 2012 measure: Prop. 30: TEMPORARY taxes to fund education, guaranteed local public safety funding. Initiative Constitutional Amendment.

TEMPORARY SHOULD MEAN TEMPORARY

Voters supported higher income and sales taxes in 2012 only because Governor Jerry Brown promised they would be temporary:

"THAT'S A TEMPORARY TAX AND, TO THE EXTENT THAT I HAVE ANYTHING TO DO WITH IT, WILL REMAIN TEMPORARY."—*Governor Brown, Sacramento Bee, 10/7/14*

Governor Brown promised the higher taxes would only last a few years and then end. Now, special interests want to extend them 12 more years—that's not "temporary."

California's economy has recovered and we now have a BUDGET SURPLUS.

WE DON'T NEED HIGHER TAXES

California has a balanced budget, we've reduced debt, increased school spending, put billions into California's "rainy day fund" and still have a \$2.7 billion budget surplus.

California takes in more tax dollars than we need each year—that's why the state budget recovered from a \$16 billion deficit in 2012 to a \$2.7 billion surplus in 2016.

Education spending has soared by \$24.6 billion since 2012—a 52% increase.

Medi-Cal spending has increased by \$2.9 billion—a 13% increase.

WE CAN FUND EDUCATION, HEALTH CARE, AND STATE GOVERNMENT WITHOUT NEW OR HIGHER TAXES

Governor Brown has stated and budget estimates from

the Legislative Analyst show that higher taxes are not needed to balance the budget.

We have adequate funds for schools and other critical requirements—we just need politicians with the backbone to cut waste and prioritize our spending.

What we don't need is the largest tax hike in California history, sending billions more to Sacramento with no accountability to voters.

PROP. 55 TARGETS CALIFORNIA'S SMALL BUSINESSES WITH HIGHER TAXES FOR 12 YEARS

This measure targets small businesses who often pay taxes on their business income through their personal tax return. Prop. 55 will kill jobs, close businesses and damage the economy.

THE SPECIAL INTERESTS JUST WANT MORE MONEY TO SPEND TODAY

It's a fair bet that Prop. 55 money will be spent to pay pension benefits and other state debt rather than making it to the classroom or building roads. It'll be just like the lottery—we'll never know where the money went.

WE CAN'T TRUST THE POLITICIANS AND SPECIAL INTERESTS

The politicians and special interests know California is NOT facing cuts to any programs now. They just want to grow government by passing Prop. 55—the largest state tax increase ever.

Check it yourself: California has a \$2.7 billion surplus, and over \$9.4 billion in budget reserves.

New and higher taxes aren't needed.

CALIFORNIA SHOULD KEEP ITS WORD: TEMPORARY MEANS TEMPORARY

VOTE NO ON PROP. 55—IT'S A BROKEN PROMISE

JON COUPAL, President

Howard Jarvis Taxpayers Association

TOM SCOTT, State Executive Director

National Federation of Independent Business—California

HON. QUENTIN L. KOPP, Retired Superior Court Judge

★ REBUTTAL TO ARGUMENT AGAINST PROPOSITION 55 ★

Vote YES on 55. Help our children thrive.

Prop. 55 makes sure we won't go back to massive cuts in school funding. It protects the education and health of our children.

Proposition 55 does not raise anyone's taxes:

- Prop. 55 *maintains current tax rates* on the wealthiest Californians to ensure couples earning more than \$500,000 a year continue paying their share.
- Proposition 55 does not raise taxes on small businesses.
- Under Proposition 55 the state sales tax is reduced as planned at the end of 2016.

Proposition 55 *prevents* up to a \$4 billion per year cut in public school funding:

- Proposition 55 helps address the teacher shortage and continues to restore the school funding that was cut during the recession.
- California's high school graduation rate rose for the sixth year in a row. Prop. 55 will help continue the progress.

Yes on 55 has strict accountability and fiscal

requirements to ensure education funds go straight to the classroom:

- Revenue is guaranteed in the Constitution to go into a special account for schools and children's health care that the *Legislature can't touch*.
- Money will be audited every year. Audit findings are posted at <http://trackprop30.ca.gov/> so taxpayers can see how their money is spent.
- There are strict requirements that funding must go to the classroom, not administration or Sacramento bureaucracy.
- Proposition 55 authorizes criminal prosecution for misuse of money.
- The continuation of the current tax rates on the wealthiest is subject to the vote and will of the people.

ERIC C. HEINS, President

California Teachers Association

BETTY T. YEE, California State Controller

ANN-LOUISE KUHNS, President

California Children's Hospital Association