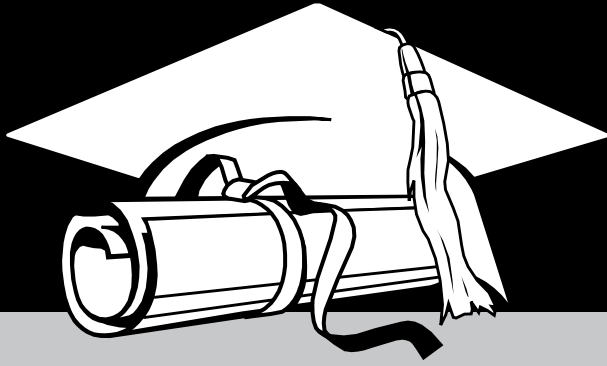


EDUCATION



LAO 
65 YEARS OF SERVICE

2007-08 Analysis

MAJOR ISSUES

Education



Reduce Current-Year Proposition 98 Spending

- Relative to the Governor's budget, the Legislature faces major General Fund challenges due to: (1) lower General Fund revenues and (2) higher General Fund Proposition 98 spending resulting from overestimates of property taxes, a higher 2007-08 minimum funding guarantee, and a risky rebenching proposal.
- To help address the state's serious budgetary situation, we recommend the Legislature reduce current-year Proposition 98 spending by slightly more than \$600 million, consistent with the drop in the 2006-07 Proposition 98 minimum guarantee. This can be done with minimal impact on education programs and generates major one-time and ongoing savings (see page E-25).



Develop Proposition 98 Roadmap

- Our five-year forecast shows sizeable Proposition 98 increases above changes in attendance and inflation on the horizon. Thus, we think this is an opportune time to develop a long-term roadmap for K-14 education. Such a roadmap could help the Legislature address high priority issues over the next few years.
- In our suggested roadmap, we highlight the achievement gap that persists between K-12 special education, low-income, and English learner students and other K-12 students. To address these gaps, we suggest the Legislature make various investments in child development programs and programs for at-risk students as well as strengthen accompanying assessment and accountability systems (see page E-39).

- Our roadmap also highlights the low graduation and transfer rates of community college students. To address these issues, we suggest the Legislature provide “student success” block grants that would create incentives for improvement while still allowing community colleges flexibility to develop local solutions (see page E-48).



Maximize Potential Benefits of Settlement Monies

- In response to a recent settlement, the state agreed to pay an additional \$2.8 billion over a seven-year period for K-14 education. In 2007-08, the state is to provide \$268 million for a new K-12 education reform program and \$32 million for community college career technical education programs. We recommend small changes to these K-14 programs that could yield big payoffs (see pages E-53 and E-109).



Fund Anticipated Higher Education Enrollment Costs

- The Governor’s budget funds 2.6 percent enrollment growth at the University of California (UC), 2.5 percent at the California State University (CSU), and 2 percent at the California Community Colleges.
- We recommend the Legislature instead provide funding for somewhat lower growth rates based on population projections and modest increases in participation rates (see pages E-178 and E-271).



Maintain UC and CSU Fee Levels at Current Share of Cost

- The Governor’s budget proposes fee increases of 7 percent and 10 percent for UC and CSU, respectively. Absent an explicit state fee policy, we recommend that fees be adjusted in 2007-08 so they cover the same share of education cost as in the current year. This would result in fee levels considerably lower than those in the Governor’s proposal (see page E-197).



Reject Unjustified Funding Requests for UC

- We recommend the Legislature reject \$149 million in augmentations for specified research and medical programs and facilities because neither the university nor the administration has been able to provide adequate information to justify them (see pages E-231, E-233, E-250, and E-251).

TABLE OF CONTENTS

Education

Overview	E-7
Crosscutting Issues	E-13
Proposition 98 Update.....	E-13
Proposition 98 Priorities.....	E-25
A Proposition 98 Roadmap.....	E-33
Career Technical Education	E-53
California Education Network.....	E-66
K-12 Education	
Introduction	E-75
Budget Issues	E-87
Home-to-School Transportation.....	E-87
Child Care and Development.....	E-90
Quality Education Investment Act	E-109
English Learners.....	E-121
Soledad Enrichment Action Charter School.....	E-144

Higher Education

Introduction	E-153
Budget Issues	E-161
Intersegmental: Making Budgeting Choices in Higher Education	E-161
Intersegmental: UC and CSU Outreach Programs...	E-165
Intersegmental: UC and CSU Enrollment Growth and funding	E-174
Intersegmental: Student Fees	E-192
Intersegmental: Higher Education Nursing Proposals	E-201
California Postsecondary Education Commission (6420)	E-215
University of California (6440)	E-222
California State University (6610)	E-252
California Community Colleges (6870)	E-262
Student Aid Commission (7980)	E-286
Findings and Recommendations	E-297

OVERVIEW

Education

The Governor's budget proposes almost \$100 billion in operational spending from state, local, and federal sources for K-12 and higher education in 2007-08. Of this amount, \$65 billion is for K-12 education. This is an increase of \$1.4 billion, or 2.3 percent, from estimated expenditures in the current year. The remaining \$35 billion is for higher education. This is an increase of \$1.3 billion, or 3.8 percent, from the current year.

Figure 1 summarizes support for K-12 and higher education for three years. (The figure includes operational spending from all sources but excludes capital outlay-related spending.) It shows that spending on education will reach almost \$100 billion in 2007-08 under the Governor's proposed spending plan.

Figure 1

K-12 and Higher Education Funding

(Dollars in Millions)

	Actual 2005-06	Estimated 2006-07	Proposed 2007-08	Change From 2006-07	
				Amount	Percent
K-12 ^a	\$60,154	\$63,257	\$64,693	\$1,436	2.3%
Higher education ^b	33,814	33,380	34,633	1,253	3.8
Totals	\$93,968	\$96,637	\$99,326	\$2,689	2.8%

^a Includes spending from state, local and federal funds. Excludes debt service for general education obligation bonds and local debt service.

^b Includes spending from state, local and federal funds and student fee revenue. Excludes debt service for general obligation bonds. For community colleges, also excludes spending from funds maintained in local budgets.

FUNDING PER STUDENT

The proposed Proposition 98 funding level for K-12 education in 2007-08 equates to \$8,524 per student, as measured by average daily attendance (ADA). Proposed spending from all funding sources (excluding capital outlay-related spending) totals \$10,932 per student.

The proposed Proposition 98 funding level for the California Community Colleges (CCC) equates to \$5,335 per full-time equivalent (FTE) student. Including other state funds and student fee revenue, CCC would receive about \$5,804 per student. This compares to proposed total funding (General Fund and student fees) of \$25,068 for each FTE student at the University of California (UC) and \$12,200 for each FTE student at the California State University (CSU).

PROPOSITION 98

California voters enacted Proposition 98 in 1988 as an amendment to the State Constitution. The measure, which was later modified by Proposition 111, establishes a minimum annual funding level for K-12 schools and CCC. (A small amount of annual Proposition 98 funding provides support for direct educational services provided by other agencies, such as the state's schools for the deaf and blind and the California Youth Authority.) Proposition 98 funding constitutes around three-fourths of total K-12 funding and total CCC funding.

The minimum funding levels are determined by one of three specific formulas. Figure 2 briefly explains these formulas (or "tests") and some other key funding provisions. The five major factors involved in the calculation of the Proposition 98 tests are: (1) General Fund revenues, (2) state population, (3) personal income, (4) local property taxes, and (5) K-12 ADA. In most years, the key determinants of the Proposition 98 minimum guarantee (or required funding level) are the year-to-year change in per capita personal income and General Fund revenues.

Proposition 98 Allocations

Figure 3 (see page 10) displays the budget's proposed allocations of Proposition 98 funding for K-12 schools and CCC. For the current year, lower-than-anticipated student attendance reduces the spending level by \$100 million—to total spending of \$55 billion. For 2007-08, the budget includes \$56.8 billion—an increase of \$1.8 billion. (These figures reflect the Governor's proposal to move the \$627 million school transportation program out of Proposition 98. This proposal, discussed in the "Home-to-School Transpor-

Figure 2

Proposition 98 Basics

- ✓ **Most years, K-14 funding increases to account for growth in K-12 attendance and growth in the economy.**
- ✓ **Three Formulas (“Tests”) Used to Determine K-14 Funding.**
 - **Test 1—Share of General Fund.** Provides roughly 40 percent of General Fund revenues to K-14 education. This test has not been used since 1988-89.
 - **Test 2—Growth in Per Capita Personal Income.** Increases prior-year funding by growth in attendance and per capita personal income. This test has been operative 12 of the last 19 years.
 - **Test 3—Growth in General Fund Revenues.** Increases prior-year funding by growth in attendance and per capita General Fund revenues. Generally, this test is operative when General Fund revenues fall or grow slowly.
- ✓ **Legislature Can Suspend Proposition 98.** With a two-thirds vote, the Legislature can suspend the guarantee for one year and provide any level of K-14 funding. It did this in 2004-05.

tation” section of this chapter, affects year-to-year comparisons of growth in Proposition 98 funding.) Most of the increase in proposed Proposition 98 spending is supported by local property tax revenues (\$1.4 billion). Proposition 98 funding issues are discussed in more detail in the “Proposition 98 Update” and “Proposition 98 Priorities” sections of this chapter.

ENROLLMENT FUNDING

The Governor’s budget assumes K-12 attendance will decline by 0.4 percent from 2006-07 to 2007-08. This would be the third consecutive year that K-12 attendance has declined. Enrollment is expected to drop even more rapidly in coming years, as the children of the baby boomers move out of their high school years. The budget funds 2 percent growth for community college enrollment, which is somewhat above the statutory guideline—based on population growth—that calls for 1.65 percent. In addition, the Governor’s budget proposes to fund 2.5 percent enrollment growth at UC and CSU, which is more than double our projection of underlying demographically driven growth (1.1 percent).

Figure 3**Governor's Proposed Proposition 98 Funding***(Dollars in Millions)*

	2006-07		2007-08 Proposed	Change From 2006-07 Revised	
	Budget Act	Revised ^a		Amount	Percent
K-12 Proposition 98					
General Fund	\$37,141	\$36,658	\$36,851	\$193	0.5%
Local property tax revenue	11,973	12,353	13,595	1,242	10.1
Subtotals	(\$49,114)	(\$49,011)	(\$50,446) ^b	(\$1,435)	(2.9%)
CCC Proposition 98					
General Fund	\$4,041	\$4,040	\$4,224	\$184	4.6%
Local property tax revenue	1,853	1,857	2,051	193	10.4
Subtotals	(\$5,894)	(\$5,897)	(\$6,274)	(\$377)	(6.4%)
Total Proposition 98^c					
General Fund	\$41,295	\$40,812	\$41,190	\$378	0.9%
Local property tax revenue	13,827	14,210	15,645	1,435	10.1
Totals	\$55,122	\$55,022	\$56,835^b	\$1,813	3.3%
<p>^a These dollar amounts reflect appropriations made to date or proposed by the Governor in the current year.</p> <p>^b Reflects Governor's proposal to reduce Proposition 98 funding level by \$627 million as part of the Home-to-School Transportation funding shift.</p> <p>^c Total Proposition 98 also includes around \$115 million in funding that goes to other state agencies for educational purposes.</p>					

SETTING EDUCATION PRIORITIES FOR 2007-08

In this chapter, we evaluate the proposed budget for K-12 and higher education, including proposed funding increases and reductions, fiscal and policy reforms, fund shifts and fee increases, and projected enrollment levels. The ongoing structural gap between state revenues and expenditures makes it all the more important for the Legislature to reassess program effectiveness and funding levels. In both K-12 and higher education, we provide the Legislature with alternative approaches to the budget's proposal.

K-14 Priorities. The Governor proposes a "baseline" Proposition 98 budget for 2007-08. This includes \$1.8 billion in net new spending, most of which goes to provide a cost-of-living adjustment (COLA) for most

programs. Given our more recent economic and revenue data, we have serious concerns with the Governor's plan. Our estimate of General Fund tax revenues, for instance, is lower than the administration's by \$1.4 billion over 2006-07 and 2007-08. This translates into a Proposition 98 minimum guarantee that is \$609 million lower for 2006-07 and \$261 million higher in 2007-08 than the Governor's budget. In addition, we believe the administration's proposal to rebench the Proposition 98 minimum guarantee as a result of the school transportation shift (\$627 million) is unconstitutional and therefore might not result in General Fund savings.

These General Fund threats serve as an impetus to explore whether other options for General Fund savings are available within the parameters of Proposition 98. We identify an alternative that creates \$609 million in one-time General Fund savings while leaving budget-year Proposition 98 spending at effectively the same level as proposed by the Governor.

Higher Education Priorities. The Governor's budget presents the Legislature with three major issues in higher education: enrollment growth, student fees, and inflationary adjustments. The Governor's budget proposal offers little rationale to justify its enrollment funding increases. In particular, CCC enrollment has failed to meet the level of growth funded in recent annual budgets. Moreover, the Governor's budget funds each additional UC and CSU student using a formula the Legislature rejected in the current year. In the "Higher Education" portion of this chapter, we recommend different enrollment targets and funding levels for the segments.

The Governor's budget proposes 7 percent and 10 percent student fee increases for UC and CSU, respectively. This is roughly double the fee increase needed to maintain students' share of cost at 2006-07 levels. We discuss how educational costs can be allocated between students and the state in a way that preserves access and allows families to plan for future educational expenses.

The Governor's budget proposes base increases for all three segments. Consistent with statutory guidelines, the CCC would receive a COLA based on the same methodology as is used for K-12 schools. In contrast, there is no statutory guideline for providing a base increase for UC and CSU. Absent such a guideline, we recommend the Legislature provide base augmentations for those segments based on inflation.

CROSSCUTTING ISSUES

K-12 Education

PROPOSITION 98 UPDATE

Compared to the Governor's budget, we estimate less General Fund revenue in both the current and budget years. Given the particular formulas that drive Proposition 98, our revenue estimates result in a higher minimum guarantee in 2007-08. This counterintuitive result means the Legislature is likely to face more challenging trade-offs in its budget deliberations. In this section, we also discuss various other issues related to Proposition 98. Specifically, we (1) provide an update on outstanding Proposition 98 "settle-up" obligations, (2) describe the effect of a declining K-12 student population on the Proposition 98 minimum guarantee, and (3) discuss factors that might lead to the Proposition 98 Test 1 factor becoming operative in the near future.

GOVERNOR'S BUDGET

Before reviewing the Governor's Proposition 98 proposals for 2007-08, we first describe the budget's adjustments to prior- and current-year Proposition 98 funding levels. These adjustments are primarily due to updated local property tax revenue and student attendance data.

Prior-Year Adjustments

Due to technical adjustments and changes in property taxes, the spending level for 2005-06 increased by \$73 million above what was assumed when the 2006-07 budget was enacted. This higher spending level offsets the obligation relating to the recent K-14 settlement, reducing it

from \$1.3 billion to \$1.2 billion. Please see the “Quality Education Investment Act” section later in this chapter for additional information about this settlement.

Current-Year Adjustments

Figure 1 shows that overall spending for Proposition 98 in the current year decreases by \$100 million—from \$55.1 billion to \$55 billion. Most of these savings are associated with a greater decline in K-12 attendance from what the 2006-07 Budget Act assumed—from -0.27 percent to -0.39 percent. Additionally, estimates for local property tax revenues increase by \$384 million. Together, these two factors result in estimated General Fund savings of \$483 million as compared to budget act levels.

Figure 1	
2006-07 Proposition 98 Funding: Changes From 2006-07 Budget Act	
<i>(In Millions)</i>	
	2006-07
Total Proposition 98 Spending Level	
<i>2007-08 Governor's Budget</i>	\$55,022
<i>2006-07 Budget Act</i>	55,122
Difference	-\$100
General Fund Share	
<i>2007-08 Governor's Budget</i>	\$40,812
<i>2006-07 Budget Act</i>	41,295
Difference	-\$483
Local Property Tax Share	
<i>2007-08 Governor's Budget</i>	\$14,210
<i>2006-07 Budget Act</i>	13,827
Difference	\$384
Totals may not add due to rounding.	

Spending Level at Minimum Guarantee Plus Appropriation for Proposition 49. When the 2006-07 budget was adopted, the Proposition 98 spending level was roughly \$600 million above the minimum guarantee. About \$426 million of this additional funding was for Proposition 49 after school programs. (Proposition 49 required Proposition 98 spending to exceed the minimum guarantee by \$426 million in the first year it took effect.)

As a result of slight changes in revenues and attendance, Proposition 98 spending now exceeds the Governor's estimated minimum guarantee only by the Proposition 49 requirement (\$426 million).

Continues to Be a Test 3 Year. As was the case when the budget was enacted, the Governor's budget continues to project 2006-07 as a Test 3 year (meaning the minimum guarantee is based on growth in per capita General Fund revenue). This is because year-to-year growth in state General Fund revenues is relatively sluggish. During such times, the state is allowed to provide less than would be required by the Test 2 factor. (In a Test 2 year, the minimum guarantee is based on growth in per capita personal income). The gap between the Test 2 and Test 3 levels is called the "maintenance factor." The maintenance factor is tracked over time and Proposition 98 contains a mechanism to restore it in future years.

Under Governor's Budget Assumptions, About \$436 Million in Maintenance Factor Created in the Current Year. The state entered the current year having restored all outstanding maintenance factor obligations, but a new maintenance factor obligation is created because 2006-07 is a Test 3 year. Specifically, under the Governor's forecast, the Test 3 minimum guarantee is \$862 million below the Test 2 level for 2006-07. Because Proposition 49 requires the state to provide \$426 million above the minimum guarantee in the current year, the new maintenance factor is \$436 million. (Because of the specific statutory language contained in Proposition 49, both our office and the Department of Finance [DOF] interpret the measure such that the additional after school funding would count as restoring maintenance factor. Some in the education community disagree with this interpretation.)

Budget-Year Estimates

As discussed in the "Overview" section of this chapter, the Governor's budget proposes a spending level of \$56.8 billion for Proposition 98 in 2007-08. This is a \$1.8 billion, or 3.3 percent, increase over revised current-year spending. The proposed Proposition 98 spending level is \$627 million less than the calculated minimum guarantee. This is a result of the Governor's proposal to pay for the \$627 million Home-to-School Transportation program from the Public Transportation Account and reduce—or "rebench"—the Proposition 98 minimum guarantee by a like amount. (We have serious legal and policy concerns with the proposed rebenching of Proposition 98, which we discuss later in this chapter.)

Around \$144 Million in Maintenance Factor Would Need to Be Restored in 2007-08. As a Test 2 year, under the Governor's budget General Fund year-to-year revenue growth requires the state to restore about \$144 million in maintenance factor obligation. (This amount is already

included in the Governor's proposed overall Proposition 98 funding level.) After adjusting the outstanding obligation by the Proposition 98 growth factors, this would leave approximately \$310 million in maintenance factor to be restored in future years.

LEGISLATIVE ANALYST'S OFFICE FORECAST

Due to the timing of the budget's release, the Governor had to develop his budget before data from the end of 2006 was available. We benefit from receiving economic information on the final quarter of 2006 as well as revenues from year-end tax payments. Based on these data, our updated economic and revenue forecasts indicate that General Fund revenues will be lower in 2006-07 and 2007-08 compared to the administration's estimates. (Throughout this chapter we use the term "General Fund revenues" to refer to revenues received from taxes—the revenues used in the Proposition 98 calculation. These differ slightly from overall General Fund revenues.) Our projections result in somewhat different outcomes for the Proposition 98 minimum guarantee, as shown in Figure 2. The figure also shows our different assumptions for local property tax revenues and the resulting General Fund obligation. Below, we discuss our estimates for Proposition 98 in the current and budget years. (None of the updated data would change the guarantee for the prior year.)

Current-Year Adjustments

State Could Reduce K-14 Spending by \$609 Million in the Current Year Due to Decrease in the Minimum Guarantee. Our forecast projects General Fund tax revenues will be roughly \$940 million lower in 2006-07 compared to the administration's estimates. This projected drop in General Fund revenues lowers the Proposition 98 minimum guarantee. Specifically, as shown in Figure 2, we estimate the minimum guarantee is \$609 million below the administration's—for a total required funding level of \$54.4 billion instead of \$55 billion. (Like the administration, our estimate for the minimum guarantee includes the additional Proposition 49 spending requirement.)

This means that the state could reduce Proposition 98 spending in the current year by up to \$609 million, realize a like amount of General Fund savings, and still meet the constitutional requirement for K-14 education. We discuss options for realizing such savings in the next section of this chapter, "Proposition 98 Priorities."

Because 2006-07 is a Test 3 year, any further reduction in Proposition 98 spending creates a like amount of additional maintenance factor. The maintenance factor would need to be restored in future years.

Figure 2		
Proposition 98 Under Different Revenue Scenarios		
<i>(In Millions)</i>		
	2006-07^a	2007-08^b
Proposition 98 Minimum Guarantee		
LAO Forecast	\$54,413	\$57,097
Governor's Budget	55,022	56,835
Differences	-\$609	\$261
General Fund Requirement		
LAO Forecast	\$40,203	\$41,656
Governor's Budget	40,812	41,190
Differences	-\$609	\$466
Local Property Tax Revenues		
LAO Forecast	\$14,210	\$15,441
Governor's Budget	14,210	15,645
Differences	—	-\$204
^a	Includes required additional appropriation for Proposition 49 after school programs.	
^b	Assumes proposed reduction of minimum guarantee for transportation funding swap.	

Budget-Year Estimates

Under Our Forecast, the Minimum Guarantee for 2007-08 Is \$261 Million Higher Than Assumed in Governor's Budget. Despite our estimates of General Fund revenues being lower than the administration's in both the current year (by roughly \$940 million) and the budget year (by roughly \$500 million), our estimate for year-to-year revenue growth actually is greater. This is because Proposition 98 drives off the year-to-year *growth* in General Fund revenues, not the actual *amount* of revenues. The stronger year-to-year growth, in turn, results in a higher minimum guarantee and more maintenance factor restoration. Specifically, as shown in Figure 2, we estimate the Proposition 98 minimum guarantee for 2007-08 is \$261 million higher than assumed in the Governor's budget—increasing total spending from \$56.8 billion to \$57.1 billion. That is, relative to the Governor's budget, the state would need to provide an additional \$261 million to meet the K-14 funding guarantee. Under our forecast, roughly all of the outstanding maintenance factor (around \$450 million) would be restored in the budget year.

Lower Property Tax Estimates Further Increase State's General Fund Obligation (by Additional \$204 Million). Also shown in Figure 2, we believe the administration overestimates property taxes for the budget year by \$204 million. The Governor's budget assumes property taxes will increase by 10 percent over 2006-07 levels—to \$15.6 billion. Given the current slowdown in the real estate market, we project an 8.7 percent growth rate (\$15.4 billion). Property tax revenues generally offset the General Fund share of Proposition 98 (except in a Test 1 year). Thus, a \$204 million drop in property tax revenues increases the Proposition 98 General Fund obligation by a like amount.

Adding the effect of lower projected property tax revenues (\$204 million) to the \$261 million resulting from the higher minimum guarantee, our forecast suggests the Proposition 98 General Fund 2007-08 obligation is actually \$466 million higher than what is assumed in the Governor's budget.

Legislature Faced With Tough Decisions

Based on our forecast, the Legislature will confront even more difficult decisions in balancing its 2007-08 budget. While these estimates will change again with the Governor's May Revision, we suggest the Legislature begin considering options now for making the needed trade-offs between K-14 education and the rest of the budget.

Reducing Current Year Spending Could Be Critical Part of Budget Solution. As noted, our forecast suggests the state is spending around \$609 million more on Proposition 98 in 2006-07 than is required by the minimum guarantee. Because the budget year's Proposition 98 requirement is based upon the spending level in the current year, reducing spending in 2006-07 would also reduce the K-14 obligation for 2007-08. We discuss this option further in the "Proposition 98 Priorities" section of this chapter.

UPDATE ON OTHER PROPOSITION 98 ISSUES

Below, we discuss three issues relating to Proposition 98: (1) outstanding settle-up and settlement obligations, (2) declining K-12 attendance, and (3) dynamics related to the Test 1 factor.

Proposition 98 Settle-Up Obligations

In some years, the state generates "settle-up" obligations (or outstanding balances which need to be paid) relating to the Proposition 98 minimum guarantee. These settle-up obligations are generated when attendance

counts or revenues change after the budget is enacted and the minimum guarantee increases above the level of funding that was provided.

Chapter 216, Statutes of 2004 (SB 1108, Committee on Budget and Fiscal Review), required the Superintendent of Public Instruction and Director of Finance to jointly determine settle-up obligations for the Proposition 98 minimum guarantee for fiscal years 1995-96 through 2003-04. This process, completed in January 2006, determined the state owed schools roughly \$1.4 billion to meet the minimum guarantee for four prior years—1995-96, 1996-97, 2002-03, and 2003-04.

Chapter 216 continuously appropriates \$150 million annually beginning in the 2006-07 fiscal year for the purposes of repaying these settle-up obligations. The 2006-07 budget included a \$133 million payment for the current year (\$17 million was “prepaid” in 2005-06), as well as an additional \$150 million to prepay the requirement for 2007-08. As directed by Chapter 216, these funds repaid schools and community colleges for the costs of prior-year mandates. This \$300 million retired the settle-up obligations for 1995-96 and 1996-97. As shown in Figure 3 (see next page), the state still has existing settle-up obligations totaling roughly \$1.1 billion—\$483 million for 2002-03 and \$618 million for 2003-04.

In addition to these settle-up requirements, the state last year created a new \$2.8 billion obligation relating to the California Teachers Association (CTA) settlement. In that settlement, the state agreed to pay \$1.6 billion for 2004-05 and approximately \$1.2 billion for 2005-06. Chapter 751, Statutes 2006 (SB 1133, Torlakson), established a seven-year payment schedule for providing these additional funds. Figure 3 also shows these new settlement-related obligations.

Although \$300 million is being provided in the budget year to meet the terms of the CTA settlement, DOF has scored these funds as an adjustment to the entering balance in 2005-06 rather than a budget-year expenditure. We have concerns with this method of accounting. For more discussion of this issue, please see the “Quality Education Investment Act” section of this chapter.

The Effect of Declining Attendance on the Proposition 98 Minimum Guarantee

Except under Test 1 or suspension scenarios, the Proposition 98 minimum guarantee is determined each year by taking the prior-year’s Proposition 98 appropriation and adjusting it by growth in statewide K-12 average daily attendance (ADA) and by growth in either per capita personal income (Test 2) or per capita General Fund revenues (Test 3). (The community college growth rate is not a factor in determining the overall Proposition 98 minimum guarantee.) In most years, the state’s K-12 population has grown, contributing to increases in overall Proposition 98 funding.

Figure 3**Update on Outstanding Proposition 98 Obligations***(In Millions)*

	Amount	Payment Schedule
Existing "Settle-Up" Obligations		
2002-03	\$483	
2003-04	618	
Total	\$1,101	\$150 million annually until obligation is met (8 years). ^a
New CTA^b Settlement Obligation		
2004-05	\$1,621	
2005-06	1,226 ^c	
Total	\$2,847	\$300 million in 2007-08, then \$450 million annually until obligation is met (7 years).
Grand Total	\$3,948	

a Obligation for 2007-08 was prepaid in 2006-07.
b California Teacher's Association.
c The obligation for 2005-06 has decreased from original estimates of \$1.3 billion down to \$1.2 billion. This is due to the Proposition 98 spending level increasing by \$73 million in 2005-06.

Proposition 98 Protected From Decline for Two Years. Proposition 98 includes a two-year "hold harmless" clause for when K-12 population declines. That is, for each of the first two years of K-12 ADA decline, the Proposition 98 guarantee is calculated using a 0 percent growth rate. In a third consecutive year, the Proposition 98 calculation uses the actual statewide K-12 ADA rate, and the minimum guarantee is reduced to reflect the decline in K-12 population from the previous year. The downward adjustment is intended to reflect fewer students and, correspondingly, less need.

Proposition 98 Will Be Adjusted Downward for First Time in 2007-08. Between 2004-05 and 2005-06, statewide ADA declined for the first time since the passage of Proposition 98 in 1988. As shown in Figure 4, the Proposition 98 growth factor of 0 percent was used in the funding formula for 2005-06. In the same way, overall K-14 funding is protected from the projected ADA decline in 2006-07. However, the figure also shows that statewide ADA is projected to decline for a third consecutive year in

2007-08. For the first time ever, this leads to a negative ADA-based adjustment for the Proposition 98 minimum guarantee.

Figure 4

Comparison of Attendance and Proposition 98 Growth Factors

	2004-05	2005-06	2006-07	2007-08
Statewide ADA ^a	0.3%	-0.3%	-0.4%	-0.4%
Proposition 98 growth factor	0.3	0.0	0.0	-0.4

^a Average daily attendance.

For as many years as ADA continues to decline, the Proposition 98 minimum guarantee will continue to be adjusted downward. However, the hold harmless clause “resets” once the state experiences one year of positive ADA growth. That is, if ADA grows and then begins to decline again, Proposition 98 funding will receive another two-year reprieve from any associated reduction.

Overall Proposition 98 Funding Still Increases. Despite the negative ADA-based adjustment, Proposition 98 funding still experiences a net increase of \$1.8 billion in 2007-08 compared to the current year. This is because in addition to ADA growth, the Proposition 98 formula also adjusts the current-year’s funding level by the Test 2 factor (per capita personal income). For the budget year the Test 2 factor—4.6 percent—provides a significant amount of growth even after accounting for the -0.4 percent attendance factor.

Proposition 98 Program Funding Based on Separate Calculation. That the overall Proposition 98 minimum guarantee reflects the decline in K-12 attendance does not necessarily mean that funding for each K-14 program will receive a negative adjustment. While some programs do experience attendance-related reductions, others actually receive increases. Still others experience no attendance-related adjustment. The K-12 revenue limit apportionments, or general purpose funding, do adjust automatically to reflect growth and declines at individual school districts. Moreover, the Governor’s budget adjusts downward about one-half of the 50-some categorical programs by the statewide ADA growth rate of -0.4 percent. In contrast, it funds several other programs at different statutory growth rates. (Most of these latter programs serve populations other than K-12 students, such as child care, adult education, and Regional Occupational Centers. Community college apportionments and categorical programs are

also funded at a different growth rate—2 percent in 2007-08.) Additionally, the budget proposes to hold about 20 categorical programs harmless at 2006-07 levels (in lieu of applying the negative adjustment).

Legislature Can Adjust Growth Funding for Categorical Programs.

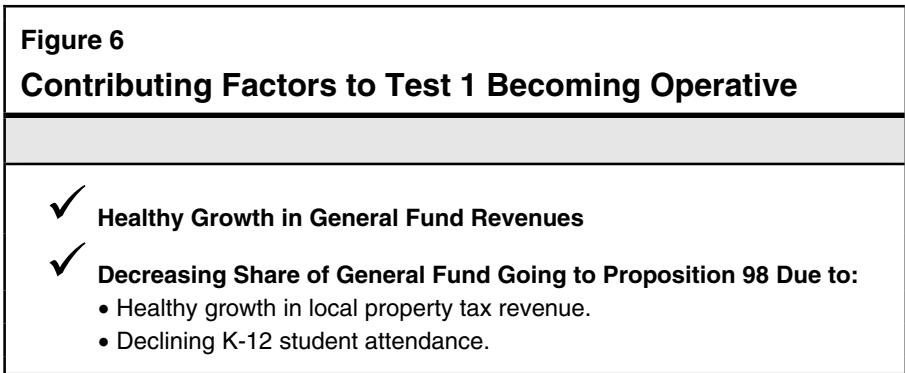
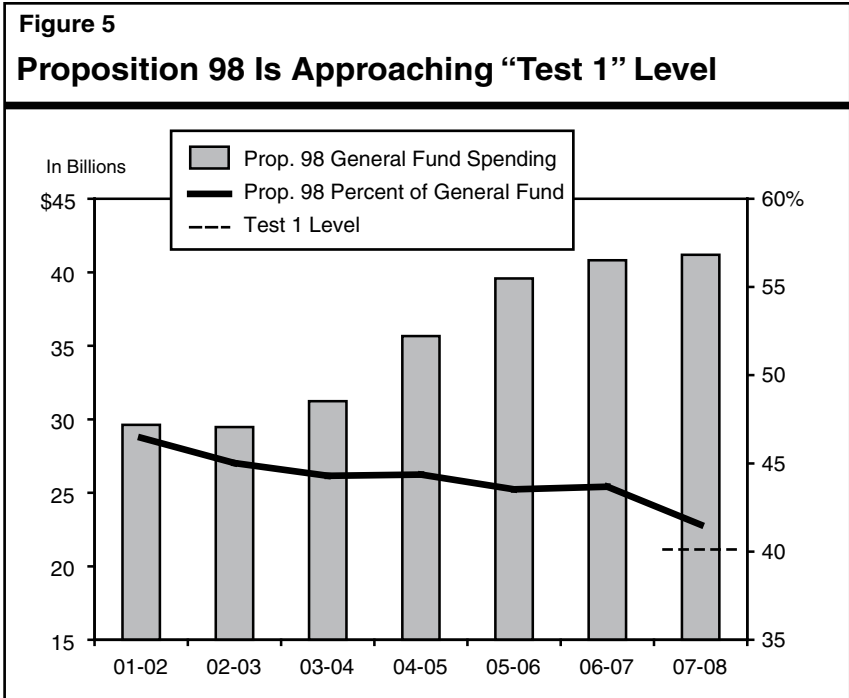
For the most part, the Governor uses his discretion as to which categorical programs to “protect” and which to adjust downward. With fewer students in the system to participate in the categorical programs, there is some question as to why certain programs would require additional funding. The Legislature has the option of decreasing by 0.4 percent all those categorical programs the Governor chooses to protect. This would free up around \$13 million in Proposition 98 funds to be redirected to other purposes. Alternatively, if the Legislature believes certain programs should receive additional funding despite the decline in student population, it can choose its own selection of programs to protect from the negative growth adjustment.

The Underlying Dynamics of the Proposition 98 “Test 1” Factor

Under Test 1, the Proposition 98 minimum guarantee is set at roughly 40 percent of General Fund revenues. The Test 1 factor is operative if it yields a higher Proposition 98 funding level than either the Test 2 or the Test 3 factors. To date, Test 1 has been operative only in 1988-89, the year after Proposition 98 was passed. In subsequent years, Test 2, which grows the prior-year K-14 funding level by the percent change in per capita personal income, quickly moved the guarantee above the Test 1 level. This was because slow growth in General Fund and property tax revenues were coupled with fast growth in K-12 attendance. The combined effect was to increase the K-14 share of total General Fund spending.

Statewide Dynamics Are Changing. Over the past several years, these dynamics have begun to reverse—a healthy economy has increased total General Fund and property tax revenues, while K-12 attendance has dropped. Figure 5 shows the effects of these changes. Since 2001-02, even as General Fund spending for K-14 education has increased, the Proposition 98 share of overall General Fund revenues has been steadily decreasing. As K-14 education’s share of the General Fund decreases, the state gets progressively closer to hitting the Test 1 level of roughly 40 percent.

Test 1 on the Horizon. Figure 6 summarizes the factors that would contribute to Test 1 becoming operative. Based on the Governor’s proposed level of spending and our estimates for revenues, attendance, and local property taxes in the future, we project that Test 1 may become operative again as early as 2009-10.



What Is the Practical Effect of Hitting Test 1? Once the K-14 share of General Fund spending declines to about 40 percent and Test 1 applies, the K-14 share of General Fund spending will be fixed at that percentage. Under this scenario, the minimum guarantee is no longer determined based on changes in ADA or the Test 2 and Test 3 factors. This has a number of policy and budgetary implications, including:

- Further declines in K-12 enrollment do not yield additional savings for the state. Instead, K-14 education will continue to get the fixed share of General Fund revenues regardless of how many students are in the system. Thus, a declining student population likely will result in higher per pupil spending levels.
- Under Test 2, increases in local property tax revenue offset General Fund contributions for Proposition 98 but do not affect the net amount of resources going to schools. Under Test 1, increases in local property tax revenues will *supplement* rather than supplant General Fund spending. This means K-14 funding levels can benefit substantially from healthy increases in local property tax revenues.

In the “Proposition 98 Roadmap” section of this chapter, we offer recommendations as to how the Legislature can effectively plan for and use the increased resources that would be available for K-14 education when Test 1 becomes operative.

PROPOSITION 98 PRIORITIES

We recommend the Legislature reduce current-year K-14 spending to the minimum permitted under Proposition 98. For the budget year, we recommend the Legislature provide baseline increases for growth and cost-of-living adjustments. These recommendations would generate substantial General Fund savings with only minor impacts to ongoing K-14 programs.

Governor Proposes a “Baseline” Budget

The Governor’s budget proposes a net increase to Proposition 98 expenditures of \$1.8 billion in 2007-08 compared to the revised 2006-07 spending level. Figure 1 (see next page) displays the major funding changes proposed in the budget year. As the figure shows, the budget provides a baseline cost increase of \$2.2 billion. A projected 4 percent cost-of-living adjustment accounts for most of the new spending in the budget year (\$2.1 billion). Net new funding for attendance adds another \$38 million, which consists of growth in the community colleges (\$115 million) offset by a projected fall in attendance in K-12 education (-\$77 million).

Baseline increases are partially offset by a net reduction of \$358 million in Proposition 98 spending that result from several budget-year policy proposals. The budget reflects a \$627 million cut in General Fund support due to the proposal to fund the K-12 Home-to-School Transportation program from the state Public Transportation Account (PTA) rather than the General Fund. The administration proposes to permanently reduce the Proposition 98 minimum guarantee (known as “rebenching”) by the same amount, thereby generating long-term General Fund savings from this funding shift.

The budget also includes a \$269 million increase for child development programs. This increase in state support would offset a reduction in federal Temporary Assistance for Needy Families funds for the program. The budget uses these federal funds to free up General Fund dollars in the California Work Opportunity and Responsibility to Kids (CalWORKs) program. Thus, similar to the transportation proposal discussed above,

the child care proposal would result in General Fund savings. Unlike the transportation proposal, this proposal does not require rebenching the Proposition 98 minimum guarantee.

For the community colleges, the budget includes \$115 million for 2 percent growth in the number of new full-time equivalent students. This is \$19 million more than what is called for by a new statutory guideline based on underlying growth in the adult population. This guideline calls for 1.65 percent growth. (The \$19 million is included in attendance growth in Figure 1 and is not separately identified).

Figure 1	
Proposition 98 Expenditure Plan	
<i>2007-08 Governor's Budget</i>	
Baseline Adjustments	
Cost-of-living adjustment	\$2,137.9
Attendance growth	38.2
Subtotal	(\$2,176.2)
Proposed Increases or Reductions	
Home-to-School Transportation	-\$626.8
Child care federal funds shift	269.0
Other K-12 proposals	-29.0
CCC ^a proposals	28.6
Subtotal	(-\$358.2)
Total	\$1,818.0
Detail may not total due to rounding.	
^a California Community College.	

LAO Proposition 98 Forecast—Lower Revenues, Higher Guarantee

Our revenue forecast results in a Proposition 98 minimum guarantee that is \$609 million lower for 2006-07 and \$261 million higher in 2007-08 than the Governor's budget. These differences are due primarily to our forecast of lower General Fund revenues. As we discuss in the "Proposition 98 Update" section of this chapter, our estimate of General Fund tax revenues is lower than the administration's by roughly \$940 million in 2006-07 and \$500 million in 2007-08.

Our forecast creates several new issues for the Legislature. The lower current-year guarantee means the enacted budget spends more than re-

quired under Proposition 98. Thus, using our estimates, the Legislature would have the option of reducing Proposition 98 spending in 2006-07 and still meet the minimum funding guarantee. Our higher 2007-08 guarantee also would increase demands on the state General Fund in the budget year. Satisfying the higher guarantee would require the Legislature to draw down the General Fund reserve by \$261 million or reduce other non-Proposition 98 spending by that amount.

The Legislature, however, could address both issues in a way that generates significant General Fund savings in both years. Specifically, reducing the overappropriation in 2006-07 would also reduce the Proposition 98 guarantee in 2007-08 by about the same amount. As a result, this option would create one-time savings in 2006-07 and ongoing savings in Proposition 98 costs beginning in 2007-08.

Achieving Proposition 98 Savings

The implications of the LAO forecast on the General Fund condition are serious. Our projection suggests the Governor's budget overestimates General Fund tax revenues by \$1.4 billion over two years. In addition, our estimate of property tax revenues going to K-14 education is \$204 million lower—and the General Fund share of Proposition 98 is \$204 million higher—than assumed in the proposed budget. Our revenue forecast also generates a budget-year Proposition 98 minimum guarantee that is \$261 million higher than under the administration's estimate.

The result of these differences means the 2007-08 year-end General Fund balance would be \$1.9 billion *lower* than assumed in the Governor's budget—basically wiping out the budget's projected year-end reserve. In addition, we have serious policy and legal concerns about the administration's proposed \$627 million transportation shift, which call into question the General Fund savings identified in the budget. Given these General Fund threats, it is important for the Legislature to consider all options for balancing revenues and spending—including any options that are available within the parameters of Proposition 98.

For these reasons, we recommend the Legislature generate General Fund savings by reducing K-14 spending in the current year to the minimum permitted by Proposition 98 (including Proposition 49 after school funds). Since this also would reduce the minimum guarantee in 2007-08, this option offers a way to maximize General Fund savings while still covering baseline costs of schools and community colleges in the budget year.

Determining how to use this option to greatest advantage requires two steps. The first step involves finding savings that permit a reduction of Proposition 98 in the current year. Under our forecast, the Legislature

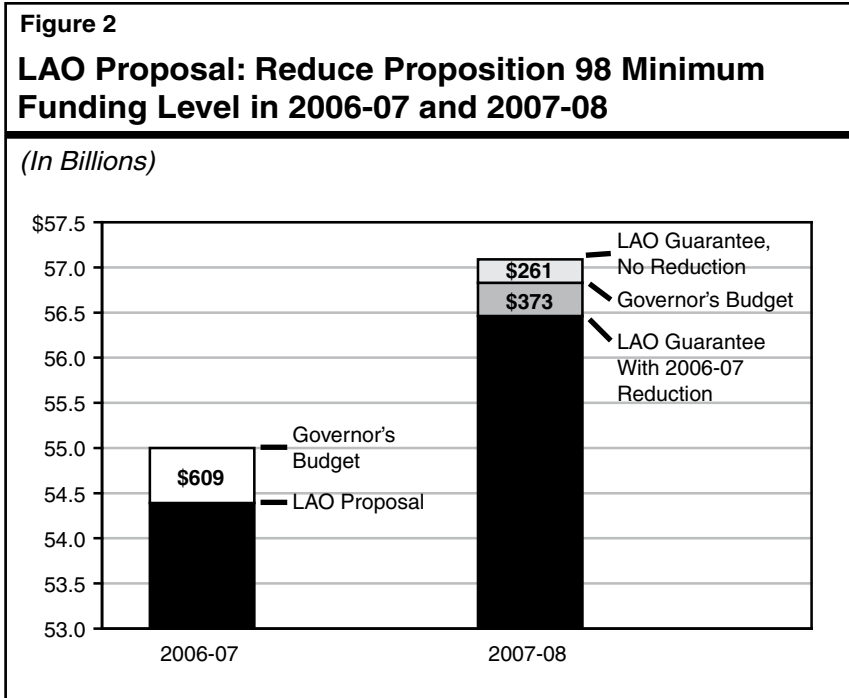
could reduce 2006-07 Proposition 98 spending by \$609 million. We have identified this amount of K-14 spending reductions, which we discuss in more detail below.

The second step involves assessing how this reduction would affect the proposed 2007-08 K-14 budget. Reducing current-year Proposition 98 spending by \$609 million lowers the 2007-08 guarantee by \$634 million (the current-year savings increase by the Proposition 98 growth factors). We believe that even at this lower level the Legislature can cover Proposition 98 baseline costs in 2007-08 (also discussed below).

Figure 2 illustrates the impact of our proposal on Proposition 98. The left-hand bar shows the current-year Proposition 98 spending level of \$55 billion under the Governor's budget. Our proposal would reduce expenditures by \$609 million, lowering the minimum funding level by that amount. The right-hand bar represents the Proposition 98 guarantee in 2007-08. Note that the LAO estimate of the guarantee is \$261 million *higher* than the Governor's budget if no current-year action is taken, but \$373 million *lower* if current-year spending is reduced to the minimum guarantee. Thus, by lowering current-year spending, our proposal would save \$634 million in Proposition 98 spending.

Reducing the guarantee by \$373 million from the Governor's proposed level in the budget year, however, would not provide sufficient funding to cover baseline K-14 costs. Therefore, we first recommend the Legislature *not* implement the child care shift in 2007-08. In effect, our option saves the \$269 million in Proposition 98 spending that was assumed in the Governor's budget by keeping those expenditures in the CalWORKs budget. (The option to do the shift, however, would still be available to the Legislature in future years.) Regarding the remaining roughly \$100 million difference, we believe the Legislature can find savings of this magnitude without affecting base programs. For example, we identify in our "California Community Colleges" analysis enrollment related-funds that will likely not be needed for their intended purposes in 2007-08.

In summary, to provide a measure of relief to the General Fund, we recommend the Legislature adopt our two-year savings option by reducing Proposition 98 spending in 2006-07 by \$609 million. This represents real one-time General Fund savings. In 2007-08, our recommendation would reduce the budget-year guarantee by about \$634 million, yet still leave K-14 education at an equivalent level of ongoing services in 2007-08 as the Governor's budget. (Partially offsetting these savings would be a cost of \$269 million in the CalWORKs budget due to the rejection of the child care proposal). In addition, our option reserves for a future year the possibility of using the child care shift to generate General Fund savings.



Current-Year Proposition 98 Savings

As previously discussed, the Legislature would need to reduce current-year Proposition 98 appropriations in order to achieve savings in 2006-07 and 2007-08. Our proposed current-year reductions come from two sources—transferring funds from the PTA and reverting unused 2006-07 Proposition 98 funds to the General Fund. Our PTA proposal has some similarities to the Governor's proposed use of these funds. We propose to use \$300 million from the PTA in the current year to replace the same amount of Proposition 98 funding for the Home-to-School Transportation program. Our review indicates that the PTA would have sufficient revenues to support this diversion of funds. Under our proposal, however, the transfer would be one-time in nature and would not involve rebenching the Proposition 98 minimum funding guarantee.

We identify \$309 million in Proposition 98 funds that we estimate will not be needed in the current year. Figure 3 (see next page) displays the source of these savings. We identify \$240 million in savings that are not captured in the proposed budget. Of this amount, \$41.7 million in special education savings result from lower growth in the student population. Similarly, the savings in CCC growth stem from differences between the amounts budgeted for enrollment growth and the amount we anticipate

they will spend this year. The \$35.2 million in child care program savings are the result of a lengthy preschool implementation process. Finally, the \$33.1 million in “overcap” funding is available as it is double-budgeted in the current year. All of these projected savings represent our best estimates of current-year overfunding. Additional information will become available later in the spring to update these estimates.

Figure 3	
LAO Proposed 2006-07 Reductions	
<i>(In Millions)</i>	
Program	Amount
Projected Program Savings	
Special education base adjustment	\$41.7
Unused CCC growth ^a	130.0
Preschool expansion	35.2
CCC “overcap” funding ^a	33.1
Subtotal	(\$240.0)
Rejection of Governor’s Augmentations	
Low-performing school enrichment	\$50.0
Encorps alternative education	10.0
CCC nursing ^a	9.0
Subtotal	(\$69.0)
Total	\$309.0
^a CCC=California Community College	

Our recommendation also would “sweep” \$69 million in current-year funds that the budget proposes to spend for other purposes. These represent 2006-07 savings that were identified by the Department of Finance and proposed for the following programs:

- \$50 million for the low-performing school enrichment program, which is designed to attract experienced teachers to low-performing schools. The budget proposal would fund the program in 2007-08.
- \$10 million for a new Encorps program that would train “experienced retirees” to become K-12 teachers.
- \$9 million for equipment, curriculum development, and other enhancements for nursing programs in the community colleges.

(These funds would *not* directly support additional nursing enrollment.)

In other words, we are suggesting using these savings in the current year for budgetary balancing, rather than new activities or expansions.

MAINTAIN PRIORITY ON REDUCING CREDIT CARD DEBT

We recommend that, if new funds become available, the Legislature place a high priority on paying for the ongoing cost of state-mandated local programs and reducing the level of deferrals.

The Proposition 98 credit card represents amounts the state owes to K-14 education for costs that were not fully funded during the fiscal year in which services were provided. This “debt,” or obligation, can be retired with one-time or ongoing Proposition 98 funds. Figure 4 displays the balance of the credit card in 2005-06 and 2006-07 and our estimate of the amount owed in 2007-08. We project the credit card balance will total \$1.9 billion by the end of 2007-08. Funding deferrals—shifting payments for services provided during the budget year to the next fiscal year—accounts for \$1.3 billion. The other \$550 million represents the ongoing costs of mandated local programs that were not addressed in past budgets.

Figure 4			
Status of the Education Credit Card Debt			
<i>(In Millions)</i>			
	2005-06	2006-07	2007-08
Deferrals			
K-12	\$1,103.4	\$1,103.4	\$1,103.4
Community college	200.0	200.0	200.0
Mandates			
K-12 ^a	\$900.0	\$275.0	\$435.0
Community college	100.0	90.0	115.0
K-12 Revenue Limits	\$300.0	—	—
Totals	\$2,603.4	\$1,668.4	\$1,853.4

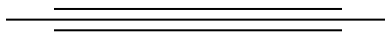
^a Excludes claims that are unlikely to be paid as the result of court decisions or recent determinations by the Commission on State Mandates.

The figure also illustrates the Legislature's actions to reduce the outstanding credit card balance as part of the *2006-07 Budget Act*. The final budget included more than \$800 million in one-time funds for state mandates, which retired almost all district and college claims (plus interest) through 2004-05. In addition, the Legislature also eliminated the K-12 "deficit factor," which represented foregone inflation adjustments to revenue limits in 2003-04.

The amount owed to K-14 education, however, actually increases again in 2007-08. This is because the proposed budget includes no ongoing funding for K-12 mandates and only \$4 million for mandates in community colleges. We expect K-14 claims for mandated local programs to reach about \$185 million in 2007-08.

In the past, we have recommended that the Legislature use available ongoing funding to restore the annual appropriation for mandates. These programs are part of the base education program. Failing to include these costs in the budget represents increased borrowing at a time when the state should be repaying the education credit card. Unfortunately, based on our estimates, there are no additional sources of discretionary K-12 funds in the 2007-08 proposed budget that could be redirected to pay for mandates.

If additional discretionary funds become available, however, we recommend the Legislature use these funds to reduce its education credit card debt. In our view, the first call on any new ongoing funds should go to pay for the budget-year cost of mandates so that the credit card debt does not increase over time. One-time funds could be used to reduce the level of program deferrals or pay past-year mandate costs. Thus, we recommend the Legislature give first priority for any additional ongoing or one-time funds that materialize this year to reducing these Proposition 98 obligations.



A PROPOSITION 98 ROADMAP

By creating a long-term funding roadmap for the use of Proposition 98 funds, the Legislature could strengthen its role in the annual budget process, increase its ability to identify and pay for high-priority policy initiatives, and help school and community college districts plan and implement state initiatives more effectively.

Budgeting—whether for one’s personal finances or for state government—entails balancing funding inflows and outflows. In either case, “needs” and “wants” typically exceed resources, which requires choices about how best to use available funds. Budgeting under a short-term perspective often means that any new resources are spent on things that appear important at the time spending decisions are made.

Short-term priorities, however, may be inconsistent with the best long-term use of extra resources. To align short-run budgeting decisions with long-term goals, financial experts counsel people and governments to make explicit their long-term program and financial goals. Once these goals are identified, short-term budget decisions can be structured to support the longer-term goals.

Proposition 98 offers the Legislature a tool for long-term budget planning. Because the minimum guarantee in most years is determined by growth in the economy and K-12 student population, the Legislature can develop a long-term estimate of the amount of new funds that may be available if the economy behaves as expected. Using these revenue projections, the Legislature could develop a long-term expenditure plan that addresses its high-priority uses for new funding. This expenditure plan would serve as a guide to the work of the budget subcommittees in allocating Proposition 98 funds each year.

MANY BENEFITS FROM TAKING A LONG-TERM PERSPECTIVE

In this section, we recommend the Legislature develop a roadmap for the use of Proposition 98 funds that we project will become available

over the next five years. We call it a roadmap because we think it would help guide the Legislature's fiscal choices so that it would more readily reach its long-term program objectives—despite the unexpected bumps and detours that inevitably occur along the way.

We see many advantages in creating a roadmap for the use of Proposition 98 funds. Figure 1 summarizes these benefits. First, the development of a plan would create a forum for the Legislature to identify its longer-term priorities. We do not see the roadmap as creating binding long-term obligations, but rather an opportunity for the Legislature to assess the progress of students and identify ways that additional funds could further support schools and community colleges in meeting the state's educational goals.

Figure 1

Benefits of a Proposition 98 Roadmap

- ✓ Helps the Legislature Identify Its Long-Term Priorities
- ✓ Strengthens the Legislature's Role in the Budget Process
- ✓ Helps Coordinate Spending Plans With Other Policy and Administrative Actions
- ✓ Facilitates Local Implementation Process

A roadmap also would strengthen the Legislature's role in the budget process. Because growth in the economy and General Fund revenues is hard to predict, the Legislature often faces the task of budgeting hundreds of millions, or even billions, in discretionary dollars at the time of the May Revision. Without a longer-term perspective on the best use of these funds, the Legislature's choices are framed by the Governor's proposals or by other policy issues facing the Legislature at that particular moment. A roadmap would provide a broader range of choices to the budget committees. It also would help members assess the relative importance of immediate needs and longer-term program goals.

A plan also would help the Legislature put in place the other policy structures that might be needed to implement its long-term priorities. Additional money often constitutes only one of several ingredients needed for successful policies or programs. Considerable planning time may be needed, for instance, if new facilities are required to implement the Leg-

islature's policy directives. A long-term plan would allow the Legislature to initiate these changes in coordination with its expenditure plan.

By making the state's policy goals more explicit—and the budget process more predictable—schools and community colleges also would benefit from a roadmap. Just as the Legislature finds itself reacting to last-minute proposals to spend significant new Proposition 98 resources, K-12 and community college districts must implement the resulting new programs under tight timeframes.

The state's experience with implementing K-3 class size reduction (CSR) shows how last-minute budget proposals—particularly ones creating complex new programs that require significant lead time for local planning and implementation—can result in unintended negative consequences. The rapid implementation of CSR in 1996-97 resulted in immediate and severe shortages of credentialed teachers and available classroom space. Studies suggest that the employment opportunities created by the program resulted in credentialed teachers moving from inner-city schools to suburban schools. Perhaps as a result of the implementation challenges created by the very short implementation timelines, evaluations of the class-size program showed little impact on student achievement. Alternatively, a Proposition 98 roadmap could signal future spending directions and give school and community college districts a better chance to implement new programs effectively.

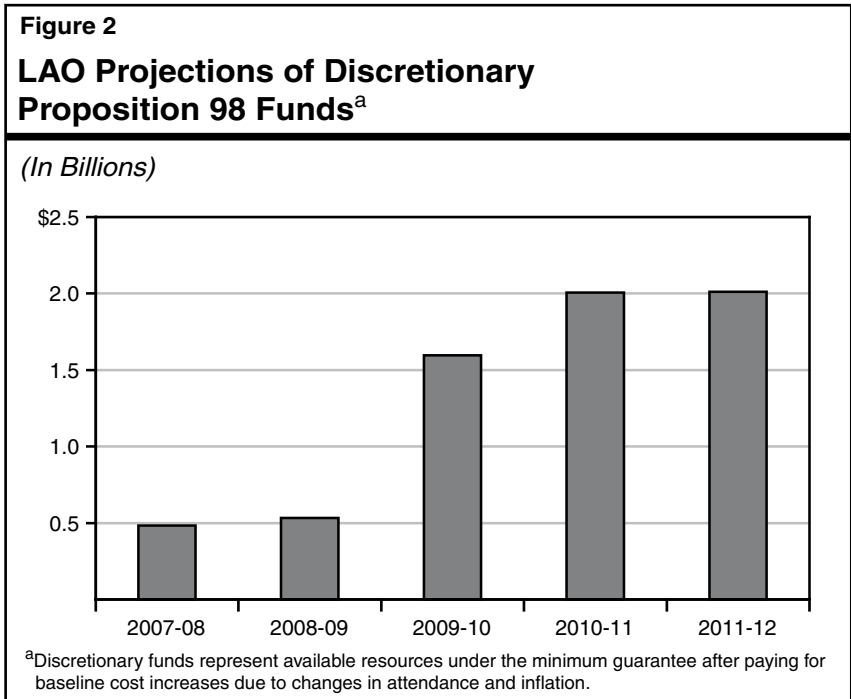
SIGNIFICANT NEW REVENUES IN FORECAST

The possibility of significant and sustained Proposition 98 increases over the next five years make this an opportune time for the development of a roadmap. Figure 2 (see next page) displays the LAO Proposition 98 projections of the annual amount of new discretionary funds that will be available from 2007-08 through 2011-12. Discretionary funds represent the growth in year-to-year Proposition 98 funds that is left after providing for baseline costs such as changes in attendance and cost of living. As the figure indicates, the amount of discretionary funds available in 2007-08 and 2008-09 is small—we project about \$500 million in each year. In 2009-10, more than \$1.5 billion in new funds is available for new programs (this is the year we project that Proposition 98 begins using Test 1 to determine K-14 funding levels). In 2010-11 and 2011-12, more than \$2 billion is available in discretionary funds each year.

When the incremental annual amounts shown in Figure 2 (see next page) are cumulated, the state will have \$6.6 billion in new discretionary resources available for Proposition 98 by 2011-12. (Using the statutory division of Proposition 98 funds, K-12 education would receive about \$5.9 billion of

these funds and community colleges would receive about \$750 million.) These are permanent, new resources that would substantially boost ongoing per-pupil funding levels for schools and community colleges.

As discussed above, actual annual increases in the minimum guarantee are rarely as orderly as projected. Our five-year projection assumes annual increases based on long-term economic and revenue trends. Since actual annual changes can vary substantially from these long-run averages, the pattern of Proposition 98 increases probably will diverge from our projection. Slower General Fund growth, for instance, could mean that Test 1 would begin determining Proposition 98 spending levels later than we currently project. Despite these caveats, we believe our projections provide a realistic starting point for planning purposes.



Recent Research Efforts Could Help Inform Planning

The 2007-08 legislative session may represent an opportune time to develop a Proposition 98 roadmap for another reason: the results of a foundation-supported effort to study the issues of funding adequacy and efficiency in K-12 education are expected to be released in the spring of

2007. These studies may help inform the Legislature's discussions about where additional funds are most needed and identify policy changes that should accompany new monies.

At the request of the Assembly Speaker, the Senate Pro Tempore, the Governor, and the Superintendent of Public Instruction, four foundations joined to fund about 20 studies covering a variety of K-12 topics. These studies have two general goals. One is to advise the Governor and legislators whether K-12 schools are "adequately" funded—that is, supported at a level sufficient to ensure that all students can achieve at levels consistent with state achievement standards. The studies will examine funding adequacy for the system as a whole as well as for specific subgroups of students, such as special education and English learner (EL) students.

The second goal is to help state policymakers identify other reforms that would help the K-12 education system operate more efficiently and effectively. Studies include a broad array of topics, including governance, teacher quality and training, and a review of the existing K-12 funding system.

If the studies on California's system conform with the experience of other states that have conducted adequacy studies, the foundation reports will call for substantial increases in support for K-12 education. The reports also are likely to call for programmatic and structural changes to improve the operation of the system. In this event, the reports will provide the Legislature with informed perspectives that can jump-start the discussion over a K-14 roadmap.

A Roadmap Expresses Priorities, Other Program Goals

Creating a long-term roadmap for K-14 expenditures requires an understanding of the critical issues facing the state's education system and how strategic investments can address those issues. Fundamentally, however, it is a priority-setting exercise. While policymakers can disagree about the critical issues in the system, the state's assessment and accountability system puts the Legislature in a much better position than in the past to inform this discussion with data on student success and other outcomes. As a result, the priority-setting discussion establishes an avenue for taking stock of the performance of schools and community colleges and charting the next steps for improvement.

While student success is the most important issue underlying the path outlined in a funding roadmap, a variety of issues may warrant attention. For example, the Legislature has an interest in maintaining the fiscal health of school and community college districts. In addition, the Legislature

may want to provide discretionary funds to let local educational agencies pursue critical local priorities.

In considering its high-priority areas, the Legislature should keep in mind some key objectives:

- ***Fix Problems With Current Formulas.*** As the Legislature contemplates adding new funds to existing funding formulas, it may first want to consider using a portion of the funds to eliminate funding disparities and simplify the formulas. In many programs, the current distribution of funding has little analytical basis because it is based on historical factors rather than district “need.” Addressing these problems would make the funding system fairer and easier to understand.
- ***Provide Flexibility, but Learn What Works.*** In general, we believe that giving school and community college districts discretion to develop local solutions to specific issues lets districts use funds most effectively. By supporting program evaluations and dissemination of “best practices,” the state can help districts learn how best to use program flexibility to meet the needs of different types of students.
- ***Link New Funds to Improved Performance.*** New investments in K-14 programs may have little impact on student performance without accompanying expectations for improved performance. As we have seen in K-12 education, effective accountability programs significantly sharpen the local focus on creating positive student outcomes. In community colleges, pressure for better performance can be strengthened in a number of ways, including making good measures of program performance easily available to policymakers and the public.

Education research has established that, by itself, additional funding may not result in higher student performance. The above factors, therefore, represent important fiscal and program elements—fairness, transparency, flexibility, accountability—that help create the necessary conditions for schools and community colleges to translate higher funding levels into improved student achievement.

We have identified two major priorities for the LAO roadmap: investing in services to students who are at-risk of low achievement and maintaining the long-term fiscal health of districts. These twin goals emerged from our sense of the major challenges facing school districts in the next five to ten years. We do not suggest, however, that these represent the *only significant* issues facing K-14 education. The critical part of developing a roadmap is for the Legislature to establish *its* priorities.

MAJOR COMPONENTS OF A K-12 ROADMAP

Our suggested roadmap would chart two main courses: (1) investing in child development programs and supplemental funding programs for the major subgroups of K-12 students who perform well below state standards, and (2) helping districts address the long-term financial challenge posed by retiree health insurance costs.

Data Reveal Significant Performance Gaps

A place to begin the planning process is to assess how students currently fare in our schools. The state's testing programs provide critical data on the achievement of students. This data reveal that major subgroups of our student population struggle to work at levels consistent with graduating from high school. In addition, data also show that schools are not adequately preparing students for the challenges of college and employment after high school.

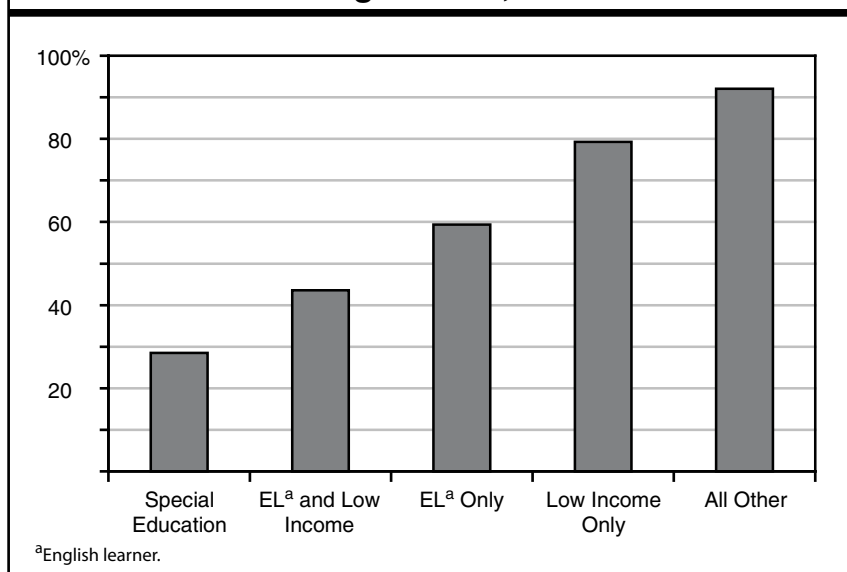
The state's Standardized Testing and Reporting (STAR) testing program provides a perspective on the achievement of students in grades 2 to 11. Figure 3 (see next page) displays the proportion of sixth graders that scored at the basic level or above on STAR in English language arts in 2006. The STAR tests report student scores in five performance levels—advanced, proficient, basic, below basic, and far below basic. While the State Board of Education identified the proficient level as the state's goal for all students, the basic performance level roughly equates to the skills needed to pass the high school exit examination.

As Figure 3 illustrates, the average performance of students in the five groups differs markedly. More than 90 percent of the "All Other" group score at basic or higher on STAR. At the other end of the spectrum, only 28 percent of special education students score at these levels. In between these two groups, 44 percent of students who are identified as "EL and Low-Income" and 59 percent of students in the "EL Only" group score at basic or above. Students in the "Low Income Only" group fare relatively well, with more than 80 percent of students scoring at or above the basic level.

Given the extensive research showing a strong relationship between income and school achievement, however, we are concerned that the current measure of income—eligibility for free or reduced price lunch—may have family income thresholds that are too high to be a good indicator of economic disadvantage. Indeed, the STAR data identify 56 percent of sixth graders as low income.

Figure 3

Percent of Students Scoring Basic and Above, Sixth Grade STAR English Test, 2006



It is also important to recognize the limitations of these data. Most importantly, students are not permanently assigned to the three “risk” groups. When an EL student becomes fluent in English, for instance, that student leaves the EL category. Similarly, special education students who successfully resolve their disability and low income students whose families move up the economic ladder leave their respective category.

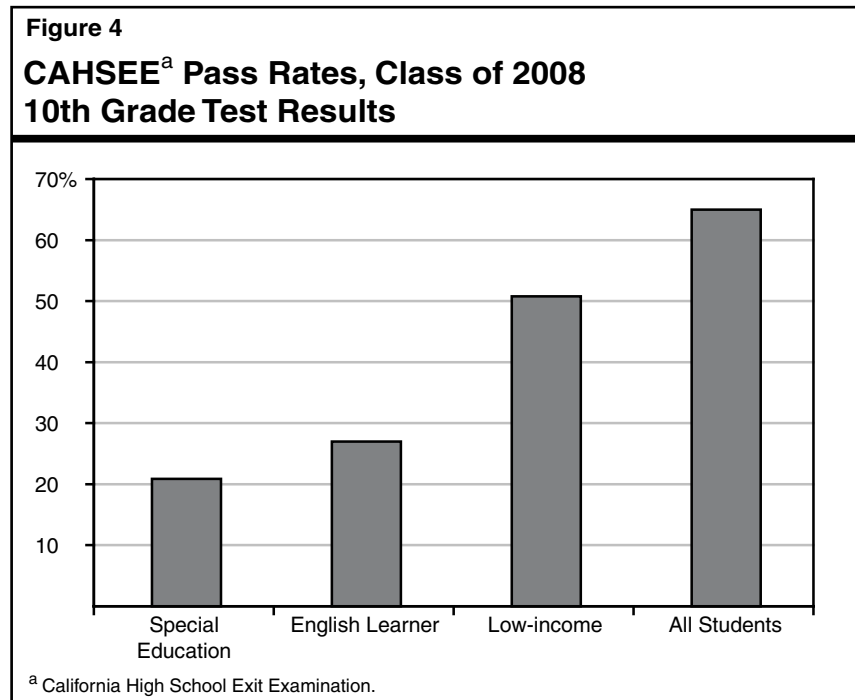
This “group transiency” has a major impact on the accuracy of STAR data over time. Part of the explanation for the low EL and special education scores is that students generally *enter* the categories due to low expected or actual performance and *leave* the category when they begin to achieve at higher levels. Because STAR tracks group scores, not the progress of individual students in the groups, group transiency means that STAR understates the progress of students in these groups. Getting a clearer picture of the progress of these groups will require California to develop measures of achievement growth for individual students.

Address Needs of High School Students

The consequences for students of the achievement trends discussed above become most evident when they reach high school. The same groups

of students that showed low performance in sixth grade continue to lag in high school. Low achievement contributes to the state's high dropout rate. Data suggest that about 30 percent of 9th grade students do not graduate with their class four years later. While the state's data is unable to reveal what types of students are most likely to drop out, research suggests that low-performing students are most at risk.

Low achievement levels also are evident in pass rates on the California High School Exit Examination (CAHSEE). The test, which students must pass to graduate, is designed to ensure students possess the mathematics and language skills needed for success as adults. Figure 4 displays the pass rates for the class of 2008. About 65 percent of the class passed the test as 10th graders last spring. Similar to the STAR data, the passing rates of low-income, EL, and special education students are significantly lower than for other students (unlike the STAR data, students may be included in more than one of these groups).



Performance problems also affect the transition of students to adult life. Specifically, data show that a significant proportion of high school students are unprepared for the challenge of college or the labor market. For instance, national data show that a quarter of high school graduates

remain unemployed six months after graduation. In addition, more than 40 percent of recent high school graduates attending community college need to repeat basic mathematics and English classes. As we discuss in our report *Improving High School: A Strategic Approach* (May 2005), research suggests that the achievement and transition issues are linked. Low-performing students see little advantage to working hard in school, and many choose to drop out. This led us to conclude that upgrading vocational education was a key part of a strategy to give students a greater range of curricular choices that help them connect academics to their post-high school education and employment goals.

Maintain School District Fiscal Health

The second major priority of our roadmap is to secure the long-term fiscal health of school districts. In our *Analysis of the 2006-07 Budget Bill*, we discussed the long-term financial challenge to K-12 districts posed by unfunded retiree health benefits. Because of a new policy adopted by the national Governmental Accounting Standards Board, districts must begin identifying the cost of retiree health care benefits that each district has promised to its current employees and retirees. The accounting requirement will be phased in over a three-year period beginning in 2007-08. Because most districts have not set aside funds to pay for these benefits (as they do with pensions), many districts are expected to report large unfunded liabilities.

About 60 percent of school districts reported providing some amount of health benefits to retirees. Some districts report very large unfunded liabilities. Figure 5 displays selected data from a 2006 survey by the California Department of Education (CDE) on the extent of district liabilities for retiree health benefits. Since only 125 districts reported their liabilities, the cost data is likely to change as more districts conduct their cost studies.

In some cases, the reported liabilities are very large. When translated into per-pupil figures, the largest per-pupil liabilities top \$20,000 per student. Unfunded costs of this magnitude pose a major financial threat. To put this into context, the average district receives about \$8,000 in state and local funds per student each year. Thus, the health benefit liabilities faced by some districts exceed twice their annual revenues. In the long-run, the financial pressure on districts with very large liabilities may become so severe they eventually will seek financial assistance from the state. Some may even require emergency loans because of this problem.

For most districts, however, liabilities are smaller. As the figure displays, districts that provide lifetime health benefits show average costs of more than \$5,500 per student. The average liabilities of districts that end coverage at a specific age—either age 65 (when retirees become eligible

for Medicare) or after age 65—are even lower, at about \$2,000. Even for these districts, the size of the liabilities remain a concern. Districts with liabilities of \$5,000 per student would need to set aside about \$350 per student each year to retire this obligation over a 30-year period. In addition these liabilities are growing because the current “pay as you go” method of budgeting followed by most districts does not cover the long-term costs of benefits for current employees.

Figure 5
Estimated K-12 Retiree Health Benefits
Unfunded Liabilities

(Dollars Per Student Enrollment)

Benefit	Number of Districts	Per-Pupil Liabilities ^a		
		High	Average	Low
Lifetime	76	\$23,734	\$5,583	\$85
Over age 65, not lifetime	116	6,662	1,878	65
Up to age 65	431	27,397	2,302	42

^a These estimates are based on a subset of districts that provide the given benefit.

Information on district liabilities will improve significantly over the next few years as districts comply with the new accounting requirements. We expect, however, that new data will paint a dark fiscal picture for many districts. Because the funding challenge posed by retiree health benefits is so significant, our roadmap allocates funding to address it.

IMPLEMENTING THE ROADMAP'S K-12 PRIORITIES

Our roadmap would invest new discretionary Proposition 98 funds in three program areas: child development programs, existing programs that support supplementary services to low-performing and at-risk students, funding, and “fiscal solvency” block grants.

Our overview of the K-12 system’s most significant issues identified *two* major areas of concern: the achievement of low-income, EL, and special education students and the fiscal threat posed by long-term retiree health benefit liabilities. To address these issues, our plan would direct new discretionary Proposition 98 funds into these areas. In crafting this plan, we have tried to use existing funding streams whenever possible. Our plan also includes complementary policy changes that would improve

existing programs, fix problems with current funding formulas, and help make new funds more productive.

Specifically, we would focus a substantial proportion of the anticipated new funds on child development activities for low-income children under the age of five, existing state programs for special education and EL students, support for high school alternative programs and vocational education, and block grants that would protect districts from the fiscal challenge posed by retiree health benefit liabilities. Below, we briefly describe our approach in these areas.

Early Child Development and Preschool

The LAO roadmap allocates a major portion of new discretionary funds for early childhood development programs and preschool. Research shows that early intervention with disadvantaged and disabled students can improve long-term student outcomes. The long-term returns to quality preschool services—higher achievement and graduation rates, fewer referrals to special education, better adult outcomes—have been documented through long-term evaluations. For California, enrolling all EL children in preschool would appear to offer the additional benefit of getting these students earlier exposure to English. Although past studies of preschool were not focused on EL students, we think it is likely that the benefits of providing preschool also extend to this group of children.

Based on research into the cognitive development of infants, however, preschool is now considered to provide support “relatively late” in the lives of children. Evaluations indicate that supporting parents of infants can have positive long-term impacts on children. As a result, other states are beginning to fund programs that promote improved parenting skills. These programs help parents learn about nutrition, health, constructive parenting and discipline techniques, literacy, and educational options. These programs also often provide referrals to other social services.

Given the strong evidence about the long-term benefits of early childhood development programs, our roadmap would set as a goal providing access to preschool classes for all low-income 3- and 4-year olds. In addition, we would include significant funding for a new infant-parent education program that would be modeled after similar programs in other states.

Accompanying this new funding would be several policy changes designed to enhance the impact of the new services. We would dedicate a modest amount of the new funds, for instance, to promote a closer working relationship between preschool providers and K-12 education. These funds would encourage the K-12 system to help preschool programs improve their educational curriculum, identify toddlers who may have disabilities, and

provide parents and kindergarten teachers with assessments of student readiness for kindergarten.

We also would place a premium on ensuring high quality preschool services. Consistent with our recent report *Developing Safety and Quality Ratings for Child Care* (January 2007), our plan would include funds to establish a child development quality rating system, which would collect and disseminate information on the quality of state-funded child care programs.

Augment Programs Targeting At-Risk Students

Our roadmap also would dedicate a significant amount of new discretionary resources for programs that support supplemental services to low-performing and at-risk students. Specifically, our plan would increase funding levels for four programs: special education, the Economic Impact Aid (EIA) program (which provides extra support based on the number of EL and low income students), alternative high schools, and vocational education programs:

- **Special Education.** Very large disparities in local special education funding rates exist. Our plan would use a portion of the new funds to bring all districts to the current 90th percentile funding level (the state's target for other equalization efforts).
- **EIA.** The Legislature streamlined the EIA formula and boosted funding by more than 60 percent in 2006-07. Despite this advance, California spends only about \$300 in supplemental funding for each disadvantaged student, about one-half of the \$600 per student target established as part of the recent reform.
- **Alternative High Schools.** As we discuss in our recent report *Improving Alternative Education in California* (February 2007), we recommend the state revamp its system for funding alternative schools, such as community and continuation schools, which serve primarily high school students. Improving the quality of this system of schools would address a major source of high school dropouts. Given the challenges many of these students face, we think additional funding would also help districts develop better options.
- **Vocational Education.** Our roadmap would include new funds to reduce significant local funding disparities among Regional Occupational Centers/Programs and to provide additional funding for introductory and high-level vocational classes.

There are other steps that we would suggest the state take to complement these funding increases. First, data need to be improved. We would require the CDE to explore ways to measure the annual growth of students on the STAR tests. As discussed above, group transiency renders STAR a poor measure of annual student growth, particularly for the subgroups of students most at risk of low performance. Thus, the development of good student growth measures would play a critical role in our plan. Additional work also is needed to refine the state's measure of family income. Our current measure—eligibility for the free and reduced price meals program—may be too broad to reveal important underlying relationships between low income and low achievement.

We also see the need to refine the state's accountability programs. As we discussed in our *Improving High Schools* report, the state needs to reconcile its policy of holding *schools* accountable under the federal No Child Left Behind Act for helping all students reach the *proficient* level of achievement while holding *students* accountable for passing the CAHSEE (which is roughly equivalent to scoring at the *basic* level on STAR). In our report on alternative high schools, we also recommend substantially revising the state's Alternative Schools Accountability System. This system fails to effectively hold alternative schools accountable for meeting the needs of students.

Create Fiscal Solvency Block Grants

Our roadmap would include significant new funding for fiscal solvency block grants. Districts with unfunded retiree health benefit liabilities would be required to use block grant funds for two purposes. First, districts would set-aside an amount in each year's budget equal to the "normal" cost of retiree health benefits—the amount that, if set aside each year over each employee's working life, would pay for all projected benefit costs during retirement. By budgeting for the normal cost of these benefits, the Legislature would ensure that district liabilities would grow no further. Second, any funds remaining would be set-aside to reduce the amount of unfunded liabilities that districts already have accrued. Districts that have no retiree health liabilities could use the block grant funds for any K-12 purpose.

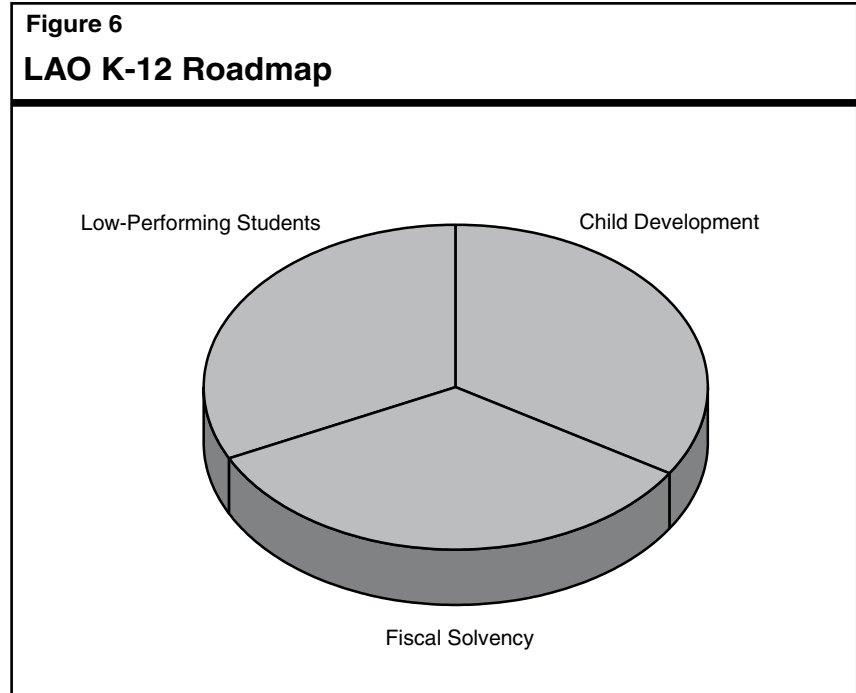
The cost of these block grants will be high. Under our plan, all K-12 districts would receive this new block grant. Although it would be less expensive for the state to target funds only to districts with significant liabilities, we would not suggest this approach. By targeting funding at only problem districts, the state would essentially reward districts whose costs threaten to spiral out of control and penalize districts that have been financially responsible. In general, we think districts should bear responsibility for the consequences of their fiscal decisions. By providing funding to all districts, therefore, districts with significant liabilities would

be “penalized” by the requirement to spend the new funds only for those costs. Districts without these liabilities, on the other hand, would be free to spend the funds on program improvements.

If the state were to provide block grants to all districts, even large grants would translate into relatively small district amounts. For instance, for every \$1 billion distributed through the block grants, the state would provide about \$175 per student to districts. This amount would fall far short of covering costs in districts with the largest liabilities. Even in districts with moderate liabilities, it might also be insufficient to pay for the unfunded past-year costs and the ongoing normal cost of these services. As a consequence, the roadmap would target a significant percentage of the new discretionary funds for the retiree health issue.

How the LAO Plan Adds Up

Figure 6 illustrates how our plan would allocate the cumulative \$5.9 billion in discretionary funds the we project over the next five years for K-12 education. In rough magnitudes, our roadmap would dedicate: \$2 billion of the new funds for child development programs, \$1.9 billion to for programs for various at-risk students, and \$2 billion for the fiscal block grants.



MAJOR COMPONENTS OF A CCC ROADMAP

Our suggested roadmap would provide new discretionary resources for two new block grants: (1) fiscal solvency grants to help districts address the long-term challenge posed by retiree health insurance costs; and (2) student success grants to help improve student performance.

We base our recommendations for a California Community College (CCC) roadmap on three connected issues: (1) recent improvements in community college funding, (2) a projected slowing of enrollment growth, and (3) continuing performance challenges in the form of low student success rates.

Major Recent Improvements in Community College Funding

In recent years, the Legislature has made major improvements in community college funding. For example, for many years the Legislature has sought to raise the per-student funding rates of many districts in order to “equalize” funding near the level of the highest-funded districts. After adding about \$300 million in base funding for this purpose over the past three years, the Legislature’s equalization goal has been achieved. In addition, Chapter 631, Statutes of 2006 (SB 361, Scott), revised CCC’s apportionment allocation formulas to help ensure that district funding rates remain equalized in the future. Moreover, most of the budget reductions enacted during the budget crisis several years ago (including reductions to matriculation, scheduled maintenance, economic development programs, and base apportionments) have been restored.

Major new investments also have been made in Career Technical Education (CTE) programs, with additional funding totaling more than \$400 million planned over the next seven years. (Please see our discussion of these CTE programs in the “Crosscutting Issues” section of this chapter.) Major new augmentations were also recently provided for financial aid services and outreach, with the result that student participation in the Board of Governors waiver program is at an all-time high. Starting in the current year, a new, enhanced funding rate is being provided to high-priority noncredit programs. (Examples include English as a second language and short-term vocational programs.) This new rate is about \$500 per student higher than the old noncredit rate and is intended to provide additional resources to districts that offer precollegiate and job-skills courses.

Reversing earlier trends, the Legislature has also addressed long-standing concerns regarding enrollment funding. Specifically, no community college district currently has enrolled more students than it is funded to serve. (During a time of rapid enrollment increase in the late 1990s, some districts experienced enrollment increases that exceeded their

budget expectations.) In fact, for the past several years, enrollment growth funding has exceeded actual enrollment growth. Some of this unused enrollment growth funding has been redirected by the Legislature to other CCC priorities, including enhancing basic skills programs and creating a new remediation program for students who fail to pass the high school exit examination.

Moreover, student fees are at their lowest point in several years, with the per-unit rate having dropped by 23 percent in January 2007. Reductions in student fee revenue were backfilled with state funds to ensure that program funding levels were not affected. We also note that under the Governor's budget proposal, the community colleges' share of Proposition 98 resources would actually exceed the statutory "split" of 10.93 percent for the first time since 1990.

Some Funding Needs Still Have Not Been Addressed. To some extent, the recent improvements in community college funding were made possible by delaying payment for some other costs. For example, \$200 million in 2003-04 apportionment funding was effectively "borrowed" from future years by continually delaying payment of this amount into the next fiscal year. Paying off this "deferral" would require a one-time cost of \$200 million. Similarly, about \$100 million in past mandates obligations is owed to community college districts. Some scheduled facility maintenance work also has been delayed as funding was moved to other priorities. And, as with K-12 school districts, community college districts have a substantial unfunded liability for future retiree health care costs. Overall, however, there have been significant funding improvements.

Projected Slowing of CCC Enrollment

As discussed in more detail in the "California Community Colleges" section of this chapter, the size of the traditional college-age population has been growing modestly (between 1 percent and 2 percent) over the past several years. We project this rate will peak at about 2.5 percent in two years, after which it will slow rapidly. We project that by 2013, this population will actually start to shrink.

Assuming constant participation rates, the leveling off of the underlying adult population means that community college enrollment will likewise slow. While some individual districts may continue to experience high growth, the amount of new funding required to accommodate enrollment growth statewide will likely decline from the levels required several years ago.

Community College Performance Challenges

A number of recent studies have highlighted several critical performance challenges facing community colleges. Of particular concern is the large percentage of CCC students who fail to either earn a degree or certificate or transfer to a four-year institution. For example, a recent study by the Institute for Higher Education Leadership and Policy found that about 60 percent of the students entering community colleges seek to earn a certificate or a two- or four-year degree. Of those students, only about one-quarter succeed in their goals within six years. Similarly, the Public Policy Institute of California recently reported that the production of associate's degrees per 100 full-time equivalent (FTE) students at California's two-year colleges is only about three-quarters the rate of the rest of the country. Other reports have made similar findings.

The causes of low rates of student completion are varied and difficult to isolate. However, two points stand out. First, existing funding mechanisms create stronger incentives to increase enrollment than to increase student completion. This is because the allocation of apportionment funding to CCC districts is based almost exclusively on enrollment (as measured in FTE students), with little linkage to student outcomes. For example, community colleges receive apportionment funding based on students being in attendance early on in the semester. The colleges' funding has nothing to do with students completing courses or being successful in them.

Second, various restrictions impinge on districts' ability to allocate resources in a way that best meets their needs. For example, a substantial portion of CCC funding is restricted for certain "categorical" purposes such as providing part-time faculty office hours, funding telecommunications services, or promoting regional economic development. In addition, state law imposes other restrictions on certain aspects of district resource allocation, such as a requirement that at least 50 percent of funding support direct instructional costs.

We believe that districts should be able to allocate financial resources in a way that best serves their students, but categorical and statutory funding restrictions, coupled with fiscal incentives to simply increase enrollment, can often work against those preferred allocation choices.

Investing New Resources to Meet CCC's Challenges

The recent new budgetary investments in the community college system, coupled with the slowing of demographically driven enrollment demand, limits the amount of new resources that will be needed for normal workload increases over the planning period of our roadmap. This creates an opportunity to direct new Proposition 98 funding to paying

off outstanding liabilities (such as retiree health benefits) and making improvements in student completion and graduation rates.

Specifically, we recommend that the Legislature consider directing roughly one-half of each year's new, discretionary Proposition 98 funding for CCC outstanding liabilities, including paying off the \$200 million deferral, reimbursing local districts for past mandates claims, and helping districts to fund their retiree health benefits liability. The latter liability could be addressed similarly to what we propose for K-12 districts—a fiscal solvency block grant.

We recommend the Legislature use the other half of new, discretionary Proposition 98 funding to improve student performance. In the "California Community Colleges" section of this chapter, we recommend redirecting a small amount of base funding in the budget year for a pilot block grant program to help targeted districts invest in programs that improve student success. In future years, the Legislature could expand this pilot and provide more grant funding to districts that is linked to improvements in student performance. Also, as noted above, we think part of the low student success rates is due to restrictions and disincentives inherent in the way community colleges are funded. Therefore, we recommend that these grants be coupled with relaxing some of these existing restrictions.

How the LAO Plan for the CCC System Adds Up

Our plan would allocate approximately \$750 million in discretionary funds for CCC education that are available by the end of our five-year fiscal forecast. Our roadmap would dedicate one-half—\$375 million—for "student success" block grants and a similar amount for fiscal solvency block grants. We also suggest that the Legislature set aside funds in the early part of the period to pay off the one-time costs of the deferral and prior-year mandate claims.

CONCLUSION

This discussion of a K-14 roadmap illuminates the benefits of a long-term legislative plan for the use of Proposition 98 funds that may be available over the next several years. Whether the substantial new discretionary funds actually become available depends primarily on the health of the economy. Even if the flow of new funds is modest, however, we think a roadmap has a number of important benefits. Most importantly, it helps the Legislature identify the problems of the K-14 system and how best to use available new funding—whenever it becomes available—to address those problems.

It is important to remember that these discretionary funds would accumulate over the five years, and that the total \$6.6 billion would be realized at the end of this period. Much smaller amounts would be available in the near term. Under our revenue forecast, for instance, only about \$500 million in discretionary funds would be available in 2008-09 for K-14 programs. Under our suggested priorities, for example, the Legislature could use a portion of these funds in that year to pay for child care facilities that would be needed to accommodate the proposed expansion of preschool programs. This would pave the way for the ramp up of preschool programs that would occur as the larger sums of discretionary funds became available in later years. Similarly, allocations for low-performing students and fiscal solvency grants would increase over the five years as the new discretionary funds became available. As a result of the roadmap approach the Legislature could ensure that its priorities for new spending were accomplished over the period.

The roadmap also illustrates that, with a long-term perspective, the Legislature can make major investments in school district and community colleges. Because our five-year projection results in so much new discretionary money, our roadmap results in funding allocations on a grand scale. Even smaller amounts, however, accumulate into large sums over time. Later in this chapter, for instance, we review the Governor's proposal on career technical education improvement grants. Our recommendations are based on a long-term perspective—that the program will receive \$400 million over the next seven years—rather than the typical short-term budget perspective. Taking a long-term perspective changes the perception of what the program can accomplish.

The process of developing a roadmap also is an important issue. Because the process includes program and funding issues, it would be important to have the budget subcommittees working jointly with the policy committees in each house on the development of a roadmap. The committees also would want to seek input from a variety of sources—including the foundation researchers who are involved in the new studies on adequacy and efficiency. While the task of developing a roadmap represents considerable work, we would hope that the Legislature would see it as an opportunity to take stock of the performance of the K-14 system and chart a long-term course for its improvement.

CAREER TECHNICAL EDUCATION

The Governor's budget proposes \$52 million for grants to strengthen secondary and post-secondary vocational education programs.

The 2007-08 proposed community college budget includes \$52 million for the career technical education (CTE) improvement grant program created by Chapter 352, Statutes of 2005 (SB 70, Scott). The program was funded at a \$20 million annual level during the first two years of operation (2005-06 and 2006-07). Chapter 751, Statutes of 2006 (SB 1133, Torlakson), includes additional funding for the SB 70 program as part of the recent *CTA v Schwarzenegger* lawsuit. Specifically, Chapter 751 appropriates \$32 million in 2007-08 and \$38 million annually from 2008-09 through 2013-14 for the CTE improvement program. Thus, Chapter 751 funds increase the amount available for the program to \$52 million in 2007-08 and \$58 million annually for the next six years.

Senate Bill 70 establishes a program to “improve linkages and career-technical education pathways between high schools and community colleges.” These “pathways” are designed to help high school students develop vocational skills needed by employers in the area while also preparing students for more-advanced academic or vocational coursework in a community college or university.

Partnership academies represent one type of pathway in which academic and vocational subjects are integrated into a unified curriculum that focuses on an industry or occupational area. Academies usually operate as a “school-within-a-school,” and students in grades 10 through 12 take all or most of their core courses in the academy. “Tech-prep” sequences are a second type of pathway that help high school students reach advanced community college courses. The distinctive characteristic of tech-prep is that the pathways span the K-12/community college divide by coordinating regular academic and vocational classes beginning in high school and continuing on to community college.

To improve CTE, SB 70 authorizes several types of activities:

- Creating new or aligning existing high school and community college technical preparation programs and curriculum.
- Expanding or promoting community college training programs.
- Testing new program models.
- Improving career-related middle school or high school programs, such as career exploration programs.

The Chancellor's Office of the California Community Colleges and the California Department of Education (CDE) jointly administer the act. Funds are allocated through a competitive grant process in which all community colleges are invited to apply. Local projects are jointly developed by community colleges and K-12 entities (high schools and Regional Occupational Centers or Programs [ROC/Ps]). Most local projects also are required to involve local business. Grants typically provide short-term improvement funding to develop or strengthen CTE programs, rather than ongoing operational support.

FIRST-YEAR GRANTS—2005-06

In the program's first year, \$15.3 million of the \$20 million annual appropriation was targeted at creating new or improving existing CTE programs (\$13.8 million) or developing middle school career exploration and counseling programs (\$1.5 million). To better understand the SB 70 program, we reviewed most of approved grants for these two activities.

The approved grants illustrate the promise of the SB 70 program. Several of the grants build on strong existing relationships among businesses and educators to develop regional approaches to improving vocational education programs. Other grants propose to coordinate the California Community College (CCC) and K-12 programs so closely that students can earn college credits for high-level CTE courses taken in high school.

Coordination Problems at All Levels

Most of the first-year grants attempt to address a similar problem—a lack of coordination between the many local interests involved in CTE. Like other parts of the education system, CTE and related courses need to be coordinated in order to work most effectively. Traditionally, introductory vocational courses and career exploration began in middle school. In high school, more advanced courses build on the middle school preparation. The ROC/P courses provide the “capstone” secondary training as a gateway to employment or continued study at the community college. The first-year

SB 70 grants show that coordination is a problem at all levels—middle school, high school, community college, and California State University (CSU). In fact, we think coordination—or the lack of it—lies at the root of many of the current problems in CTE.

Middle School Foundation Skills. Middle school provides the foundation for many CTE programs. One part of this foundation is a program of career exploration and counseling that helps students think about careers and the options available to them in high school and college. The second component to the foundation is pre-requisite academic or vocational skills that are needed for high school CTE programs.

District applications for SB 70 funds often acknowledged that one or both of these foundational elements is missing in their middle schools. For instance, several of the applications noted the absence of any counseling program for their middle school students. One large urban district provided college counseling, but not career counseling. Several applications also noted the lack of vocational or academic preparation needed to participate in high-level high school CTE programs. For instance, a biotech pathway project noted that science programs in middle school were inadequate to prepare students for the program. Another project cited the need for introductory middle school vocational classes that would help students “understand and experience the personal connection between what is taught in the classroom and its relation to the real world.”

Coordination Between K-12, CCC, and CSU. A number of projects cited a lack of coordination between K-12 and CCC vocational programs. Interestingly, sometimes the high school and ROC/P had an exemplary program for which no complementary CCC program existed to help take students to higher skill levels. In other cases, the community college operated a high-level program that lacked a quality secondary “feeder” program from the high school and ROC/P.

Grant applications suggest a similar lack of coordination can occur among community colleges and CSU campuses. At least two proposals included a CSU campus as part of the grant participants—but the CSU was located 100 miles from the high schools and community college that were leading the project. In each case, another CSU campus was located nearer the high school and community college but did not participate in the project. Clearly, involving the local CSU campus would seem a better arrangement for students.

Education-Business Coordination. Failure to fulfill the manpower needs of business represents another coordination problem, one between education agencies and the local employer communities. In several grants, the local Workforce Investment Board (WIB) played a major role in assessing the needs of local employers and convening the business and

education communities to address those needs. Local WIBs administer job training programs under the federal Workforce Investment Act. Since both community colleges and ROC/Ps are required to maintain employer advisory boards, the role played by the local WIB suggests these boards are not always effective in communicating the needs and interests of a broad range of employers in the region.

PROGRAM NEEDS A LONG-TERM FOUNDATION

The Chancellor's Office and the California Department of Education have not identified the long-term goals of the program. In addition, the competitive grant approach incorrectly assumes that the state can "fine tune" the program on a statewide basis. These problems raise significant questions about the two agencies' approach to implementing SB 70 and the budget-year plan.

In our view, the problems identified in the first-year grant applications—communication and coordination—define the core objective of SB 70: building the local relationships that are needed to connect all levels of education in a way that meet the needs of students and business. Clearly, the grant funds also pay for other inputs to the improvement process, such as curriculum development, equipment, and other materials. A review of the proposals, however, shows that SB 70 grants mostly pay for people's time—primarily K-12 teachers, CCC faculty, and local administrators of both education agencies—to sit down and work together to create programs that are more responsive to industry needs and student interests.

The question facing the Legislature in its review of the 2007-08 budget, therefore, is whether the proposed SB 70 spending plan allocates funds in a way that maximizes the opportunities for this local coordination process to unfold. Figure 1 displays how the SB 70 appropriations were spent in 2005-06 and 2006-07 and the proposed uses of funds in the budget year. In 2005-06, funds were concentrated in four areas—strengthening or creating local career technical pathways, developing middle-school exploration course curricula, supporting region-wide course articulation, and funding teacher/faculty in-service activities. In 2006-07, the emphasis on local pathways was reduced and new grants were available for other types of "system development" activities, such as establishing a vocational education teacher "pipeline," articulation between community colleges and four-year universities, and linking CCC economic development programs to CTE programs.

Figure 1			
Career Technical Education Grant Program			
<i>2005-06 Through 2007-08 (In Millions)</i>			
Program	2005-06	2006-07	Proposed 2007-08
Local improvement grants	—	—	\$20.0
New or existing pathways	\$13.8	\$5.0	1.0
“Career advancement” academy	—	—	5.0
Expand partnership academy program	—	—	4.0
Teacher preparation pipeline	—	4.1	2.0
High technology pathways	—	—	4.0
Middle school exploration	1.5	2.7	1.5
Health careers pathways	—	2.5	—
Articulation with universities	—	2.0	—
Preapprenticeship programs	—	2.0	—
Entrepreneur centers	—	—	2.0
Student organizations	—	—	2.0
CCC economic development	—	—	1.5
Regional articulation	4.0	—	1.5
K-12/CCC summer internships	—	—	1.5
K-12/CCC inservice	0.7	1.4	1.4
New teacher workshop	—	—	1.2
On-line curriculum resources	—	—	1.0
Other (six programs)	—	—	2.0
Evaluation/other research	—	0.3	0.5
Totals	\$20.0	\$20.0	\$52.0

In 2007-08, the budget proposes a wide variety of new programs. Most significantly, the budget would distribute on a formula basis \$20 million for local improvement grants. According to the Chancellor’s office, funds would be distributed to each of the 72 community college districts. Funds would be available for a wide variety of local activities, including aligning curriculum with the state’s CTE standards, planning and implementing new partnership academies, and sequencing secondary and post-secondary vocational education courses.

The budget also proposes a significant number of new grant programs. The budget would establish 16 new programs. All told, the proposal would fund 239 separate contracts, according to the Chancellor's Office. In 2005-06, only 69 contracts were proposed under SB 70. Thus, the large budget-year increase in funding appears to be generating an even larger increase in the number of contracts that are proposed.

We were unable to review the budget-year plan in any depth as we were able to obtain very limited information on these new programs. A cursory examination of the proposals, however, suggests several issues. Most striking is the significant overlap among the programs. The \$20 million local improvement grant, for example, could be used to increase the number of local partnership academies. The budget plan also proposes to spend \$4 million on a *separate* grant program to expand the number of the academies. No rationale is provided on the need for the separate program. We identified several other instances of overlap among elements of the plan. The Department of Finance advises that additional detail will be available before the beginning of budget hearings.

Program Needs to Define Long-Term Goals

From a broader perspective, however, we think the administration's approach reflects two major problems. First, the agencies have not identified specific long-term goals for the program. Without such goals, there is no framework for determining annual spending priorities or for evaluating the impact of chosen strategies. Instead, the budget presents a long list of programs that are based on unclear goals and priorities and no expectation of what statewide outcomes the programs will produce. While we understand the logic and relevance of most of the proposed uses of funds, we do not see how these pieces fit into a broader plan for the revitalization of the state's CTE programs.

Most significantly, the agencies have not described what a "good" CTE program looks like at the local level. This would help define the long-term objectives of SB 70. How many pathways should be available to high school students? What are the state's goals for the pathways—higher wages for those students who work, greater numbers enrolling in community college CTE programs, more students enrolling in four-year programs? Without this long-term foundation, it is difficult to evaluate the rationale for the various programs proposed in the budget. Perhaps more critically, without an idea of where the program should be headed, it is unlikely to reach that goal.

Competitive Grants Pose Problems

The second problem with the current approach is the heavy use of competitive grants to support the local improvement process. The competitive grant process implicitly assumes that the Chancellor's Office and CDE have enough information and insight to fine tune the improvement process from Sacramento. The budget plan for 2007-08, with its many small grant programs, seems to suggest the two agencies know exactly what types of improvements are needed around the state. Because the agencies are working without a clear statement of goals, however, it is unclear whether the list of proposed programs represents a reasonable implementation plan.

Using competitive grants to promote statewide reform of CTE also suggests that deep involvement of the state agencies is necessary for the local improvement process to succeed. We suggest the contrary—that improving CTE is mostly a local process that needs strong local commitment to succeed. As discussed above, improving CTE involves coordinating education, business, and labor to ensure all elements needed for successful programs are in place. From this perspective, therefore, competitive grants represent the wrong approach to building these local relationships. Below, we discuss some of the problems that result from the heavy reliance on competitive grants.

Limited Scope of the Projects. Revitalizing CTE through the development of pathways will require a major effort by employers and educators to develop and implement new vocational options. A significant number of the approved projects, however, propose programs that will involve only a few students in specialized occupational areas. These projects typically involve one or two high schools, one community college, and one or two employers. If there were already a robust system of vocational options in all parts of the state, adding these small pathways would make sense as a way to meet the particular needs of local employers and further expand student choices. Given the desire to make high quality vocational options available to most high school students, however, we think the state would be better served by focusing SB 70 funding on larger regional projects that would expand CTE options for a greater number of students.

Similarly, the grants also frequently limit the scope of participating groups. Despite the fact that each grant has a community college and K-12 sponsor, many grants do not include major local K-12 entities that are crucial to the success of the project. Many grants, for instance, do not include either high schools or ROC/Ps as direct participants. Many grants also exclude middle schools as participants. Given the importance of each level of education in creating successful CTE programs, we think

the state should encourage local improvement projects to include all of these entities.

Competitive Grants Help Only the Winners. Competitive grants are useful in creating competition that helps the state obtain the highest value for its dollar. For SB 70, however, we don't see the value of pitting parts of the state against another. Improving CTE is a statewide goal—all parts of the state should participate. In addition, competitive grants tend to favor areas that can afford talented grant writers who develop high-scoring projects. As a consequence, the competitive grant process may make it difficult for some regions to win grants to improve local programs.

Similarly, friction between local community colleges and K-12 entities may make agreement on joint projects difficult to reach. While the competitive grant approach may, in some cases, create sufficient financial incentives for these agencies to work together, it also allows areas of the state to opt out of the improvement process. It is our view that SB 70 should be a tool to help reduce friction between these agencies. The program should provide the business community, parents, and other local officials and community members with leverage to get the educational agencies to work cooperatively to meet the needs of students. The competitive grant process doesn't provide much standing for these other groups to generate the local pressure needed to break through such obstacles. Thus, we think the Legislature should consider a different approach to strengthening local CTE programs.

Addressing Special Needs of Rural Areas. Issues faced by rural areas illustrate another problem with using a competitive grant process for the local improvement process. Only 5 of the 35 approved projects for expanding or improving existing pathways were located in rural parts of the state. We think there are several possible reasons for this. First, some areas of the state have no local community college within a reasonable distance. Since proposals could be submitted only by community colleges, the process made it difficult for some rural areas to apply.

Second, while the emphasis on connections with employers is a critical factor in successful CTE programs, rural areas often have few major employers to work with. In these cases, it is hard to see how rural areas can compete for grants with parts of the state where large employers are located.

The lack of community colleges and major employers illustrate the types of problems facing rural areas as they attempt to upgrade local CTE programs. As a result, a traditional pathway approach may not work in many rural communities. Rather than create a grant program specifically for rural areas, however, we think it makes more sense to encourage each area to develop local solutions to upgrading local CTE programs. These

solutions may require some “out of the box” thinking. Are there innovative solutions that allow high schools and ROC/Ps to work with community colleges that are 100 miles away? Should the state authorize ROC/Ps to provide community college courses in areas that would otherwise be underserved? We think SB 70 should work under the assumption that improving CTE programs in different parts of the state may require different solutions than are offered in the existing grant programs.

Is Coordination a One-Time Activity? Although SB 70 grants provide one-time funding, a number of projects use the grants for ongoing operational costs. One grant, for example, used funds to support a summer program for middle and high school students. The project acknowledged that this component was not sustainable without new funds. In our view, this did not seem to represent a prudent use of SB 70 funds.

Sustainability is an important issue, but in another sense. The “one-time” costs of virtually all the SB 70 projects are not really one-time activities. Instead, coordination is needed on an ongoing basis to update programs as business practices change, modernize equipment, align courses, and train teachers and faculty. Viewing them as one-time activities suggests that the updating done by SB 70 will erode in effectiveness over time—leaving future CTE programs with the same problems SB 70 is addressing. If the core of SB 70 is building relationships, maintaining these relationships as people and programs change over time represents part of the ongoing process of maintaining CTE programs.

\$400 MILLION IS ENOUGH TO UPGRADE CTE STATEWIDE

We recommend the Legislature enact legislation directing most of the \$52 million proposed for SB 70 to pay for the first year of a seven-year grant program that would support a comprehensive program of improvement at the county or regional level.

Achieving the long-term goals of SB 70 requires a broader, long-term strategy based on the needs of each region in the state. The strategy should provide a clear statement of the goals and objectives of the program. It also should move away from a reliance on competitive grants to fund the local improvement process and, instead, establish a local process that focuses on building the needed relationships on a regional level.

As discussed above, the Governor’s budget would provide \$20 million for noncompetitive local improvement grants. The proposal, however, does not specify clear priorities for the use of these funds, which local entities should participate in planning, or how the state would evaluate local uses of funding. The funds also would be distributed to each community college

district, which would shape the development of CTE around the 72 districts rather than the needs of the regions. Thus, while the proposal heads in the right direction, it needs a solid foundation to work most effectively.

There is another reason to think strategically about the long-term goals of SB 70—over the next seven years, the state will spend \$400 million on the program. During the first two years of operation, the program was funded at \$20 million each year. Under the Governor's budget, funds from the CTA settlement would increase CTE funding to \$52 million. This amount would then increase to \$58 million annually in 2008-09 through 2013-14. Absent other legislative action, annual funding for the program would return to \$20 million beginning in 2014-15.

Thinking of SB 70 as a \$400 million program, however, changes one's perspective on what the program could accomplish. It is a lot of money. In addition, because the settlement funds are appropriated for a limited number of years, the program's funding structure encourages a defined multiyear approach to the improvement process. To state it another way, the limited-term settlement funding raises the question: "What should CTE look like at the end of the seven years?"

Indeed, we think \$400 million provides sufficient funding to support a substantial statewide improvement process for CTE. This change in perspective would also allow the state to adopt a different approach to the local improvement process. Specifically, rather than provide a variety of grant programs for isolated components of CTE programs, the state could focus on laying the foundations for all the essential components throughout each county or region. By determining regional grants on a formula basis (such as the number of high school students), the state would ensure funding for all parts of the state. Finally, the \$20 million base appropriation could provide permanent support for the regional partnerships after the end of the seven-year program.

By providing grants to each county or region of the state, the Legislature would invite all levels of education and the business and labor communities to begin the process of coordination and communication that strong CTE programs require. In general, we think counties represent a reasonable proxy for a regional approach because it provides a scale that is sufficiently large to capture regional labor markets but also small enough to allow the development of close working relationships that are needed in CTE. Clearly, however, there will be situations that call for establishing CTE regions within counties or for multicounty regions.

A regional approach also could bring all the education agencies and a broad array of business interests to the improvement process. In some areas, these parties may have good working relationships that permit a collaborative approach to improving CTE. In other areas, relationships

may need to be built or rebuilt, which will take time. In some areas, local interests—or even the state—may need to intervene to help build these relationships. Although a regional approach cannot guarantee success, it can create positive pressure that can lead to better working relationships.

The regional partnerships also would alter the state's role in SB 70. Rather than developing and administering a wide variety of grant programs, the state's primary role would be to monitor the progress of the regional collaboratives—providing technical assistance, sharing best practices, holding the local agencies accountable for making progress, and providing feedback to the Legislature on changes that are needed for SB 70 or other state programs. We do think that a relatively small amount of grant funds for state-level activities makes sense. This would provide the two state agencies with resources to conduct activities that provide statewide benefits, such as curriculum development.

Establish Regional CTE Improvement Grants

For these reasons, we recommend the Legislature enact legislation to create within the SB 70 program a seven-year program of county or regional grants that would address all aspects of the improvement process. Grants would be determined on a formula basis, so that all parts of the state would participate in the program. The regional partnerships would be guided by a plan that would be developed during 2007-08 that assessed the current status of career tech and described the region's approach to improving CTE.

The plans would constitute a regional "master plan" for the improvement of career technical education. The K-12 entities, community colleges, and four-year universities in the region would participate in the development of the plan. To ensure the broad participation of business interests, we recommend including the local WIB in the collaborative. We also suggest inviting the participation of labor organizations so that apprenticeship and pre-apprenticeship programs are included in the coordination process.

Our proposed legislation also would identify the program elements that would be included in the local plans, such as:

- ***Middle School Foundation.*** Plans would include a middle school component so that students get the counseling and other prerequisite courses needed for success in high school and college.
- ***High School-Community College Coordination.*** Each region's plan would create a sufficient number of CTE options to allow each high school to offer at least two vocational choices. These options could be pathways, tech-prep sequences, or other options that help students develop both academically and vocationally.

The plan also would describe how the region plans to sequence high school, ROC/P, and community college CTE courses. Once the basic structure of pathways and sequencing is in place, regions also would be free to develop more specialized sequences based on needs of employers and student interest.

- **Coordination Among CCC and Four-Year Universities.** The pathways and sequences would be incomplete if they did not extend into the public four-year universities. In our view, involving the CSU campuses is critical because it accepts many more CCC transfer students than the University of California.
- **Other Uses of Funds.** The grant money would support the different coordination activities discussed above. In addition, however, grant funds could be spent on a wide variety of other goods and services, such as materials and equipment, in-service training, summer internships for both teachers and students, and research or evaluation.

Our proposal would distribute funds based on the number of high school students in the region. Figure 2 illustrates the amounts that our proposal would provide to selected counties if these counties were established as regions. As the figure shows, even the grants to smaller counties

Figure 2		
LAO Proposed Regional CTE^a Grants		
Selected County Allocations		
<i>(In Millions)</i>		
	2007-08	Seven-Year Total
Alameda	\$1.6	\$12.4
Butte	0.3	2.1
Contra Costa	1.3	9.8
Los Angeles	12.6	97.6
Mendocino	0.1	0.9
Orange	3.8	29.8
Sacramento	1.8	13.8
San Diego	3.7	29.0
Santa Clara	1.8	14.3
Santa Cruz	0.3	2.3

^a Career Technical Education.

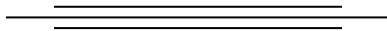
accumulate to large sums over the seven-year time frame. The figure also shows that our formula distributes only \$47 million of the \$52 million in funds that are proposed in the budget year. Our proposal would set aside the other \$5 million for state-level grants.

Finally, we also recommend the Legislature include in legislation performance measures for the regional partnerships that indicate the impact of the improvement process on students. Indicators could include the number of high school students (1) enrolled in a high school career pathway or other sequence of CTE courses and (2) who successfully complete a pathway or other sequence of CTE courses. We would also suggest that legislation require partnerships to collect data on the number of high school graduates who participated in a pathway or sequence (1) who attend college or a university with the goal of getting a four-year degree and (2) who enroll in community college with the goal of getting a vocational degree. Finally, data on wages earned by students who worked after high school also would be useful outcome data on the value of the pathways.

CONCLUSION

Our proposal for regional grants is similar to the Governor's proposal to use \$20 million for new or expanded pathways. The budget proposal would allocate the \$20 million on a formula basis to all community college districts, and would be used for a wide variety of local CTE activities, such as developing model projects, aligning curriculum with the state's CTE standards, planning and implementing new partnership academies, and developing advisory councils to link education with labor, business, and industry.

The budget proposal, however, provides little direction about the larger purpose of these grants or what the state expects the grants to produce. Instead, it provides a menu of possibilities. In a sense, this is our concern with the overall SB 70 proposal for 2007-08—the budget contains many solutions to a problem that is not clearly defined. We think the problems are primarily at the local level. As a result, our proposal would focus most of the funds at the regional level accompanied by a clear statement of what the state hoped to accomplish through the program and a set of performance measures. We think this system of local grants supplemented with supportive state agencies provides the Legislature with the best opportunity to make a permanent improvement to CTE throughout the state.



CALIFORNIA EDUCATION NETWORK

The California Education Network (CEN) provides advanced networking services to California's public education institutions. A 2005 audit found that the network was technically sound but lacked important contractual and accountability measures. Actions taken in recent years have improved transparency, particularly of the K-12 portion of CEN (known as the High Speed Network, or HSN). Given these improvements, we recommend the Legislature provide \$12.6 million (Proposition 98) to continue HSN. However, we recommend the Legislature enact legislation that would extend the accountability measures to the higher education segments.

Background

The CEN is comprised of two components: the California Research and Education Network (CalREN) and the K-12 HSN. The CalREN is a statewide high-speed, high-bandwidth network that connects the majority of higher education institutes in California to each other, the Internet, the federal Internet2, and other research entities around the country. The HSN is a network of node sites in all 58 counties through which the majority of California's public K-12 education entities connect to each other. The HSN also connects to CalREN, thereby allowing K-12 entities to connect to higher education institutes, the Internet, Internet2, and other research organizations. For students, faculty, and staff, these networks provide services ranging from basic Internet connectivity to the advanced high-speed networking needed for certain research activities.

Below, we: (1) provide additional background on CalREN and HSN, (2) discuss the 2007-08 budget proposal for HSN, (3) explain actions taken in recent years to increase the transparency of CalREN and HSN, and (4) provide recommendations for further increasing transparency and strengthening accountability.

All Public Education Systems in California Now Participate in CalREN. In 1997, a consortium of higher education and research institutions, led by the University of California (UC), combined their network-

ing resources (funding, equipment, and expertise) to form the nonprofit Corporation for Education Network Initiatives in California (CENIC). This corporation operates CalREN on behalf of its member institutions. It is governed by a board composed of member representatives, with input from a technical advisory committee and a business advisory committee. Over time, the number of educational institutes belonging to CENIC has grown and today the UC, California State University (CSU), California Community College (CCC), and K-12 systems are all members (as are eight private and out-of-state education institutions). The CalREN currently supports over 7.5 million students, faculty, and staff across California's public education system.

CalREN Supports Research and Collaboration. While the majority of students and faculty primarily use CalREN to access Internet services, CalREN also provides advanced high-speed networking capabilities needed for many higher education research opportunities. CalREN's relationships with other networks, such as Internet2 (the national advanced services network for higher education and research institutes), allow researchers to collaborate nationally and globally. For these services, each member pays an annual fee to CENIC. For 2007-08, the annual fee for CalREN services, as established by its member board, is approximately \$4 million per member. Many members receive additional services from CENIC, such as consulting and equipment leasing.

The HSN Supports K-12 Students and Teachers in Various Academic Endeavors. In 2000-01, the state created HSN (originally named the Digital California Project) to provide network connectivity and Internet services to support California's K-12 public schools. The administration decided that one viable option to bring connectivity to K-12 entities was to expand upon the statewide high-speed network that already linked the majority of California's higher education institutes. Thus, HSN was created as an extension of CalREN, funding was appropriated to UC, and CENIC was responsible for managing the network. Today, over 7,000 school sites are able to connect to HSN and use the Internet, videoconferencing, and distance learning tools. They also have access to learning management systems and curriculum planning tools that are hosted centrally by the network. The HSN, and in turn the fees HSN pays to CalREN on behalf of the K-12 system, is funded with Proposition 98 monies.

Fund Baseline Budget and Technology Refresh

We recommend the Legislature provide \$12.6 million (\$10 million ongoing Proposition 98 and \$2.6 million one-time Proposition 98) for the High Speed Network (HSN) in 2007-08. This level of funding would support a baseline budget plus implementation of phase one of a HSN technology refresh plan.

The Governor's budget proposes \$10 million ongoing Proposition 98 for the HSN. In addition, it sets aside \$3 million in one-time Proposition 98 monies pending further review of a HSN technology refresh plan submitted by Imperial County Office of Education (ICOE, the lead agency administering the project).

Baseline Budget Appears Reasonable. After examining the detailed HSN budget, we recommend providing the \$10 million ongoing Proposition 98 for the project. When combined with federal eRate and California Teleconnect monies, as well as cash reserves, the project would have sufficient funding to support a baseline budget.

Technology Refresh Plan Appears Reasonable. In addition to funding the HSN baseline budget, we recommend providing \$2.6 million in one-time Proposition 98 to implement phase one of a technology refresh plan. Specifically, the technology refresh plan would:

- ***Increase Network Capacity.*** More capacity would be added to the existing network infrastructure to support greater use and more demanding applications.
- ***Replace Aging Equipment.*** Equipment that has reached its contractual "end of life" would be replaced.
- ***Upgrade Technology.*** Network enhancements would be made so that new types of applications could be supported. (For example, upgrading to Internet Protocol version 6 (IPv6) will be required to interact with all federal backbone networks by 2008.)
- ***Improve Performance Monitoring.*** New performance monitoring equipment would be installed to allow for improved growth planning, problem resolution, and network evaluation.

We think the plan is realistically scheduled, reasonably priced, and needed to maintain reliable service.

ENSURING TRANSPARENCY

Recent Actions Taken to Improve Transparency

Originally, CalREN and CENIC were created primarily to serve the needs of the UC system. The CENIC was governed with a member board and was treated more as an extension of UC rather than a vendor. As more state entities became members of CENIC and more state monies were expended on CalREN, and later HSN, oversight of the programs became more complicated. Although CENIC members were governing CalREN and HSN, standard project items such as clearly defined project objectives,

evaluation criteria, fee calculations/payment structures, and contractual protections for state assets were missing. As a result, questions about the management of CENIC, CalREN, and HSN began to arise, and a series of steps were taken to provide more transparency.

State Law Initially Provided Limited Project Guidance and Oversight. The CalREN project historically has been treated as a UC project with very little state direction, involvement, or oversight. Thus, the higher education members of CENIC have been allowed wide discretion in building and operating the network. In 2000-01, the state funds UC received to develop and implement HSN by expanding the existing CalREN infrastructure came without any specific guidance, stated goals, or measurable objectives. The *2000-01 Budget Act* required only that the funds be used for “expanding Internet connectivity and network infrastructure for K-12 schools and county offices of education.”

Responsibility for the HSN Project Shifted From UC to the California Department of Education (CDE) in 2004. Between 2000-01 and 2004-05, the state provided more than \$100 million for HSN with still virtually no statutory guidance. While the substantial state investment resulted in network connectivity to all 58 counties, it also magnified the need for more transparency and accountability. In 2004-05, the Legislature shifted funding for HSN from UC to CDE which, in turn, awarded a contract to ICOE to administer the project. This shift of responsibilities was made to ensure HSN would be better aligned with K-12 priorities and support the specific needs of K-12 schools. As questions continued to mount about project transparency, protection of state assets, and large cash reserves, no additional funding was provided for HSN in 2005-06.

Bureau of State Audits (BSA) Finds Notable Contract Irregularities. In 2005, BSA conducted a review of HSN and assessed whether the resources supporting it were being used appropriately and efficiently. The report concluded that the technology was sound but that opportunities existed to improve use of the network and administration in such a way as to better safeguard state assets. The audit report made several recommendations, the most significant of which related to better definition of goals and objectives and contractual terms to protect the state’s interests. Figure 1 (see next page) provides a summary of the BSA recommendations.

Recent Legislation Applies BSA Recommendations to HSN. Chapter 552, Statutes of 2006 (AB 1228, Daucher), addressed each of the BSA audit recommendations relating to the HSN project. Specifically, it requires ICOE to define goals and objectives, increase usage of the network, create a methodology by which to evaluate the success of HSN, and report back to the Legislature by March 1, 2007. Additionally, Chapter 552 specifies provisions that must be in all future HSN contracts to protect the state’s

<p>Figure 1</p> <p>Audit Finds Network Objectives and Contractual Terms Need Improvement</p>
<p>Recommendations by Bureau of State Audits (2005)</p>
<p>Goals and Objectives</p> <p>Define goals and objectives of K-12 High Speed Network</p> <p>Increase use by:</p> <ul style="list-style-type: none"> Offering more videoconferencing Developing more academic content and applications Providing incentive grants Connecting more schools <p>Identify method to evaluate network</p>
<p>Contract Terms</p> <p>Service Level Agreement</p> <p>Require service level agreements</p> <p>Protect State Property</p> <p>Protect state's interest in property purchased with state monies</p> <p>Protect state intellectual property</p> <p>Protect State Monies</p> <p>Ensure interest on state monies accrues to the state</p> <p>Ensure interest earned on state monies used to reduce the California Research and Education Network fees</p> <p>Ensure interest earned on any monies designated for network accrues to the state</p>

interests, such as the assurance that interest earned on state monies will accrue to the state, protection of state intellectual property, and transparent fee structures. Chapter 552 did not address the state's interests regarding monies paid to CENIC by UC, CSU, or CCC. For more detail on Chapter 552, see the nearby box.

In 2006-07, Legislature Conducts More Oversight of CalREN and HSN. In the 2006-07 Budget Act, the Legislature adopted Control Section 24.55 requiring CENIC to submit additional program documentation no later than December 1, 2006. Specifically, the report was to include service level agreements, details on assets purchased with state monies, documentation showing how interest earned on state monies was used, and information on fees charged to private clients. (See box on page 72 for a more detailed listing of the control section requirements.) The Governor's 2007-08 budget proposal does not contain this control section.

Chapter 552, Statutes of 2006 (AB 1228, Daucher)

Chapter 552 established the K-12 High Speed Network (HSN). In doing so, it attempted to address several Bureau of State Audits (BSA) recommendations directly as well as provide the Imperial County Office of Education (ICOE) with the leverage to negotiate a contract with the Corporation for Education Network Initiatives in California (CENIC) that addressed remaining BSA recommendations. Below, we summarize the major provisions of the bill.

- **Purpose:** Enriching pupil educational experiences and improving pupil academic performance by providing high-speed, high-bandwidth Internet connectivity.
- **Goals and Objectives:** Defines high-level goals and objectives and requires the advisory board to define evaluation criteria for HSN and report back to the Legislature by March 1, 2007. Also requires implementation of videoconferencing and authorizes ICOE to oversee use grants as well as grants to connect unconnected schools. Directs ICOE to coordinate network use to benefit teaching and learning.
- **Services:** Internet service, interconnectivity among K-12 entities, connection to higher education institutes, connections to state and local agencies, videoconferencing, distance learning tools, and statewide coordination of network use.
- **Administration:** A competitively selected local educational agency (LEA) administers the network on behalf of the Superintendent of Public Instruction. An advisory board, primarily composed of county and school district representatives, will meet quarterly to provide policy and operational guidance.
- **Oversight:** Fiscal oversight provided by an annual independent audit. Technical oversight provided by an independent evaluation to be completed by March 1, 2009. Requires ICOE to submit annual budget request to the Department of Finance.
- **Contract Requirements:** The ICOE must include the following in all contracts they enter into: a service level agreement, protection of intellectual property ownership rights, asset protection, documentation of appropriate fee structures, and assurance that any interest earned on state funds are used to the benefit of the project.

Enhanced Transparency and Contractual Improvements Should Be Applied to All Education Segments

We recommend the Legislature further protect state interests by enacting legislation that would extend the major provisions of Chapter 552 to the higher education segments. In addition, we recommend the Legislature request the Corporation for Education Network Initiatives in California to provide more information on its assets and fee structure by April 1, 2007, consistent with the intent of Section 24.55 of the 2006-07 Budget Act.

2006-07 Budget Act Control Language

Section 24.55 of the 2006-07 Budget Act, placed the following requirements on the Corporation for Education Network Initiatives in California (CENIC) and the Imperial County of Education:

- Ensure that any interest earned on state monies held by CENIC accrues to the segment providing the excess monies and is used to operate the California Research and Education Network (CalREN) for that segment.
- Create a service level agreement (SLA) for CalREN and the High Speed Network (HSN).
- Establish fee payment schedules that do not require prepayment.
- Submit a report to the Legislature and the Governor by December 1, 2006, with the following:
 - Information on revenues and expenses over \$100,000 in 2005-06.
 - A financial accounting of all primarily state-funded assets for CalREN and HSN.
 - The SLA for CENIC.
 - A list of all prepayments made in 2005-06 and the first quarter of 2006-07 and an explanation of savings resulting from each.
 - Fees charged by CENIC to all private and out-of-state educational institutes using CalREN.
 - Revised budget for 2006-07 for CalREN and the HSN.

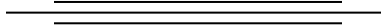
Chapter 552 addressed BSA audit concerns about the HSN project, but significant accountability issues still exist with regards to the higher education segments. We think the transparency, safeguards, and accountability provisions laid out in Chapter 552 for the HSN project should be extended to the higher education segments. Ideally, the Legislature would make these improvements in a bill, though it also could adopt a budget control section (as was done in 2006-07).

State Monies From All Education Segments Should Be Protected. Chapter 552 protects state assets and interests by requiring specific terms be included in the contract between K-12 and CENIC. This will not, however, protect state monies paid to CENIC on behalf of, or assets acquired by, UC, CSU, or CCC. We believe contracts between CENIC and each of these systems should have the same provisions that Chapter 552 required for the K-12 project. We recommend legislation (or control language) that requires each segment, no later than January 1, 2008, to negotiate contracts (or contract amendments, as appropriate) with CENIC that include the five contract terms required in Chapter 552.

CENIC Has Yet to Provide Required Information on State-Funded Assets. Although CENIC submitted a detailed report on December 1, 2006, as required by Section 24.55 of the *2006-07 Budget Act*, it did not provide the requested information about state-funded assets or its fee structure. The control language required a “financial accounting of all primarily state-funded assets associate[d] with CalREN and HSN.” In response, CENIC provided a list of all assets, without dollar values or information about ownership, and separately provided a total dollar value of shared assets, claiming that determining which of these shared assets was primarily state-funded is difficult. CENIC did provide a total dollar value for non-shared state assets but no inventory or supporting documentation. CENIC should be required to provide the required level of asset information to protect the state’s property. If CENIC were to cease managing the project the state would need an accurate inventory of state-funded assets.

CENIC Has Yet to Provide Required Information on Fee Structures. The control language also asked CENIC to provide a list of fees charged to out-of-state and private members. The intent of this request was to assess whether California entities are paying a “fair” price compared to other members and ensure state monies are being used to provide services to state entities, not to subsidize smaller private organizations. CENIC complied with the request by providing the name and total annual revenue earned from each of the seven out-of-state and private members in 2005-06. While this list met the letter of the request, it did not satisfy the intent of the request. The annual revenues from these seven members varies from a low of \$62,000 to a high of \$1.4 million, all of which are much lower than California’s public members pay annually. CENIC should be required

to provide more transparency on its fee structure. Specifically, it should show how fees are calculated for each member and how interest earnings reduce fee levels that otherwise would be charged. This information would help the Legislature determine if fees are being applied consistently to all members for services provided. We recommend that CENIC report these items to the Legislature by April 1, 2007.



INTRODUCTION

K-12 Education

The budget proposes to provide a \$1.4 billion (2.9 percent) increase in K-12 Proposition 98 funding from the 2006-07 level. Schools would receive \$8,524 per pupil—3.3 percent more than revised per-pupil expenditures in the current year. New funding is used primarily to provide a cost-of-living adjustment and increase the Proposition 98 share of the state’s child care program.

Overview of K-12 Education Spending

Figure 1 (see next page) displays all significant funding sources for K-12 education for 2005-06 through 2007-08. As the figure shows, Proposition 98 funding constitutes over 70 percent of overall K-12 funding. Proposition 98 funding for K-12 education increases \$1.4 billion (2.9 percent) from the 2006-07 level. This increase is supported mainly by local property taxes (\$1.2 billion). Other funding for K-12 education increases by a combined \$346 million (1.9 percent).

Proposed School Transportation Funding Shift Affects Year-to-Year Comparisons. The budget proposes to shift the \$627 million Home-to-School Transportation program out of Proposition 98—funding it instead from the Public Transportation Account (PTA). In a related action, it proposes to “rebench” the Proposition 98 minimum funding guarantee downward by a like amount. Because funding for the transportation program is included in the K-12 Proposition 98 totals in Figure 1 for 2006-07 but *not* for 2007-08, comparing the two amounts understates the actual year-to-year change in resources for K-12 education. If the \$627 million shift were not to occur and the guarantee was not rebenched downward, total K-12 Proposition 98 funding would increase by \$2.1 billion, or 4.2 percent, from 2006-07. Shifting funding for the transportation program to PTA also explains the notable increase in the “other” funds category (\$596 million).

Federal Funding—Decrease of \$545 Million. The largest decrease in non-Proposition 98 funding is due to a drop in federal funds. The Governor’s budget assumes a year-to-year decrease in federal funding of

\$545 million. About half of that reduction is due to the Governor's proposal to reduce federal funding for child care and instead use the funds to cover other California Work Opportunities and Responsibility to Kids (CalWORKs) costs (\$269 million). (In a related action, Proposition 98 support for child care would be increased by roughly the same amount.) Another sizable decline (\$77 million) is related to an expected decline in caseload for Stage 2 child care. In addition to these child care-related reductions, the budget assumes considerable reductions in federal support for the Even Start program (\$50 million) and 21st Century Learning Centers (\$34 million).

Figure 1
K-12 Education Budget Summary

(Dollars in Millions)

	Actual 2005-06	Revised 2006-07	Proposed 2007-08	Changes From 2006-07	
				Amount	Percent
K-12 Proposition 98					
State General Fund	\$34,582	\$36,658	\$36,851	\$193	0.5%
Local property tax revenue	11,959	12,353	13,595	1,242	10.1
Subtotals	(\$46,541)	(\$49,011)	(\$50,446) ^a	(\$1,435)	(2.9%)
Other Funds					
General Fund					
Teacher retirement	\$999	\$876	\$966	\$91	10.4%
Bond payments	1,681	1,857	2,201	345	18.6
Other programs	160	554	413	-140	-25.4
State lottery funds	1,036	1,012	1,012	—	—
Federal funds	6,931	7,113	6,568	-545	-7.7
Other	6,147	6,352	6,948	596	9.4
Subtotals	(\$16,954)	(\$17,763)	(\$18,109)	(\$346)	(1.9%)
Totals	\$63,495	\$66,774	\$68,555	\$1,781	2.7%
K-12 Proposition 98					
Average daily attendance (ADA)	5,964,108	5,940,989	5,917,948	-23,041	-0.4%
Budget amount per ADA	\$7,803	\$8,250	\$8,524 ^b	\$275	3.3%
Totals may not add due to rounding.					
^a Reflects Governor's proposal to fund Home-to-School Transportation (\$627 million) from the Public Transportation Account and rebench the Proposition 98 guarantee downward by a like amount. If the swap were not to occur, the change from 2006-07 would be \$2.1 billion—a 4.2 percent increase.					
^b Assumes transportation funding swap. If swap were not to occur, the per-pupil rate would be \$8,631, reflecting a 4.6 percent increase over 2006-07.					

Repaying Bonds for School Facilities—Increase of \$345 Million.

The bulk of this increase in debt service is due to recent investments the state has made in school facilities through Proposition 47 (2002) and Proposition 55 (2004). These measures authorized the state to sell a total of \$21.4 billion in bonds for school facilities. Proposition 1D, approved by the voters in November 2006, authorized an additional \$7.3 billion for school facilities. (Not reflected in Figure 1, and distinct from debt-service payments on already sold bonds, is the Governor's proposed \$6.9 billion in expenditures from yet unused prior-year bond monies as well as new bond monies available from Proposition 1D.)

Teachers' Retirement Costs Increase by \$91 Million. The Governor's budget includes \$966 million in 2007-08 for the state's annual K-12 contribution to the California State Teachers' Retirement System (CalSTRS). Year-to-year comparisons are complicated because of a one-time reduction in the state's contribution in 2006-07. (The reduction is related to prior-year accounting errors that had resulted in overpayments.) Absent this factor, state contributions would have risen steadily since 2005-06 due to expansion of teacher payroll. The Governor's budget for 2007-08, however, proposes to constrain costs by making a change in one of CalSTRS' benefit programs. Thus, the \$91 million increase from 2006-07 to 2007-08 is the net result of continued growth in teacher payroll offset by the proposed change.

Proposition 98 Per-Pupil Funding

Budget Continues Recent Growth Pattern, Increasing Per-Pupil Funding by \$275. The Governor's budget provides an additional \$275 per pupil in Proposition 98 funding, a 3.3 percent increase from the current year. Figure 2 (see next page) shows per-pupil spending levels over the last decade. The numbers are in "nominal" dollars—that is, not adjusted for inflation. The figure shows three distinct trends—a fast growth period in the late 1990s, a slow growth period between 2000-01 and 2004-05, and significant increases over the past three years (reflecting an average annual increase of 6.6 percent).

Even After Adjusting for Inflation, Per-Pupil Funding Has Experienced Healthy Increases in Recent Years. Figure 3 (see next page) adjusts per-pupil spending for inflation. While K-12 spending still shows rapid growth in the late 1990s, between 2000-01 and 2004-05 it did not keep pace with rising costs (declining at an average annual rate of 1.2 percent). This trend began to change in 2005-06 with a substantial 6.4 percent increase over the previous year. The Governor's proposal would grow adjusted per-pupil spending an additional 0.6 percent in 2007-08. Looking at changes over the last decade, spending (in inflation-adjusted terms) has increased by approximately \$1,130 per pupil (15 percent).

Figure 2

Proposition 98 K-12 Per Pupil Spending

(Nominal Dollars)

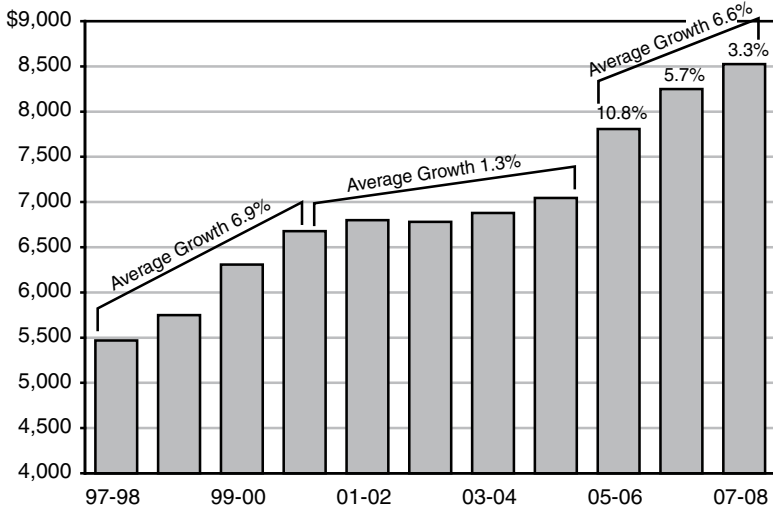
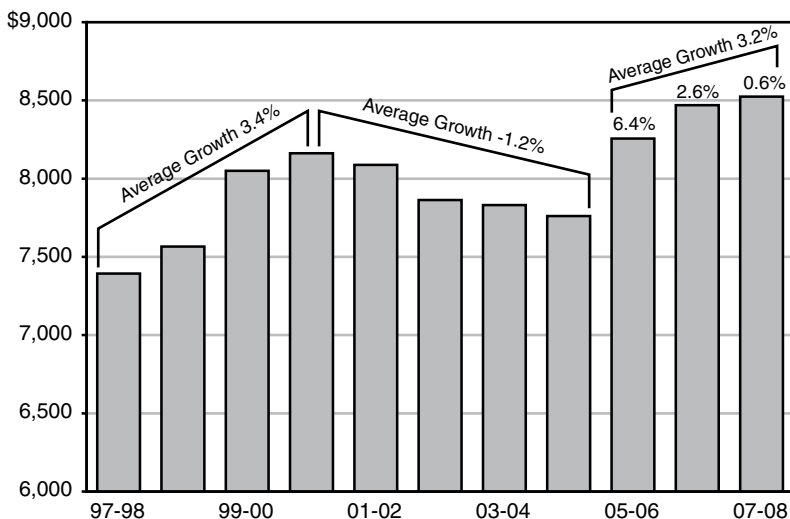


Figure 3

K-12 Per Pupil Spending Adjusted for Inflation

(2007-08 Dollars)



Including Additional Funding Sources Raises Per-Pupil Totals. As discussed above, the Governor’s proposal to shift transportation funding out of Proposition 98 complicates year-to-year comparisons. These comparisons also are complicated by a settlement agreement related to Proposition 98 K-14 funding requirements (referred to as the California Teacher’s Association, or CTA, settlement). As a result of that seven-year, \$2.8 billion settlement, schools in 2007-08 will receive an additional \$268 million to use primarily for class size reduction (CSR) in grades 4-12. Figure 4 shows how per-pupil spending levels would increase if the transportation and settlement monies were included. Adjusting for the transportation funds, the Proposition 98 per-pupil funding would be \$8,630, or \$380 over 2006-07 levels. This equates to an increase of 4.6 percent in actual dollars, and an increase of 1.9 percent after adjusting for inflation. Were the CTA settlement funds to be included as well (roughly \$45 per pupil), funding per pupil would be \$8,675, an increase of \$426 over 2006-07. This is an increase of 5.2 percent over the current year (2.4 percent adjusted for inflation).

Figure 4

Three Approaches to Calculating Proposition 98 K-12 Per-Pupil Spending

Per Average Daily Attendance

	2007-08	Change From 2006-07 Revised		
		Amount	Percent (Nominal)	Percent (Adjusted)
Governor’s Budget	\$8,524	\$275	3.3%	0.6%
Including transportation funding	8,630	380	4.6	1.9
Including transportation and settlement funding ^a	8,675	426	5.2	2.4

^a The CTA settlement provides \$268 million to K-12 education in 2007-08. This equates to around \$45 per average daily attendance.

Settlement Differs in Important Ways From Other “Settle-up” Funds. Typically, our per-pupil totals do not include one-time settle-up funds provided to meet a prior year’s Proposition 98 obligation. Because these funds are provided in one year and not the next, they skew year-to-year comparisons. Because the CTA settlement funds will be provided over a seven-year period and will fund items that are ongoing in nature—such as hiring teachers to reduce class sizes—we believe it is important to show how they affect per-pupil funding levels. (However, it is also important to

note that these funds will be used to support only about 500,000 students at high per-pupil rates—\$500 for each K-3 student, \$900 for each grades 4 through 8 student, and \$1,000 for each high school student.)

Major K-12 Funding Changes

Figure 5 displays the major K-12 funding changes from the 2006-07 revised budget. In 2007-08, the Governor's budget proposes \$1.4 billion in new Proposition 98 K-12 expenditures for the following purposes.

- **Revenue Limits—\$1.3 Billion.** The Governor's budget funds a 4 percent cost-of-living adjustment (COLA) (\$1.4 billion) and captures savings from a decline in statewide attendance of 0.4 percent (\$110 million savings).
- **Categorical Programs—\$555 Million.** The Governor fully funds all statutorily required COLAs for categorical programs and also provides COLAs for most other programs (\$516 million). In addition, the budget captures savings from the 0.4 percent decline in attendance from roughly half of the categorical programs; it maintains approximately 25 programs at 2006-07 levels; and for the remaining programs, which have statutory growth rates different from the statewide rate, the budget provides applicable growth funding. The net effect of all attendance-related adjustments is an additional cost of \$39 million.
- **Shift Home-to-School Transportation—\$627 Million Savings.** As noted above, the budget proposes to use PTA in lieu of Proposition 98 to fund the \$627 million Home-to-School Transportation program. It also proposes to rebench the Proposition 98 guarantee downward, thereby reducing overall K-12 Proposition 98 funding by a like amount.
- **Increase Proposition 98 Share of Child Care Costs—\$269 Million.** In the current year, Proposition 98 funds support \$1.4 billion of the state's child care program. The remainder of program costs are supported through federal Temporary Assistance for Needy Families (TANF) and state General Fund monies. The budget proposes to shift an additional \$269 million in costs—all for Stage 2 CalWORKs child care—from TANF to Proposition 98. This proposal is simply a shift in funding source and would not affect total monies available for child care, the level of child care services, or the Proposition 98 minimum guarantee.

Figure 5	
Major K-12 Proposition 98 Changes	
<i>(In Millions)</i>	
2006-07 Revised K-12 Spending Level	\$49,010.9
Revenue Limit	
Cost-of-living adjustments (COLAs)	\$1,383.6
Decline in average daily attendance	-110.4
PERS/UI ^a	-6.1
Subtotal	(\$1,267.2)
Categorical Programs	
COLAs	\$515.7
Growth	38.8
Shift Home-to-School Transportation	-626.8
Shift child care Stage 2	269.0
Other	-29.0
Subtotal	(\$167.7)
Total Changes	\$1,434.9
2007-08 Proposed	\$50,445.8
^a Public Employees' Retirement System/Unemployment Insurance.	

Proposition 98 Spending by Major Program

Figure 6 (see next page) shows Proposition 98 spending for major K-12 programs. The budget provides \$35.5 billion for revenue limits, which includes roughly \$500 million for the state's declining enrollment adjustment. (This adjustment allows districts to be funded at the greater of the current- or prior-year's attendance level.) The budget also includes \$3.5 billion for special education and \$1.8 billion for K-3 CSR. The figure shows a significant increase in funding for child care (\$358 million), although \$269 million of this amount reflects the Governor's proposed funding swap, not a net enhancement to the program. Similarly, the elimination of funding for Home-to-School Transportation reflects the proposed shift to PTA, not an elimination of state contributions for school transportation.

Figure 6
Major K-12 Education Programs
Funded by Proposition 98

(Dollars in Millions)

	Revised 2006-07 ^a	Proposed 2007-08 ^a	Change	
			Amount	Percent
Revenue Limits				
General Fund	\$22,234.2	\$22,303.6	\$69.4	0.3%
Local property tax	11,949.6	13,147.8	1,198.2	10.0
Subtotals	(\$34,183.8)	(\$35,451.4)	(\$1,267.6)	(3.7%)
Categorical Programs				
Special education ^b	\$3,440.2	\$3,513.4	\$73.2	2.1%
K-3 class size reduction	1,763.5	1,820.7	57.2	3.2
Child care and development	1,388.6	1,747.0	358.4 ^c	25.8
Targeted Instructional Improvement Block Grant	1,034.1	1,071.7	37.6	3.6
Economic Impact Aid	973.4	1,012.7	39.3	4.0
Adult education	703.5	750.2	46.7	6.6
After School Education and Safety Program	547.4	547.4	—	—
Regional Occupation Centers and Programs ^b	486.4	514.2	27.7	5.7
School and Library Improvement Block Grant	447.4	463.7	16.3	3.6
Summer school programs	402.6	419.0	16.4	4.1
Instructional Materials Block Grant	403.5	418.2	14.7	3.6
Deferred Maintenance	269.9	276.3	6.4	2.4
Professional Development Block Grant	264.1	273.7	9.6	3.6
Public School Accountability Act	249.2	249.2	—	0.0
Grades 7-12 counseling	200.0	208.1	8.1	4.0
Home-to-School Transportation	602.4	—	-602.4 ^d	-100.0
Other	1,591.2	1,649.2	58.0	3.6
Deferrals	59.9	59.9	—	—
Subtotals	(\$14,827.2)	(\$14,994.5)	(\$167.3)	(1.1%)
Totals—Governor's Budget	\$49,010.9	\$50,445.8	\$1,434.9	2.9%

^a Amounts include deferrals.

^b Includes both General Fund and local property tax revenues.

^c Of this amount, \$269 million reflects the Governor's proposed funding swap rather than an inflationary adjustment or a programmatic enhancement.

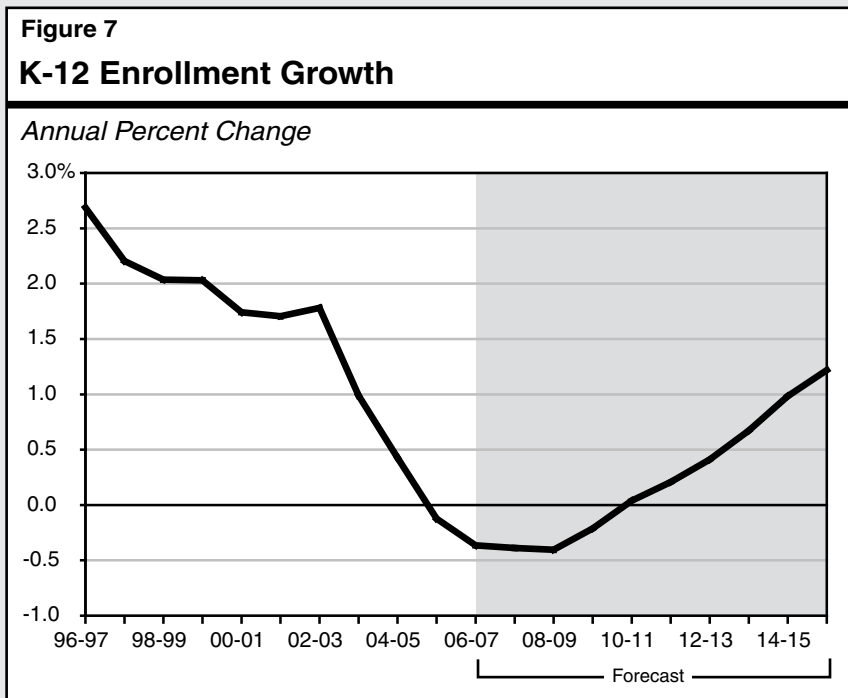
^d Reflects proposed funding shift from Proposition 98 to the Public Transportation Account rather than a reduction in funding or program elimination.

Enrollment Trends

Enrollment levels significantly shape the Legislature’s annual K-12 budget decisions. When enrollment levels increase slowly or decline, for example, fewer resources are needed to meet statutory funding obligations for revenue limits and categorical programs. This can leave more General Fund resources available for other budget priorities. Conversely, when enrollment grows rapidly (as it did in the 1990s), the state must dedicate a larger share of new resources to meeting statutory K-12 funding obligations. In light of the important implications of enrollment levels, we describe below two major trends in the K-12 student population.

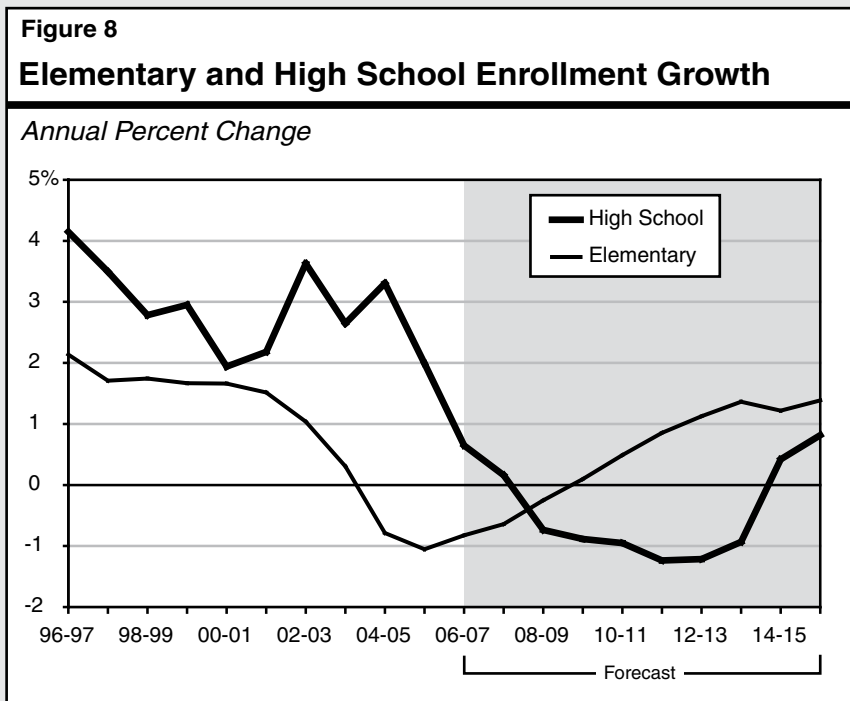
The enrollment numbers used in this section are from the Department of Finance’s Demographic Research Unit and reflect aggregate, statewide enrollment. While the enrollment trends described here will likely differ from those in any given school district, they reflect the overall patterns the state is likely to see in the near future.

K-12 Enrollment Levels on the Decline. K-12 enrollment is projected to decline in 2007-08 for the third consecutive year—dropping by about 0.4 percent, for total enrollment of 6.2 million students. Figure 7 shows how enrollment growth has steadily slowed since the mid-1990s, with enrollment levels actually dropping since 2005-06. The figure also shows that K-12 enrollment is projected to continue declining until 2010-11.



Divergent Trends in Elementary and High School Enrollment.

Figure 8 shows that the steady decline in K-12 enrollment growth masks two distinct trends in elementary (grades K-8) and high school (grades 9 through 12) enrollment. Elementary school enrollment growth has slowed since 1996-97, with actual declines in recent years. It is projected to begin growing again in 2009-10. In contrast, high school enrollment grew rapidly, from 1996-97 through 2004-05. Beginning in 2005-06, however, high school enrollment growth also began to slow. This trend is expected to continue, with actual declines projected beginning in 2008-09. Between 2007-08 and 2013-14, high school enrollment is projected to fall by almost 115,000 students.



Budget and Policy Implications. These enrollment trends have significant budgetary and policy implications for issues such as CSR, teacher demand, and facilities investments. Decreasing K-12 average daily attendance (ADA) also could lead to a significant change in future Proposition 98 requirements. Below we discuss a few of the major fiscal and policy implications.

- In most years, the Proposition 98 minimum funding requirement—referred to as the minimum guarantee—is based partially

on growth in K-12 attendance. Thus, as enrollment continues to decline, a smaller share of the state's new revenues will be required for K-14 education. For the next few years, therefore, the Legislature will have the option of devoting a larger share of revenues to other budget priorities or else increasing per-pupil spending beyond what is required by the minimum guarantee. However, as discussed in the "Proposition 98 Update" section of this chapter, once the Test 1 component of Proposition 98 becomes operative, spending for K-14 education will be locked in at roughly 40 percent of the General Fund. As a result, the state will no longer experience savings from declines in enrollment.

- Despite the general downward trend in enrollment growth, significant variation is expected to occur across counties. For example, over the next ten years, Los Angeles' enrollment is expected to decline by about 200,000 students (a 12 percent decline), whereas Riverside's enrollment is expected to increase by about 140,000 students (a 34 percent increase).
- Declining enrollment will likely affect the uses of new capital outlay bond funding. Fewer students indicate a decreasing statewide need for new construction dollars, and suggest that an increasing proportion of bond funding might be needed instead for modernization of existing school facilities. (Proposition 1D, approved in November 2006, allocates \$1.9 billion for new construction and \$3.3 billion for modernization. In contrast, the administration's plan for 2008 and 2010 bond measures would provide \$5.1 billion for new construction and \$2.5 billion for modernization.)
- The percent of Hispanic students will continue to increase. In 1995-96, 36 percent of the school-age population was Hispanic. By 2015-16, 48 percent will be Hispanic. Since many of these students will be English learners, the state will need to increase its focus on the language development skills of this group.

BUDGET ISSUES

K-12 Education

HOME-TO-SCHOOL TRANSPORTATION

The Governor proposes to shift ongoing funding for the Home-to-School Transportation program (\$627 million) from Proposition 98 to the Public Transportation Account (PTA). In a related action, the administration proposes to reduce the Proposition 98 minimum guarantee by a like amount. Taken together, these actions are intended to achieve ongoing General Fund savings. (The administration has stated, however, that if the PTA is insufficient to maintain the same funding level for school transportation in the future, General Fund would be used to backfill the difference.) Given serious legal and policy concerns, we recommend the Legislature reject the set of proposals. Instead, we recommend using a smaller amount of PTA monies on a one-time basis to support the Home-to-School Transportation program in 2006-07. Such action also would produce ongoing savings by lowering the Proposition 98 obligation for 2007-08.

Reject Home-to-School Transportation Proposals

Given serious legal and policy concerns, we recommend the Legislature reject the Governor's school transportation proposals.

The Home-to-School Transportation program provides funding for school districts to purchase and operate school buses for transporting students to and from school. Recent data indicate that almost all school districts (930) participate in the program, transporting a total of approximately 936,000 students (including special education students), or about one in six K-12 students.

We have three major concerns with the Governor's school transportation proposals—one related to the viability of the PTA as an ongoing funding source for the school transportation program and two related to the rebenching of the Proposition 98 minimum guarantee.

PTA Might Not Have Sufficient Funds to Support Program in Future. Although school bus transportation appears to meet the eligibility requirements for PTA funding, it is uncertain whether PTA will have sufficient funds to support the Home-to-School Transportation program on an ongoing basis after 2007-08. In "Funding for Transportation Programs," in the Crosscutting Issues section of the Transportation chapter, we provide a detailed review of PTA, its funding sources, and its cost pressures. We find that the PTA fund condition can fluctuate significantly from year to year because one of its underlying revenue streams is very volatile—fluctuating based on changes in both the economy and gasoline prices. Given such volatility, PTA might not have sufficient funds to cover school transportation costs in future years.

Rebenching Proposal Appears Unconstitutional. After consulting with Legislative Counsel, we think the administration's proposed rebenching of the Proposition 98 minimum guarantee is likely unconstitutional. The State Constitution does not contain any language authorizing such a rebenching of the minimum guarantee. On the contrary, the clear intent behind the voter-approved measure was to ensure a minimum level of funding for Proposition 98 and insulate K-14 education from other potentially competing state priorities. Given this legal concern, we think the administration's rebenching proposal is very risky.

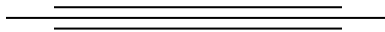
Rebenching Minimum Guarantee Sets Bad Policy Precedent. We also believe implementing the Governor's proposal would set a bad policy precedent. Given that Proposition 98 is intended to offer protection to K-14 programs from funding reductions, a rebenching proposal that lowers the guarantee seemingly would require some underlying policy rationale. The Governor's proposal, however, offers no reasonable explanation as to why a program historically funded from Proposition 98 should now be excluded from it. Under the administration's approach, the state could shift funding for any K-14 program from Proposition 98 to another source and reduce the minimum guarantee anytime it wanted to achieve savings. Once the program was removed from the "protected" guarantee, the state could then defund it in future years and realize additional ongoing savings. As a result of such shifts and subsequent eliminations, the minimum guarantee—and the "protection" it is supposed to provide to K-14 funding—would be rendered meaningless.

Use PTA to Maximize Current- and Budget-Year Savings Without the Risk

We recommend the Legislature use roughly \$300 million in Public Transportation Account (PTA) monies on a one-time basis in the current year to support the Home-to-School Transportation program. Using PTA monies in such a way could produce substantial savings not only in the current year but also in the budget year.

Using PTA for School Transportation Could Be Major Part of Current-Year Budget Solution. In the “Proposition 98 Update” section of this chapter, we discuss our current estimates of the minimum guarantee in 2006-07 and 2007-08. Revenues have fallen substantially from initial estimates for 2006-07—lowering the Proposition 98 guarantee by roughly \$600 million. Thus, the Legislature could reduce spending and still meet the minimum guarantee. In the “Proposition 98 Priorities” section of this chapter, we recommend the Legislature take several actions to reduce spending and meet the minimum guarantee in the current year without making disruptive cuts to school districts. One action we recommend is swapping available PTA monies for Proposition 98 monies on a one-time basis. This would provide the school transportation program with the same level of funding while generating substantial General Fund savings. Because the transfer would be one-time in nature, and the PTA is carrying a large balance in 2006-07, the account would have sufficient funds to support a swap in the magnitude of \$300 million.

Action Produces Potential Out-Year Savings. Reducing Proposition 98 spending in the current year also reduces the minimum guarantee by roughly a like amount in the budget year. This means the Legislature would have additional savings options available as it builds its 2007-08 budget plan. (In the “Proposition 98 Priorities” section of this chapter, we have additional recommendations for how the Legislature can reduce Proposition 98 spending in 2007-08 while holding school districts essentially harmless.)



CHILD CARE AND DEVELOPMENT

The state supports a variety of child care and development programs. It also supports activities and efforts to improve the quality and availability of these programs through community, parent, and provider education. Although the specific objective of each program is unique, collectively the programs aim to provide high-quality supervision and/or early education experiences to children from birth through age 12 (or longer for children with special needs). As shown in Figure 1, in 2007-08, the Governor proposes to spend \$3.7 billion on these programs to provide services to an estimated 978,000 children.

In the remainder of this write-up, we:

- Provide background on child care and development programs, including details on program objectives, administrative control, enrollment levels, and funding.
- Discuss the administration's proposal to decrease federal support and increase Proposition 98 support for Stage 2 child care (thereby achieving \$269 million in non-Proposition 98 General Fund savings).
- Summarize research findings on the benefits of preschool for low-income children and recommend building a plan to expand preschool over the next several years as additional Proposition 98 monies become available.
- Recommend various cost-neutral changes to the Governor's proposed budget that would help lay the foundation for preschool expansion. Specifically, we make recommendations in the areas of (1) wrap around child care, (2) facilities, and (3) program quality.

Figure 1				
California Child Care and Development Programs				
<i>2007-08 All Funds (Dollars in Millions)</i>				
Program^a	2006-07	Proposed 2007-08	Change	
			Amount	Percent
Child Care				
CalWORKs ^b :				
Stage 1 ^{c, d}	\$418	\$510	\$92	22.0%
Stage 2 ^{d, e}	539	462	-77	-14.3
Stage 3	390	393	3	0.8
Subtotals	(\$1,347)	(\$1,365)	(\$18)	(1.3%)
Non-CalWORKs ^b :				
General child care	\$698	\$762	\$64	9.2%
Other child care programs	327	344	17	5.2
Subtotals	(\$1,025)	(\$1,106)	(\$81)	(7.9%)
Child Development				
State preschool	\$392	\$418	\$26	6.6%
After school programs	710	676	-34	-4.8
Subtotals	(\$1,102)	(\$1,094)	(\$8)	(-0.7%)
Growth and COLA	\$108	\$76	-\$32	-30% ^f
Support Programs	\$91	\$102	\$11	12.1%
Totals—All Programs	\$3,673	\$3,743	\$70	1.9%
<p>^a Except where noted otherwise, all programs are administered by the California Department of Education.</p> <p>^b California Work Opportunity and Responsibility to Kids.</p> <p>^c Administered by California Department of Social Services.</p> <p>^d Does not include reserve funding.</p> <p>^e Includes \$15 million for centers run by California Community Colleges.</p> <p>^f The bulk of the decline is due to the difference in the cost-of-living adjustment (COLA) rates (5.92 percent in 2006-07 and 4.04 percent in 2007-08).</p>				

CHILD CARE AND DEVELOPMENT PROGRAMS

As Figure 1 shows, approximately two-thirds of this budget is used for child care programs, 30 percent is for child development programs, and about 3 percent is for related support activities.

Child Care Programs

In general, child care programs are designed primarily to supervise children. The state programs serve children of families in the California Work Opportunity and Responsibility to Kids (CalWORKs) program as well as non-CalWORKs low-income families.

CalWORKs Guarantees Families Child Care. In exchange for engaging in work or work preparation activities, the state guarantees child care to CalWORKs recipients. Thus, the demand for CalWORKs child care is driven by CalWORKs' caseload. CalWORKs child care is supported by state Proposition 98, federal Temporary Assistance for Needy Families (TANF), and federal Child Care and Development Fund (CCDF) monies. The program involves three stages of child care.

CalWORKs Stage 1. This stage begins when a participant enters the CalWORKs program. The child care component is administered by the Department of Social Services (DSS) through county welfare departments. It is funded completely with TANF monies. In 2007-08, the Governor's budget includes slightly more than \$500 million to serve more than 67,000 children in Stage 1 care.

CalWORKs Stage 2. The CalWORKs families are transferred to Stage 2 when the county determines that participants' schedules become stable. Families remain eligible for Stage 2 as long as they are participating in CalWORKs and up to two years after the family stops receiving a CalWORKs grant. This stage is administered primarily by the California Department of Education (CDE) (although the California Community Colleges also have a small administrative role). It is funded with a combination of Proposition 98 and TANF monies. In 2007-08, the Governor's budget includes over \$450 million to serve more than 76,000 children in Stage 2 care (including about 3,000 children served in community college centers).

CalWORKs Stage 3. A family is eligible for Stage 3 when they have exhausted their two-year limit in Stage 2 (referred to as "timing out")—as long as their income remains below 75 percent of the state median income level and their children are below age 13. Stage 3 also is administered by CDE. It is funded with a combination of Proposition 98 and CCDF grant monies. In 2007-08, the Governor's budget includes almost \$400 million to serve more than 62,000 children in Stage 3 care.

Non-CalWORKs Families Receive Child Care if Space Is Available. In addition to CalWORKs Stage 2 and 3, CDE administers general and targeted child care programs to serve non-CalWORKs, low-income children at little or no cost to the family. Because the number of eligible low-income families exceeds available child care slots, waiting lists for this

care are common. (See the box on the next page for a brief description of the various types of non-CalWORKs child care.) These non-CalWORKs programs are funded with a combination of Proposition 98 and CCDF monies. In 2007-08, the Governor's budget includes \$1.1 billion to serve approximately 158,000 low-income, non-CalWORKs children.

Child Development Programs

Compared to child care programs, child development programs typically have a focus on early childhood education and enrichment. In California, CDE administers both preschool and after school programs for low-income and/or disadvantaged children.

Over 100,000 Children Currently Served by State Preschool Each Year. State preschool programs are part-day developmental programs for 3- to 5-year-old children from low-income families. In addition to educational activities, the state preschool programs require some level of parental education or involvement, provide meals or snacks to children, and provide families with referrals to health and social services agencies. These programs are run by local educational agencies, community colleges, community-action agencies, and private nonprofit agencies. Providers contract directly with CDE and are reimbursed using the Standard Reimbursement Rate (SRR) for preschool (proposed to be \$21.12 per child per day in 2007-08). Funding comes entirely from the state.

State Preschool Program Recently Expanded. State preschool is a three-hour development program available to low-income children. With the passage of Chapter 211, Statutes of 2006 (AB 172, Chan), the state expanded preschool funding by \$50 million, adding approximately 12,000 slots. This brought total preschool funding in 2006-07 up to almost \$400 million and total participation up to approximately 110,000 children. (We describe Chapter 211 in more detail later in this write-up.)

After School Programs Significantly Expanded in 2006-07. With the triggering of Proposition 49, after school programs also were expanded significantly in the current year. Proposition 49, approved by voters in 2002, required the state to increase funding for the After School Education and Safety (ASES) program by \$426 million (for total 2006-07 funding of \$548 million). In addition to the ASES program, after school activities are supported by the federally funded, state-administered 21st Century Child Learning Centers. In total, the Governor's 2007-08 budget includes more than \$676 million to provide after school services to approximately 500,000 children.

Types of Non-CalWORKs Child Care

There are various types of non-CalWORKs child care available to low-income families in California.

- **General Child Care.** State licensed child care, in a center or Family Child Care Home (FCCH), providing supervision and child development services for children from birth through 12 years of age as well as older children with exceptional needs. Also includes campus child care for the children of parents enrolled in community college.
- **School Age Community Child Care Services (Latchkey).** A safe environment with age and developmentally appropriate activities for school-age children during the hours when school is not in session.
- **Severely Handicapped Care.** Available in the San Francisco Bay Area only. Child care, developmentally appropriate activities, and therapy for eligible children and young adults (with an authorizing plan from a special education program) from birth to 21 years of age.
- **Migrant Child Care.** Child care in a licensed facility for children of agricultural workers. Hours and locations of care are structured around local agricultural activities. These programs are also required to reserve slots for children of migrant workers in anticipation of families moving.

Support Activities and Services

A small portion of total Proposition 98 and CCDF monies are used to fund programs that do not provide direct services to children but rather provide support services designed to improve program effectiveness. Some support programs are geared toward parents and providers. For example, resource and referral agencies provide information to parents and the community about child care available in the area and offer training to providers. By comparison, some are geared more toward government planning. For example, the county-based Local Planning Councils are responsible for assessing need, planning, and coordinating child care services within the county. The CDE also maintains a Centralized Eligibility (Wait) List. Other support programs collectively called "Quality Programs," are intended to improve the quality and availability of child care. (We discuss these quality programs in more detail later in this chapter.) In sum, the

Governor proposes to spend approximately \$100 million on these support services in 2007-08.

GOVERNOR'S STAGE 2 CHILD CARE PROPOSAL

Assuming the Governor's fiscal outlook, we would recommend the Legislature adopt the Governor's proposal to increase the state share of Stage 2 child care costs. This proposal is a reasonable option for achieving \$269 million in General Fund savings to address the state's structural shortfall. Based on our updated fiscal forecast, however, we recommend the Legislature take a series of other actions including not doing the Stage 2 shift in 2007-08.

The Governor proposes to achieve \$269 million non-Proposition 98 General Fund savings by reducing federal TANF support and increasing Proposition 98 support for CalWORKs Stage 2 child care. The proposal allows TANF monies to cover CalWORKs costs that currently are covered by the state General Fund. That is, the basic purpose of the proposal is to free up General Fund monies, thereby decreasing the state's structural shortfall.

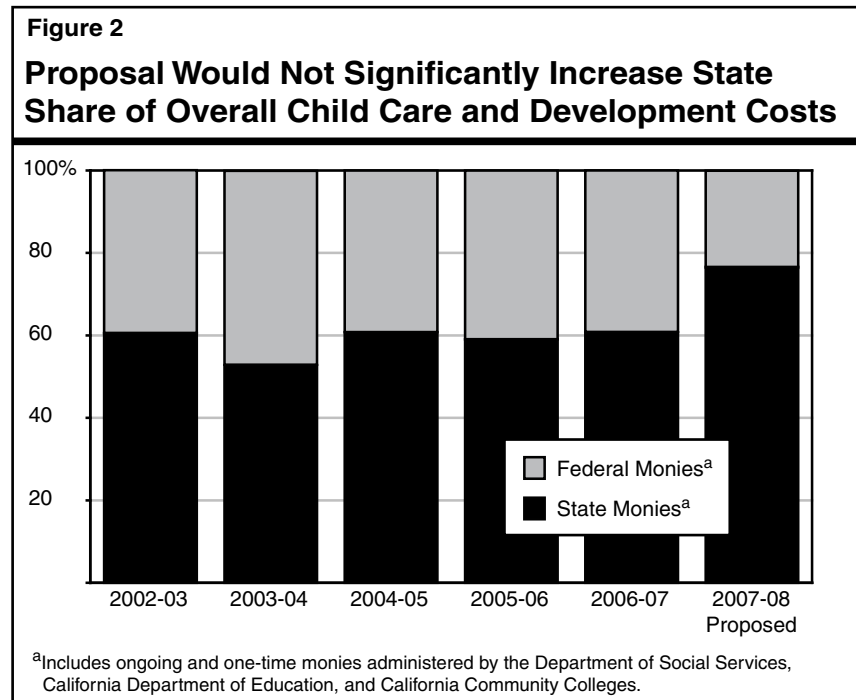
Governor's Proposal Achieves Sizeable General Fund Savings Without Risk. Since the initial implementation of Proposition 98, child care has been deemed a legal and appropriate Proposition 98 expenditure. Moreover, even since the inception of CalWORKs Stage 2 in 1997-98, the state has chosen to designate Proposition 98 monies to cover a portion of the associated costs. In short, the Governor's proposal does not deviate from common practice. Additionally, as shown in Figure 2 (see next page), the Governor's proposal would result in a relatively modest increase in the state's share of overall child care and development costs—increasing from 61 percent of overall costs in 2006-07 to 77 percent in 2007-08.

Governor's Proposal Would Fully Fund Child Care Without Cutting K-12 Programs. Not only does the Governor's proposal achieve sizeable General Fund savings, it does so without cutting either child care or K-12 education. Indeed, under the Governor's budget, K-12 education would receive a healthy increase in Proposition 98 spending—including \$1.9 billion for a 4 percent cost-of-living adjustment—and no K-12 programs would be eliminated or reduced as a result of the proposal.

If Budget Outlook Worsens, Governor's Proposal Would Not Be Enough to Address Structural Shortfall. In the "Proposition 98 Update" section of this chapter, we discuss in detail our updated fiscal forecast. The bottom line is that the budget outlook has worsened and the Legislature likely will need to find additional budget solutions. Thus, in the "Proposi-

tion 98 Priorities” section of this chapter, we recommend the Legislature take a series of actions to reduce Proposition 98 spending in both the current and budget years. The current-year actions we recommend would generate one-time General Fund savings of about \$600 million. By reducing Proposition 98 spending in 2006-07, the minimum guarantee for 2007-08 would drop by a comparable amount. At this lower level, there would not be enough growth in the guarantee to cover baseline adjustments *and* accommodate the proposed increase in Proposition 98 support of child care. Consequently, under this scenario, we would recommend that the Legislature not adopt the child care funding shift. The Governor’s proposal, however, would remain a viable budget solution in future years.

In short, we have no legal, policy, or fiscal concerns with the Governor’s proposal to increase the state’s share of child care costs as a way to achieve General Fund savings. If the budget outlook worsens, we think this proposal simply will not go far enough. As a result, we recommend the Legislature take an entirely different set of actions that would generate more General Fund savings.



EXPANDING CHILD DEVELOPMENT PROGRAMS FOR LOW-INCOME CHILDREN

In the “Proposition 98 Roadmap” section of this chapter, we discuss our fiscal forecast for the next five years—over which time we project Proposition 98 will grow by substantially more than is needed to cover existing program costs. In that section, we provide data showing a large achievement gap between low-income and higher-income students. To help address this achievement gap, we suggest the Legislature consider expanding early childhood education opportunities for low-income children. Specifically, the Legislature could invest in preschool (including wrap around child care) for low-income 3- and 4-year olds and parent education and home visit services for low-income families with children up to age two. Below, we provide data on the number of children currently in state preschool programs and summarize research findings relating to the effects of preschool, particularly for low-income children.

As shown in Figure 3, slightly more than 40 percent of California’s 3- and 4-year olds currently attend preschool. Approximately one-third of children from households earning less than \$33,000 per year are estimated to attend preschool. While some families may choose not to send their children to preschool even if it were available, the current preschool attendance rate is at least partly the result of limited supply. Currently, more than 34,000 children who meet eligibility requirements for state preschool are on CDE’s wait list.

Figure 3

Preschool Participation in California

	California Population	In State Preschool	In Other Preschool (Private or Head Start)	Total in Preschool	Percent in Preschool
Three-year olds	520,000	57,298	55,000	112,298	22%
Four-year olds	523,425	57,575	272,949	330,524	63
Totals	1,043,425	114,873	327,949	442,822	42%

Source: Total state preschool numbers provided by the California Department of Education for the 2005-06 school year. All other figures come from the RAND Corporation and Policy Analysis for California Education 2005 data or are extrapolated from that data.

Returns From Investment in Targeted Preschool Programs. Research shows that high-quality preschool programs for disadvantaged children can have substantial benefits. In particular, research shows that disad-

vantaged children who participate in preschool programs have higher reading achievement, are less likely to repeat the same grade, less likely to use special education, and more likely to complete high school than disadvantaged children who do not attend preschool. In addition, research shows that disadvantaged children who attend preschool are less likely to become involved in the juvenile justice system and have higher adult employment rates and income earnings.

Expansion of Preschool Requires More Support Services, Additional Physical Capacity, and Better Ways to Measure and Monitor Quality. In our "Proposition 98 Roadmap" write-up, we suggest to the Legislature that one priority should be a significant expansion of state preschool slots by 2011-12. An expansion of preschool as large as this would require planning and preparation. Even if funding were available today, not enough preschool facilities or providers are available to meet demand. Before any major expansion of the program, we recommend developing better measures of program quality as well as creating stronger incentives to improve program quality on an ongoing basis. We think these refinements are needed so that greater quantity is not provided at the expense of quality.

Below, we recommend some steps the Legislature can take this year to accommodate a preschool expansion over the next several years. These recommendations are minor changes that do not increase operating expenditures in the budget year. They would, however, help lay the foundation and facilitate the future expansion of quality preschool.

WRAP AROUND CHILD CARE

In 1997-98, California began allowing state preschool providers to offer general child care before and after preschool programs (referred to as "wrap around" child care). Such providers operate as a state preschool part of the day but follow general child care rules and regulations for the remainder of the day. Providers are reimbursed for the state preschool portion of the day and the wrap around portion of the day at the applicable SRRs. The proposed 2007-08 SRRs are \$21 per day per child for preschool and \$13 per day per child for wrap around care (for a maximum full-day reimbursement rate of \$34).

Wrap Around Care Provided to Few Children Statewide. State preschool and wrap around programs serve children from low-income families ages 3 through 5. In 2005-06, just over 6,000 children received wrap around care. This equates to approximately 5 percent of all children in state preschool programs. According to the latest estimates, more than

31,000 eligible, low-income 3- and 4-year olds are currently on the CDE waiting list for wrap around care.

Funding Provided in 2006-07 to Expand Preschool and Wrap Around Child Care. Chapter 211 appropriated \$50 million of ongoing Proposition 98 monies to expand state preschool programs in targeted neighborhoods. This expansion will provide up to 12,667 new preschool slots in the enrollment areas of low-performing elementary schools. Additionally, the bill appropriated \$5 million in one-time monies for wrap around services for children in these preschool classes. This modest expansion will allow up to 1,094 children to receive wrap around care for one year. This is about a 17 percent increase in the number of funded wrap around slots.

New Programs Are More Restrictive. In an attempt to target funds to certain children, Chapter 211 placed additional requirements on providers. In the box on the next page, we discuss the differences between the Chapter 211 programs—commonly referred to as Pre-Kindergarten and Family Literacy (PKFL) programs—and the standard preschool and wrap around programs. The PKFL programs will operate as a state preschool, adhering to many of the existing program requirements, and will be reimbursed at the same per child rates as state preschool. Eligibility for PKFL programs, however, is more restricted than for state preschool.

Approve New Ongoing Monies for Wrap Around Care Without Restrictions

We recommend the Legislature approve the \$5 million in new ongoing monies that the Governor's budget provides for wrap around child care. We recommend approving the proposal because such care promotes preschool attendance among low-income children, which, in turn, has been shown to result in significant long-term benefits. Instead of limiting the ongoing funds for Pre-Kindergarten and Family Literacy (PKFL) wrap around care, we recommend, however, that the Legislature designate the funding for the much larger standard wrap around child care program. This would still allow PKFL providers to receive slots but would reduce administrative burden and ensure the monies are used as quickly and effectively as possible.

The Governor's budget proposal provides \$5 million in new ongoing monies to support wrap around care for children participating in the new PKFL programs. Effectively, the Governor's budget does not expand wrap around child care but instead converts the approximately 1,100 slots funded with one-time monies in 2006-07 into ongoing slots.

Wrap Around Child Care Shown to Promote Preschool Attendance. Because wrap around child care operates on the general child care schedule

New Programs More Restrictive Than Existing Programs

Chapter 211 established the Pre-Kindergarten and Family Literacy (PKFL) program, with the intent to expand state preschool and wrap around child care services. However, it added various restrictions that essentially result in new programs targeting specific geographic areas. The table below compares standard state preschool and wrap around child care to the newly created Chapter 211 programs.

Standard System	Chapter 211 (PKFL) System
Eligibility	
<p>Age: Three and four year olds. 10 percent of participants may be older.</p> <p>Participation: Two-year maximum.</p> <p>Income: Families must earn less than 75 percent of State Median Income (SMI). 10 percent of participants may earn more after initial enrollment.</p> <p>Location: Statewide.</p>	<p>Age: One year prior to enrollment in Kindergarten.</p> <p>Participation: One-year maximum.</p> <p>Income: Families must earn less than 75 percent of SMI. 20 percent of participants may earn more at initial enrollment.</p> <p>Location: Provider must be located in the enrollment area of an elementary school ranked in bottom three deciles of the Academic Performance Index.</p>
Program Details	
<p>Preschool Minimum Day/Year: 3 hours per day and 175 days per year.</p> <p>Wrap Around Minimum Day/Year: 6.5 hours per day. Number of days per year depends on contract.</p> <p>Preschool Curriculum: Includes education, nutrition, health and social services.</p> <p>Wrap Around Standards: Must comply with all Title V child care requirements.</p>	<p>Preschool Minimum Day/Year: "Part-day" not defined. 175-180 days per year.</p> <p>Wrap Around Minimum Day/Year: Minimum hours per day not specifically defined. Minimum of 246 days per year.</p> <p>Preschool Curriculum: Same as state preschool with added requirement of parental involvement and education.</p> <p>Wrap Around Standards: Same as standard system.</p>
Funding (Proposed 2007-08 Rates)	
<p>Preschool Rate: \$21.12 per day per child.</p> <p>Wrap Around Rate: \$13.10 per day per child.</p>	<p>Preschool Rate: Same per child rates as standard. \$2,500 per classroom per year.</p> <p>Wrap Around Rate: Same as standard system.</p>

(before and after school and all day on school holidays) and is provided at the preschool site, it promotes preschool attendance of children from low-income families by allowing their parents to maintain employment. Research indicates that a successful expansion of preschool (especially targeting low-income students) typically requires a proportionate expansion of wrap around child care. In essence, an investment in wrap around child care is an investment in preschool.

New Eligibility Restrictions Increase Administrative Burden. The unique specifications of the new PKFL programs requires CDE to issue a separate request for applications and to appropriate and track PKFL funds separately from the standard state preschool and wrap around child care programs. This not only creates ongoing work in tracking and reporting for state staff and providers but can reduce the potential impact of the funds. For example, because of the special PKFL requirements, little, if any, of the funds will be used in 2006-07—even though some 30,000 low-income children are on waiting lists for wrap around care.

All Low-Income Children Should Be Eligible for New Ongoing Slots. We believe the \$5 million in new ongoing funds can be more efficiently used if they are available to any otherwise eligible low-income child. That is, we think the Legislature should designate the new funding for the standard wrap around child care program. (Under this approach, PKFL providers still could apply for slots.) By expanding the standard wrap around child care, the Legislature ensures a timely fund release and offering of services to approximately 1,000 low-income, disadvantaged children currently on the state waiting list for wrap around care.

CHILD DEVELOPMENT FACILITIES

In this section, we discuss the state's existing child care facility programs and recommend improvements. These recommendations are intended to ensure that existing facility programs are well administered and effective. We think such refinements are important for maintaining existing program capacity and are especially critical if the Legislature chooses to expand future capacity.

The CDE currently offers two programs intended to help child care and preschool providers purchase and maintain facilities. The Child Care Facilities Revolving Fund (CCFRF) is a loan program intended to increase program capacity. It does this by helping providers purchase portable facilities and make major renovations and repairs to existing facilities. By comparison, the Facilities Renovation and Repair (FRR) program is not intended to increase capacity but rather sustain existing capacity. It does

so by awarding grants to existing providers for minor repairs needed to meet health and safety requirements.

The CCFRF Program. Chapter 299, Statutes of 1997 (AB 1578, Migden), established the CCFRF loan-to-purchase program. The program provides no-interest loans of up to \$150,000 per portable facility. Loan recipients have an initial three years to use the loan and then ten years to repay it. Loan repayments are made to the fund, such that there is a revolving income stream (in addition to any monies the state might provide into, or take out of, the fund through the annual budget process). Since the fund's inception, the state has awarded 590 CCFRF contracts—equating to roughly the same number of portable facilities—for a potential increase in capacity of over 20,000 program slots.

The FRR Program. The FRR fund provides grants of up to \$1,000 for minor renovation and repair of existing buildings. Most of these projects are intended to meet health and safety requirements and/or comply with Americans with Disabilities Act (ADA) requirements. Recipients have up to two years to spend the grants. There is no income source for this program other than annual budget appropriations. Historically, all monies appropriated are expended in the same year.

Approve Proposal to Transfer CCFRF Monies to FRR Program

Given the large carryover balances in the Child Care Facilities Revolving Fund (CCFRF) program and high demand for the Facilities Renovation and Repair (FRR) program, we recommend the Legislature approve the Governor's proposal to use up to \$5 million from CCFRF for the FRR program.

For the second consecutive year, the Governor proposes using up to \$5 million in existing CCFRF monies for FRR grants. Given the large carryover balances in the CCFRF program and high demand for the FRR program, we recommend approving this proposal.

Large Carryover Balances in CCFRF Program. The CCFRF has consistently carried a healthy balance over recent years. The fund balance so routinely exceeds demand that the Legislature has reverted funds from CCFRF to support other K-12 programs four times since 2002—for a total reversion of \$93.2 million. Heading into 2007-08, CDE estimates that CCFRF will have a beginning balance of almost \$52 million. The CCFRF has sufficient monies available in 2007-08 to award all anticipated loans (even those expected due to the implementation of Chapter 211) and still use \$5 million in support of the FRR program.

High Demand for FRR Grants. While the CCFRF program has a large carryover balance and no waiting list, the FRR program consistently has

a long waiting list. For example, in 2005, the last time applications were accepted for FRR grants, requests for funding were three times greater than available monies (374 applications were received and 132 grants were awarded). The CDE is expecting a similar response when applications for the \$7.5 million available for FRR grants in 2006-07 are accepted in spring 2007. Given such high demand, the Legislature authorized in 2006-07 the spending of up to \$5 million in CCFRF monies for FRR grants. We recommend it do the same thing for 2007-08.

Reexamine CCFRF's Major Renovation and Repair Program

We recommend the Legislature direct the California Department of Education (CDE) to report at spring budget hearings on the status of the Child Care Facilities Revolving Fund's major renovation and repair loan program. Specifically, we recommend CDE explain why the program has not yet been implemented and present options for expediting that process. As one of these options, we recommend the Legislature consider shifting program administration back to CDE's School Facilities Division.

In 2001, the Legislature authorized the use of CCFRF loans for major renovations and repairs. It did so because many providers already own facilities but either are not able to use all existing capacity because of needed repairs or else could expand capacity with major renovations. Additionally, these major renovation and repair (MRR) projects tend to be both cheaper and faster than new construction projects.

After Six Years, CDE Still Has Not Implemented Program. After six years, the MRR program still is not in operation. The CDE claims this is because of limited staff resources and legal complexities that relate to safeguarding the state's interests. Given these issues, CDE has yet to create the needed regulations.

Legislature Should Reexamine Program. We recommend the Legislature require CDE to testify at spring hearings on the current status of the implementation of the MRR program. The CDE should explain its delay in implementing the program and present options for improving the program and/or speeding implementation. As part of the Legislature's consideration of options for refining the program, we recommend it assess the benefit of shifting program responsibility from CDE's Child Development Division to its School Facilities Planning Division. (When the CCFRF program was first created, it was administered by the School Facilities Division.)

CHILD CARE AND DEVELOPMENT QUALITY

Despite spending over \$3.7 billion a year on subsidized care and child development programs for more than 900,000 children and their families, the state currently does not uniformly measure and assess program quality. Lacking both a clear definition of quality and an agreed-upon method for measuring it, the Legislature cannot meaningfully assess the effectiveness of the state's existing network of child care and development programs. These issues of program quality become even more important when considering program expansions.

California Is Concerned About Quality but Efforts Are Not Coordinated

Although many public and private organizations in California are involved in operating, coordinating, and regulating child care and development programs, no common definition of program quality exists. Instead, organizations tend to use and apply different definitions of program quality and standards.

State Agencies Apply Different Standards. Among state agencies, the Community Care Licensing Division (CCL) of DSS enforces minimum child care licensing standards, primarily in the areas of health and safety. The DSS also administers the Title 22 subsidized child care program, for which providers, whether licensed or license-exempt, are expected to adhere to a set of standards. In contrast, CDE administers the Title 5 program for which providers, all of whom are licensed, must adhere to Title 5 standards. These Title 5 standards are typically more stringent than either CCL licensing standards or Title 22 standards.

Nonstate Agencies Apply Different Standards. In addition to these state agencies, many federal, local, and private child care and development organizations working in California have their own definitions of program quality and standards. Head Start—the federal early childhood education program—and First 5—a state and federally funded local program—each has unique definitions of quality. Additionally, numerous organizations review child care providers—including the National Association for the Education of Young Children, which offers highly coveted program accreditation. Somewhat ironically, because of the confusion surrounding program quality and standards, many local councils have tried to coordinate quality efforts in their area, and, in doing so, have developed their own definitions of quality. This means California does not have a widely agreed-upon definition of quality or standards.

No Way to Measure Quality, No Information for Parents to Use in Assessing Quality. As described in our report, *Developing Safety and Quality Ratings for Child Care* (January 2007), no consistent, comparable information about the quality of child care providers is publicly available statewide. Neither CCL, DSS, nor CDE publicly disseminate any ratings or assessments of provider quality. The CCL health and safety inspection results are available only if parents call CCL and request results for specific providers. Similarly, CDE conducts quality assessments of Title 5 providers but uses the information for internal purposes only and the assessment results are not available to parents.

No Incentives for Providers to Improve Quality, No Rewards for Those That Achieve High Quality. California currently uses two rate structures to reimburse providers. Title 22 providers are compensated using a regional market rate (RMR), whereas Title 5 providers are compensated according to SRR. (The RMRs vary greatly by region, age of the child, and type of provider. Currently, the rates range from \$23 per child per day in the lowest cost region to \$56 in the highest cost region. By comparison, SRR for 2007-08 is \$34 per child per day throughout the state.) Neither of the current rate structures reimburses providers for actual costs or rewards them for providing a higher-quality program. Thus, a low-quality program receives the same compensation as a high-quality program. (For more information on how providers are reimbursed, please refer to the child care sections of the *Analysis of the Budget Bill* for 2005-06 and 2006-07.)

No Way to Evaluate Effectiveness of Quality Funds. The federal CCDF program requires states to spend not less than 4 percent of aggregate spending on activities designed to improve the quality and availability of child care. In response to this requirement, California currently spends a total of roughly \$100 million each year for more than 40 “quality improvement” programs. Between 2001 and 2003, CDE hired outside consultants to evaluate 11 of these programs (at a total cost of \$3.4 million). Although these evaluations try to determine if the program is meeting its stated objectives and provide some recommendations for specific program improvements, they do not assess whether the program actually is “improving the quality and availability of child care.” This again is because the state does not have clear goals against which the programs can be measured. In short, despite investing approximately \$700 million in “quality activities” over the past seven years, California cannot determine whether the quality and availability of child care has improved over that time.

A Child Care and Development Quality Plan

We recommend the Legislature convene a working group of relevant stakeholders and direct it to create a strategic child care and development quality plan by March 1, 2008.

Academic research as well as the experience of 13 other states suggests that a child care and development quality plan is a critical first step toward improving program quality. Thus, we recommend the Legislature convene a working group to develop a comprehensive integrated plan for achieving long-term improvement in child care and development programs. Consistent with the lessons learned by other states, we recommend such a plan include clear objectives, highly publicized measurements of success, and provider support programs aligned to program standards. We recognize that developing such a plan would be an intensive task requiring significant input and time and that full implementation of that strategic plan would realistically take several years. We think beginning the planning process now is important for spurring improvement in existing programs and becomes even more important if the state decides to undertake any significant program expansions over the next few years.

An Inclusive, Collaborative Group Likely to Yield More Enduring Plan. We recommend the working group include staff from CCL, DSS, CDE, legislative staff, and the administration as well as representatives from local agencies, parents, providers, and advocacy groups. Inclusion of all these parties would promote familiarity, understanding, buy-in, and acceptance of the final plan. Such an inclusive working group also would combine state-level experts—those knowledgeable of state standards and regulations—with providers and parents—those with real world experience operating and using child care and development programs. Thus, such a group would be more likely to balance the needs of state and local groups. Moreover, such a broadly representative group would be better able to align quality expectations and standards across programs and agencies. For instance, preschool expectations could be more easily aligned with kindergarten curriculum standards.

Plan Should Be Based on Proven Best Practices Tailored to California's Unique and Diverse Needs. The working group could benefit from the wealth of quality definitions, measurement and rating systems, incentive programs, and other best practices that have already been researched and tested across the country. The group, for example, could build on the frameworks used by the 13 other states that have developed quality rating systems, CDE's Desired Results program, and/or the regional quality rating programs in Los Angeles and San Francisco.

Key Elements of a Plan

Below we describe of the key elements of a child care and development quality plan.

Define Program Quality. Any quality plan should include a clear definition of quality. Specifically, the working group should define the factors of quality to be assessed (for example, health and safety, academic curriculum, staff/child interactions, and parental involvement). The working group also should define tiered levels of quality for each factor. This would allow the state to distinguish among providers and establish clear goals for providers aiming to improve their programs.

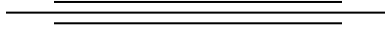
Develop Method for Measuring and Rating Quality. Any quality plan should develop a method by which to regularly and consistently measure quality and publicize information about those measures. Thus, the working group should propose a method for measuring each of the quality factors it has identified and defined. In selecting a method, the working group should consider available resources, the cost-effectiveness of each method, and the ability of parents and the community to easily understand and use the resulting information. The working group also should consider when to update the data, how to synthesize it for public consumption, and how to release it such that information sharing is maximized. (For a more detailed discussion of measuring and rating quality, please see our report *Developing Safety and Quality Ratings for Childcare*, January 2007.)

Create Stronger Incentives for Providers to Improve Quality. A quality plan should create incentives, including appropriate reimbursement and rewards, for different levels of quality. We think the working group should consider creating one reimbursement system for all child care and development providers that compensates providers based on cost and quality. We recommend the reimbursement rate be tiered—with providers offering higher-quality services receiving higher compensation. The working group should build on the extensive work already done in this area. Over 30 states already have tiered reimbursement rate structures tied to quality.

Reevaluate Use of Quality Improvement Monies. Lastly, a plan should identify appropriate uses of state funds to support program quality. Specifically, the working group should review how the state is spending its quality improvement monies. Once quality has been defined and performance measures developed, the working group should assess the existing programs against them and determine if any program changes or funding reallocations are needed.

In sum, California has neither a common definition of program quality nor a means to measure it. As a result, parents have difficulty obtaining

information on provider quality, providers have difficulty knowing how to improve, and the state has difficulty assessing and rewarding quality improvements. In response to these shortcomings, we recommend the Legislature convene a working group to create a child care and development plan that would define, measure, publicize, and reward program quality.



QUALITY EDUCATION INVESTMENT ACT

The approach taken to school reform in the Quality Education Investment Act (QEIA) has several shortcomings that we think the Legislature could address by enacting relatively modest program changes. Specifically, we recommend the Legislature build on the existing experimental features of the QEIA program by allowing participating schools to select one of three teacher-oriented reform options. This would have the double benefit of allowing schools to select the reform most likely to benefit their students while allowing the state to study the effectiveness of several reform strategies. Later in this section, we also recommend the Legislature identify QEIA payments in the annual education trailer bill to ensure transparency.

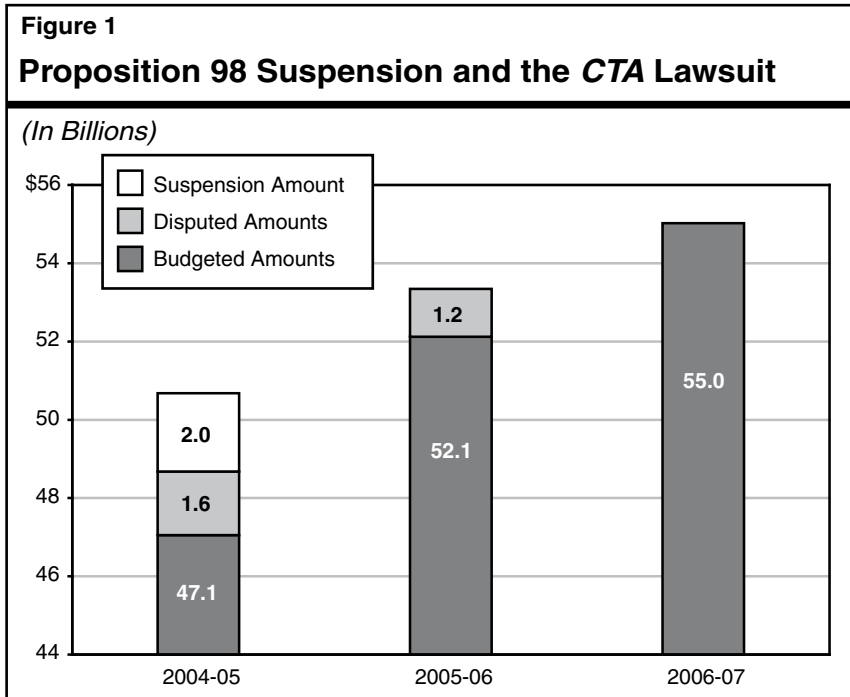
Introduction

This write-up contains six parts. The first three parts provide background on the recent California Teachers Association (CTA) lawsuit, the resulting settlement reached by CTA and the administration, and the subsequent enactment of QEIA, which allocates settlement funds to particular programs. The fourth part highlights shortcomings of the QEIA program as currently structured. The fifth part identifies some modest changes the Legislature could adopt to address these concerns and significantly improve the potential benefits of the program. The last part discusses the accounting and tracking of QEIA monies.

Lawsuit Sought Additional \$2.8 Billion for K-14 Education

In 2004-05, the state suspended the Proposition 98 minimum guarantee. The suspension was effectuated by Chapter 213, Statutes of 2004 (SB 1101, Budget Committee), which stated that funding for K-14 education in that year was to be \$2 billion lower than the guarantee. Final General Fund revenues for 2004-05 came in substantially higher than initially assumed, thereby raising the Proposition 98 minimum guarantee. As a result, the 2004-05 funding level ended up being \$3.6 billion lower than the guarantee—or \$1.6 billion lower than the designated Chapter 213 level.

Because the Proposition 98 minimum guarantee is calculated based on the prior-year funding level, the 2005-06 funding level also was affected—being \$1.2 billion less than what it would have been had the Chapter 213 level been met. As shown in Figure 1, the difference between the Chapter 213 levels and funded levels totaled \$2.8 billion over the two years (see nearby box for why this number has changed over time). In August 2005, CTA sued the Governor regarding his application of Chapter 213, which it claimed resulted in a loss of \$2.8 billion for K-14 education.



K-14 Education to Receive Additional \$2.8 Billion Over Next Seven Years

In May 2006, the Governor decided to settle with CTA—agreeing to provide the additional \$2.8 billion over a seven-year period (2007-08 through 2013-14)—\$2.5 billion for K-12 education and approximately \$300 million for the California Community Colleges (CCC). In September 2006, the Governor signed legislation reflecting the terms of the settlement. As specified in the settlement, Chapter 751, Statutes of 2006 (SB 1133, Torlakson), designates a first payment of \$300 million in 2007-08 (\$268 million for K-12 education and \$32 million for CCC). In each subsequent year, Chapter 751 designates payments of \$450 million (\$402 million for K-12

Technical Note on the Numbers

Because the disagreement over Chapter 213, Statutes of 2004, (SB 1101, Budget Committee), is ultimately linked with the Proposition 98 minimum guarantee and the guarantees for 2004-05 and 2005-06 have been fluctuating based on updated revenue data, the dollar amount at stake in the disagreement also has been fluctuating. Early last year, the amount was estimated at \$3.2 billion (\$1.7 billion for 2004-05 and \$1.5 billion for 2005-06). When the 2006-07 budget was enacted, the amount was estimated at \$2.9 billion (\$1.6 billion for 2004-05 and \$1.3 billion for 2005-06). The underlying data have since been updated, with the amount at stake now estimated at \$2.8 billion (\$1.6 billion for 2004-05 and \$1.2 billion for 2005-06). This most recent revision is the result of approximately \$75 million more-than-expected Proposition 98 funding now being provided for 2005-06, thereby dropping the outstanding obligation for that year by a like amount. Given the applicable revenue data are now finalized, the \$2.8 billion amount should no longer fluctuate.

education and \$48 million for CCC) until the full obligation has been met. Figure 2 shows this payment schedule.

Figure 2				
Settlement Payment Schedule				
<i>(In Millions)</i>				
	2007-08	2008-09 Through 2012-13^a	2013-14	Total Payments
K-12 education	\$268	\$402	\$265	\$2,543
Community colleges	32	48 ^b	32	304
Totals	\$300	\$450	\$297	\$2,847

a Annual payments.

b Includes \$38 million for career technical education and \$10 million for block grants.

Payments on Top of Ongoing Proposition 98 Funding. These annual payments will count toward the agreed-upon 2004-05 and 2005-06 Proposition 98 obligations. State funding for 2006-07 assumed these obligations

already had been fulfilled. As a result, the state essentially has erased any ongoing effect of the 2004-05 Proposition 98 suspension—leaving only the “back” payments to 2004-05 and 2005-06. These annual settlement payments therefore will be in addition to otherwise required ongoing Proposition 98 funding.

Funding Source Identified Only for First Few Payments. The state currently is in the process of selling approximately \$900 million in tobacco securitization bonds to fund the first few settlement payments. Once these bond monies are exhausted, the General Fund will likely be needed to pay remaining obligations.

Funds Designated for Major New Program. The settlement itself did not specify how the additional monies were to be used. The Legislature therefore is not bound by court order to use the funds to support any specific education activities. Chapter 751, however, statutorily established the QEIA program. The act designates that the funds are primarily to be used for class size reduction (CSR) in grades 4 through 12 and expanding career technical education in community colleges. Below, we describe the K-12 provisions of QEIA. For more information about the major community college provisions, please see the “Career Technical Education” write-up in the “Crosscutting Issues” section of this chapter.

K-12 Monies Support New CSR Initiative

In this section, we describe QEIA’s eligibility criteria, selection process, funding provisions, “regular” program requirements, and “alternative” program requirements for K-12 education. We also provide a timeline showing the progression of required start-up activities.

Almost 1,500 Schools Eligible for QEIA Funds. Public schools, including charter schools, are eligible to receive QEIA funds if they are ranked in deciles 1 or 2 of the 2005 Academic Performance Index (API). Based on this criterion, 1,455 schools are eligible for funding. Figure 3 shows the number of eligible schools by county. (Regulations specify that schools with less than 99 students are not eligible because of the statistical uncertainty of their API scores.)

Random Draw at State Level, Districts Prioritize at Local Level. The act contains little direction on how eligible schools are to be selected. It specifies only that the Superintendent of Public Instruction SPI and Secretary for Education are jointly to recommend schools to be funded, ensuring selected schools are representative of geographic areas of the state and grade levels. Regulations require districts to submit applications on behalf of schools and rank them in priority order for funding. The state will then randomly draw district slots for the regular and alternative programs, and top-ranked schools will be selected. Funding is sufficient to support about 1 in 3 eligible schools.

Figure 3**Eligible QEIA Schools by County**

None	1-9	10+	50+
Alpine	Butte (7)	San Joaquin (45)	Los Angeles (409)
Amador	Sonoma (7)	Tulare (44)	San Bernardino (110)
Calaveras	Mendocino (6)	Contra Costa (38)	Fresno (93)
Glenn	Yuba (5)	Monterey (35)	Riverside (84)
Lassen	Lake (4)	Santa Clara (33)	San Diego (78)
Mariposa	Yolo (4)	Ventura (26)	Kern (75)
Modoc	Sutter (3)	San Francisco (23)	Alameda (67)
Nevada	Colusa (2)	Santa Cruz (18)	Orange (59)
Placer	Humboldt (2)	Stanislaus (17)	Sacramento (55)
Plumas	Napa (2)	Kings (15)	
Sierra	San Benito (2)	Solano (15)	
Tehama	Siskiyou (2)	Merced (14)	
Trinity	Del Norte (1)	San Mateo (14)	
Tuolumne	El Dorado (1)	Imperial (13)	
	Inyo (1)	Santa Barbara (12)	
	Marin (1)	Madera (10)	
	Mono (1)		
	San Luis Obispo (1)		
	Shasta (1)		

High Per-Pupil Funding Rates. For schools chosen, QEIA designates annual funding rates of \$500 per K-3 pupil, \$900 per grades 4 through 8 pupil, and \$1,000 per grades 9 through 12 pupil. Figure 4 shows how many students are to be funded in each of these grade spans. The act allows first-year funding (\$300 million) to be used for facilities—if those facilities are needed to meet the program’s CSR requirements. In general, all funds provided on behalf of a QEIA school must be spent at that school.

Figure 4**Estimated Funding Allocations by Grade Span**

Grade Levels:	K-3	4-8	9-12	Totals
Number of students	160,000	209,000	133,900	502,900
Per-pupil funding rate	\$500	\$900	\$1,000	—
Total funding	\$80,000,000	\$188,100,000	\$133,900,000	\$402,000,000

Student Achievement Goals Similar to Regular Standards. Every school in the state is expected to meet annual student achievement growth targets (equal to 5 percent of the difference between its current API score and the state target of 800). The QEIA program has a similar achievement standard—requiring that participating schools exceed their API growth target averaged over the second through fourth years of the program. (“Exceeding” typically is defined as at least one point above the target.) Beginning in the fifth year of the program, QEIA schools are expected to meet their annual API growth targets, but they continue receiving funding even if they fail to meet those targets. Instead of a fiscal repercussion, they become subject to review and assistance under the state’s other intervention program for low-performing schools (the High Priority Schools Grant Program, or HPSGP).

Strict Regular Program Requirements. Schools that receive QEIA funding and participate in the regular program must meet the following requirements:

- **Maintain Class Size in Grades K-3 at No More Than 20 Students.** Schools are required to maintain their participation in the state’s K-3 CSR program. That program provides incentive funding (\$1,066 per pupil) for schools to maintain K-3 classes at no more than 20 students. The 20-student cap applies to each class (that is, no class above 20 students is eligible for any funding). Virtually all districts already participate in this program.
- **Reduce Class Size in Grades 4 through 12 to an Average of No More Than 25 Students.** The most significant QEIA requirement is to reduce average class size in grades 4 through 12 to 25 students, or by 5 students, whichever is less. (As their baseline, schools are to use the 2005-06 or 2006-07 school year, whichever has the lower average class size.) The average class size is calculated by grade level, but no class may have more than 27 students. The requirement applies to all grades 4 through 8 multi-subject (or self-contained) classrooms and all grades 4 through 12 English language arts, reading, mathematics, science, history, and social science classes. Other classes may not increase class size above their 2005-06 level.
- **Reduce High School Pupil-to-Counselor Ratio.** High schools must ensure they have at least 1 counselor for every 300 students. Counselors must hold a state certificate authorizing them to provide pupil personnel services.
- **Ensure All Teachers Highly Qualified.** Schools must ensure that all their teachers are highly qualified, as defined in federal law. To be highly qualified, teachers must demonstrate they are com-

petent in the subjects they teach. Elementary school teachers are required to demonstrate competency by passing a state-approved exam whereas secondary school teachers may demonstrate competency either by passing an exam or completing an academic major (or its coursework equivalent), graduate degree, or a program of advanced certification in the applicable subject(s). (Teachers hired before 2002-03 had the additional option of demonstrating competency based a “high objective uniform state standard of evaluation.”)

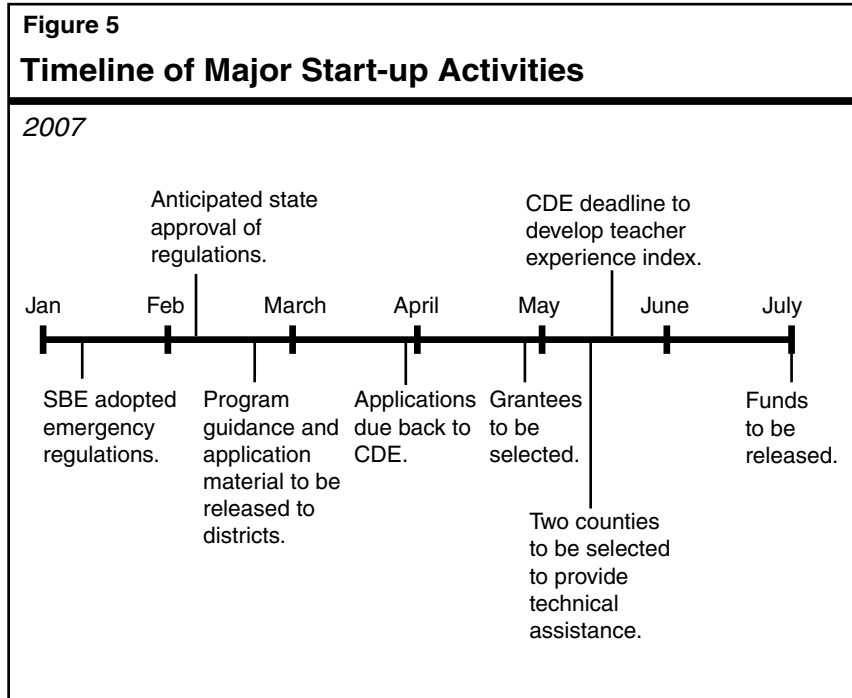
- ***Ensure No Disparity in Teacher Experience Among QEIA and Non-QEIA Schools.*** The level of teacher experience at participating schools must equal or exceed that at other district schools. Schools need to calculate and report teacher experience using a uniform process that the California Department of Education (CDE) is to develop.

Strict Timeline Requirements. If one or more of these program requirements are not met, schools have until the end of the subsequent school year to meet them or else risk losing funding. Specifically, schools must be at least one-third the way toward meeting the input-oriented requirements by the end of the second year of the program. (For example, they must have reduced average class size by at least 1.7 students—one-third of the 5 student goal.) By the end of the second year, schools also must meet all the requirements of the Williams settlement (which relate to teacher qualifications, instructional materials, and school facilities), and school districts must ensure that each administrator in a funded school has “exemplary qualifications and experience.” Schools must be two-thirds of the way toward meeting QEIA requirements by the end of the third year of the program and then achieve full implementation by the end of the fourth year of the program. At that time, all funded schools also must have increased pupil attendance and high schools must have increased graduation rates. In addition, schools must provide professional development to at least one-third of their teachers annually.

Strict Alternative Program Prerequisites. School districts may apply on behalf of schools to use an alternative program. Up to 15 percent of the pupils funded under QEIA may be served by one of these alternative programs. High schools that are unable to decrease class sizes because of facility constraints receive priority for the use of alternative programs. To be approved for such a program, a school district must demonstrate that the alternative program would result in a higher level of academic achievement than the regular QEIA program. The proposed alternative program also must be based on sound scientifically based research and reliable data. Schools approved for alternative programs must meet the

same general progress requirements as schools using regular programs or else risk losing funding.

Next Six Months Critical Oversight Period. Figure 5 provides a timeline of required start-up activities. As shown, CDE will be making several critical decisions over the next six months—including issuing application guidelines, selecting which schools to fund, and creating a teacher experience index. Thus, the next several months will be a critical period for conducting oversight activities.



QEIA Approach to School Reform Has Several Shortcomings

We think the QEIA program has five major shortcomings, which we discuss below. In the following section, we recommend a few small changes to the program that we think would address some of these shortcomings and significantly improve its potential benefits.

School-Based Approach Already Found Unlikely to Work. As a school-based reform program, QEIA perpetuates an approach already found unlikely to work. Independent evaluations of the state's existing school-based intervention programs show lackluster results, with participating schools generally not performing better than nonparticipating

schools. Across a series of evaluations of the state's Immediate Intervention/Underperforming Schools Program and HPSGP, the American Institutes for Research found virtually no difference in student achievement between participating and nonparticipating schools. The evaluations of both programs suggest that school-based interventions might fall short of expected results because they ignore the critical role of the district. District leaders, for example, hire and assign school administrators and teaching staff, negotiate the terms of collective bargaining agreements, and determine how to distribute discretionary resources. The QEIA program, as with the state's other school-based intervention programs, do not attempt to influence those types of decisions.

Decile Approach Too Limited. Although decile rank can show that some schools are scoring lower than other schools, it fails to distinguish between schools that are making great strides in improving student performance and those whose performance is not only low but worsening. For example, the average growth of all deciles 1 and 2 schools between 2002-03 and 2005-06 was 23 API points, but 35 percent of these schools had gains of more than 100 points. The QEIA program, however, treats all these schools the same—presuming that all are “low-performing” and all are equally needing and deserving of additional funding.

Top-Down, One-Size-Fits-All Approach Can Undermine Local Reform Efforts. The QEIA approach also can undermine local reform efforts. Over the last several years, many low-decile schools have received special state funding to develop and implement local improvement plans. Other low-decile schools have initiated their own systemic reforms tailored to local needs. Rather than trying to bolster existing reform efforts, QEIA creates a new top-down, one-size-fits-all, highly prescriptive reform program that assumes all low-decile schools can benefit from the same class size reduction initiative. Such an approach can disrupt and/or undermine local reforms—some of which might have the potential to be much more effective at improving student achievement.

Funding Approach Creates New Inequities. By providing such high per-pupil funding rates to roughly 5 percent of schools, QEIA creates new funding inequities. Over the life of the program, for example, a mid-size decile 1 high school would receive \$14 million in QEIA funding whereas neighboring schools, even those serving equally disadvantaged students, would receive no QEIA monies. Such large funding inequities run counter to the Legislature's longstanding efforts to reduce such disparities. In 2006, for example, the Legislature provided a \$350 million augmentation to further equalize school districts' per pupil general purpose monies (or revenue limits) and a \$350 million augmentation to further equalize Economic Impact Aid per-pupil funding rates.

Also Creates Significant Out-Year Cost Pressures. Although QEIA is set to end in 2014-15, it creates large out-year cost pressures. Given QEIA schools are required to implement a major CSR initiative, ending abruptly would create staffing and facility issues. Thus, participating schools likely will seek to sustain the program. In addition, (1) eligible QEIA schools that were not funded and (2) higher performing schools serving equally disadvantaged students that were not eligible under the initial rules very likely will seek funding in future years.

Small Changes Could Yield Significant Benefits

We recommend the Legislature build on the existing experimental features of the Quality Education Investment Act program. Specifically, we recommend (1) allowing schools to self-select themselves into one of three reform groups and (2) funding an independent evaluator to assess the performance of the groups over the seven-year life of the program.

Although addressing all of the above shortcomings would require a different approach to school reform, the Legislature could address some of the shortcomings by making relatively modest changes to the basic QEIA structure. Below, we describe these recommended changes.

Allow Schools to Select One of Three Teacher-Oriented Reform Options. We think the potential benefits of QEIA would be maximized if it were run as a pilot program. Specifically, as described in Figure 6, we recommend the Legislature allow participating schools to pick one of three reform strategies (with an independent evaluator ensuring that a sufficient number of schools are in each group to yield statistically significant findings). One group would adhere to the existing QEIA program requirements and implement CSR in grades 4 through 12. A second group would be required to hire the same number of teachers as under the QEIA program but be allowed to deploy these teachers as it thought fit. For example, it could hire additional teachers to be reading specialists, language specialists, or on-site professional development coaches. A third group would be exempt from most QEIA requirements. Instead, we suggest it be allowed to use QEIA funds for any teacher quality initiative—including new teacher recruitment or retention programs, compensation bonuses, enhancements to working conditions, or additional professional development opportunities.

Fund Independent Evaluator. Chapter 751 requires CDE to perform, or contract with an independent evaluator to perform, two interim and one final evaluation. The interim reports are due January 1 of 2010 and 2012, with the final report due January 1, 2014. The reports are to include student achievement data. We recommend the Legislature provide \$250,000 each year of the program, beginning in 2007-08, to fund these evaluations

and require CDE to contract with an external evaluator. The evaluator would play an important role in setting up the reform groups, identifying an appropriate control group, collecting needed achievement and implementation data, conducting site visits and interviews, and preparing the required reports.

Small Changes Could Yield Significant Benefits. These relatively modest changes could significantly improve the program by ensuring that the state learned as much as possible from the \$2.5 billion investment in K-12 education. By having at least a few different types of reforms implemented, the state could begin comparing which types of strategies appear to work best for which types of schools and students. Rather than allowing only 15 percent of schools to select an alternative reform program, the experimental approach offers considerably more flexibility while simultaneously ensuring that the various reform options can be studied and systemic lessons gleaned from them. Having most schools able to self-select their reform strategy also would help cultivate local support for the endeavor. Finally, officially declaring the program an experiment could reduce out-year cost pressures while allowing the state to use the findings of the experiment to determine which future investments likely would be worthwhile.

Figure 6

**Running QEIA as Pilot Program
Would Maximize Benefits**

Reform Group 1	Reform Group 2	Reform Group 3	Control Group
Must adhere to all QEIA requirements—including class size reduction (CSR) requirements.	Exempt from CSR requirements but require schools to hire same number of teachers as otherwise required under QEIA. Allow schools/districts to deploy teachers as they see fit.	Exempt from essentially all QEIA requirements. Require schools/districts to use QEIA funds for any teacher quality initiative—including teacher recruitment, retention, compensation, and professional development initiatives.	A group of comparable schools that receive no QEIA funding and participate in no state intervention program.

In sum, we think QEIA's approach to school reform has several shortcomings that the Legislature could address by enacting relatively modest program changes. Specifically, we recommend the Legislature build on the existing experimental features of the QEIA program by allowing participating schools to select one of three reform options. This would have the double benefit of allowing schools to select the reform most likely to

benefit their students while allowing the state to study the effectiveness of several reform strategies.

Make Accounting of QEIA Monies More Transparent, Accurate

We recommend the Legislature reflect the Quality Education Investment Act payments in the annual education trailer bill. Over the life of the program, this would enhance transparency—making the payments easier for all parties to track.

Below, we describe the administration's treatment of QEIA monies. From an accounting perspective, this treatment both lacks transparency and distorts the state's budget picture.

Lacks Transparency. As described above, the state is to make its first QEIA payment in 2007-08. Consistent with the intent of the settlement, the administration has decided to attribute the payment back to 2004-05 on the grounds that it is meant to satisfy the Proposition 98 obligation for that year. That fiscal year, however, already is "closed" from a budget accounting perspective. Thus, the payment is not showing up in 2004-05. For that matter, it is not showing up in any year but rather is accounted for through a downward adjustment to the prior-year carry-in balance. As a result of this treatment, the \$300 million payment does not appear as a budget-year expenditure—even though the funds are being used to support programs in 2007-08. Such treatment also means that interested parties cannot directly "find" the monies in any budget-year document. It does not appear in the budget bill, the proposed education trailer bill, or any of the Proposition 98 budget documents the administration routinely prepares. In short, such accounting treatment lacks transparency from both an overall budget perspective and an education perspective.

Distorts Budget Picture. Whereas the administration does not reflect the \$300 million QEIA payment as a budget-year expenditure, it does reflect related tobacco securitization bond monies as budget-year revenue. That is, the budget reflects QEIA-related revenue but not QEIA-related expenditures. As a result of such accounting treatment, the 2007-08 operating shortfall is underestimated by \$300 million.

Enhance Transparency, Ensure Accuracy. We recommend the Legislature include language in the annual education trailer bill that would identify the amount of the QEIA payment being made in that year. This would greatly improve the transparency of QEIA payments, thereby helping all parties track the payments over the life of the seven-year program. We also would encourage the Legislature to work with the administration to develop a method for reflecting QEIA revenues and expenditures that would result in a more accurate portrayal of the state's operating condition.

ENGLISH LEARNERS

Data from several statewide assessments suggest there is a significant gap between the academic achievement of English learner (EL) students and their English-speaking peers. We recommend the Legislature fund an evaluation to identify “best practices” in educating EL students. We also recommend improving the state’s assessment system so EL student progress can be measured and tracked.

Roughly one in four children in California’s public K-12 system is classified as an EL student, defined in statute as “a child who does not speak English or whose native language is not English and who is not currently able to perform ordinary classroom work in English.” As discussed in a previous section, “A Proposition 98 Roadmap,” a significant performance gap exists between EL and English-speaking students. The state faces considerable challenges in closing this gap and addressing the needs of its 1.6 million EL students.

In this section, we first summarize EL students’ demographics and academic performance and then provide an overview of major EL issues. This EL overview examines various issues relating to funding, instructional approaches, instructional materials, teacher quality, and assessment and accountability. It also contains various recommendations for some next steps the Legislature can take to help improve student outcomes.

EL STUDENTS IN CALIFORNIA

Below, we provide information on the state’s EL students. Specifically, we discuss available data regarding EL students’ primary language, socioeconomic status, age, the school districts they attend, and their performance on state assessments.

EL Student Demographics

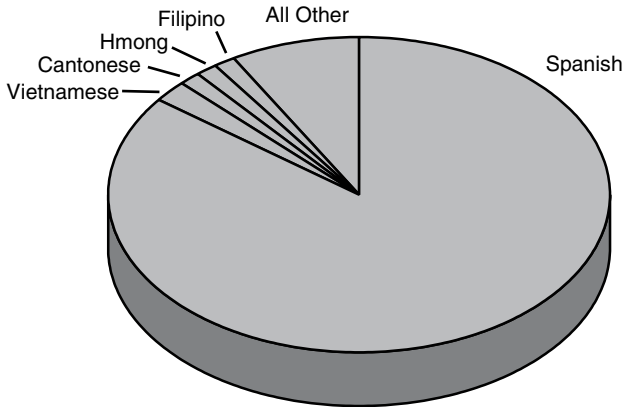
Figure 1 summarizes some basic facts about the state's EL student population.

Figure 1 Facts About California's EL Students	
2005-06	
✓	25 percent (1.6 million) of California's K-12 students are English learners.
✓	85 percent speak Spanish as their primary language.
✓	85 percent are economically disadvantaged.
✓	11 percent receive special education services.
✓	At least 6 percent have attended California schools less than 12 months.
✓	8 percent-10 percent are redesignated as "Fluent English Proficient" each year.
✓	Of all EL students, 61 percent are in elementary school (grades K-5), 20 percent are in middle school (grades 6-8), and 19 percent are in high school (grades 9-12).

Most of State's EL Students Speak Spanish as Their Primary Language. Figure 2 shows the distribution of EL students by primary language. Roughly 85 percent, or 1.3 million students, speak Spanish. This group accounts for about 21 percent of all students in the state. The second largest EL student group speaks Vietnamese (34,000 students, or 2 percent of all EL students). The next largest language groups are Cantonese, Hmong, and Filipino, each with roughly 1 percent of EL students. The remaining 8 percent speak one of 51 other languages. While Spanish is the language spoken by most EL students, Figure 2 helps to highlight why state- and local-level EL policies should not focus exclusively on this group—there are 230,000 other EL students in the state who have differing needs and characteristics.

Figure 2

Spanish Is Most Common Primary Language Among EL Students



Significant Majority of EL Students Are Economically Disadvantaged. Roughly 85 percent of EL students are economically disadvantaged (as measured by participation in the state’s Free and Reduced Meal Program). This compares to 41 percent of the non-EL population. This data suggests most EL students face multiple challenges. Not only do they confront the difficulties of learning a new language (often without English-speaking support at home), they also must cope with the academic challenges typically associated with poverty. As discussed in “A Proposition 98 Roadmap,” students identified as both EL and economically disadvantaged perform more poorly on state assessments than students with just one of those risk factors.

Majority of EL Students Are Elementary School Age. The majority (61 percent) of EL students are in elementary school. Middle and high schools each serve about 20 percent of the state’s EL student population. This distribution is significant because the most effective approach to educating an EL student likely will vary depending on the student’s age and associated factors—such as literacy in the primary language, previous exposure to English, and specific grade-level content standards.

Redesignation Likely Accounts for Some Decrease in Older EL Students. Nearly 40 percent of the state’s kindergarteners and roughly

one-third of the state's elementary school students are classified as EL. By comparison, only 19 percent of all ninth graders and 12 percent of all twelfth graders are classified as EL. Some of this decline in the upper grades is due to redesignation. Each year 8 percent to 10 percent of the state's EL students meet their local school districts' criteria for attaining proficiency in English and are redesignated as "Fluent English Proficient" (FEP). (It is important to note this is a statewide statistic. Redesignation rates at individual districts may be much higher or lower.) The change in EL population due to redesignation is partly offset each year by new ELs entering the state—typically around 6 percent of all EL students.

Lack of Data Makes Understanding Trends Difficult. Anecdotal data suggests that some of the decline in the proportion of EL students in upper grades also might be due to EL students dropping out of school or moving out of California. Because the state currently does not have the capacity to track individual students' progress across grades, developing a clear understanding of the driving factors behind EL student trends is difficult. Later, we discuss this issue in greater detail and make recommendations for how the state can develop the capacity to measure EL student progress.

Many EL Students Concentrated Within Small Number of Districts. Figure 3 shows the 20 districts in the state that serve over 10,000 EL students. The figure also shows the proportion of the statewide EL population concentrated in these districts. In total, these districts serve over 600,000 EL students, or about 40 percent of the state EL student population. Fourteen of these districts are among the state's 20 largest school districts. Additionally, the figure shows the proportion of EL students compared to total district enrollment. The EL concentrations vary significantly across the districts—from around 60 percent of the student body in Coachella, Anaheim and Santa Ana, to around 20 percent in Long Beach and Elk Grove. A district's size and concentration of EL students can make a difference in the amount of resources and special programs dedicated to EL student needs.

EL Student Performance

As discussed in "A Proposition 98 Roadmap," EL student achievement consistently trails that of English-speaking pupils. Here we discuss EL student performance on three state assessments: (1) the California English Language Development Test (CELDT), which is administered to all EL students every fall; (2) the English language arts (ELA) portion of the Standardized Testing and Reporting (STAR) examination, given to all students every spring; and (3) the California High School Exit Examination

(CAHSEE), a prerequisite for all students to graduate from high school. (Students take the CAHSEE for the first time in 10th grade. If they do not pass, they may retake the exam in the 11th and 12th grades.)

Figure 3

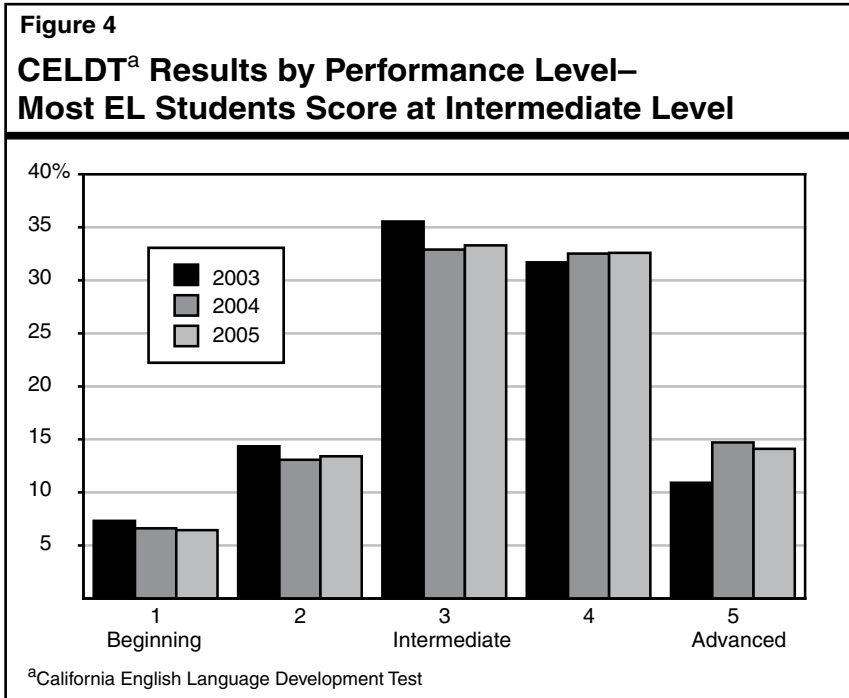
Roughly 40 Percent of State's EL Students Attend Just 20 Districts

District	Number	Percent	
		EL Students In State	District Enrollment
Los Angeles	283,861	18.6%	41%
San Diego	32,674	2.1	27
Santa Ana	32,552	2.1	58
Garden Grove	23,133	1.5	47
Fresno	22,081	1.4	29
Long Beach	21,785	1.4	24
San Bernardino	18,920	1.2	33
Fontana	16,971	1.1	40
Compton	16,338	1.1	54
San Francisco	16,068	1.1	30
Pomona	14,804	1.0	44
Sacramento	13,363	0.9	29
Montebello	13,245	0.9	38
Anaheim	12,255	0.8	59
Ontario-Montclair Elementary	11,956	0.8	47
Oakland	11,348	0.7	27
Moreno Valley	11,110	0.7	30
Sweetwater Union High	10,437	0.7	25
Elk Grove	10,363	0.7	17
Coachella Valley	10,246	0.7	62
Totals	603,510	39.6%	

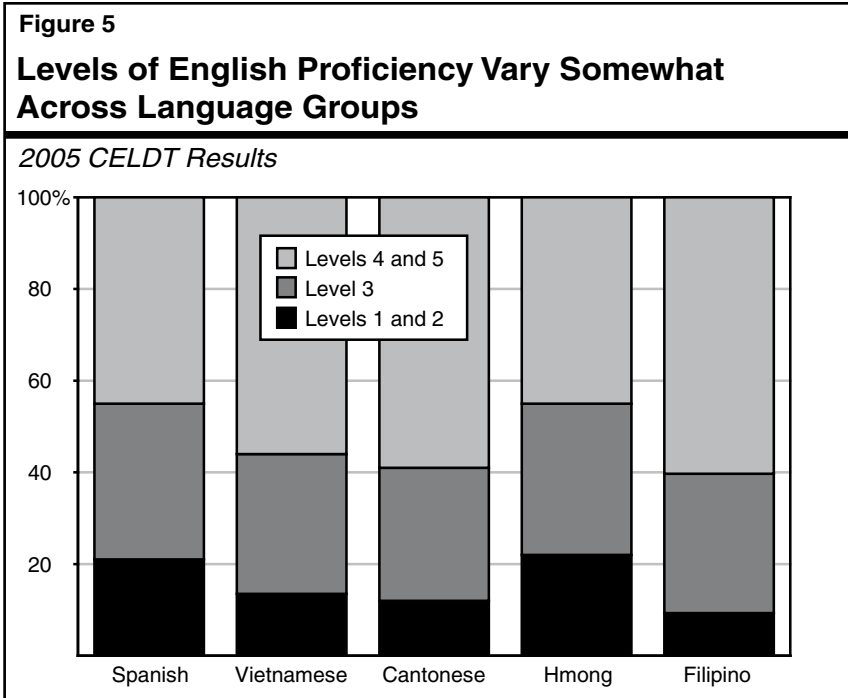
CELDT Results

Majority of EL Students Score at Intermediate or Early Advanced Level. Figure 4 (see next page) displays EL student performance on the CELDT from 2003 to 2005. This test measures proficiency in English. Scores are grouped into 5 levels, with Level 1 reflecting “beginning” EL students and Level 5 reflecting “advanced” EL students. The figure shows that in each year most students score at levels 3 and 4—“intermediate” and

“early advanced.” These results tend to differ by grade level, with more elementary-age students scoring at lower levels and more older students at higher levels.



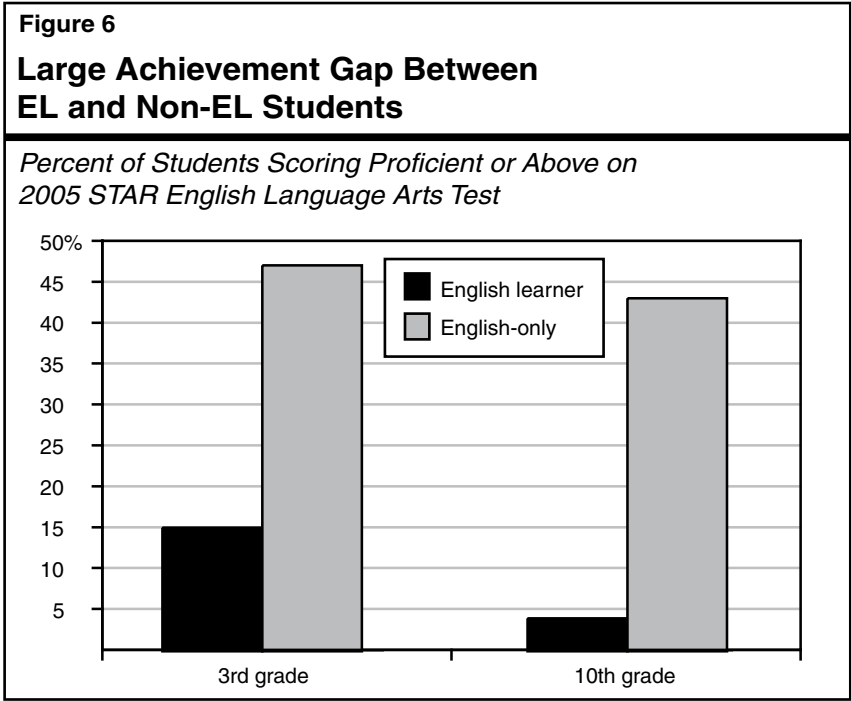
EL Student Performance on CELDT Differs by Language. Figure 5 displays 2005 CELDT scores for the five largest primary language groups. It shows that the distribution across English proficiency levels varied considerably among different languages. Of the EL students who speak Spanish as their primary language, 21 percent scored in levels 1 and 2 whereas 45 percent scored in levels 4 and 5. By comparison, a higher proportion of EL students speaking Vietnamese displayed advanced or early advanced proficiency on the CELDT—56 percent—while only 13 percent were in the beginning two levels. These data suggest the experience of learning English may differ based on a student’s background. Correspondingly, a school or teacher may also need to vary their instructional approaches to be effective for students who speak different languages.



Analyzing Individual Student Progress Yields More Meaningful Comparison. In previous publications (*A Look at the Progress of English Learners* [February 2004] and *Progress of English Learners: Update 2002-2004* [January 2006]), we have argued that in addition to identifying how many students score at each level every year, the state should measure student *progress* on the CELDT. Unlike the STAR tests, CELDT does allow for comparing student progress across years (albeit for only two years). Our analyses of CELDT scores suggest that overall EL student progress is slow. Specifically, we used CELDT data to simulate the experience of EL students who begin attending California schools in kindergarten. Our projections suggest it takes about six years before half of these students are reclassified as FEP. About 40 percent are still not proficient in English when they begin seventh grade. Our look at the progress of EL students also showed that a notable number of students score at the two advanced levels for several consecutive years. These data suggest that while many EL students may make gains in attaining English proficiency, they still lack the academic skills required by their local districts to be reclassified FEP.

STAR Results

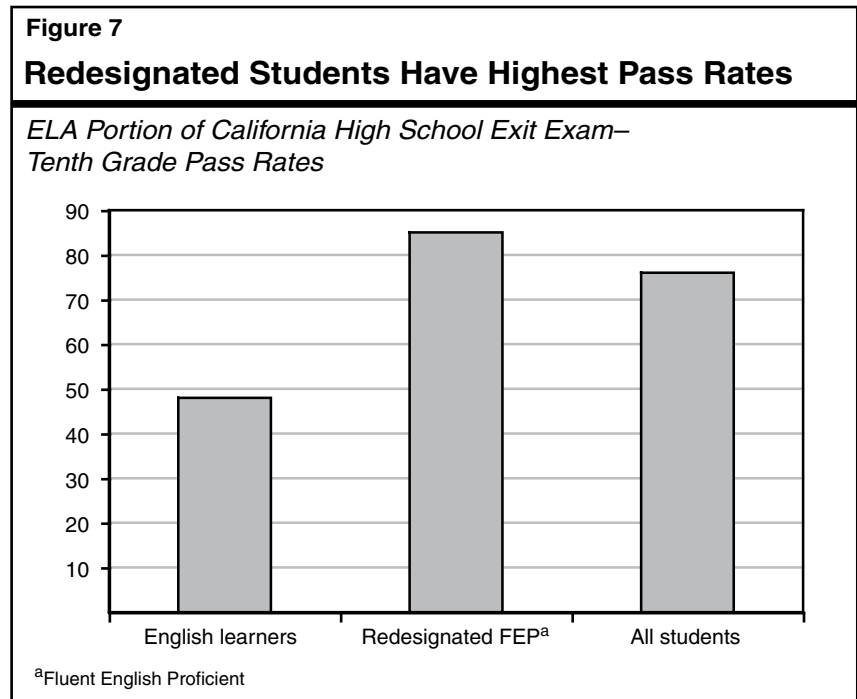
EL STAR Results Significantly Trail Non-EL Peers. Figure 6 compares EL and non-EL student performance on the ELA portion of the 2005 STAR assessment. Specifically, it shows the percentage of EL and non-EL third and tenth graders scoring proficient or above (the state’s goal for all students). The figure shows that while only a minority of each group score at proficient or above on the exam, a significantly smaller percentage of EL students do so (15 percent of EL third graders and 4 percent of EL tenth graders) compared to non-EL students (47 percent and 43 percent, respectively).



State Unable to Track EL Student Progress Across Years. Although a larger percentage of third graders scored proficient than did tenth graders (15 percent compared to 4 percent), we cannot conclude from Figure 6 that EL students perform more poorly as they progress through the grades. This is because the individual students labeled as ELs change every year due to immigration and redesignation. Without the capacity to track individual student progress and compare assessment results across years, the state cannot accurately measure EL student progress on STAR. Later, we discuss this problem in greater detail.

CAHSEE Results

Around Half of EL Tenth Graders Passed English Portion of High School Exit Exam in 2005-06. Figure 7 displays the performance of EL tenth graders on CAHSEE. This figure compares current EL student passage rates on the ELA portion of the 2005 exam to those of former EL students who have been redesignated FEP and to all tenth graders in the state. The figure shows that just under half (48 percent) of EL tenth graders passed the ELA portion of the test. This compares to 51 percent of all students. Redesignated FEP students did significantly better, with a passage rate of 76 percent.



OVERVIEW OF MAJOR ISSUES AND RECOMMENDED NEXT STEPS

State decisionmakers can influence the education of English learner (EL) students through the funding structures, instructional approaches, instructional materials, teacher preparation and professional development programs, and assessment and accountability systems they

support. Yet, in each of these areas, the state lacks adequate data to make informed decisions about which approaches are likely to improve student outcomes. Below, we make various recommendations for how the Legislature could acquire additional information to better serve EL students. Most importantly, we recommend the Legislature fund evaluations to identify effective practices and upgrade the state assessment system to better measure EL student progress.

While the state has created several programs and funding streams specially designed for EL students, it still lacks a strategic approach to EL education. The size and diversity of California's EL population make developing an approach that would work for all students a difficult exercise. Research on the topic of EL offers some direction but provides no conclusive path toward a cohesive statewide policy. Nonetheless, as ELs make up a quarter of the state's student body and are performing significantly worse on state assessments than other students, we think the state needs to seek improvements.

Funding

We recommend the Legislature adopt a more strategic approach to funding English learner students.

The Governor's budget includes around \$68.6 billion for K-12 education from all sources. The majority of these funds go to support all students. Proportionally, only a small amount—roughly \$1.3 billion—is targeted specifically for EL students or EL instruction. Below, we discuss how these funds are spent, compare the “weight” at which the state funds EL students compared to mainstream students, and identify steps the state could take to improve its approach to funding ELs.

Current State Approach to Funding EL Students

Figure 8 (see page 132) summarizes the EL programs included in the Governor's budget proposal. The figure shows that total support for EL programs in 2007-08 is roughly \$1.3 billion—around \$1.2 billion in state support and around \$160 million in federal funds. (The largest program, Economic Impact Aid, or EIA, supports both EL and economically disadvantaged students. However, districts report they use around 85 percent of these funds for EL services.) The figure also shows the three EL initiatives funded with one-time monies in the current year—instructional materials for EL students (\$30 million), a best practices pilot project (\$20 million), and translation of commonly used documents (\$450,000).

Most EL Funds Provided to Districts. The figure shows that the bulk of funds—\$1.2 billion—flow to districts and is somewhat discretionary. (That is, districts’ only requirement is to use the funds to supplement the core academic program for ELs. The \$63 million provided through the English Language Acquisition Program is further restricted for use with EL students in grades 4 through 8.) The remaining funds go to either districts or the California Department of Education (CDE) for various activities including professional development programs, testing, and outreach to parents. (See box on page 134 for a discussion of the Community-Based English Tutoring program.)

California Provides 13 Percent More Funding for EL Students Than Other Students. Altogether, state and federal support in current programs designed to assist EL students totals around \$860 per English learner. State funding alone accounts for about \$750 of this per-student amount. Comparing the state rate to the average revenue limit amount (or base general purpose funding) provided for *every* student, the state spends around 13 percent more per EL student. That is, for every \$1 the state invests in the base education program for all students, it invests an additional 13 cents in EL programs.

State’s Weights for EL Students Implicit, Not Intentional. Some states use a “weighted student” funding approach, whereby they provide schools with additional funding based on the level of resources they believe is required to educate special populations (such as EL, poor, and special education students) relative to the general student population. By comparison, California distributes supplementary funding for ELs through various categorical programs. Under such an approach, EL funding decisions remain largely disconnected from overall funding decisions and cost determinations. That is, the state has not expressly determined that it costs 13 percent more to educate an EL student. Rather, the state has created a series of EL programs over the years that have resulted in a comparative funding weight for EL students of 1.13.

State’s Weights for Economically Disadvantaged Students Also Not Intentional. Because such a high percentage of EL students are economically disadvantaged, we also calculate the state’s implicit funding weight for this demographic group. Depending on the measure of poverty used in the calculation, we estimate the state provides between 11 percent and 26 percent more for poor students. (This analysis compared EIA and Targeted Instructional Improvement Grant funding to revenue limits.) As is the case for EL student funding, these weights are implicit. That is, the state did not make a strategic decision that economically disadvantaged students require this amount of additional funding. Rather, the state allocated funding for certain categorical programs targeting poor students, and these are the weights that resulted.

California's Weights Appear Low Compared to Other States. Our cursory review indicates that California's implicit weight for EL and economically disadvantaged students is lower than the weights used by other states. Florida, for example, funds EL students at a weight of 1.275. Maryland is increasing funding—over a period of years—to weights of

Figure 8**Current Programs and Funding for EL Students***(In Millions)*

Program	2007-08 (Proposed)	Description
Discretionary Funds		
Economic Impact Aid	\$1,012.7	Funds districts to provide supplementary services to EL and economically disadvantaged students.
Title III Limited-English Proficient	158.6 ^a	Funds districts to provide supplementary services to EL students.
English Language Acquisition Program	63.4	Funds districts to provide supplementary services to EL students in grades 4-8.
Professional Development		
Mathematics and Reading Professional Development Program—EL component	\$25.0	Funds districts to provide teachers of EL students with professional development in reading and mathematics.
Bilingual Teacher Training Program	2.1	Funds county offices of education to assist K-12 teachers in attaining the training and authorizations necessary to teach EL students.
Assessment/Accountability		
CELD ^b	\$9.7 11.9 ^a	Funds state-level contract and administration costs. Also provides \$5 per EL to assist districts with local administration.
Parent Outreach		
Community-Based English Tutoring program	\$50.0	Funds schools to provide free or subsidized English language instruction to parents or other adult members of the community who pledge to tutor EL students.
Clearinghouse for Multi-Lingual Documents (CMD)	0.3 ^a	Funds the California Department of Education (CDE) to develop an electronic clearinghouse for districts to access and share translated documents.
Totals	\$1,333.7	

Continued

2.1 for economically disadvantaged and 2.0 for EL students (including federal funds). Oregon has identified target weights of 1.5 for EL students and 1.25 for poor students (although the state budget has not yet supported these levels of funding). The discrepancy among these states indicates the need for reliable studies on the cost differences associated with educating different types of students. Some states, including Oregon and New York, have undertaken studies to determine such cost differences.

Revisiting State's Approach to Funding EL Students

State Should Adopt a More Strategic Approach to Funding EL Students. Regardless of what level of overall support the Legislature decides to provide, we recommend the state adopt a clear strategy for funding EL students. Rather than continuing to create a series of disconnected categorical programs that result in an implicit weight, we recommend the Legislature determine an *explicit* weight at which EL students should be funded. Specifically, we recommend the state set a target weight, and a timeline for reaching it. Funding could then be distributed through a weighted student formula, a large EL block grant, or existing categorical programs—the method for distributing dollars is less important than developing an underlying rationale for determining the funding level. This type of strategic approach would provide the Legislature with a framework to help guide annual budget decisions.

Upcoming Studies May Provide Insight. The question of just what the state's EL funding weight *should* be remains difficult to answer. As mentioned in the "Proposition 98 Roadmap" section of this chapter, researchers in California are conducting a series of studies examining school finance and governance that are to be released in spring 2007. One of these studies, entitled "Resource Needs for California's English Learners," intends

One-Time Funds	2006-07 Budget	
EL instructional materials	\$30.0	Funds districts to purchase materials for EL students to supplement the core instructional program.
Best practices pilot project	20.0	Provides three-year competitive grants to schools to support or expand successful programs for EL students. Corresponding evaluation (unfunded) is intended to identify best practices for the state.
Document translation	0.5 ^a	Funds CDE to translate commonly used documents into multiple languages and post them on its CMD Web site.

^a Federal funds.

^b California English Language Development Test.

to address the “estimated costs for providing education for California’s ELs that will prepare them to meet the goals California has set for them.” This research may provide the Legislature with some additional insight into funding EL students.

Funding Reform Should Be Coupled With Accountability Reform.

In addition to rethinking how much funding to provide for EL students, we believe the state should ensure proper accountability is in place for monitoring the progress of ELs. Without the ability to measure student outcomes, the state has no way of knowing whether funding increases are making a difference or if additional reform is needed. Moreover, an effective accountability system helps clarify goals and improve incentives for districts to serve EL students. While our current assessment program is a solid foundation for monitoring student outcomes, we believe additional reform is needed. Specifically, we recommend the state revise the

Community-Based English Tutoring (CBET) Program

The Governor’s budget proposes spending \$50 million to extend the CBET program. This program was originally created in 1998 as part of Proposition 227. Since that year, the state has spent \$50 million annually for school districts to offer free or subsidized English language instruction to adults. Adults who receive English tutoring through the CBET program are in turn expected to tutor English learner (EL) students in grades K-12. Proposition 227 required the program be funded through 2006-07. Moving forward, the Legislature may decide to continue the program or redirect funding for another education purpose.

Lack of Clarity Regarding Program’s Primary Goal Leads to Uneven Implementation. The goal of the CBET program, as defined in statute, is to “encourage family members and others to provide personal English language tutoring [to EL children], and support these efforts by raising the general level of English language knowledge in the community.” A recent evaluation of the CBET program found notable differences in its implementation, due largely to inconsistent interpretations of the program’s goal. While some program sites were focused on helping support school-age EL children, many other programs reported their primary goal was providing English as a second language classes (ESL) to adults in the community. Thus, programs were found to vary considerably in the degree to which they supported adult tutoring of K-12 EL students and were aligned with the district’s

STAR assessment system so that it measures annual student-level gains in achievement. Later, we discuss this recommendation in further detail.

Instructional Approach

We recommend the Legislature fund an evaluation of the recently established best practices pilot program to identify effective approaches to educating English learner students.

While most ELs in the state receive instruction in English, educators use a wide variety of specific EL instructional approaches. Prior to 1998, primary language instruction (often referred to as bilingual instruction) was the most common model used to educate the state's EL students. Proposition 227, approved by California voters in 1998, required students to be taught "overwhelmingly in English" (although parents can apply to have their children participate in an alternative program). Not surprisingly,

K-12 EL instructional program. Furthermore, the CBET evaluation found that while the program was popular, there was no evidence that the program had improved EL student achievement.

If CBET Program Continues, Improving EL Student Achievement Should Be Primary Goal. Chapter 632, Statutes of 2006 (SB 368, Escutia), made substantive changes to CBET accountability requirements. Specifically, the new legislation requires districts to annually adopt a plan that outlines both their objectives for the CBET program and how they will measure program results. Should the Legislature continue funding the CBET program, it may want to consider further modifying statute to emphasize that K-12 EL students—not adult participants—should be the primary beneficiaries of the program. This would clarify to program providers that offering ESL classes to adults is intended as a means to an end, that end being improved K-12 student proficiency in English. School districts also could be required to include improved EL student proficiency (measured by CELDT) as a measurable objective in their local CBET plans.

Legislature May Want to Consider Other Uses for These Funds. The Legislature is not required to continue funding the CBET program beyond the current year. Given the state's limited resources and EL students' considerable needs, the Legislature may want to consider whether the \$50 million proposed for extending the CBET program might serve EL students more effectively in another way.

an independent evaluation found that one of Proposition 227's primary effects was to decrease the proportion of EL students receiving bilingual instruction. Between 1997-98 and 2005-06, the proportion of EL students in primary language programs dropped from around 30 percent to 7 percent. As shown in Figure 9, most EL students currently are educated in structured English immersion classrooms (47 percent) or mainstream classrooms (41 percent).

Figure 9			
EL Students by Instructional Setting			
<i>2005-06</i>			
Instructional Setting	Description	Number	Percent
Structured English immersion	Setting is specially designed for EL students but all instruction is in English.	737,243	47%
Mainstream class	No EL-specific setting, although sometimes special EL services are provided.	656,657	41
Alternative course of study	Waiver has been granted to use alternative instructional methodologies (mostly bilingual education).	105,833	7
Other	Any other instructional setting.	70,721	5
Totals		1,570,454	100%

Instructional Setting Not the Most Important Factor in EL Student Success. The Proposition 227 evaluation concluded that instructional setting might not be a primary factor in determining EL student outcomes. Specifically, the evaluators found little to no evidence of differences in EL performance by model of instruction. Rather, the report suggests that certain local factors have a greater effect on EL student outcomes than the instructional setting employed, including: staff quality, schoolwide focus on English language development, systematic and ongoing assessments, and data-driven decision making. In addition, the concentration of EL students, students' primary languages, parents' experience with and attitudes toward education, and students' previous exposure to English and American culture are all factors that might affect how schools and districts go about educating their EL students.

Recently Established Pilot Project Intended to Identify EL Best Practices. While no one approach will fit the needs of all districts, schools,

and EL students, enough commonalities exist that educators should be able to learn from each other to help improve EL services across the state. Chapter 561, Statutes of 2006 (AB 2117, Coto), implements one of the primary recommendations of the Proposition 227 evaluation by creating a pilot project to identify “best practices” of schools where EL students are demonstrating successful outcomes. The project intends, at a minimum, to identify best practices in the areas of curriculum, instruction, and staff development. The *2006-07 Budget Act* provided \$20 million over three years to support or expand these practices at selected schools.

Fund Evaluation to Help Disseminate and Replicate Successful Approaches. Although Chapter 561 requires CDE to contract with an independent research organization to evaluate the project, funding for this purpose has not yet been provided. We recommend the Legislature provide a total of between \$500,000 and \$800,000 in one-time monies for the evaluation (to be conducted from 2007-08 through 2011-12). Federal Title III carryover funds likely will be available to cover this cost. We think the evaluation is a critical part of the pilot project and is needed to ensure a rigorous assessment and comparison of existing practices. We also think the evaluation can play an important part in helping to share information on successful approaches among districts and to replicate these best practices around the state. Thus, we recommend the Legislature require that the final evaluation report include practical suggestions for disseminating its findings across the state.

Instructional Materials

We recommend the instructional materials component of the best practices evaluation include a rigorous assessment of the effectiveness of different types of materials on English learner student performance.

The State Board of Education (SBE) has ruled that EL students must have access to the same standards-aligned instructional materials as all other students. The *2007-08 Governor’s Budget* includes almost \$420 million for instructional materials. Districts may spend these funds on state-adopted, standards-aligned textbooks and materials for use with all of their students. The budget proposal does not set aside funding specifically for EL materials.

Districts May Select Additional Materials to Supplement Core Curriculum. Although districts are required to provide EL students equal access to the core standards-aligned curriculum, they can opt to provide *additional* instruction (beyond the required 120 to 150 minutes per day) using other materials. The Legislature provided \$30 million in one-time funds in both 2004-05 and 2006-07 specifically for districts to purchase

supplemental materials to help EL students improve their English reading, writing, and speaking skills. To ensure these materials were aligned to state standards, districts had to get approval from CDE prior to purchasing them.

Debate Over EL Students and State-Adopted Instructional Materials. In 2006, SBE developed the criteria that publishers will use in developing new reading and language arts (RLA) instructional materials. Publishers will submit these materials to SBE for state adoption in 2008. Because all districts in the state will have to use these materials, the framework discussion included considerable debate over what kinds of materials would best meet the needs of EL students. Whereas teachers currently are required to use the same core curriculum materials for EL students as they do for mainstream students, some parties believed that publishers should be able to develop a separate curriculum option specially designed for EL students. This proposal was referred to as “Option 6.” The debate over Option 6 led the Legislature to eliminate funding for SBE in 2006-07.

The SBE Decides EL Students Must Continue to Use Core Instructional Materials. Because EL students are held accountable for meeting the same academic standards as all other students, SBE ultimately ruled they should be educated using the same standards-aligned instructional materials. That is, the finalized RLA core materials adoption criteria do not allow publishers to develop separate materials for EL students, as proposed by Option 6. The new RLA criteria, however, do require core materials to include an English language development (ELD) component designed to meet the special needs of EL students. Specifically, the curriculum must provide adequate materials so that 30 to 60 minutes of the required 120 to 150 minutes of RLA instruction per day may be ELD.

Unclear What Kinds of Materials Actually Lead to Positive Outcomes for EL Students. Despite the heated debate, it is still unclear which approach to instructional materials is most effective at improving EL students’ performance. Should materials integrate academic and language instruction, or must these skill areas be taught separately to be taught well? Are materials most effective when differentiated based on English proficiency, or does such differentiation dilute content? Can materials that supplement the core curriculum contribute to improved EL student outcomes, as compared to relying upon the core curriculum alone? If so, which types of supplemental materials are most effective? To date, state policymakers have had to make decisions about instructional materials without the benefit of this information.

State Should Identify How Successful Districts Use Instructional Materials for EL Students. For practical purposes, the recent debate over

the RLA materials is over—SBE has made its decision and publishers already are at work designing new materials for the 2008 RLA adoption cycle. However, decisions over how the state's core instructional materials can best meet the needs of EL students will return with the next textbook adoption cycle in 2014. To ensure the state obtains adequate information regarding the effectiveness of instructional materials programs available for EL students, we recommend the instructional materials component of the best practice evaluation be reasonably comprehensive and rigorous. To this end, the Legislature may want to grant certain districts waivers from the requirement they rely on the core RLA curriculum to educate their EL students. This would help ensure different types of instructional materials could be assessed and compared. Not only would findings from such a study help inform the next statewide RLA adoption, the state also could collect information on how additional materials can best be used to supplement the core curriculum for EL students. These data would help inform future budget decisions regarding instructional materials.

Teacher Quality

We recommend the state fund a separate evaluation to identify effective approaches to preparing new teachers to work with English learner (EL) students. In addition, we recommend the EL best practices evaluation include an in-depth assessment of the effectiveness of commonly used approaches to professional development for teachers of EL students.

Research cites teacher quality as among the most important school-level factors contributing to EL student success. While the prevalence of properly credentialed teachers and state support for professional development both have increased in recent years, it is still unclear how effective these efforts have been at preparing teachers to work with EL students.

Teacher Preparation

Because such a high proportion of the state's students are ELs, teacher preparation programs have increasingly emphasized techniques for teaching this population. Despite this effort, research suggests many teachers still do not feel sufficiently prepared for the challenges of meeting EL students' needs.

Teachers Must Hold Special Credential to Teach EL Students. The state requires that teachers with one or more EL students in their classrooms attain special authorization and training. Beginning in 2002, training on how to work with EL students has been embedded in all teacher preparation programs, and new teachers acquire EL certification as part

of their regular credential. Veteran teachers must attain a special certificate—the Cross-cultural, Language and Academic Development (CLAD) credential—to be considered qualified to work with ELs. Requirements for CLAD certification may be satisfied by coursework or through examination. (The Bilingual CLAD certificate, also meets state requirements for teaching EL students and may be attained by passing an examination.)

Many Teachers Still Lack Proper Certifications to Teach EL Students. Despite state requirements, a 2005 study by The Center for the Future of Teaching and Learning (CFTL) reported that only 48 percent of fully credentialed teachers with more than five years of teaching experience hold proper EL authorization. (The researchers note this is an improvement over 1999-00, when only 29 percent were qualified.) Likewise, in a 2003 CFTL survey, 87 percent of California teachers reported having EL students in their classrooms, but only 47 percent reported holding the proper certifications.

Teachers Do Not Feel Sufficiently Prepared to Work With EL Students. The 2005 CFTL report also shows that only about 40 percent of teachers working with EL students—including those who had met state certification requirements—report having adequate training related to second language acquisition. Moreover, the report found that many new teachers who received EL training as part of their credentialing program were unaware or unaffected by this training. Specifically, two-thirds of new teachers surveyed did not even *know* they were properly certified. These findings suggest that even teachers who have met the state's requirements for teaching EL students may not feel properly prepared.

Additional Data Needed to Evaluate Whether Teacher Preparation Programs Need Improvement. Despite the state's additional certification requirements, little research has been done on what makes teacher preparation programs effective in preparing teachers of EL students. Does attaining CLAD certification make a teacher more effective? Do certain types of preparation programs better prepare teachers to meet EL student needs? Requiring teachers of EL students to hold a special authorization might be beneficial, but without additional data and analysis, the state cannot ascertain which teacher preparation requirements actually benefit EL students.

Evaluating Teacher Preparation Programs Will Help Identify What Works. We recommend the Legislature provide between \$250,000 and \$500,000 in one-time monies for CDE—in consultation with the Commission on Teacher Credentialing—to contract for an independent evaluation of the effectiveness of teacher preparation programs in improving EL student achievement. Federal Title II or Title III carryover funds likely would be available to cover this cost. Using data from the statewide teacher and

student information systems (both currently under development), the evaluation should link preparation programs with student outcome data, including achievement gains and FEP redesignation rates. The evaluator should use statistical methods to control for the effects of student factors, such as primary language and socioeconomic status, as well as school factors, such as the concentration of EL students. The study also should include surveys and focus groups with teachers to identify what about their preparation programs they thought worked or needed improvement. The information from such a study could be used to identify and replicate effective practices at particular teacher preparation programs as well as to inform future state-level decisions regarding teacher credentialing requirements.

Professional Development

Preparation programs are only the beginning of a teacher's training. Through various incentive programs the state promotes ongoing professional development. In 2006-07, the Legislature augmented the Mathematics and Reading Professional Development Program by \$25 million to provide training specifically for teachers of EL students. In addition, the Governor's 2007-08 budget includes \$670 million for various other professional development programs. In most cases, districts can opt to use these funds to offer training activities related to EL student instruction. Despite these investments, however, the state knows little about which professional development approaches foster the greatest EL achievement gains.

Many EL Teachers Do Not Feel They Get Sufficient Training. A 2005 survey asked 5,300 EL teachers in the state about their professional development activities over the previous five years. Survey results show many teachers had little or no professional development designed to help them teach EL students. Specifically, over the five-year period, 43 percent of teachers with 50 percent or more EL students in their classrooms reported they had received no more than one in-service training focused on the instruction of ELs. Teachers with fewer than 50 percent EL students were even less likely to have received specialized in-service training. Furthermore, the survey found the quality of the training was uneven and often disconnected from teachers' needs. Roughly one-third of teachers reported that training sessions were poorly planned, provided by presenters who had limited knowledge and experience with EL students, and did not contain adequate or appropriate information to help them improve EL instruction.

Best Practices Project Can Help Identify Effective Approaches to Teacher Training. While decisions about how to structure professional sessions are largely left up to districts, the state can play a role in helping

to identify and disseminate training approaches that have been found to work well. Although professional development is already specified as one component of the best practices pilot program, we recommend the evaluation emphasize a rigorous assessment of professional development approaches and their effect on EL student achievement. Such an assessment should examine which types of delivery models are most effective. It also should examine how the duration and content of training affect teacher and student outcomes.

Assessment and Accountability

We recommend the Legislature require state assessments to be vertically scaled so that English learner (EL) student progress can be measured. We believe this change is vital to strengthening district accountability for serving EL students.

The state's main assessment system does not allow for measuring student progress from one year to the next. This is because "basic" or "proficient" levels on the STAR assessment do not necessarily describe the same level of mastery in each grade. An improvement in students' scores could mean one of two things—either they have made significant learning gains and are achieving closer to the state's standards, or the test was slightly easier in the second year. As a result, comparing results across years does not allow one to determine whether a student's achievement actually is improving, getting worse, or staying the same. While this weakens the accountability system for all students, it makes accountability for serving EL students especially tenuous. That is, policymakers cannot hold schools accountable for improving student outcomes.

Measuring Individual Level Progress Is Especially Important for EL Students Because Group Is Always Changing. While being able to measure gains and losses is important for all students, it is essential for EL students. Aggregate comparisons of how EL students perform as a group from one year to the next are not particularly meaningful because the students classified as EL change every year due to immigration and redesignation.

By definition, the students who get redesignated are those who have developed greater competence in English and therefore are likely to be higher performers on the STAR exams. Because the highest performing EL students tend to "fall out" of the EL group each year, aggregate EL student STAR scores remain low, and the gains of the most successful students are not reflected. Moreover, the new immigrants who "join" the EL group each year typically have low proficiency in English. Because of these dynamics, comparing aggregate EL student test scores across years can be mislead-

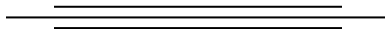
ing. Measuring individual student progress is the only way to accurately assess whether EL student achievement is improving.

Vertically Scaled STAR Test Would Allow State to Track EL Student Progress and Better Highlight Problem Areas. We think it is critical that the state's assessment and accountability system be able to measure annual student-level gains in achievement, especially for EL students. Therefore, we recommend revising the STAR assessment system so that the tests are "vertically scaled"—that is, so that performance levels mean the same thing in each grade. This would allow the state to measure student gains and losses across years. As a first step in this process, we recommend requiring CDE to contract out for a report on the feasibility and costs of vertically scaling the STAR tests and to report findings to the Legislature by April 1, 2008.

CONCLUSION

With such a large and diverse population of students, closing the achievement gap between ELs and their English-speaking peers presents a significant challenge for the state. Despite the obstacles, some schools and districts are achieving positive outcomes with their ELs. Both state and local entities would benefit from learning from these success stories. The Legislature could develop policies and funding mechanisms that support these approaches, and local educators could begin to replicate the effective practices in their own classrooms. While there are no obvious answers to this issue, more information on what *is* working for educators of EL students would help policymakers at both the state and local levels make better-informed decisions.

Any discussion of best practices is predicated on the assumption that educators can tell what approaches are effective because they yield the desired results. Thus, the ability to measure outcomes is essential to refining and improving EL student services. In order to ensure it is meeting the needs of its EL—and all—students, the state must develop the capacity to measure student progress across years.



SOLEDAD ENRICHMENT ACTION CHARTER SCHOOL

We recommend the Legislature extend the sunset date for the Soledad Enrichment Action charter school for two years.

The Soledad Enrichment Action School (SEA) operates as a charter school under the oversight of the Los Angeles County Office of Education (LACOE). Chapter 58, Statutes of 1997 (SB 1318, Polanco), allowed the school to receive the higher per-pupil funding levels that are available to districts through the community day school program. Soledad is the only charter school that also operates as a community day school.

Chapter 467, Statutes of 2002 (SB 1416, Polanco), extended the statutory authorization allowing Soledad to operate as a community day school until July 1, 2008. The chapter also requires the Legislative Analyst's Office to evaluate Soledad's educational program and make a recommendation to the Legislature in its *Analysis of the 2007-08 Budget Bill* about whether to extend the authorization. To fulfill this requirement, we examined SEA's performance data and recommend extending the school's authorization for two more years.

Community Day Schools

Current law authorizes school districts and county offices of education (COE) to operate community day schools as an alternative to a student's regular school. The Legislature established these schools in the mid-1990s to give districts resources to educate students who are expelled from school or who are involved with local law enforcement agencies.

Community day schools usually operate as short-term placements for students. Typically, students attend a community day school for one or two semesters before returning to their regular high school. Because students at community day schools often have fallen behind academically, curricula at many schools are designed to help students earn credits at an accelerated rate.

Community day schools operated by COE received \$12,380 per average daily attendance (ADA) in 2005-06, roughly twice the amount provided to districts for regular students. This funding comes from two sources. First, they receive the county office base revenue limit for juvenile court programs (in the case of Soledad—\$8,624 per ADA). In addition, the community day school program provides county office programs another \$3,245 per ADA as an incentive to encourage programs to offer a six-hour instructional day. County office community day schools get about \$1,623 per ADA for attendance in each of the fifth and sixth hours of instruction each day (programs receive no additional funding if students leave school at the end of four hours).

Community day schools are also eligible for two hours of “after school” funds. After school programs provide tutoring and recreational activities to students. Community day schools were eligible to receive \$4.74 per student hour of attendance in after school classes in 2005-06—if the after school program constituted the seventh and eighth hour of attendance for students.

Soledad Operates Large Program

Soledad serves more than 2,600 students each year at 18 sites that are located across the Los Angeles basin. Most of these sites are located in neighborhoods served by the Los Angeles Unified School District, but Soledad also has school sites located in Compton, Montebello, and Long Beach. In total, Soledad serves students from about 30 school districts in the county.

Compared to community day schools operated by most school districts, Soledad is quite large—the school’s enrollment accounts for 8.5 percent of the state’s total enrollment in community day schools in 2005-06. The LACOE, which oversees Soledad, also operates several other large community day schools. The combined enrollment of SEA and LACOE community day schools accounted for 28 percent of the state’s total enrollment in community day schools in 2005-06.

The school offers classes on a year-round basis, with three 80-day semesters (rather than two 90-day semesters that are common in most schools). Soledad is open nine hours each day—the school day accounts for seven hours (six hours of instruction plus lunch and other breaks). The school also offers two hours of after school services.

Students are assessed upon entry and at the end of each semester. Each class rotates students through direct teacher instruction, individual or small group assignments, and computer-aided practice. In addition, the school coordinates services and counseling to students and parents

from a variety of social, health, and law enforcement agencies. Soledad also provides classes to parents as a way of engaging them to support the education of their children.

Turnover in Students Typical of Community Day Schools. Soledad provides short-term assistance to students in grades 9 through 12. According to Soledad officials, students typically attend the school for one or two semesters and then return to their regular school. As a result, Soledad enrolls many more students throughout the year than it has enrolled at any one time.

Figure 1 displays enrollment and attendance for Soledad and the community day schools administered by LACOE. As the figure shows, total enrollment far exceeds total attendance. Soledad enrolled 2,695 students during 2004-05 but claimed ADA funding for only 1,163 students. The significant difference between enrollment and attendance is typical of community day schools and occurs primarily because most community day schools operate as a short-term placement for students. Soledad's 2004-05 enrollment data show, for example, that about 27 percent of students were enrolled for 90 days or longer; only 13 percent stayed enrolled for most of the regular school year (October to May). The enrollment trends for LACOE community day schools were similar.

Figure 1		
Soledad Enrichment Action Charter School Enrollment and Attendance Data		
<i>2004-05</i>		
Enrollment	Soledad	Los Angeles County Office^a
Total	2,695	5,963
Percent at least 90 days	26.9%	34.4%
Percent enrolled October-May	12.6	9.1
Average daily attendance	1,163	1,986
^a Six community day schools administered by the county office.		

In 2005-06, Soledad was eligible for total funding of \$18 million. Of this amount, \$17.5 million was for SEA's base educational program, including funding for the fifth and sixth hour of classes. An additional \$415,000 was earned in after school funds. Because of a deficit in the statewide funding

for community day schools, the school received only \$17.7 million for the fiscal year.

State Accountability System Does Not Permit Evaluation of SEA

The state has several school accountability programs to help policy-makers and the public understand how well schools are helping students learn. The primary state and federal accountability measures do not work well for community day schools, however, because of the rapid turnover of students during the school year. The state Academic Performance Index (API) and federal Adequate Yearly Progress (AYP) are based on the assumption that student mobility is relatively low. That is, both measures exclude the scores of students who move from one school to another or from one district to another during the school year. In addition, by emphasizing growth in student scores, API assumes a relatively constant student population at the school from year to year.

Since the *majority* of students in community day schools change schools during the year, the API and AYP scores of a community day school are based on the test scores of a small fraction of the students served by the school. For SEA, for instance, only about 13 percent of students who attended the school in 2005-06 were counted in its 2005 API and AYP scores. It is not known whether these students are representative of all the students who enrolled in the school in 2005-06. In addition, because virtually none of the students counted in SEA's 2005 API were also included in the school's 2004 API, growth in this measure does not represent a meaningful indicator of SEA's effectiveness in promoting student learning.

Alternative Accountability System Is Ineffective

Recognizing that alternative schools such as community day schools require a different type of accountability measure, the Legislature required the California Department of Education (CDE) to develop accountability measures for alternative schools. In response, CDE created the Alternative Schools Accountability Model (ASAM).

Chapter 467 requires our office to evaluate Soledad's performance based on its ASAM performance outcomes. Unfortunately, ASAM suffers from a number of problems that render it ineffective as an accountability tool. We discuss these problems in greater detail in our February 2007 report, *Improving Alternative Education in California*. Later, we briefly review several of these shortcomings using the measures for Soledad and the other LACOE community day schools as an example.

Choice of Performance Measures Prohibit Comparisons. The ASAM requires alternative schools to choose three performance measures from

among 14 indicators. By allowing each school to define its own accountability measures, ASAM fails to define performance expectations in a way that permits comparison. Soledad and LACOE schools, for instance, chose two common measures—the percent of students attending each day and the proportion of credits earned by students. As its third measure, SEA chose the percentage of students who were suspended or expelled each year. The LACOE schools opted for the graduation rate as its third measure. Statewide, about two-thirds of community day schools choose attendance as a performance indicator and 45 percent choose credit completion. By allowing schools to choose their performance measures, ASAM fails to establish a common performance standard for community day schools, which is a necessary element of any accountability system.

Performance Data Covers a Fraction of Total Students. The ASAM collects performance data only on students that stay enrolled at an alternative school for at least 90 days. This means the schools are not held accountable for the *majority* of students served each year. For Soledad, only about one-quarter of students meet the 90-day requirement for inclusion into ASAM; for LACOE schools, performance data is reported for about one-third of its students. Thus, ASAM provides data only on a small proportion of students at the school.

Most Indicators Do Not Measure Educational Performance. Most of the 14 indicators in ASAM are not direct measures of student academic progress. Among the nonacademic measures are the rates of suspension or expulsion, attendance, promotion to the next grade, and course completion. As a result, depending on the indicators chosen, ASAM may provide no information on the educational performance of students at a school.

In addition, the five measures linked to student achievement have problems that undercut their usefulness. For Soledad and LACOE, for example, the credit completion rate could be a measure of student academic progress. The significance of this measure, however, is clouded by the fact that credit-granting policies are locally determined—a school with high standards would tend to show lower completion rates than a school with lower standards, for instance. Without uniform standards on credit granting policies, therefore, even this measure does not provide meaningful data.

Provide Extension for Soledad

Due to ASAM's shortcomings, we are unable to fulfill the specific evaluation requirements contained in Chapter 467. Despite this barrier, we provide the Legislature with our assessment of Soledad's program based on our site visits to Soledad and other alternative education programs around the state, and on other available information.

In short, we conclude that Soledad's education program appears at least comparable to other similar schools and, in some areas, the school offers attractive features that many other alternative schools do not. While this may seem like faint praise, we are wary of stating our conclusion more definitively than the data permit. This conclusion is based on the following:

- ***Soledad Serves At-Risk Students.*** Community day schools typically serve students who have been expelled, are on probation, or are far behind academically—groups that are often at risk of dropping out of school. According to Soledad, about one-third of its students are on probation. Another one-third have been expelled or are referred to the school in lieu of expulsion. Testing conducted by SEA also shows that entering students—all in grades 9 through 12—perform far below grade level, with average scores at about a fourth or fifth grade competency level in English and mathematics.
- ***Soledad's Enrollment and Attendance Data Are Comparable to Other "Short-Term" Schools.*** The proportion of students at Soledad who stay enrolled for at least 90 days was comparable to LACOE-operated community day schools and to other alternative schools around the state that are designed as short-term placements for students. In addition, the school's attendance rate for the 90-day students in 2005-06 was 82 percent—slightly below the "sufficient" rate identified by CDE but identical to the LACOE community day school attendance rate.

Soledad Provides Enriched Program. In other areas, elements of the school's program are impressive. The school, for instance, is much more successful than other alternative programs we visited in obtaining on-site services from local social and health services agencies, local law enforcement agencies, and probation. The school's parent counseling classes also seems like a valuable component that is lacking in most alternative programs. Finally, Soledad operates the most significant after school program of all the community day schools in the state, accounting for more than one-third of all statewide claims for the seventh and eighth hour funding. The school stands out from other alternative programs we visited in its success in providing these support services. We have no way to determine, however, the extent these services make the educational program more effective.

LAO Recommendation. Based on this assessment, we recommend the Legislature extend by two years Soledad's ability to receive the higher community day school funding levels. We recommend a two-year exten-

sion because, in the longer run, we suggest a different approach to funding alternative education, which we describe in more detail later.

Make Major Changes in Alternative Programs

In our *Improving Alternative Education* report, we recommend the Legislature undertake a comprehensive revision of the state funding system for alternative programs to eliminate negative incentives in the existing programs and reinforce each district's responsibility for creating effective options for students.

The thrust of our recommendations is to increase accountability for students who are referred to alternative school. We recommend two specific changes. First, we recommend fixing the API and AYP measures so that students referred to alternative programs continue to be included in the accountability scores of the students' "home" school. This will eliminate a current incentive for schools to send "problem" students to alternative schools rather than taking steps to assist the students. With this change, the Legislature would strengthen the focus of comprehensive high schools on the needs of students who are at risk of dropping out.

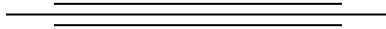
Second, we also recommend the Legislature revamp ASAM. Like our regular accountability programs, we think the alternative system should be based on comparable measures of what students actually learn while they attend alternative programs.

Revise Funding for Alternative Programs. Our recommendations also would recast the funding for alternative programs to reinforce the district's responsibility for creating effective options for students. Specifically, our proposal would provide alternative school funding only to districts (rather than county offices or charter schools), thereby making the district determine how best to provide the educational services needed by students who are struggling with academic or behavioral problems. In a sense, directly funding Soledad as a community day school lets the neighboring districts "off the hook" for providing an appropriate alternative setting for these students. Our recommendations are designed to put districts back "on the hook" for serving these students well.

Our recommendation also would encourage Soledad to work closely with its "feeder" high schools and districts to ensure that Soledad adequately meets the needs of students referred to the school. Soledad may not be the "right" school for certain students. Directly funding SEA as a community day school creates no incentive for either the school or the neighboring districts to consider whether the additional funding might be used more effectively if certain types of students attended a different alternative school.

Conclusion

In summary, we recommend extending Soledad's authority to operate as a community day school for two additional years. Unfortunately, state data yield little insight into the effectiveness of Soledad and similar alternative programs, but what we do know about the school is generally positive. Over the longer term, however, we think Soledad and other county alternative programs should be integrated into a district-centered system. Because of the focus on districts, legislative adoption of our comprehensive proposal would end the special funding authorization for Soledad in the future. Because the school offers services most districts would find difficult to replicate, we believe, however, that SEA would thrive in the new fiscal environment. By extending the school's authorization to operate as a community day school for two years, the Legislature would give the school time to work with its neighboring districts to establish these fiscal and program relationships within a new funding process.



INTRODUCTION

Higher Education

The Governor's budget proposes a net augmentation of \$539 million in General Fund support for higher education in 2007-08. This represents a 5 percent increase from the revised 2006-07 amount. Proposed augmentations would fund cost-of-living adjustments and enrollment growth funding at all three public segments, increased expenses of the Cal Grant program, and other costs. In addition, the Governor's budget assumes student fee revenue will increase by a net \$238 million, due largely to fee increases at the University of California and the California State University. The Governor's budget assumes no fee increase at the California Community Colleges. The budget also would support 112 capital outlay projects at the three segments, using \$1.5 billion in funding from higher education bonds.

Total Higher Education Budget Proposal

As Figure 1 (see next page) shows, the 2007-08 budget proposal provides a total of \$34.6 billion from all sources for higher education support costs. (Capital outlay expenditures are discussed at the end of this section.) This amount is \$1.3 billion, or 3.8 percent, more than the Governor's revised current-year proposal. The total includes funding for the University of California (UC), the California State University (CSU), the California Community Colleges (CCC), Hastings College of the Law, the California Student Aid Commission, and the California Postsecondary Education Commission. Funded activities include instruction, research, and related functions, as well as other activities, such as providing medical care at UC hospitals and managing three major U.S. Department of Energy laboratories.

Major Funding Sources

The 2007-08 budget proposal provides \$11.4 billion from the General Fund for higher education. This amount is \$539 million, or 5 percent, more than proposed current-year funding. The budget also projects that local property taxes will contribute \$2.1 billion for CCC in 2007-08, which reflects an increase of \$193 million, or 10 percent, more than proposed current-year funding.

Figure 1 Governor's 2007-08 Higher Education Budget Proposal

(Dollars in Millions)

	2006-07	2007-08	Change	Percent
UC				
General Fund	\$3,078.0	\$3,270.1	\$192.1	6.2%
Fees	1,998.0	2,151.0	153.0	7.7
Subtotals	(\$5,076.0)	(\$5,421.1)	(\$345.0)	(6.8%)
All other funds	\$13,252.8	\$13,738.3	\$485.5	3.7%
Totals	\$18,328.8	\$19,159.3	\$830.6	4.5%
CSU				
General Fund	\$2,811.4	\$2,976.3	\$165.0	5.9%
Fees	1,243.4	1,366.4	123.0	9.9
Subtotals	(\$4,054.8)	(\$4,342.7)	(\$287.9)	(7.1%)
All other funds	2,631.9	2,433.2	-198.7	-7.5
Totals	\$6,686.7	\$6,775.9	\$89.2	1.3%
CCC				
General Fund ^a	\$4,115.6	\$4,232.9	\$117.4	2.9%
Local property tax	1,857.4	2,050.5	193.1	10.4
Fees	321.7	281.9	-39.8	-12.4
Subtotals	(\$6,294.7)	(\$6,565.4)	(\$270.6)	(4.3%)
All other funds ^b	\$262.8	\$267.2	\$4.4	1.7%
Totals	\$6,557.6	\$6,832.6	\$275.1	4.2%
CSAC				
General Fund	\$827.2	\$891.6	\$64.4	7.8%
All other funds	832.5	832.2	-0.3	—
Totals	\$1,659.7	\$1,723.8	\$64.1	3.9%
Other agencies				
General Fund	\$12.8	\$12.8	—	-0.2%
Fees	26.4	28.3	\$1.9	7.4
Other	24.9	17.9	-6.9	-27.9
Totals	\$64.1	\$59.1	-\$5.0	-7.8%
Grand Totals				
General Fund	\$10,845.0	\$11,383.8	\$538.8	5.0%
Fee revenue	3,589.6	3,827.7	238.1	6.6
Local property tax	1,857.4	2,050.5	193.1	10.4
All other funds	17,004.9	17,288.8	284.0	1.7
^a	Excludes teachers' retirement funds and bond payments.			
^b	Excludes other funds maintained in local budgets.			

Student fee revenue at all the public higher education segments (including Hastings College of the Law) supports \$3.8 billion of proposed expenditures. This is \$238 million, or 6.6 percent, greater than fee revenue in the current year. Most of this increase comes from an assumed 7 percent fee increase at UC (generating \$105 million) and an assumed 10 percent fee increase at CSU (generating \$98 million). Fee revenue at CCC is projected to *decline* by about \$33 million, due mainly to the full-year effect of a \$6 per unit fee reduction that went into effect in the middle of the current fiscal year.

The budget also includes about \$17.3 billion in other funds, which reflects an increase of \$284 million, or 1.7 percent. About \$16.8 billion of these other funds constitute nonstate revenue—including federal funding and private contributions. The remainder is made up of various state revenues, including lottery and tobacco funds. In addition to the amounts reflected in Figure 1, local community colleges are projected to receive an additional \$1.6 billion from locally budgeted resources. (These funds are identified in the “California Community Colleges” section of this chapter.)

Funding by Segment

For UC, the budget proposes General Fund appropriations of \$3.3 billion, which is \$192 million, or 6.2 percent, more than the proposed current-year estimate. The other major source of funding for UC’s educational programs is student fee revenue. This is projected to total \$2.2 billion in 2007-08, which is 7.7 percent above the current-year estimate. When General Fund and fee revenues are combined, UC’s budget would increase by 6.8 percent.

For CSU, the budget proposes \$3 billion in General Fund support, which is an increase of \$165 million, or 5.9 percent, from the revised current-year level. Fee revenue would increase by \$123 million, or 9.9 percent, to \$1.4 billion. Total General Fund and fee revenue combined would increase by 7.1 percent.

For CCC, the Governor’s budget proposes \$4.2 billion in General Fund support, which is \$117 million, or 2.9 percent, above the current-year amount. Local property tax revenue (the second largest source of CCC funding) would increase by 10.4 percent, to \$2.1 billion. Fee revenue would provide an additional \$282 million, reflecting a reduction of \$39.8 million, or 12.4 percent. Combined, these three sources of district apportionments (General Fund support, property taxes, and fee revenue) would amount to \$6.6 billion, which reflects an increase of \$271 million, or 4.3 percent.

Major Cost Drivers for Higher Education

Annual base adjustments for higher education generally arise from three major factors: (1) enrollment growth, (2) inflation, and (3) student fee levels. Specifically, these factors influence costs in the following ways:

Enrollment Growth. For UC and CSU, the state uses a “marginal cost” formula that estimates the added cost imposed by enrolling one additional full-time equivalent student. This estimate includes instructional costs (such as faculty salaries and teaching assistants), related educational costs (such as instructional materials and libraries), administrative costs, and student services. Because faculty (particularly at UC) spend part of their time performing noninstructional activities such as research, the marginal cost formula “buys” part of these other activities with each additional student enrolled. A different methodology is used to calculate funding for community college enrollment growth, although functionally the approaches are similar.

Inflation. Like other parts of the state budget, general inflationary pressures cause higher education costs to rise over time. For example, inflation increases the cost of supplies, utilities, and services that are purchased by campuses. In addition, inflation creates pressure to provide cost-of-living adjustments to maintain the buying power of faculty and staff salaries.

Student Fees. Student fees comprise a portion of total revenue available to the segments. When fees are increased, this generates new revenue that either can substitute for General Fund revenue (thus creating General Fund savings) or increase total funding for the higher education segments. Either way, fee revenue and General Fund support work together interchangeably to support a given level of services.

Major Budget Changes

The Governor’s higher education budget proposal results primarily from increases in the base budget (somewhat higher than inflation), enrollment and student fees, as well as increased financial aid costs. Figure 2 shows the major General Fund budget changes proposed by the Governor for the three segments.

Enrollment Growth. The Governor proposes enrollment increases from budgeted levels of roughly 2.5 percent at UC and CSU, and 2 percent at CCC. Figure 3 (see page 158) shows enrollment changes at the three segments. We discuss proposed enrollment levels in more detail later in this chapter.

Figure 2		
Higher Education		
Proposed Major General Fund Changes		
University of California	Requested:	\$3.3 billion
	Increase:	\$192 million (+6.2%)
<p>Base Augmentation: Provides \$117 million for a 4 percent base funding increase to pay for increased salaries and other costs. (A proposed student fee increase would provide an additional \$105 million in unrestricted revenue.)</p> <p>Enrollment Growth: Provides \$54.4 million for 2.6 percent enrollment growth (5,000 full-time equivalent [FTE] students).</p> <p>Research Augmentations: Provides \$20 million for new and expanded research programs.</p> <p>Outreach Reductions: Reduces funding for outreach programs by \$19.3 million.</p>		
California State University	Requested:	\$3 billion
	Increase:	\$165 million (+5.9%)
<p>Base Augmentation: Provides \$109 million for a 4 percent base funding increase to pay for increased salaries and other costs. (A proposed student fee increase would provide an additional \$97.8 million in unrestricted revenue.)</p> <p>Enrollment Growth: Provides \$65.5 million for 2.5 percent enrollment growth (8,355 FTE students).</p> <p>Outreach Reductions: Reduces funding for outreach programs by \$7 million.</p>		
California Community Colleges	Requested:	\$4.2 billion
	Increase:	\$117 million (+2.9%)
<p>Cost-of-Living Adjustments (COLAs): Provides \$238 million for a 4.04 percent COLA for apportionments and selected categorical programs.</p> <p>Enrollment Growth: Provides \$109 million for 2 percent enrollment growth (about 23,000 FTE students).</p> <p>Local Property Tax Savings: A \$193 million projected increase in local property tax revenue would offset a like amount of General Fund expenses.</p>		

Student Fees. As shown in Figure 4 (see page 159), the Governor proposes that student fees increase by 7 percent at UC and 10 percent at CSU. These increases would generate an additional \$105 million for UC and \$97.8 million for CSU. Fees at CCC were reduced by 23 percent in January 2007, and the Governor proposes that this reduced fee remain in place through 2007-08. The full-year effect of the fee reduction will reduce annual fee revenue by \$33.2 million in 2007-08, requiring a General Fund backfill of the same amount.

Figure 3 Higher Education Enrollment

State-Supported Full-Time-Equivalent Students

	Actual 2005-06	Budgeted 2006-07	Proposed 2007-08	Change	
				Amount	Percent
University of California (UC)					
Undergraduate	151,895	156,163	160,824	4,661	3.0%
Graduate	23,718	25,355	25,400	45	0.2
Health Sciences	12,672	11,937	12,231	294	2.5
UC Totals	188,285	193,455	198,455	5,000	2.6%
California State University (CSU)					
Undergraduate	266,324	271,265	278,047	6,782	2.5%
Graduate/postbaccalaureate	45,835	46,686	47,853	1,167	2.5
CSU Totals	312,159	317,951	325,900	7,949	2.5%
California Community Colleges	1,107,294	1,153,025	1,176,086	23,061	2.0%
Hastings College of the Law	1,281	1,250	1,250	—	—
Grand Totals	1,609,019	1,665,681	1,701,691	36,010	2.2%

Capital Outlay

As shown in Figure 5, the Governor's budget proposal includes about \$1.5 billion in new capital outlay funding for 2007-08. In addition to this funding, the budget provides \$592 million in carryover and reappropriated funding that was originally appropriated in prior years. For CSU, the budget also includes \$50 million in bond funding for special repairs that is counted as part of CSU's support budget.

Of the proposed funding, \$70 million would come from lease revenue bonds and the remainder from general obligation (GO) bonds. All but \$87 million of GO bond funding would come from bonds authorized by voter approval of Proposition 1D in November 2006. Under the Governor's proposal, just under \$700 million in Proposition 1D bonds would be available for future years. Prior bond authorizations would be virtually exhausted.

Figure 4**Annual Education Fees for Full-Time Resident Students^a**

	Actual 2005-06	Actual 2006-07	Proposed 2007-08
University of California^b			
Undergraduate	\$6,141	\$6,141	\$6,571 ^c
Graduate	6,897	6,897	7,380 ^c
Hastings College of the Law	\$19,725	\$19,725	\$21,303
California State University			
Undergraduate	\$2,520	\$2,520	\$2,772
Teacher education	2,922	2,922	3,216
Graduate	3,102	3,102	3,414
California Community Colleges	\$780	\$690 ^d	\$600

a Figures do not include campus-based fees.

b The University of California charges special fee rates for 12 professional programs, such as medicine and nursing. These fees would range from \$3,444 to \$19,107 in 2007-08. We describe these fee rates in the "Student Fees" section of this chapter.

c Does *not* include a \$60 temporary surcharge to cover income losses associated with a student fee lawsuit.

d Reflects average fee over the academic year. Actual fees were \$26 per unit in fall 2006 and \$20 per unit in spring 2007.

Figure 5**Governor's Proposed
New Higher Education
Capital Outlay Appropriations**

*2007-08
(In Millions)*

University of California	\$573
California State University	346
California Community Colleges	546
Total	\$1,465

BUDGET ISSUES

Higher Education

INTERSEGMENTAL: MAKING BUDGETING CHOICES IN HIGHER EDUCATION

The Governor's budget includes \$11.4 billion in General Fund support for higher education in 2007-08. This is about 11 percent of all proposed state General Fund expenditures. Although the Governor's budget would increase overall General Fund spending by about 1 percent from the current-year level, higher education would increase by about 5 percent, or \$539 million.

Higher Education Choices Will Be Important. Given the significant share of state General Fund resources committed to higher education, as well as the magnitude of new resources that would be dedicated for these purposes, the Legislature's decisions about the Governor's higher education proposals could have important consequences for the state's overall fiscal picture. In addition, the budget proposal presents the Legislature with some important policy choices with regard to access, affordability, and accountability.

In the following "Intersegmental" sections we discuss three budget themes on which the Legislature will have to make important choices: enrollment growth funding, outreach programs and student fees. In addition, we include an "Intersegmental" section on higher education nursing programs, in which we discuss a number of related budget proposals. After these "Intersegmental" sections, we examine specific issues for each of

the higher education segments and agencies in analyses of the California Postsecondary Education Commission, the University of California (UC), the California State University (CSU), the California Community Colleges (CCC), and the California Student Aid Commission. In the remainder of this section, we (1) outline the basic choices the Legislature faces each year with regard to the higher education budget and (2) summarize our recommendations on each of these key issues.

Higher Education Budget—Key Choices

Although the state's higher education budget involves billions of dollars of expenditures and a variety of interrelated issues, the Legislature's budgetary choices involve three basic steps.

Adjust Base Budgets. In any given year, funding contained in a segment's base budget may need to be adjusted to account for one-time costs or anomalies. For example, if the base budget contained funds for expected enrollment growth that never materialized, it could be appropriate to reduce that segment's enrollment funding to match actual experience. Similarly, the inclusion of funds for a one-time purpose (such as start-up costs for a new campus) would normally be backed out of a segment's base budget for the following year.

Determine What New Higher Education Costs the Budget Should Accommodate. Given the state's current fiscal circumstances, we believe that first priority for budget increases should be given to those new costs that are necessary to maintain existing services. The largest costs in this area typically include enrollment growth and inflationary adjustments. After addressing these base issues, the Legislature then typically considers proposals for program expansions or new programs. The sum of these various changes results in new costs to each higher education segment or agency.

Determine How Costs Should Be Covered. After making decisions about the total budget for each segment, the Legislature then has to decide how these costs are to be covered by various funding sources. In general, education-related programs at the three higher education segments are funded with a combination of state General Fund support and student fee revenue. These funds are essentially interchangeable. The key decision for the Legislature in this area is: What share of total costs should students (and their families) bear?

Summary of LAO Recommendations

Based on the approach described above, we provide specific recommendations to the Legislature throughout the rest of this chapter. We summarize our major recommendations below.

Fund Expected Levels of Enrollment Growth. The Governor's budget proposal would fund enrollment increases of 2.6 percent at UC, 2.5 percent at CSU, and 2 percent at CCC. These increases far exceed the projected 1.1 percent growth in the underlying college-age population. They also exceed the Department of Finance's own projections of increases in the enrollment at the segments. In the "UC and CSU Enrollment Growth and Funding" section later in this chapter, we recommend the Legislature fund 2 percent enrollment growth at UC and CSU. In the "California Community Colleges" section, we recommend funding 1.65 percent enrollment growth at CCC, as well as capturing savings from unspent CCC enrollment funding from the current and prior years.

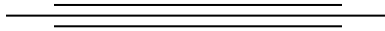
Fund Cost Increases Caused by Inflation. The Governor proposes 4 percent unrestricted base increases for UC and CSU in 2007-08. We estimate that inflation will cause costs to increase by about 2.4 percent in 2007-08. Accordingly, in the "University of California" and "California State University" sections of this chapter, we recommend base increases of 2.4 percent. Because a statutory formula using a lagged index is customarily used to fund cost-of-living adjustments at CCCs, we do not take issue with the Governor's proposed augmentation based on that formula.

Maintain Current Share of Cost Covered by Fees. The Governor's budget proposes fee increases of 7 percent and 10 percent for UC and CSU respectively. No fee increase is proposed for CCC. Absent an explicit state fee policy, we recommend that fees be adjusted in 2007-08 so that they cover the same share of education cost as in the current year. Given our recommendation to fund inflation-based increases of 2.4 percent at UC and CSU, maintaining the same share of cost in the budget year would require 2.4 percent increases in fee levels. This would increase full-time resident undergraduate fees at UC and CSU by \$147 and \$60, respectively, in 2007-08. The corresponding increase for student fees at CCC would be less than 50 cents per unit. Given that CCC fees are traditionally charged in whole dollars, and given that current fee levels were adjusted very recently (January 2007), we do not recommend any change to CCC fee levels in 2007-08.

Address New Nursing Program Costs Using Standardized Funding Approach. The Governor's budget includes augmentations for nursing programs at all three segments. While we agree with the need to increase the supply of nursing graduates, we have concerns with several of the Governor's proposals. In the "Higher Education Nursing Proposals"

Intersegmental section later in this chapter, we recommend a more consistent, simpler way to fund the expansion of nursing enrollment in order to improve outcomes and budgetary transparency.

General Fund Savings. We estimate that the Legislature could free up more than \$150 million in General Fund support in the budget year if the recommendations we have made for the segments are adopted. (We also identify considerable potential savings in the current year.) The Legislature could apply these savings toward the state's 2007-08 budget deficit (which we estimate to be about \$726 million under the Governor's budget proposal) or to other priorities.



INTERSEGMENTAL: UC AND CSU OUTREACH PROGRAMS

Currently, the state provides over \$83 million in funding to the University of California (UC) and the California State University (CSU) to support over 20 different K-14 outreach programs that focus on preparing and encouraging students from disadvantaged backgrounds to attend college. For 2007-08, the Governor's budget proposes a \$26.3 million General Fund reduction to these programs. In this write-up, we (1) provide perspectives on UC and CSU's outreach programs and efforts to evaluate their effectiveness and (2) present different approaches for the Legislature to consider in funding and evaluating these programs.

GOVERNOR PROPOSES OUTREACH REDUCTIONS

The 2006-07 Budget Act includes a total of \$83.3 million for various outreach programs (also known as academic preparation programs) at UC and CSU, as shown in Figure 1 (see next page). (The State Department of Education [SDE], the California Student Aid Commission, and the California Community Colleges [CCC] also administer a few outreach programs.) These programs are intended to help disadvantaged students enroll in college, thus increasing the college participation rates of such students. For the fourth year in a row, the Governor's budget proposes to reduce support for UC and CSU's outreach programs. Specifically, the budget includes a total General Fund reduction of \$26.3 million to these programs, which consists of:

- **UC (\$19.3 Million Reduction).** The Governor's budget proposes a \$19.3 million General Fund reduction to UC's outreach programs. Under the proposal, UC would maintain \$12 million to allocate across its various outreach programs.
- **CSU (\$7 Million Reduction).** The Governor's budget proposes a \$7 million General Fund reduction to CSU's outreach programs.

Under the proposal, CSU would maintain \$45 million to allocate across its various outreach programs.

Figure 1
Total Funding for UC and CSU
K-14 Outreach Programs

(In Millions)

	Budgeted 2006-07	Proposed 2007-08
University of California	\$31.3	\$12.0
California State University	52.0	45.0
Totals	\$83.3	\$57.0

WHAT IS OUTREACH?

In general, outreach refers to a variety of activities aimed at helping K-12—mainly at the middle and high school grades—and community college students from disadvantaged backgrounds (such as English learner [EL] students and students from low-income families) enroll in college for either an undergraduate or graduate education. However, the term outreach can take on many different meanings depending on the context of the discussion. This often makes it difficult to clearly define the state’s outreach efforts. For example, over the years UC and CSU have repeatedly changed their definition of outreach, and have reclassified which programs fall under their definition. In our view, outreach efforts seek to address three basic obstacles that can restrict students’ access to and success in higher education: (1) inadequate academic preparation, (2) lack of information concerning the accessibility and purposes of a college education, and (3) lack of information on and assistance with financial aid and the college application process.

The state has long supported K-14 outreach programs that focus on preparing disadvantaged students for college. For example, UC’s Early Academic Outreach Program (EAOP) and the Mathematics, Engineering, Science Achievement (MESA) program have been in existence for over 25 years. On the other hand, some outreach programs are relatively new, while others have been eliminated or changed their scope over the years. Figure 2 (see page 168) summarizes the goals and services of selected K-14 outreach programs currently administered by UC and CSU. Though not

a comprehensive listing of the over 20 different programs, it includes the major programs administered by each university system. As the figure shows, many programs have overlapping goals and services.

In many ways, the evolving nature of UC and CSU's outreach efforts were the result of (1) changes in state funding for outreach programs and (2) a desire by the Legislature to ensure that the services provided by these programs are in fact effective in preparing disadvantaged students for college.

STATE FUNDING FOR OUTREACH PROGRAMS HAS VARIED

As we discuss below, the amount of state funding available to support UC and CSU's outreach programs has varied in the past ten years.

Outreach Funding Increased Rapidly in Late 1990s

UC Outreach Expansion. In 1995, the UC Board of Regents approved SP-1, a policy that prohibited campuses from using race, religion, sex, color, ethnicity, or national origin as criteria in granting admission. In 1996-97, UC began a major initiative to improve and expand outreach efforts at the university. As part of this new effort, the Regents established an Outreach Task Force (OTF). This task force proposed a comprehensive plan, which the Regents adopted in 1997, to help make disadvantaged students better aware of and prepared for higher education. The plan generally called for the university to improve its partnerships with K-12 schools, expand student academic preparation programs, and increase efforts to encourage students to pursue a higher education.

In order to implement this strategy, the state provided UC with substantial General Fund augmentations to its K-14 outreach budget. Prior to the implementation of the OTF strategy, UC spent about \$17 million in General Fund support on systemwide K-14 outreach in 1997-98. The majority of this money supported K-14 student academic programs (such as EAOP and MESA) and informational outreach and recruitment. In 1998-99, UC's K-14 outreach budget received a major General Fund augmentation of about \$43 million—more than tripling its General Fund outreach budget to roughly \$60 million. (The university also received significant additional funding from the federal government.) The state augmented UC's outreach budget again by \$9 million in 1999-00 and \$13 million in 2000-01. The above augmentations allowed UC to expand its student academic development programs and to implement a number of new initiatives which broadened its scope of K-14 outreach.

CSU Outreach Expansion. During this same period, the state also increased funding for CSU's outreach programs. In 1990-00, CSU General Fund support for outreach grew by about \$14 million (36 percent), increasing from about \$39 million to \$53 million. This augmentation was

Figure 2

Major UC and CSU Outreach Programs

University of California (UC)

Early Academic Outreach Program

- **Goals:** Increase number of disadvantaged students that (1) complete UC's A through G course requirements, (2) are ready to attend 4-year colleges, and (3) enroll in college.
- **Services:** Academic advising, academic enrichment, parent workshops, and test preparation.

Graduate and Professional School Programs

- **Goals:** Increase number of disadvantaged students that enroll in graduate and professional school programs.
- **Services:** Academic advising, tutoring, test preparation, mentoring, and academic research internships.

K-20 Regional Intersegmental Alliances

- **Goals:** Increase student capacity to raise student achievement.
- **Services:** Academic advising, mentoring, and professional development for teachers and counselors.

Mathematics, Engineering, Science Achievement Program

- **Goals:** Increase number of disadvantaged students that (1) complete UC's A through G course requirements, (2) are ready to attend 4-year colleges, and (3) enroll in college.
- **Services:** Academic and career advising, academic enrichment in math and science, tutoring, parent workshops, and test preparation.

Puente Project High School Program

- **Goals:** Increase number of disadvantaged students that (1) complete UC's A through G course requirements, (2) are ready to attend 4-year colleges, and (3) enroll in college.
- **Services:** Academic advising, academic enrichment in language arts, field trips, parent workshops, and professional development for high school teachers and counselors.

UC College Prep Online

- **Goals:** Increase number of disadvantaged students that complete UC's A through G course requirements.
- **Services:** Online college preparatory courses (such as A through G and advanced placement), tutoring, and professional development for high school teachers.

Continued

to expand programs aimed at increasing the number of K-12 students from underrepresented backgrounds that become eligible and prepared for CSU admission. The state augmented CSU's outreach budget again in 2000-01 by \$6 million.

Outreach Funding Declined for Next Few Years

UC Outreach Reductions. After peaking in 2000-01 at about \$82 million, UC's outreach budget declined for the next few years. From 2001-02 through 2004-05, UC received a total General Fund reduction of about \$53 million to its outreach programs, thus resulting in \$29.3 million for outreach in 2004-05. However, UC mitigated the impact of these funding reductions on the quality and magnitude of its outreach efforts by eliminating certain programs and services that were not targeting students most in need of assistance (such as efforts that encouraged already qualified students to enroll at a particular campus). Although General Fund support for UC's outreach programs was again reduced by \$12 million in 2005-06, the budget act instructed the university to redirect an equal amount of funding from other programs in order to maintain total outreach spending at its 2004-05 level of \$29.3 million.

CSU Outreach Reductions. During roughly the same time period, CSU's outreach budget also declined, from about \$65 million in 2002-03 to \$52 million in 2003-04. In response to this reduction, CSU streamlined

California State University (CSU)

Campus-Based Programs^a

- **Goals:** Prepare disadvantaged students for higher education.
- **Services:** Informational outreach, academic advising, academic enrichment, tutoring, mentoring, field trips, financial aid counseling, and retention services.

Early Assessment Program

- **Goals:** Improve high school students' proficiency in English and mathematics prior to entering CSU.
- **Services:** Early assessments to determine college readiness, academic enrichment, tutoring, and professional development for high school teachers.

Educational Opportunity Program

- **Goals:** Increase the college enrollment and success of low-income, disadvantaged students.
- **Services:** Academic counseling, academic enrichment, tutoring, application workshops, and financial aid grants.

^a Consists of many different programs independently developed and administered by individual CSU campuses.

many of its outreach programs in order to more efficiently serve more students with fewer fiscal resources. For example, CSU consolidated many of its programs into a new Early Assessment Program, which is intended to improve high school students' proficiency in English and mathematics prior to entering CSU. Although the General Fund support for CSU's outreach programs was reduced by another \$45 million in 2004-05, the budget act instructed the university to redirect an equal amount of funding from other programs in order to maintain total outreach funding at its 2003-04 level of \$52 million.

Outreach Funding Has Remained Stable, Despite Recent Efforts to Reduce Funding

Although the Governor has proposed in his recent budget requests to reduce funding for UC and CSU outreach programs, the Legislature has made it a priority to keep the amount of funding provided for these programs stable for the past few years. The 2006-07 budget essentially provides the same amount for these programs as provided in the prior year, which is \$31.3 million for UC and \$52 million for CSU. In fact, UC received a \$2 million General Fund augmentation in the current year for a new initiative between UC and CCC to assist potential transfer students.

PROGRAM EVALUATIONS HAVE NOT BEEN CONCLUSIVE

Over the years, the Legislature has sought to evaluate how well outreach programs are helping disadvantaged students enroll in college. As part of the past several budget acts, the Legislature adopted provisional language to ensure oversight of the use of UC and CSU's outreach funds. Specifically, the Legislature has required UC and CSU to annually report on the outcomes and effectiveness of their outreach programs. In fact, as shown in Figure 3, UC has received a combined total of about \$10 million since 1998-99 for the purpose of evaluating its own outreach efforts. For example, UC's 2006-07 outreach budget includes \$1.2 million for program evaluation. In contrast, CSU has never been provided funding specifically to evaluate its outreach programs.

Despite the significant amount of funding spent on evaluating UC's outreach programs, the universities past evaluations have not been structured in a manner to provide evidence of program effectiveness. This is not to say that outreach programs are ineffective in helping disadvantaged students enroll in college. Rather, UC's data did not conclusively demonstrate whether students participating in outreach programs would have been eligible for or likely to attend college without these services. In order to reach such conclusions, there would need to be a controlled comparison

to a similar group of students who did not participate in the programs. Thus far, the university has only done such a comparison with a small sample of students participating in EAOP. In addition, it is unclear from these studies whether the state's current outreach efforts are cost-effective in comparison to alternative approaches. Finally, the results of the evaluations provide little information as to which particular types of services (such as test preparation and tutoring) are the most effective in helping disadvantaged students enroll in college.

Figure 3	
Funding for Evaluation of UC Outreach Programs	
<i>(In Thousands)</i>	
1998-99	\$1,500
1999-00	1,530
2000-01	1,386
2001-02	1,530
2002-03	700
2003-04	353
2004-05	820
2005-06	1,180
2006-07	1,180
Total	\$10,179

DIFFERENT APPROACHES FOR EVALUATING AND FUNDING OUTREACH

We withhold recommendation on the proposed General Fund reductions to the University of California and the California State University's outreach programs, pending our review of the program evaluation reports to be submitted this spring. If the Legislature decides to restore funding for this purpose, we recommend requiring an external evaluation of these programs. Also, as an alternative approach for funding and delivering outreach services, the Legislature could establish a College Preparation Block Grant targeted at K-12 schools with very low college participation rates.

The 2006-07 *Budget Act* required that UC report to the Legislature by April 1, 2007, on the outcomes and effectiveness of its outreach programs. Similarly, the budget required CSU to report on the effectiveness of its Early Assessment Program by March 15, 2007. Until we have had an opportunity to review these reports this spring, we withhold recommendation on the Governor's proposal to reduce General Fund support for UC and CSU outreach programs. In recognition that the Legislature has made outreach a priority in recent years and may wish to provide a certain level of state funding for this purpose, we present below two issues for consideration.

External Evaluation of UC and CSU Programs

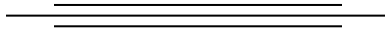
As mentioned above, the Legislature has minimal information on the effectiveness and efficiency of UC and CSU outreach programs. In part, this is because the universities are often the ones charged with evaluating the effectiveness of their own programs, and thus have little incentive to be critical in the evaluations. Rather than continue to ask and fund the universities to evaluate their own programs, we recommend calling for an external evaluation. Thus, if the Legislature decides to restore General Fund outreach funding for UC and CSU, we recommend transferring evaluation funding from UC to another state agency for the purpose of contracting out for an independent evaluation of both UC and CSU's outreach programs. An advisory committee consisting of representatives from interested parties (such as the universities, community colleges, SDE, legislative staff, and the Department of Finance) could be established to assist in selecting an appropriate evaluator. This approach would be similar to how other programs of statewide significance (such as charter schools and programs for EL students) in K-12 education have been evaluated in the past. We believe that improved evaluations would help the Legislature better understand the investments it is making in outreach and what the impact would be if it decided to reduce, increase, or reallocate its investments.

College Preparation Block Grant for K-12 Schools

In our *Analysis of the 2004-05 Budget Bill*, we reviewed the state's outreach programs and found that (1) some programs do not provide direct services to students, (2) some programs have overlapping goals and services, and (3) K-12 schools have very little control over the amount and type of outreach services that are provided to their students. For example, we found that directing a majority of outreach funding to higher education institutions makes it difficult for K-12 schools to coordinate multiple programs and integrate outreach with other education reforms. Based on our findings, we recommended that the Legislature create a College Preparation Block Grant for K-12 schools, with funds allocated to schools

with very low college participation rates. We continue to believe that this proposal merits legislative consideration.

Our proposed College Preparation Block Grant is designed to (1) target limited resources to students most in need of additional help to enroll in college and (2) leverage local schools' knowledge of their students to determine the best mix of outreach interventions. Schools would have the flexibility to use outreach funds as part of an overall strategy to assist disadvantaged students. This is because schools would have broad latitude over the use of funds, selecting a service delivery model that best meets the needs of their students. Schools could implement their own programs, or could contract with UC, CSU, or whichever provider could best meet those needs. As a condition of receiving funds through the block grant, we propose requiring schools to submit a plan to SDE specifying the types of outreach services that will be provided and how these services will accomplish measurable objectives. While we acknowledge that our proposed block grant would make significant changes to how the state currently provides outreach services, we continue to believe that it merits legislative consideration.



INTERSEGMENTAL: UC AND CSU ENROLLMENT GROWTH AND FUNDING

The Governor's budget proposes about \$120 million to fund 2.6 percent enrollment growth at the University of California (UC) and 2.5 percent enrollment growth at the California State University (CSU). This amount would provide \$10,876 in General Fund support for each additional student at UC and \$7,837 for each additional student at CSU. The proposed budget also provides \$109 million for a 2 percent enrollment increase at the California Community Colleges (CCC). In this write-up, we analyze the Governor's proposed enrollment growth and funding rates for UC and CSU in 2007-08 and recommend alternatives to those rates. (We discuss enrollment at CCC in the "California Community Colleges" section of this chapter.)

One of the principal factors influencing the state's higher education costs is the number of students enrolled at the public higher education segments. Typically, the Legislature and Governor provide funding in the annual budget act to support a specific level of enrollment growth at the state's public higher education segments. The total amount of funding provided each year to UC and CSU is based on a per-student funding rate (typically referred to as the "marginal cost" of instruction). For example, the 2006-07 Budget Act included a total of \$112 million from the General Fund to support (1) 5,149 additional students at UC at a per-student funding rate of \$9,901 and (2) 8,490 additional students at CSU at \$7,225 per student. In approving these funding amounts, the Legislature employed a new methodology for calculating the per-student funding rates. (The previous methodology—developed in 1995—was used to calculate enrollment funding from 1996-97 through 2005-06.)

For 2007-08, the Governor proposes 2.6 percent growth for UC and 2.5 percent for CSU using a new marginal cost methodology which differs significantly from the methodology recently approved by the Legislature. In the following sections, we (1) review recent enrollment trends, (2) ex-

amine the Governor's proposed enrollment growth and funding rates, and (3) recommend alternatives to those rates that are more aligned to our baseline enrollment projections and the marginal cost methodology approved for the current year.

HIGHER EDUCATION ENROLLMENT

Essentially, there are two methods of measuring higher education enrollment levels: headcount and full-time equivalent (FTE).

- **Headcount.** Headcount refers to the number of individual students attending college, whether they attend on a part-time or full-time basis.
- **FTE.** In contrast to headcount, the FTE measure converts part-time student attendance into the equivalent full-time basis. For example, two half-time students would be represented as one FTE student.

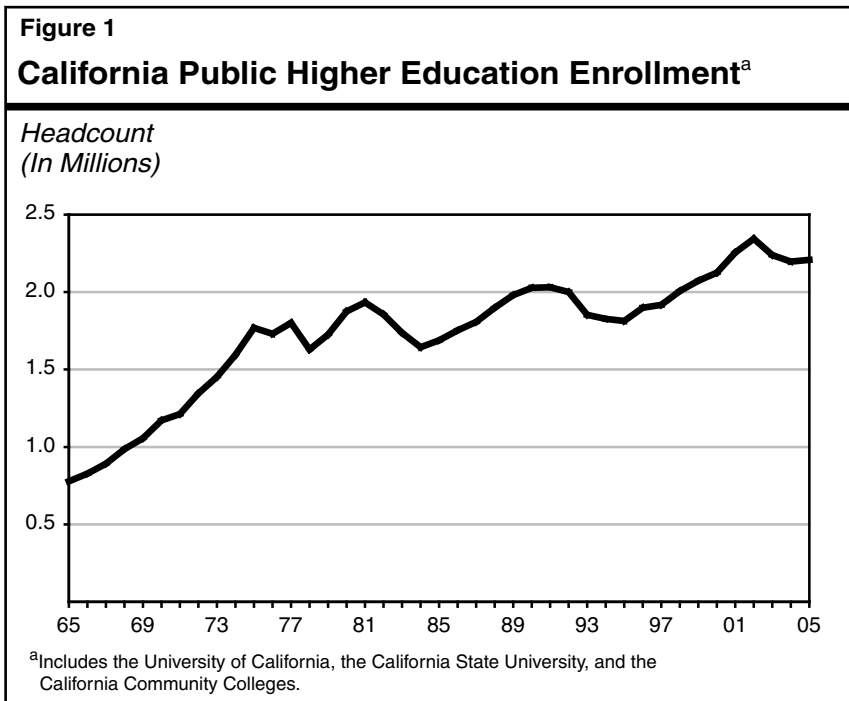
Headcount Enrollment—Higher Education Participation

Headcount measures are useful for indicating how many individuals are participating in higher education at a given point in time. For example, in fall 2005 approximately 2.2 million students (headcount) were enrolled either full-time or part-time at UC, CSU, and CCC. Figure 1 (see next page) summarizes actual headcount enrollment for the past 40 years. The figure shows that enrollment grew rapidly through 1975 and then fluctuated over the next two decades. Since 1995, enrollment grew steadily until a modest decline in 2003 and 2004, after which enrollment slightly increased. The recent decline in enrollment was largely made up of part-time community college students who were taking relatively few courses. Despite this drop in headcount, there was a much smaller decline in community college FTE enrollment. The remainder of this analysis focuses exclusively on enrollment growth funding for UC and CSU.

FTE Enrollment—Budgeted Enrollment Targets

In contrast to headcount, the FTE measure better reflects the cost of serving students (that is, the number of course units taken) and is the preferred measure used for state budgeting purposes. For example, the Legislature provides General Fund support in the annual budget act to support a specific number of state-supported FTE students at UC and CSU. (The enrollment targets specified in the budget act exclude students who do not receive state support, such as nonresident students and students enrolled in non-state supported summer programs.) Typically, this includes

funding for enrollment growth. Because the number of eligible students enrolling at the segments cannot be predicted with complete accuracy, in any given year UC and CSU typically serve slightly more or less FTE students than budgeted. In recent years, however, actual enrollment has deviated more significantly from funded levels.



In recognition of the disconnect between the number of students funded at each segment and the number of students actually enrolled, the Legislature adopted budget bill language as part of the past three annual budget acts to ensure that UC and CSU use enrollment funding only for enrollment. For example, the language in the *2006-07 Budget Act* requires that the segments report in the spring on whether they met their enrollment target for the current year. If the segment does not meet its enrollment target within 5 percent of the additional students funded (or 257 FTE students for UC and 425 FTE students for CSU), the Director of the Department of Finance (DOF) is to revert to the General Fund the total amount of enrollment funding associated with the unmet enrollment. As a result of the language in the state's recent budgets, the amount of funds reverted to the General Fund include (1) \$15.5 million in enrollment funding provided to CSU in 2004-05 and (2) \$3.8 million in funding provided

to UC in 2005-06. The proposed budget bill for 2007-08 includes similar provisions as those contained in the *2006-07 Budget Act*.

GOVERNOR'S BUDGET PROPOSAL

The budget requests a total of \$120 million in General Fund support to increase enrollment at UC and CSU. The \$120 million total consists of:

- \$54.4 million to UC for 2.6 percent enrollment growth (or 5,000 additional FTE students) above current-year budgeted enrollment, which is based on a marginal General Fund cost of \$10,876 per additional student.
- \$65.5 million to CSU for 2.5 percent enrollment growth (or 8,355 additional FTE students) above current-year budgeted enrollment, which is based on a marginal General Fund cost of \$7,837 per additional student.

In reviewing the Governor's enrollment growth proposal, the Legislature must determine the following:

- How much enrollment growth (or additional students) to fund at UC and CSU for 2007-08.
- How much General Fund support to provide the segments for each additional student.

Below, we examine each of these issues and make recommendations concerning the Governor's enrollment funding proposals.

HOW MUCH ENROLLMENT GROWTH TO FUND?

Determining the amount of additional enrollment to fund each year can be difficult. Unlike enrollment in compulsory programs such as elementary and secondary school, which corresponds exclusively with changes in the school-age population, enrollment in higher education responds to a variety of factors. Some of these factors, such as population growth, are beyond the control of the state. Others, such as higher education funding levels and fees, stem directly from state policy choices. As a result, enrollment projections must consider the interaction of demographic changes and state policies that influence enrollment demand.

There are two main factors influencing enrollment growth in higher education:

- **Population Growth.** Other things being equal, an increase in the state's college-age population causes a proportionate increase in

those who are eligible to attend each segment. Population growth, therefore, is a major factor driving increases in college enrollment. Most enrollment projections begin with estimates of growth in the potential student “pool” (18- to 24-year old population), which for the rest of the decade is expected to range from 1.4 percent to 2.4 percent annually. However, as we explain in a later section, between 2014 and 2020, this particular population is expected to shrink.

- **Participation Rates.** For any subgroup of the general population, the percentage of individuals who are enrolled in college is that subgroup’s college participation rate. California’s participation rates are among the highest in the nation. For example, California ranks fifth in college enrollment among 18- to 24-year olds. However, predicting future participation rates is difficult because students’ interest in attending college is influenced by a number of factors (including student fee levels and the availability of financial aid).

Provide 2 Percent Enrollment Growth

Based on our demographic projections, we recommend the Legislature fund budgeted enrollment growth of 2 percent for the University of California and the California State University. Our proposal should allow the segments to easily accommodate enrollment growth next year due to increases in population, as well as modest increases in college participation.

If college participation rates remain constant for all categories of students next year, we project that enrollment at UC and CSU will grow by about 1.1 percent from 2006-07 to 2007-08. (See accompanying text box for a description of the demographics-based methodology we employ to estimate future higher education levels.) Since this projection is driven solely by projected population growth, it serves as a starting point for considering how much enrollment to fund in 2007-08. In other words, the Legislature can evaluate how various related budget and policy choices could change enrollment compared to this baseline.

DOF Projects Less Growth Than Governor’s Budget. We note that DOF’s Demographics Unit also develops enrollment projections using demographic data on the projected growth in the number of high school graduates and in the adult population. However, unlike our model, DOF also assumes changes in college participation rates. According to the department, its projections are guided by the “compact” that the Governor developed with UC and CSU in spring 2004 in which he commits to seek funding for 2.5 percent enrollment growth each year through 2010-11. Thus, DOF’s projections are largely designed to *average* out to 2.5 percent

LAO Higher Education Enrollment Projections

In our demographically driven model, we calculate the ethnic, gender, and age makeup of each segment's student population, and then project separate growth rates for each group based on statewide demographic data. For example, we estimate a distinct growth rate for Latino females ages 17 through 19, calculate the resulting additional higher education enrollment that this group would contribute assuming constant participation rates. When all student groups' projected growth rates are aggregated together, we project that demographically driven enrollment at the University of California and the California State University will grow annually between 1.1 percent and 1.8 percent from 2007-08 through 2011-12. Enrollment growth near the end of this forecast period is expected to slow significantly due to slowing growth in the college-age population.

In addition to underlying demographics, enrollment growth is affected by participation rates—that is, the proportion of eligible students who actually attend the segments. Participation rates are difficult to project because they can be affected by a variety of factors—state enrollment policies, the job market, and changes in the financial situation of students and their families. We have assumed that California's participation rates will remain constant. This is because the state's rates have been relatively flat over recent years, and we are not aware of any evidence supporting alternative assumptions. We do acknowledge that participation rates could change to the extent that the Legislature makes various policy choices affecting higher education. As such, our projections provide a baseline reflecting underlying population trends.

annually from 2007-8 through 2010-11. For the budget year (2007-08), the department projects that enrollment at UC and CSU will grow respectively by 1.9 percent and 1.2 percent, which are significantly *less* than the 2.6 percent and 2.5 percent budgeted enrollment growth rates proposed by the Governor.

LAO Recommendation Accounts for Increases in Participation. Over the years, the Legislature has taken deliberate policy actions (such as funding outreach programs and expanding the availability of financial aid) in an effort to increase college participation rates. Consistent with these actions, the state has provided funding for enrollment growth in some of those years that significantly exceeded changes in the college-age population. In view of the Legislature's interest in increasing college participation, we recommend funding 2 percent enrollment growth at UC and CSU for the

budget year. This is about 80 percent higher than our estimate of population-driven enrollment growth, and therefore should allow the segments to easily accommodate enrollment growth next year, due to increases in population, as well as modest increases in college participation.

Accordingly, we recommend that the Legislature reduce the Governor's proposed enrollment growth for UC from 2.6 percent to 2 percent and for CSU from 2.5 percent to 2 percent. In a subsequent section on per-student funding rates, we discuss the General Fund savings associated with reducing the Governor's proposed growth rates.

Plan for State's Long-Term Higher Education Priorities

In view of the decline in the state's college-age population that is projected to occur in a few years, we believe that the Legislature has a special opportunity to determine and fund its long-term higher education priorities.

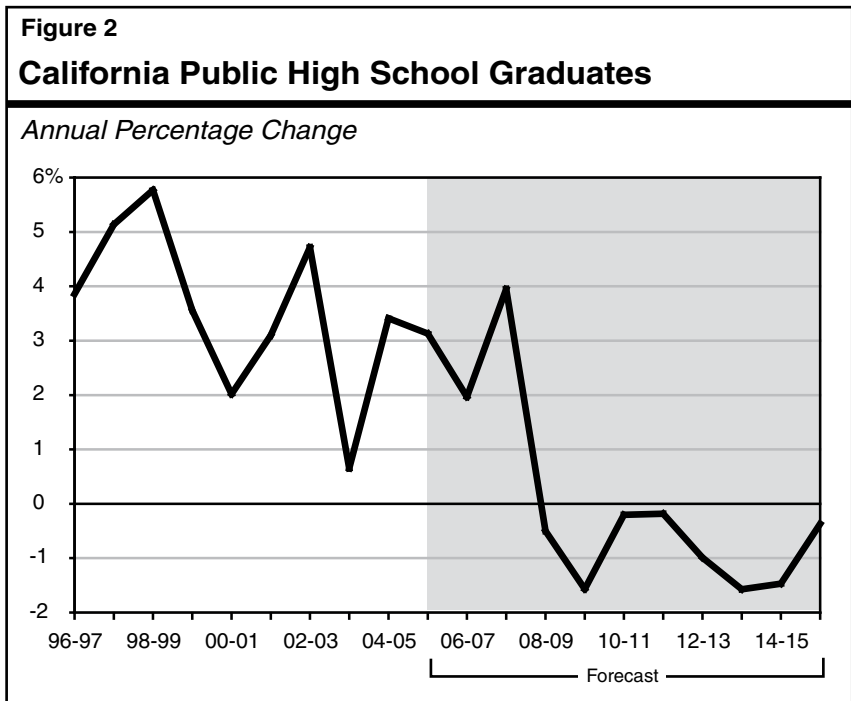
As discussed above, the state college-age population (18- to 24-year olds) is expected to shrink between 2014 and 2020. This downward trend reflects an anticipated reduction in the number of California public high school graduates starting prior to that time. As shown in Figure 2, the average growth rate in the number of high school graduates was relatively high in the past decade. Beginning in 2008-09, however, the size of this cohort is expected to decline. Between 2008-09 and 2015-16, the number of students graduating from the state's high schools is projected to fall by roughly 26,000 students.

These long-term enrollment trends have significant budgetary and policy issues implications for higher education. This is because a decline in the pool of students from which UC and CSU draw their undergraduate students—particularly at the freshman level—will consequently reduce undergraduate enrollment demands. Unlike in recent years, the state will not face demographic pressures to provide funding for undergraduate enrollment growth in order to meet the state Master Plan's promise of undergraduate education. Thus, some of the annual undergraduate growth augmentations in the future might be redirected to other priorities.

As we discuss in the "University of California" section of this chapter, much of the projected growth assumed in UC's recent long range development plans are based on campus desires to expand and create new graduate and professional school programs (such as in law and public policy). The Legislature might choose instead to fund growth in different programs—perhaps to meet identified research and workforce needs. Moreover, the Legislature might decide that increasing graduate enrollment is not as high a priority and that greater efforts should be made to

increase the percentage of eligible high school graduates that enroll at the universities (in other words, increase participation rates). Alternatively, the Legislature may desire to focus more resources on student support services rather than enrollment growth.

In view of the above, we believe that the projected decline in the state’s college-age population provides an opportune time for the Legislature to consider and plan for the state’s long-term needs in higher education from both a policy and fiscal standpoint. (In our “University of California” and “California State University” write-ups, we recommend the Legislature direct UC and CSU to provide updated systemwide enrollment projections—including an explanation of the assumptions and data used to calculate them—at budget hearings this spring.)



HOW MUCH GENERAL FUND SUPPORT SHOULD BE PROVIDED FOR EACH ADDITIONAL STUDENT?

In addition to deciding the number of additional FTE students to fund in 2007-08, the Legislature must also determine the *amount* of funding to provide each additional FTE student at UC and CSU. Consistent with past

practice, this funding level would be based on the marginal cost imposed by each additional student for additional faculty, teaching assistants, equipment and various support services. The marginal cost is less than the average cost because it reflects what are called “economies of scale”—that is, it excludes certain fixed costs (such as central administration) which may change very little as new students are added to an existing campus. The marginal costs of a UC and CSU education are funded from the state General Fund and student fee revenue. (A similar, but distinct, approach is used for funding enrollment growth at community colleges.)

From 1996-97 through 2005-06, the state essentially used the same methodology (as initially established in 1995) to calculate the marginal cost of instruction. As part of his budget proposal for 2006-07, the Governor last year proposed a new marginal cost methodology for funding enrollment growth at UC and CSU. In adopting the 2006-07 budget, however, the Legislature rejected the Governor’s marginal cost proposal and instead used its own alternative methodology for funding enrollment growth. As we discuss below, the Governor’s budget for 2007-08 employs the same marginal cost methodology that the Legislature rejected last year. Based on his proposed methodology, which differs significantly from the one assumed in the 2006-07 budget, the Governor’s budget provides \$10,876 in General Fund support for each additional student at UC and \$7,837 for each additional student at CSU. In this section, we analyze the Governor’s proposed methodology and recommend funding rates based on the methodology recently approved by the Legislature.

Development of the Marginal Cost Methodology

For many years, the state has funded enrollment growth at UC and CSU based on the marginal cost of instruction. However, the formula used to calculate the marginal cost has evolved over the years. In general, the state has sought to simplify the way it funds enrollment growth and more accurately reflect costs. As we discuss below, the state has moved from utilizing a large number of complex funding formulas for each segment to a more simplified approach for calculating enrollment funding that is more consistent across the two university systems.

UC and CSU Used Different Methodologies Before 1992

From 1960 through 1992, CSU’s enrollment growth funding was determined by using a separate marginal cost rate for each type of enrollment category (for example, lower-division lecture courses). In other words, the different marginal cost formulas took into account education levels—lower division, upper division, and graduate school—and “instructional modes” (including lecture seminar, laboratories, and independent study). Each

year, CSU determined the number of additional academic-related positions needed in the budget year (based on specific student-faculty ratios) to meet its enrollment target. These data were used to derive the separate marginal cost rates.

Similar to CSU, annual enrollment growth funding provided to UC before 1992 was based on a particular mix of new students, with different groups of students funded at different rates. However, UC's marginal cost methodology was simpler and did not require the calculation of different rates based on modes of instruction. The university calculated separate funding rates for undergraduate students, graduate students, and for each health science program based on an associated student-faculty ratio. Each cost formula also estimated the increased costs for library support due to enrolling additional students.

New Methodology Adopted in 1990s

Beginning in 1992-93, the Legislature and Governor suspended the above marginal cost funding practices for UC and CSU. While the state did provide base budget increases to the universities, it did not provide funding specifically for enrollment growth during that time. In the *Supplemental Report of the 1994 Budget Act*, the Legislature stated its intent that, beginning in the 1996-97 budget, the state would return to the use of the marginal cost as the basis for funding enrollment growth. Specifically, the language required representatives from our office, UC, CSU, and DOF to review the 1991-92 marginal cost formulas and propose improvements that could be used in developing the 1996-97 budget.

Compromise Methodology Adopted for 1996-97. After a series of negotiations, the four agencies developed a new methodology for estimating the amount of funding needed to support each additional FTE student at each segment. This methodology reflected a compromise that all parties agreed should be the basis for funding future enrollment growth. The methodology was first implemented in 1996-97 and was generally used to calculate enrollment funding through 2005-06. Some of the key features of this methodology included:

- ***Single Marginal Cost Formula for Each Segment.*** Enrollment growth funding was no longer based on differential funding formulas by education level and academic program. Instead, each university segment used one formula to calculate a single marginal cost that reflected the weighted costs of all the system's education levels and academic programs.
- ***Marginal Cost for Additional Program Areas.*** The working group concluded that the marginal cost formula should include

additional cost components beyond academic salaries. As a result, the 1995 methodology took into account costs for eight program areas—faculty salary (based on entry-level, rather than average, salaries), faculty benefits, teaching assistants, academic support, instructional support, student services, institutional support, and instructional equipment. These program costs were based on current-year funding and enrollment levels, and then discounted to adjust for fixed costs that typically are not affected by year-to-year changes in enrollment.

- ***Student Fee Revenue Adjustments.*** The working group agreed that both General Fund and student fee revenue contribute toward the total marginal cost. This reflected a long-standing practice that students and the state share in the cost of education. It also acknowledged that fee revenue is used for general purposes—the same as General Fund revenue. Therefore, under the methodology, a portion of the student fee revenue anticipated from the additional students was subtracted from the total marginal cost in order to determine how much General Fund support the state should provide for each additional student.

Marginal Cost Review Requested for 2006-07

In adopting the 2005-06 budget, the Legislature called for a review of the marginal cost methodology that was developed in 1995. Specifically, the *Supplemental Report of the 2005 Budget Act* directed our office and DOF to jointly convene a new working group, including representatives from UC and CSU, to examine possible modifications to the 1995 methodology for the 2006-07 budget. Although our office and DOF worked collaboratively during the summer and fall of 2005, we were not able to reach consensus on a new methodology, and the Governor's budget proposal for 2006-07 included enrollment funding based on an entirely new methodology developed by the administration. (In our *Analysis of the 2006-07 Budget Bill*, we recommended an alternative methodology.)

Legislature Rejected Governor's Proposal and Adopted a New Methodology. In adopting the 2006-07 budget, the Legislature rejected the Governor's marginal cost proposal and instead used its own alternative methodology to fund UC and CSU enrollment growth. Based on this methodology, the *2006-07 Budget Act* provides enrollment growth funding at rates much higher than would have been provided under the 1995 methodology—\$9,901 for each additional UC student and \$7,225 for each additional CSU student. (These represent increases of about 30 percent for UC and 15 percent for CSU compared to the marginal costs rates provided in 2005-06.) In signing the budget, the Governor vetoed provisional

language specifying that future budgets be based on the methodology adopted by the Legislature.

The legislative methodology maintains the same underlying basis of the 1995 methodology—that is, determining a total marginal cost based on current-year expenditures and “backing out” a student fee component to determine the state’s share. However, it more accurately accounts for increased costs associated with enrollment growth. In developing the methodology, the Legislature incorporated many of the suggestions made by the segments during the marginal cost working group discussions and during budget deliberations last spring (such as including costs for operation and maintenance and adjustments to the faculty salary amounts). The major features of the legislative methodology include:

- ***Bases Faculty Costs on Salaries of All Recently Hired Professors.*** The 1995 methodology calculated the cost of hiring additional faculty based on the published salary of an entry-level assistant professor. The legislative proposal bases faculty costs on the average annual salary paid to all new professors (regardless of level) that were hired in the past year.
- ***Modifies Marginal Cost Components.*** Rather than discount each program by a particular percentage to adjust for fixed costs, the legislative methodology excludes the specific activities under each program area that typically are not affected by year-to-year changes in enrollment. For example, the methodology excludes funding for museums and galleries from the marginal cost of academic support. In addition, the methodology adds operations and maintenance as a new cost component.
- ***Changes Definition of CSU Graduate FTE Student.*** The marginal cost methodology adopted by the Legislature redefines a full-time CSU graduate student from 30 units per year to 24 units, as requested by the university.
- ***More Accurately Accounts for Available Student Fee Revenue.*** In order to determine how much state support is needed for each additional student, the marginal cost formula must back out the fees that the segments anticipate collecting from each student. Under the 1995 methodology, this was based on the percentage of the university’s entire budget supported by student fee revenue. For example, if fee revenue supported 30 percent of UC’s budget, then new fee revenue would be deemed to support 30 percent of the marginal cost. In contrast, the “fee backout” amount in the legislative methodology is based on the average systemwide fee revenue collected from each FTE student, discounted for fee revenue that supports financial aid programs.

Governor Proposes Same Methodology That Legislature Rejected

For 2007-08, the Governor uses the same marginal cost methodology that he used last year in his January budget for 2006-07, which the Legislature rejected. As mentioned above, the Legislature approved enrollment growth funding for 2006-07 based on the revised marginal cost methodology. The major ways that the Governor's methodology deviates from the legislative methodology are:

- ***Calculates Only General Fund Contribution.*** As mentioned above, the legislative methodology—as did the previous methodology established in 1995—calculates a total marginal cost, and then subtracts from this cost the fee revenue UC and CSU anticipate from each additional student, in order to determine how much General Fund support is needed from the state. In contrast, the Governor's methodology attempts to isolate the amount of General Fund spent on each program affected by changes in enrollment in order to determine the General Fund cost of each additional student. Because General Fund and fee revenue are entirely fungible, the Governor's approach must make arbitrary assumptions about the distribution of General Fund and fee support at each segment, which may over-estimate or underestimate the amount of General Fund actually spent on each program.
- ***Assumes Average Costs for All Existing Faculty.*** Based on a fixed student-faculty ratio, the legislative methodology calculates the cost of hiring a new professor to serve a specified number of students (based on the salaries paid to recent faculty hires). In contrast, the Governor's proposal bases the faculty costs on the average salary paid to all existing professors (regardless of how long they have been employed at the university).
- ***Adjusts for Base Increases Assumed in Governor's Compact.*** The legislative methodology—as did the 1995 methodology—is based only on current-year expenditures and, therefore, does not account for any funding changes proposed for the budget year. The Governor, however, calculates a General Fund marginal cost for each segment using current-year data, and then adjusts that cost by the base increase specified in his compact with UC and CSU (4 percent for 2007-08). This adjusted amount would be used to fund enrollment growth in 2007-08.

Based on the Governor's marginal cost methodology, the proposed budget provides \$10,876 in General Fund support for each additional student at UC and \$7,837 for each additional student at CSU. In comparison,

we estimate that the legislative marginal cost methodology would call for a UC General Fund cost of \$10,586 and a CSU General Fund cost of \$7,710. Figure 3 provides a detailed description of the marginal cost calculations for 2007-08 based on the legislative methodology. In the following section, we raise concerns about the Governor's proposed marginal cost methodology.

Figure 3		
Marginal Cost Calculations Based on Legislative Methodology		
<i>2007-08</i>		
	Marginal Cost Per FTE^a Student	
	UC	CSU
Faculty salary	\$4,611	\$3,415
Faculty benefits	821	1,290
Teaching assistants	504	17
Instructional equipment replacement	598	119
Instructional support	3,938	836
Academic support	1,363	1,345
Student services	1,083	1,039
Institutional support	872	973
Operations and maintenance	1,679	933
Totals	\$15,469	\$9,967
Less student fee revenue	-\$4,883	-\$2,257
State Funding Rate	\$10,586	\$7,710
Governor's Proposed Methodology	\$10,876	\$7,837
^a Full-time equivalent.		

Concerns With Governor's Proposal

As we advised the Legislature last year, we believe that the Governor's proposed marginal cost methodology has significant shortcomings (such as assuming average faculty costs), which in large part is why the Legislature rejected it last year. The Governor's methodology represents a significant departure from the underlying rationale behind the methodology approved by the Legislature in the 2006-07 budget and the methodology previously used for the past ten years. We also find that the Governor's proposal does

not accurately capture the increased costs associated with enrollment growth, and is unnecessarily complex and lacks transparency. Figure 4 summarizes our concerns, which we discuss in further detail below.

Figure 4

Legislature Should Again Reject Governor's Marginal Cost Proposal

- ✓ ***Ignores Contribution of Student Fees.*** The proposed methodology does not account for new student fee revenue resulting from fee increases that is available to support a greater share of the marginal cost of instruction. In addition, the methodology does not recognize that General Fund and fee revenue are “fungible” resources that support the total marginal cost.
- ✓ ***Overbudgets Faculty Costs.*** The Governor's proposal assumes faculty costs at the University of California and the California State University will increase on the average (rather than on the margin) with each additional full-time equivalent student.
- ✓ ***Limits Legislative Budgetary Discretion.*** The methodology assumes that the Legislature will approve the annual base budget increase contained in the Governor's compact each year. Moreover, it “shields” the marginal cost from policy decisions, such as changes to the share of education cost paid by students.

Ignores Contribution of Student Fees

In adopting its marginal cost methodology, the Legislature recognized that both General Fund and student fee revenue together fund the marginal cost of serving an additional FTE student. After a total marginal cost is calculated, the fee revenue UC and CSU anticipate collecting from each additional student gets subtracted from this cost, in order to determine the state's share. Thus, this methodology acknowledges that because General Fund and fee revenue are fungible resources used for general purposes, it is difficult—and unnecessary—to determine (based on complex calculations and arbitrary assumptions) how much of specific program costs are borne by the General Fund as opposed to student fee revenue.

Unlike this approach, the Governor's proposal does not account for new student fee revenue resulting from the increases. Since the methodology calculates only General Fund contributions, it ignores the availability of fee revenue to account for a greater share of the marginal cost

of instruction. Rather, we believe that the Legislature should continue to consider new fee revenue as available to meet legislatively determined needs of the segments.

Overbudgets Faculty Costs

The Governor's proposed methodology assumes that faculty costs at UC and CSU will increase on average (rather than on the margin) with additional FTE students. To put it in another way, the proposal assumes that a cohort of faculty hired at each segment because of enrollment growth will reflect the make-up of existing faculty at that segment, in terms of level or classification. However, the most recent data available from UC and CSU on the salaries and make-up of recently hired faculty compared to all existing faculty indicates that this is not the case. In fact, the opposite is true.

In 2005-06, UC hired a total of 354 new faculty members. Of this amount, 68 percent were hired at the assistant professor level. In comparison, only about 18 percent of UC's current faculty members are assistant professors. About 63 percent of the current faculty is at the higher-paid level of full professor. In terms of actual salary, the average salary of all faculty members at UC is \$100,548, which is significantly higher than the \$83,714 average salary of recent hires. The CSU reports similar differences in the make-up and salaries of new faculty hires compared to those faculty members already at the university. In view of the above, we find that the Governor's marginal cost proposal overbudgets the marginal cost of hiring additional faculty.

Limits Legislative Budgetary Discretion

The proposed methodology assumes that the Legislature will approve the annual General Fund base budget adjustments contained in the Governor's compact with UC and CSU. This is because the methodology calculates a General Fund marginal cost for each segment using current-year expenditures, and then adjusts that cost by the General Fund base budget increase specified in the compact for the budget year. We believe that there is no reason to assume that the base increase called for in the compact is the appropriate amount each year. The right amount could be more or could be less. Moreover, although the Governor's marginal cost rate for the 2007-08 is based on an adjustment for his proposed 4 percent base increase, it ignores his other proposal to increase student fees by 7 percent at UC and 10 percent at CSU. (We analyze the Governor's student fee proposals in a subsequent section of this chapter.) In other words, the proposed methodology "shields" the marginal cost from policy deci-

sions, such as increasing or decreasing the share of education cost paid by students.

Fund Enrollment Growth Based on Legislative Methodology

We recommend the Legislature fund enrollment growth at the University of California (UC) and the California State University (CSU) based on the marginal cost methodology it developed and approved as part of the 2006-07 budget. Using this methodology and our proposed 2 percent enrollment growth, we recommend deleting \$27.3 million from the \$120 million requested in the budget for enrollment growth at UC and CSU. Our proposal would leave sufficient funding to provide \$10,856 for each additional UC student and \$7,710 for each additional CSU student. We further recommend the Legislature (1) amend the proposed budget bill language to reflect these marginal cost and enrollment growth rates and (2) adopt supplemental report language specifying that enrollment growth funding provided in future budgets be based on the legislative methodology. (Reduce Item 6440-001-0001 by \$13.4 million and Item 6610-001-0001 by \$13.9 million.)

Given our concerns above, we recommend the Legislature once again reject the Governor's proposed marginal cost methodology. Rather, we support the underlying basis of the legislatively determined marginal cost methodology—that is, determining a total marginal cost based on current-year expenditures and backing out a student fee component to determine the state's share. We find that it more appropriately funds the increased costs associated with enrollment growth and preserves legislative prerogatives. Accordingly, we propose funding enrollment growth at UC and CSU based on the marginal cost methodology that the Legislature developed and approved as part of the 2006-07 budget. Specifically, we recommend the Legislature provide \$10,856 in General Fund support for each additional FTE student at UC and \$7,710 for each additional student at CSU—which are slightly lower than the Governor's proposed funding rates.

After incorporating our earlier proposal to fund enrollment growth at a rate of 2 percent at both UC and CSU, we therefore recommend reducing the Governor's proposed General Fund augmentation for enrollment growth by a total of \$27.3 million, including \$13.4 million from UC and \$13.9 million from CSU. Under our proposal, the segments would still receive sufficient funding to cover the estimated enrollment growth due to increases in population and college participation. At the same time, the Legislature could use our identified General Fund savings for other priorities, including the state's budget problem.

We further recommend the Legislature amend the proposed budget bill language to reflect our recommended marginal cost and enrollment growth rates for state-supported students. Moreover, we recommend the Legislature adopt supplemental report language specifying its intent that enrollment growth funding provided to UC and CSU in subsequent budgets be based on the legislative methodology for determining the marginal cost of instruction.

INTERSEGMENTAL: STUDENT FEES

The Governor's budget assumes that the University of California and the California State University will enact fee increases of 7 percent and 10 percent for resident students at their respective campuses. We recommend lower fee increases of 2.4 percent for both systems. The 2.4 percent fee increase would match the increase in overall costs experienced by the segments due to inflation, and would ensure that students continued to pay the same share of their educational cost as they are paying in the current year. We also recommend that the Legislature not "buy out" any portion of the Governor's proposed fee increase because such an approach confuses the role of fees and undermines the Legislature's role in budgeting. We do not recommend any change to the Governor's proposed fee level for the community colleges, which would maintain the \$20 per unit fee that went into effect in January 2007.

Setting Student Fee Levels

Student fees are an important component of higher education budgets, both as a source of revenue and as a factor in affordability. Formally, the Legislature sets student fee levels for the California Community Colleges (CCC) in statute, while the University of California (UC) Board of Regents and the California State University (CSU) Board of Trustees set student fees for their respective systems. As a practical matter, however, the Legislature assumes a certain level of revenue to be generated by student fees when it approves funding for all three of the segments in the annual budget act. That is, the Legislature takes projected student fee revenue and other sources of funding into consideration when it decides what level of General Fund support to appropriate for the higher education segments. (See nearby box for a discussion of how the Legislature can affect fee levels at UC and CSU.)

State Has No Explicit Fee Policy. The state currently does not have an explicit policy for setting fee levels at any of the higher education segments.

How Can the Legislature Influence Fee Levels?

As noted in the text, the Legislature sets fees for the California Community Colleges while fees at the University of California (UC) and the California State University (CSU) are set by their respective governing bodies. However, in adopting the annual state budget, the Legislature can wield considerable influence over UC and CSU fee levels.

Assuming a Fee Level. In its deliberations over the annual budget, the Legislature assumes a particular level of fee revenue that will be generated by student fees. That revenue estimate could assume that fees increase, decrease, or remain at their current levels. The Legislature takes this assumed amount of fee revenue into account as it decides what level of General Fund revenue to appropriate for each segment.

What if the Segments Want a Lower Fee? Even if UC or CSU desired to enact a lower fee level than assumed by the Legislature, there is a strong fiscal incentive for the university to enact the Legislature's assumed fee. This is because a lower fee level would cause the segment to receive less total revenue than assumed in the budget act.

What if the Segments Want a Higher Fee? The situation is different if a segment desires to enact a fee that is *higher* than the level envisioned by the Legislature. A higher fee level would result in the segment receiving more revenue than assumed in the budget act. And because fee revenue is continuously appropriated to UC and CSU, it is available for their use without an appropriation in the budget act.

However, there are still ways that the Legislature can encourage the segments to adopt fee levels more in line with its assumptions. For example, the Legislature could adopt budget bill language stating its intent with regard to fee levels, and providing for a reduction in the segment's General Fund appropriation by the same amount as any "excess" fee revenue. This would eliminate any financial benefit the segment would receive from raising fees above the prescribed level. Alternatively, the Legislature could take the excess fee revenue into account when it decided on a General Fund appropriation for the segment in the following fiscal year.

Legislature Has a Role in Making Annual Fee Decisions. Because of these and other options available to the Legislature, the university segments have an incentive to work with the Legislature when setting annual fee levels.

The state's 1960 *Master Plan for Higher Education* recommends against charging student "tuition" to support instructional costs for resident students. It does, however, call for students to pay "fees" that support operating costs "not directly related to instruction." Given that the state provides over \$10 billion per year for the support of the three segments and given the broad variety of costs that the segments regularly incur, it is difficult to identify which specific costs are borne by students and which are borne by the state. As a result, the distinction between fees and tuition has been largely a semantic one. A 2002 report by a joint legislative committee to review and expand the Master Plan acknowledged the practical and semantic difficulties with the "no tuition" approach, and recommended that this be replaced by a more explicit policy—one in which student fees were increased in a "gradual, moderate, and predictable fashion...." Over the years, the Legislature has made various efforts to establish such a policy. At this time, however, the state continues to lack a formal, explicit policy that would unambiguously guide annual fee levels.

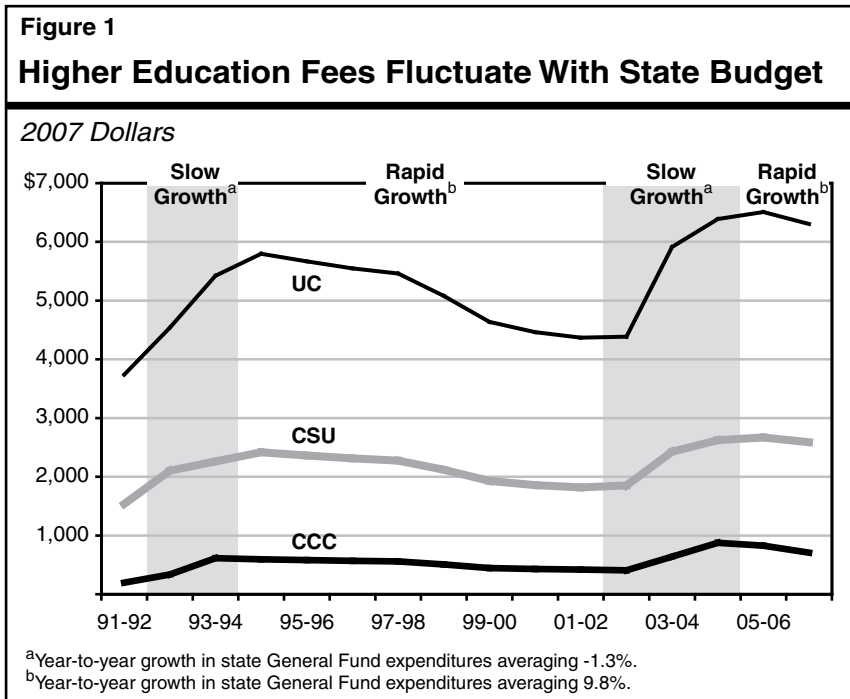
Instead, the state generally operates under an *implicit* policy whereby students and the state are expected to share educational costs, but with the relative proportions dependent on the state's fiscal situation. As shown in Figure 1, over the past fifteen years student fees have increased quite steeply during tight budget years and have gradually declined when the state budget situation improved. This approach works against the interests of students in two important ways. First, the unpredictability and volatility of the fee levels make it difficult for students and their families to plan for educational costs. Second, fee changes tend to move in the opposite direction of the average students' ability to pay—increasing when per capita income tends to slow, and decreasing when per capita income tends to increase.

Explicit Student Fee Policy Needed

For these reasons, we recommend that the Legislature adopt an explicit fee policy that maintains rational and predictable fee levels at all three segments. In previous reports (see for example our *Analysis of the 2005-06 Budget Bill*, pages E-184 through E-187), we have recommended a policy that bases student fees at each segment on a fixed share of their total educational costs. Such a policy would both provide an underlying rationale for fee levels and a simple mechanism for annually adjusting them. This would promote clarity by establishing an expected contribution from all nonneedy students, regardless of when they enter college. (Financial access for *needy* students is addressed through financial aid programs, rather than fee policies.) It would promote consistency by routinely adjusting fee levels such that nonneedy students pay the same share of cost over time. It also would recognize that college is a partnership between

students and the general public—expecting both to contribute to its costs and intending for both to benefit from its activities. Lastly, a share-of-cost policy would ensure that students and the university share the cost of any new program or program enhancement, thereby providing a strong incentive for students to hold their campuses accountable for making quality investments at reasonable cost.

For all these reasons, an explicit share-of-cost fee policy can be an important component of the state’s higher education policy and one that is consistent with the state’s goals concerning access and accountability.



ABSENT POLICY DIRECTION, MAINTAIN CURRENT SHARE OF COST FOR 2007-08

Without an explicit fee policy in place to guide legislative action on the higher education budgets, we recommend that the Legislature at least maintain the share of cost that student fees cover in the current year. This would result in fee increases of 2.4 percent, or about one-third and one-quarter of what the Governor proposes for the University of California and the California State University, respectively.

Current Fee Levels Modest by National Standards

By almost any state comparison measure, student fees at California's public higher education segments are relatively low. The average fee charged by California's public universities is only about four-fifths of the national average; only 15 states have lower average fees. Looking at the interaction of fees, financial aid, and other factors in a 2006 report, the National Center for Public Policy and Higher Education found California's higher education system to be the most affordable (tied with Utah) in the nation. In part this is due to California's Cal Grant entitlement program, which guarantees fee coverage for all eligible students. In addition, California's community college fees are by far the lowest in the nation (and about one-quarter of the national average).

Given California's relatively low fees and its extensive financial aid programs, we think the state could make a policy choice to increase the share of costs borne by students in the form of fees. However, until such a time as the Legislature has made such a policy decision about fee levels, we recommend the Legislature simply maintain the current shares of cost. In other words, fees would increase at the same rate as each segment's overall cost of education. This would also reduce pressure to subject students to larger year-to-year fee increases in subsequent years.

Governor Proposes Fee Increases for 2007-08. After experiencing no fee increase in 2006-07, UC and CSU students would face fee increases of 7 percent and 10 percent, respectively, in 2007-08 under the Governor's proposal. (In addition to the proposed 7 percent increase, UC fees for 2007-08 would also include a new, temporary surcharge of \$60 per student. The UC is levying this surcharge on all students to compensate for some student fee revenue it had to forgo in response to a lawsuit brought by some graduate students.) The Governor proposes no fee increase for the community colleges. The CCC fee was reduced by 23 percent (to \$20 per unit) halfway through the current fiscal year, and under the Governor's proposal would remain at \$20 per unit in the budget year.

Figure 2 shows the Governor's proposed fee levels and the associated changes to fee revenue. The UC and CSU fee increases would generate \$105 million and \$98 million, respectively, in additional revenue. For CCC, the fees paid by a full-time student would decline by \$90 between the current year and the budget year due to the full-year effect of the fee increase in 2007-08. This would reduce year-to-year total fee revenue by an estimated \$33.2 million. The Governor's budget includes this amount in General Fund revenue to backfill the forgone fee revenue.

The Governor provides no rationale for the proposed fee levels. The UC and CSU increases are tied to neither an inflationary index nor a specified share of cost.

Figure 2
Governor's Resident Student Fee Proposal

	Actual 2006-07	Proposed 2007-08	Change	
			Amount	Percent
University of California				
Undergraduate	\$6,141	\$6,571 ^a	\$430	7%
Graduate	6,897	7,380 ^a	483	7
Special Fees:				
Veterinary Medicine	10,882	11,646	764	7
Dentistry	15,798	16,902	1,104	7
Business/Management ^b	15,824	17,192	1,368	9
Law ^b	15,674	17,241	1,567	10
Medicine	13,440	14,380	940	7
Optometry	9,542	10,210	668	7
Pharmacy	11,098	11,874	776	7
Nursing	3,218	3,444	226	7
Theater, Film, and TV	5,959	6,375	416	7
Public Health	4,000	4,281	281	7
Public Policy	4,000	4,281	281	7
International Relations/Pacific Studies	4,000	4,281	281	7
California State University				
Undergraduate	\$2,520	\$2,772	\$252	10%
Teacher Education	2,922	3,216	294	10
Graduate	3,102	3,414	312	10
California Community Colleges	\$690	\$600	-\$90	-13%

^a Does *not* include \$60 temporary surcharge to cover income losses associated with student fee lawsuit.
^b Amount represents midpoint of range of fees.

Recommend Lower Fee Increases at UC and CSU

Absent an explicit fee policy, we recommend that the current share of educational costs borne by students through fees be maintained in the next year. In the "University of California" and "California State University" sections of this chapter, we recommend funding new costs (primarily those resulting from inflation) that would increase the cost of education by about 2.4 percent. We recommend, therefore, that UC and CSU fees be increased by the same percentage. (The \$60 temporary surcharge would raise the UC fee increase to about 3.4 percent.) Increasing CCC fees by the same percentage as educational costs would only increase fees by less than

50 cents per unit. Given that community college fees have historically been set in increments of one dollar, and given the recent implementation of the new fee level, we do not recommend a change to CCC fees in 2007-08. Figure 3 shows our recommended fee levels.

Figure 3
LAO Recommended Resident Fee Levels

	Actual 2006-07	Proposed 2007-08	Change	
			Amount	Percent
University of California				
Undergraduate	\$6,141	\$6,288 ^a	\$147	2.4%
Graduate	6,897	7,063 ^a	166	2.4
Special Fees:				
Veterinary Medicine	10,882	11,143	361	2.4
Dentistry	15,798	16,177	379	2.4
Business/Management ^b	15,824	16,203	380	2.4
Law ^b	15,674	16,050	376	2.4
Medicine	13,440	13,763	323	2.4
Optometry	9,542	9,771	229	2.4
Pharmacy	11,098	11,364	266	2.4
Nursing	3,218	3,295	77	2.4
Theater, Film, and TV	5,959	6,102	143	2.4
Public Health	4,000	4,096	96	2.4
Public Policy	4,000	4,096	96	2.4
International Relations/Pacific Studies	4,000	4,096	96	2.4
California State University				
Undergraduate	\$2,520	\$2,580	\$60	2.4%
Teacher Education	2,922	2,992	70	2.4
Graduate	3,102	3,176	74	2.4

^a Does *not* include \$60 temporary surcharge to cover income losses associated with student fee lawsuit.
^b Amount represents midpoint of range of fees.

Our proposed fee increases would generate \$36 million and \$23.5 million in additional revenue for UC and CSU, respectively. (This is less than the new fee revenue that would be generated by the Governor's proposed fee levels.) In the "University of California" and "California State University" sections later in this chapter, we account for these new fee revenues and address related affordability issues. In the "Student Aid Commission"

section, we also show how our recommended fee levels would generate General Fund savings in the Cal Grant program.

Implementing Our Recommended Fee Levels. As noted earlier in this write-up, there are various ways for the Legislature to act on whatever decision it makes about fees. Although the Legislature does not formally set fees for UC and CSU, it can explicitly incorporate its expectations into the budget act and, if deemed necessary, adopt provisions that create incentives for the segments' governing boards to enact the fee levels assumed in the budget. In any case, however, there is no need for the Legislature to "buy out" any portion of the Governor's proposed fee increases, as we discuss below.

"Buying Out" Proposed Fee Increases Does Not Make Sense

Last January in his 2006-07 budget proposal, the Governor characterized as a "fee buyout" part of his proposed General Fund augmentations for UC and CSU. Specifically, the Governor proposed to provide the segments with General Fund support in lieu of revenue they would have received from planned fee increases of 8 percent to 10 percent. The Governor in effect argued that his proposed augmentation was the "cost" of forgoing the fee increases. We believe that the notion of buying out a fee increase confuses the role of fees and undermines the Legislature's role in budgeting.

Confuses Needs and Resources. Student fees are a form of revenue that supports the general operations of the universities. Fee revenue is completely interchangeable with General Fund revenue in supporting university programs. The notion of a fee buyout, however, improperly treats a fee increase not as a resource to cover costs, but as a need in itself. Therefore, we believe a decision by the Governor or a segment to raise fees is not evidence of new need that must somehow be covered, but rather it is a policy choice about the share of total need that should be covered by students.

Undermines Legislature's Budgeting Role. Under the mistaken logic of a fee buyout, if the Legislature does not want for a segment to enact a proposed fee increase, then it must provide the same amount of General Fund support that would have been generated by the fee increase. This improperly limits the Legislature's budget choices in two ways:

- It permits the segment to set whatever price it wants as the cost of avoiding a fee increase. It could propose a fee increase of 10 percent or 25 percent, or whatever it wished, and this would in turn define the amount of state support that the Legislature would have to provide to avoid a fee increase.

- It shields the fee buyout amount from scrutiny as to what it would purchase. For example, in 2006-07 the Governor proposed fee buyouts for UC and CSU that totaled \$130 million, but offered no explanation as to what specifically these augmentations would fund.

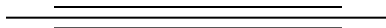
The joint legislative committee that reviewed the Master Plan in 2002 recognized the dangers of giving in to the temptation to avoid annual fee increases, and thus recommended that the state *not* “buy out these fees with taxpayer dollars.”

Legislature Should Decide Funding Needs First and Fee Levels Second. It is easy for the Legislature to avoid the trap presented by the notion of a fee buyout. Instead of starting by considering the fee increase amount to be a “need,” the Legislature should start by considering what total funding needs the segment will face. New costs might include enrollment growth, inflationary effects, and perhaps new programs or services. The total of these new costs could then be divided in some way between the students’ share and the state’s share. The level of fee increase to be imposed on students would result from a choice about how these new costs should be split between students and the state.

What About the Backfill of CCC’s Fee Reduction?

As noted earlier, the Governor’s budget includes \$33.2 million to backfill the remaining annualized cost of the CCC fee reduction that went into effect in January 2007. We do not take issue with this backfill. In fact, we believe the CCC backfill is a good example of the budgeting approach we recommend the Legislature take with regard to the relationship between fees and General Fund support.

The Legislature made its decision to reduce CCC fees near the end of its 2006-07 budget deliberations, after it had made most of its decisions about what levels of program funding it wanted to provide. The decision to reduce fees was based not on a desire to increase or reduce total program funding, but rather sought to reduce the amount of total costs that would be paid by students. Thus, the backfill of the fee reduction reflects an effort to maintain support for a particular, agreed-upon level of programs and service. In contrast, starting with a decision simply to buy out the fee increases proposed by the Governor for UC and CSU would be based on achieving a particular level of funding augmentations which have not yet been approved by the Legislature.



INTERSEGMENTAL: HIGHER EDUCATION NURSING PROPOSALS

The Governor's budget contains several augmentations for registered nursing programs at the University of California, California State University, and California Community College systems. We recognize the need to increase the number of registered nurses in the state, and find merit with some of the Governor's proposals. Other proposals, however, lack adequate justification. We thus recommend approval of some proposals and reductions in others, as well as additional steps the Legislature could take to improve nursing programs.

In recent years, numerous studies have forecasted that—absent corrective actions—there will be an increasing mismatch between the supply of and demand for nurses as the state's population increases and grows older. In response, the Legislature has taken a number of steps to increase the supply of nurses. In particular, the Legislature has focused on increasing capacity in the state's higher education system, which plays a central role in training students to become registered nurses. The Governor's budget includes several new nursing-related proposals for the University of California (UC), California State University (CSU), and California Community Colleges (CCC). In this write-up we provide an overview of state's nursing programs, discuss the administration's proposals to expand them, and offer our recommendations to the Legislature.

BACKGROUND ON STATE NURSING REQUIREMENTS AND PROGRAMS

State Requirements to Becoming a Registered Nurse

All registered nurses in the state must have a license issued by the California Board of Registered Nursing (BRN). To obtain a license, students must complete a number of steps, including graduating from an approved nursing program and passing the national licensing examination.

In California, there are three types of prelicensure educational programs available to persons seeking to become a registered nurse. All three types are generally full-time programs, and each combines classroom instruction and “hands-on” training in a lab with clinical placement in a hospital or other health facility. The first two options are for students to enroll in either an associate’s degree in nursing (ADN) program at a two-year college, or a bachelor’s degree in nursing (BSN) program at a four-year institution. Students that already hold a bachelor’s or higher degree in a non-nursing field are eligible to apply for an entry-level master’s (ELM) program at a university. Generally, students in an ELM program complete educational requirements for a registered-nurse license in about eighteen months, then continue for another eighteen months to obtain a master’s degree in nursing.

Graduates of these nursing programs are eligible to take the National Council Licensing Examination. Applicants that pass the examination and a criminal background check are licensed by BRN to practice as a registered nurse in California. (Registered nurses from other states and countries that want to work in California must also pass the national licensing examination and background check, as well as show proof of completion of a nursing educational program that meets state requirements.)

Nursing Programs in California

Currently, 108 public and private colleges in California offer a total of 121 prelicensure nursing programs. As Figure 1 shows, most of these are ADN programs offered at CCC. In addition, there are 17 BSN programs offered by CSU and UC, and 12 BSN programs offered at private four-year institutions. There are a total of 14 ELM programs in the state.

Nursing Program Applications Far Exceed Admissions. Statewide, the number of applicants to nursing schools in California far exceeds the number of available slots. According to a 2006 BRN study, there was a total of 22,750 qualified applications for just 8,750 first-year slots for the 2004-05 school year. The mismatch between potential students and actual slots applies to all types of nursing programs in the state, including the ADN, BSN, and ELM programs. Figure 2 (see page 204) breaks out nursing-school applications and available slots by program type.

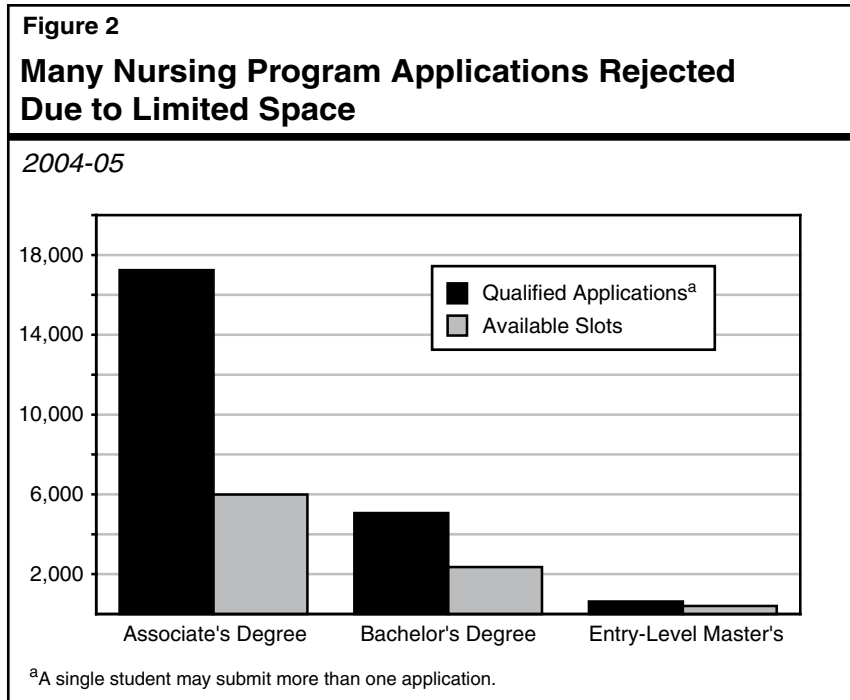
Nursing Program Admissions Policies Vary

California nursing schools have developed different strategies in order to choose which applicants to accept into a program. Generally, nursing programs at four-year institutions and two-year private colleges require students to take several prerequisite courses (such as anatomy and microbiology) as well as a standardized test in order to apply to a program.

Applicants are then evaluated based on their prerequisite grades, test-score results, and other criteria (such as ability to speak a second language). The students with the top qualifications are admitted to the program in accordance with the number of available first-year slots. For example, the forty highest-ranking applicants would be admitted into a program with space for forty nursing students.

Figure 1	
Prelicensure Nursing Programs In California	
Associate's Degree in Nursing	
California Community Colleges	70 ^a
Private colleges	7 ^b
County of Los Angeles program	1
Total	78
Bachelor's Degree in Nursing	
CSU system	15
UC system	2
Private institutions	12 ^c
Total	29
Entry-Level Master's Degree	
CSU system	7
UC system	2
Private institutions	5
Total	14
Grand Total	121
^a Two programs admit only licensed vocational nurses. ^b Three programs admit only licensed vocational nurses. ^c One program admits only licensed vocational nurses.	

In contrast, ADN programs at community colleges rely heavily on nonmerit-based or only partially merit-based selection processes. This follows a legal settlement concerning equal access (see box on page 205). All community college nursing programs require at a minimum that applicants obtain at least a "C" average on several science prerequisite courses in order to qualify for admission. Some nursing programs require that applicants meet stricter criteria (such as at least a "B" average on science



and nonscience prerequisites) in order to apply, though these requirements must be justified through validation studies.

Because there are more applicants that qualify for admission than enrollment slots, community college nursing programs must decide which applicants to admit. The method of selecting students varies by program. Many programs use a lottery system, which randomly selects students from a pool of applicants. Others admit students on a first-come, first-serve basis, or give priority to “wait-listed” applicants that were not chosen in prior years. As discussed above, the Chancellor’s Office does not allow programs to select from among eligible students based strictly on merit criteria.

A recently enacted statute (Chapter 837, Statutes of 2006 [SB 1309, Scott]), allows community colleges to administer a nationally validated diagnostic assessment test to admitted students before they start a nursing program. Students that are unable to obtain a passing score must demonstrate readiness for the program by, for example, passing remedial courses (such as English or math classes) or receiving tutorial services from community college staff. The intent of this new policy is to reduce attrition in CCC nursing programs by ensuring that students are sufficiently prepared for success in a nursing program.

CCC Assessment and Selection Policies

Until the early 1990s, many California Community College (CCC) nursing programs chose students by ranking them according to factors such as prerequisite grades and test-score results. Students in various other programs, meanwhile, were required to take assessment tests for course placement purposes. In 1988, the Mexican American Legal Defense and Educational Fund (MALDEF) filed a lawsuit against the CCC system. The MALDEF contended that CCC's assessment, placement, and prerequisite policies were disproportionately excluding Latino students from certain courses and programs (including nursing).

The organization agreed to drop the lawsuit in 1991 after the CCC Chancellor's Office committed to develop a new set of regulations. Under these regulations, nursing programs, for example, are allowed to continue requiring prospective students to achieve a minimum grade point average on science and nonscience (such as English composition) prerequisites to be eligible to apply. However, districts must first conduct validation studies showing that students who fail to satisfy these requirements are unlikely to succeed in the district's nursing program. Districts also must offer programs (such as English-as-a-second-language instruction) to help applicants achieve minimum eligibility requirements. The regulations also require nursing programs to adopt nonevaluative selection methods (such as a lottery system) when there are more eligible applicants than enrollment slots.

Recent Trends

Graduates Up... Figure 3 (see next page) shows that nursing programs have increased the number of graduates significantly in the past few years. A total of about 7,500 students graduated from a nursing school in California during the 2005-06 school year. This is over 800 graduations more than the previous year. Most (about 70 percent) of these nursing-school graduates completed a two-year college's ADN program. About one-quarter received a BSN from a four-year university, and 4 percent completed an ELM program. As discussed in more detail below, the state has made additional investments in all three types of nursing programs, which are expected to increase graduation totals to over 8,000 annually in future years.

...But Attrition Is a Concern. A large number of nursing students, particularly at community colleges, never complete their degree. As Figure 4 (see next page) shows, only about one-half of the roughly 6,000 students that enrolled in a community college ADN program in 2002-03

Figure 3

Graduates of Nursing Programs Have Increased in Recent Years

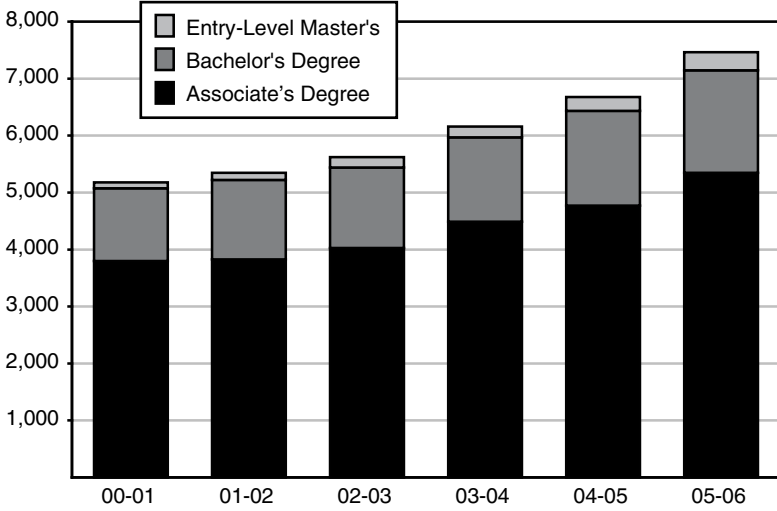
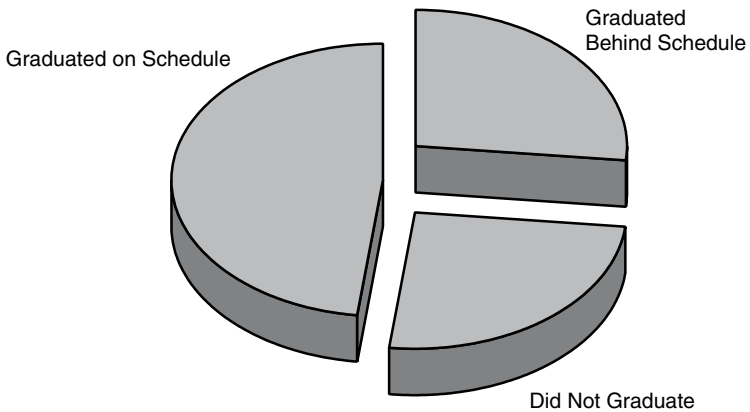


Figure 4

One-Quarter of Community College Nursing Students Never Graduate

2002-03 Cohort of Students



graduated on schedule. About one-quarter of the students graduated in longer than two years, and another one-quarter (about 1,500 students) never graduated. By contrast, the average attrition rate for BSN and MSN students is about 11 percent.

Recent Nursing Program Augmentations

Typically, the Legislature provides funding in the annual budget act for enrollment growth at each of the three segments. With minor exceptions, each segment's enrollment augmentation is based on a single rate of funding for each new full-time equivalent (FTE) student. The rate represents an average of enrollment costs in different programs and campuses within each segment. The segments themselves then make decisions about how the new enrollment slots will be distributed among their campuses and programs.

The segments, therefore, are able to expand nursing enrollment each year using their regular enrollment growth allocations. However, in recent years the Legislature has taken the unusual steps of: (1) providing supplemental funding beyond the regular growth funding in order to expand nursing programs, and (2) specifying the number of additional nursing students it expects the segments to serve. The extra funding recognizes three special factors concerning nursing programs:

- Nursing programs are considerably more expensive than average. In fact, they are among the most expensive programs on many campuses.
- Nursing programs train professionals who serve critical functions relating to public health.
- There is a substantial shortage of nurses in California's workforce. To address this concern, the Legislature has sought to expand nursing programs much more rapidly than average enrollment growth.

The *2006-07 Budget Act* provides support for a number of nursing program expansions, as shown in Figure 5 (see next page). In addition, the current-year budget package authorizes 140 new loan forgiveness awards for nursing students, and creates new programs to recruit and retain nursing faculty.

Another way that colleges have funded the higher costs of nursing programs is through partnerships with hospitals and others (such as foundations). These organizations provide funding, or in-kind support, in order to improve the pipeline of nursing graduates that may end up working for them. For example, in recent years a number of health care organizations have supplied faculty, equipment, facilities, and student scholarships to increase enrollment at nursing programs.

Figure 5**Major Nursing-Related Appropriations in 2006-07 Budget Package***(In Thousands)*

Description	Appropriation
University of California	
Increase entry-level master's students by 65 FTE students	\$860
Increase master's degree nursing students by 20 FTE students	103
California State University	
Fund startup costs to prepare for nursing program expansions in 2007-08	\$2,000
Increase entry-level master's students by 280 FTE students	560
Increase baccalaureate nursing students by 35 FTE students	371
California Community Colleges	
Fund new Nursing Enrollment Growth and Retention Program	\$12,886
Fund enrollment and equipment costs for nursing programs	4,000
Fund new Nursing Faculty Recruitment and Retention Program	2,500
California Student Aid Commission	
Authorize 100 new SNAPLE awards	__a
Authorize 40 new nurses in State Facilities APLE awards	__a

^a State will not incur costs for forgiving loans under this program until subsequent years.

FTE=full-time equivalent; SNAPLE=Student Nursing APLE; APLE=Assumption Program of Loans for Education.

GOVERNOR'S PROPOSAL

The Governor's budget proposes a number of augmentations and budget provisions concerning nursing enrollment. Several different budgeting approaches are taken. For example, in some cases augmentations are provided to fund the entire cost of additional nursing students, while in others only the regular per-student funding rate is provided.

University of California

The Governor's budget proposal includes an augmentation of \$757,000 to fund 57 FTE students above the current-year level. The Governor proposes to fund these enrollment slots on top of UC's normal enrollment growth

allocation. The average cost per funded student is \$13,254. This compares to the regular per-student funding rate (or “marginal cost”) of \$10,876.

California State University

Proposed budget bill language would require CSU to increase enrollment in its BSN programs by 340 FTE students. These students would be counted as part of CSU’s overall enrollment growth, and would thus receive the regular marginal cost funding of \$7,837 per FTE student. The budget maintains ongoing funding from recent nursing augmentations providing support for about 475 FTE nursing students at funding rates of around \$10,000 per student.

California Community Colleges

One-Time Costs for New Programs and Simulation Laboratories. The Governor’s budget proposes to augment CCC’s current-year budget (through trailer bill appropriation) by \$9 million for two, one-time purposes. First, the budget requests a total of \$5 million to create five new CCC nursing programs. The funding would cover start-up costs, such as hiring staff to develop the program curriculum. The programs would be selected through a competitive grant process. The budget proposes to spend the remaining \$4 million in one-time funds to establish four nursing simulation laboratories. Simulation laboratories, which consist of medical equipment and computerized mannequins, allow students to practice medical procedures (such as inserting intravenous needles) and respond to realistic situations (such as heart attacks) involving mannequin “patients.” The Chancellor’s Office indicates that the laboratories would be shared with other nursing programs (including CSU). The locations would be determined based on a competitive process.

Ongoing Costs to Reduce Attrition and Increase Prerequisite Course Offerings. Beginning in 2007-08, the budget proposes \$9 million in new base funding for two purposes. The budget requests \$5.2 million to provide a variety of programs (such as tutoring and academic counseling) to reduce attrition among nursing students. This amount would be in addition to \$2.9 million in CCC’s base budget, which, pursuant to Chapter 837 (discussed earlier), is to fund diagnostic assessment testing and related services for nursing students. The Governor’s proposal includes budget bill language authorizing nursing programs with attrition rates below 15 percent to use these funds instead to expand enrollment.

The remaining \$3.8 million would be provided to community college districts as an incentive to increase science prerequisite course offerings in anatomy, physiology, and microbiology. Generally, students must take

these courses in order to apply to a nursing program. It is not clear whether districts would receive a certain amount of money to offer each new course, or whether the money is intended to provide a funding increment per FTE that supplements what is already provided by general apportionments.

LAO RECOMMENDATIONS

Standardize Approach for Funding Nursing Expansion

Given the rapid increases in nursing enrollment, we recommend that the Legislature provide the University of California (UC) and California State University (CSU) with additional funding above the normal marginal cost to cover recognized higher costs of nursing students. However, we recommend that growth in nursing enrollment be treated as part of the overall enrollment growth provided in the budget, which already includes funding for marginal cost. Consistent with this principle, we recommend that UC receive \$621,000 less for this purpose than it has requested, while CSU receive an increase of \$939,000 in supplemental funding. (Reduce Item 6440-001-0001 by \$621,000 and increase Item 6610-001-0001 by \$939,000.)

As previously noted, the Governor's budget provides \$757,000 for UC to expand its nursing program by 57 FTE students. This amounts to \$13,254 per FTE student, and would provide full funding for these students *outside* of UC's regular enrollment growth allocation. By contrast, the budget requires CSU to expand its BSN programs by 340 students *as part of* its regular enrollment growth allocation. In effect, the budget provides the marginal cost rate of \$7,837 per FTE student.

The Governor's approach continues and expands a practice that has grown over the past several years whereby nursing enrollment is treated inconsistently and, at times, outside of normal enrollment growth. The result is an increasingly complicated and confusing set of expectations with regard to nursing enrollment. Accountability is uneven as well, with new funding sometimes tied to actual increases in enrollment, and at other times simply intended for additional enrollment.

Recommend Funding Nursing Enrollment Within Regular Enrollment Growth. As discussed above, the annual budget includes funding for overall enrollment growth at each segment. The segments allocate this funding among the programs they judge to require expansion. Although different programs incur different costs per student, the growth funding is based on an average, and thus enables all programs—both high and low cost—to grow in proportion to the growth funding provided. For

example, funding for 2 percent system growth would enable all programs to grow by 2 percent.

However, in response to the Legislature's intent of addressing the nursing shortfall, nursing programs are expanding more rapidly than the funded growth rate for overall programs. For this reason, as well as the usually high cost of these programs, we see justification for providing additional funding for nursing enrollment. We note that this supplemental funding would not be necessary in years in which nursing programs grew at a level more in line with overall system funded growth.

Accordingly, we make the following recommendations:

- **Reduce UC Funding.** We recommend that UC's expansion of nursing programs be considered part of its regular enrollment growth. Because this would provide the marginal cost amount of \$10,876 for each of the 57 additional FTE students requested, achieving the Governor's proposed funding level of \$13,254 for each of these students would require a total supplement of \$136,000 (beyond marginal cost funding). Because the Governor's budget provides \$757,000 for these students, we recommend this augmentation be reduced by \$621,000.
- **Increase CSU Funding.** Similarly, we recommend that supplemental funding be provided for the proposed expansion of CSU's BSN programs. Because these students are considered part of regular enrollment growth, the Governor's budget provides \$7,837 for each of these students. Raising funding for these students to the \$10,600 already provided for 35 BSN slots created last year would require \$939,000. We recommend CSU's budget be increased by this amount.

In recent years, the Legislature has provided ongoing funding to enhance the per-student funding rate for community college nursing students. The Governor's budget, however, does not propose any new funding for expanded nursing enrollment in 2007-08.

CCC—Reject Current-Year Augmentations

We recommend the Legislature reject the Governor's current-year request for \$9 million to establish five new nursing programs and four simulation laboratories, as the need for these proposals has not been justified.

Existing Programs Have Room to Grow. We recommend the Legislature reject the Governor's request for \$5 million in current-year start-up funds for nursing programs and instead direct the CCC system to increase

enrollment through more cost-effective means. The Chancellor's Office plan is to open five new programs of about 25 students each by fall 2009 or spring 2010. This means that up to 125 additional nursing students would be produced by the CCC system beginning in spring or fall 2011. While we think that increasing enrollment is warranted given the statewide demand for more nurses, we believe that a more cost-effective approach would be to add slots at existing CCC nursing programs. Additional capacity appears to be available. According to BRN, for example, only 23 of the community college's 70 nursing programs offer evening courses. An even smaller number of programs offer courses on weekends or during the summer term. Many nursing programs could increase enrollment by adding a part-time program. An annual increase of just two additional graduates per existing program would exceed the number of graduates (up to 125 in 2011) proposed for these new programs.

Proposed Simulation Laboratories Not Justified. We further recommend the Legislature reject the Governor's request for simulation laboratories. Community college nursing programs already have laboratories for students to practice medical procedures. The administration has not made a case as to why the current laboratories are inadequate.

Rejection of One-time Proposals Would Reduce Current-Year Overappropriation. As we discuss earlier in this chapter (please see "Proposition 98 Priorities"), our forecast indicates that Proposition 98 is overappropriated by more than \$600 million in the current year. Rejection of the administration's proposals for new nursing programs and simulation laboratories would reduce this amount by \$9 million, thereby creating current-year General Fund savings and lowering the minimum guarantee in the budget year.

CCC—Budget-Year Request

We recommend rejection of \$3.8 million in additional funds for science prerequisite courses because an enhanced funding rate has not been justified. (Reduce Item 6870-101-0001 by \$3,786,000.)

Support Services Would Help Reduce Attrition. We recommend the Legislature approve the administration's request for \$5.2 million to provide additional support services to students. The Governor's budget proposes to use the additional funds primarily for academic counseling and other services for students. Research has shown that these types of programs can be effective tools for improving retention. Given the current problem with student attrition in most CCC nursing programs, we believe that these additional services are justified. Moreover, it seems appropriate to direct nursing programs that already have relatively low attrition rates to use these funds for enrollment expansion.

Funding Request for Science Prerequisites Is Problematic. We recommend the Legislature reject the Governor’s request to allocate additional funds to community college districts for science prerequisite courses. The administration contends that the funding districts receive from the state for anatomy, physiology, and microbiology courses does not cover their actual costs. As a result, the administration maintains that districts cannot provide enough of these courses to meet student demand, thus making it more difficult for prospective nursing students to become eligible to apply to a program. The administration contends that the proposed funds will create an incentive for districts to offer more science prerequisite courses, thereby improving the applicant pipeline to nursing program.

We have two serious concerns with Governor’s proposal. First, the rationale behind the requested supplemental funding is to improve student access to prerequisite courses, thereby increasing the number of nursing applicants. Yet, as we noted earlier, there are already thousands more eligible applications than enrollment slots. The large applicant pool has continued even with recent increases in nursing-program capacity. To the extent the proposal achieved its stated goal, the result would be an even larger number of applicants turned away or placed on wait lists.

Second, we do not see justification for providing an enhanced funding rate. Unlike nursing courses, which incur unusually high costs and address a significant statewide shortage in registered nurses, the science prerequisite courses have not been shown to require such an enhancement. Indeed, we are concerned that the Governor’s proposal moves down a slippery slope where many programs with only moderately above-average costs could seek additional funding. Without making commensurate reductions for below-average-cost programs, this would skew CCC enrollment funding well above justifiable levels.

CCC—Assess Admissions Policies

We recommend that the Chancellor’s Office report at the budget hearings on potential changes to nursing school admissions processes.

As discussed earlier, community college policies in such areas as student assessment and placement stem largely from a nearly twenty-year old lawsuit settlement involving the Mexican American Legal Defense and Educational Fund. The regulations that resulted from the legal dispute require, among other things, that districts use nonevaluative admissions strategies (such as random selection) when selecting students for over-subscribed programs. Research indicates that these admissions practices reduce the ability of districts to select students most likely to succeed in a program, and may be a contributing factor to the high attrition rates in CCC nursing programs.

Given the state's interest in reducing attrition, we recommend that the Legislature direct the Chancellor's Office to report at budget hearings concerning the extent to which regulations could be changed to improve the selectivity of the admissions process, promoting fairness as well as student success. This could include, for example, implementing merit-based admissions policies that take into account applicants' academic performance as well as other skills and special circumstances (such as the ability to speak a second language, community service, and life experiences).

CALIFORNIA POSTSECONDARY EDUCATION COMMISSION (6420)

The statutory mission of the California Postsecondary Education Commission (CPEC) includes analysis of long-term higher education needs, evaluation of policies and programs, and collecting and disseminating relevant data and other information. The commission has 16 members, representing the public and private university segments, the State Board of Education, students, and the general public.

Proposed Budget. The Governor proposes total General Fund expenditures of \$2.2 million, which is an increase of \$9,000 from the revised current-year level. The proposed budget funds 21 positions, including an executive director, staff counsel, 7 policy and programs analytical staff, 6 information services staff, and 5 administrative and support staff. Two positions are supported with federal funds.

REASSESSING CPEC RESPONSIBILITIES

State law assigns to CPEC a number of different responsibilities related to higher education coordination and oversight. In general, statutory direction is broad and permits CPEC considerable latitude in defining the scope and frequency of its activities. In addition to its statutory tasks, CPEC is occasionally asked to perform other duties (such as convening working groups or studying a particular issue) by the Governor or Legislature. The commission also initiates some work on its own.

Earlier Budget Reductions Prompted Examination of CPEC's Focus

In an effort to cope with declining General Fund revenues in 2002-03, CPEC's funding was reduced by \$1.6 million, or 43 percent, from the prior year. Recognizing that such a reduction would affect CPEC's workload, the

Supplemental Report of the 2002 Budget Act directed our office to re-examine CPEC's statutory functions.

Legislative Analyst's Office (LAO) Report Found Conflict Among CPEC's Roles. In our response to the supplement report (released in January 2003), we found that CPEC generally was fulfilling its role as a clearinghouse of higher education information, but was unable to effectively carry out a number of its other statutory functions. Among other reasons for this, we found that tension exists between some of CPEC's responsibilities. Some of these responsibilities put CPEC in a coordination and advocacy role that requires it to work cooperatively with the higher education segments—gathering and processing information on issues that are generally more technical in nature (such as academic program review) and facilitating communication on cross-segmental issues (such as transfers). Other responsibilities, however, require CPEC to play more of an oversight role—dispassionately evaluating higher education performance and analyzing each segment's effectiveness in delivering services to students. We recommended to the Legislature that the commission focus on only one of the two roles (coordination/advocacy or oversight/analysis). We also noted the benefits to the state of maintaining CPEC's data management capacity, which we consider a core function of the commission.

2007-08 Proposal Would Focus CPEC's Responsibilities

The *2007-08 Governor's Budget* maintains CPEC's General Fund support at approximately its current-year level, and also includes language that would make three responsibilities the highest priority for CPEC:

- All reviews and recommendations of the need for new institutions for the public higher education segments.
- All reviews and recommendations of the need for new programs for the higher education segments.
- A determination of options and a recommendation for a new methodology for assessing the adequacy of the University of California (UC) and the California State University (CSU) faculty compensation and comparing it with compensation at other university systems and campuses.

Focus on Coordination Role Makes Sense. By placing priority on reviewing the need for new institutions and programs, the proposed budget bill language would emphasize CPEC's role as a coordinator of the state's higher education system. The third priority in the proposed language—recommending a new faculty compensation methodology—is consistent with CPEC's role as a higher education data clearinghouse.

We therefore think the Governor's approach is a good start. Reviewing the need for additional campuses, centers, and other institutions will continue to be important as the college-age population and participation rates continue to change. Reviewing proposals to expand academic programs also will be important as workforce needs continue to evolve. However, as discussed below, we recommend the Legislature adopt substitute language that (1) assigns priority to these coordination roles and CPEC's data management responsibilities, and (2) directs CPEC to report specified compensation data for UC, CSU, and a broad range of other institutions.

Other Data Management Responsibilities Should Be Retained

We recommend the Legislature include among the California Postsecondary Education Commission's priorities its data management responsibilities.

We believe that CPEC's level of staffing is sufficient to perform other duties beyond those identified in the Governor's proposal. In particular, we think CPEC should be expected to continue its core data management responsibilities. We therefore recommend the Legislature adopt substitute language assigning priority to the maintenance of CPEC's comprehensive higher education database, as well as performing new campus and program reviews. Moreover, we recommend a different approach to faculty compensation than that proposed by the Governor, as discussed below.

New Approach to Faculty Compensation Needed

The Governor's proposed budget bill language directs the California Postsecondary Education Commission (CPEC) to recommend a new methodology that compares total faculty compensation at the University of California and the California State University, as well as options for assessing the appropriateness of these compensation levels. We agree that CPEC's current approach to faculty compensation is flawed. However, we recommend the Legislature rethink the basis for comparing faculty compensation and direct CPEC take an alternative approach to collecting and reporting specified faculty compensation information.

In most years, CPEC produces a report on faculty salaries at UC and CSU. The report compares these salaries with the salaries at a selected group of other public and private universities. The CPEC selects these "comparison institutions" in consultation with a Faculty Salary Advisory Committee that includes representatives of the segments, the Department of Finance, and our office. The comparison institutions are intended to represent the segments' competitors in the labor market.

Among other things, the faculty salary reports identify “parity figures” for UC and CSU which, represent the percentage difference between the segment’s current faculty salaries and the projected average salary of its comparison institutions for the coming year. In other words, the “parity figure” represents the percent increase in the California segment’s salaries that would be required to match the average of the comparison institutions in the budget year. In its most recent report (from March 2006), CPEC estimated that CSU’s faculty salaries would need to increase by 18 percent to match its comparison institutions, while UC’s would have to increase by 14.5 percent. We have two major concerns with the current methodology, as discussed below.

Other Forms of Compensation Should Be Included. The CPEC’s faculty salary reports only measure base salaries. Faculty typically receive various other forms of compensation as well, including retirement and health benefits, sabbaticals, housing allowances, and bonuses. Several studies commissioned by the segments have found that the nonsalary benefits provided to UC and CSU faculty are worth considerably more than the average of their comparison institutions. In fact, when all forms of compensation are considered, UC and CSU appear to be at or above their comparison averages. Thus, reporting a parity figure based only on salaries can be misleading.

Basis for Comparison Needs to Be Rethought. The comparison institutions currently used in CPEC’s methodology (see Figure 1) were last updated in 1993 (for CSU) and 1988 (for UC). Five of CSU’s comparison institutions are private, as are four of UC’s.

We believe it is time to rethink the basis for comparing faculty compensation. The UC and CSU are large, diverse, multicampus systems, while most of their comparison institutions are single campuses. While some UC and CSU campuses may appropriately be compared with the institutions listed in Figure 1, many UC and CSU campuses are far different in terms of selectivity, national ranking of programs, and other factors. A very general illustration is provided by *US News & World Reports’* 2007 academic rankings of the nation’s top research universities. The highest-rank UC campus (Berkeley, at 21) is in the middle of the CPEC salary comparison institutions (4 are ranked higher and 4 are ranked lower). But other UC campuses do not compare as well, with UC Riverside, for example, ranked lower (at 88) than all but one comparison institution. Variation within the CSU system is similarly broad. For example, CSU campuses are spread fairly evenly among the four quartiles of “master’s universities” ranked by *US News*. While rankings of any individual institution in this or any other survey is subject to debate, they do give a rough relative measure of a school’s standing. In other words, they provide one reasonable indicator of who the segments are competing against in the labor market.

Figure 1	
Current Comparison Institutions	
California State University Comparison Institutions	
Public Institutions	Private Institutions
Arizona State University	Bucknell University
Cleveland State University	Loyola University, Chicago
George Mason University	Reed College
Georgia State University	Tufts University
Illinois State University	University of Southern California
North Carolina State University	
Rutgers, the State University of New Jersey, Newark	
State University of New York, Albany	
University of Colorado, Denver	
University of Connecticut	
University of Maryland, Baltimore County	
University of Nevada, Reno	
University of Texas, Arlington	
University of Wisconsin, Milwaukee	
Wayne State University	
University of California Comparison Institutions	
Public Institutions	Private Institutions
State University of New York, Buffalo	Harvard University
University of Illinois, Urbana	Massachusetts Institute of Technology
University of Michigan, Ann Arbor	Stanford University
University of Virginia, Charlottesville	Yale University

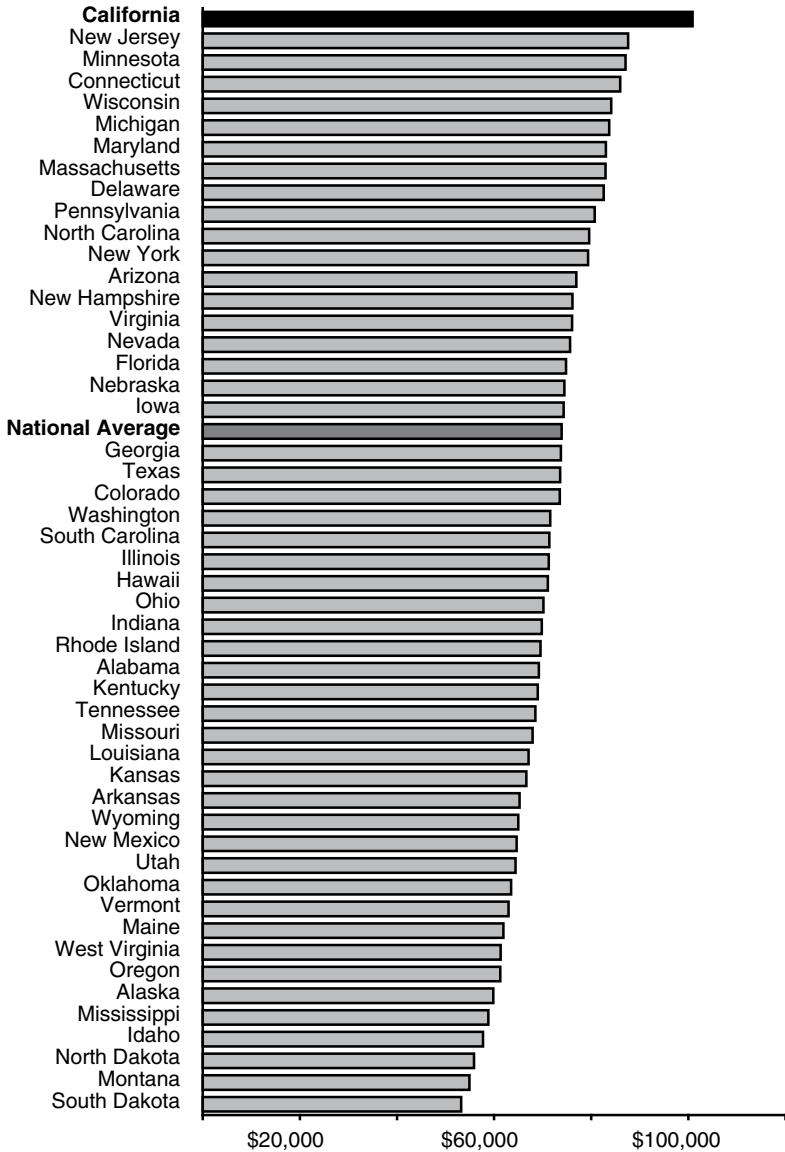
Comparing UC and CSU with different groups of institutions can tell a very different story than what CPEC's recent reports have suggested. For example, as shown in Figure 2 (see next page), the *Chronicle of Higher Education* recently reported that the average faculty salary at state public universities is higher in California than any other state in the nation.

LAO Recommendation: CPEC Should Provide Data on Faculty Compensation. We think that CPEC could perform a useful data collection role in helping the Legislature assess the adequacy of faculty compensation. We therefore recommend the Legislature direct CPEC to collect and report specified compensation information, including regular salaries, fringe benefits, vehicle use, housing and mortgage assistance, life insurance, and additional forms of compensation. We recommend that CPEC be directed to use these factors to annually measure faculty compensation at

Figure 2

California's Public Universities Have Highest Average Faculty Salary

2004-05



Source: Chronicle of Higher Education

UC and CSU (by campus and system). This information would provide a more complete measure of an important cost of the state's public university systems. Even without comparison institution information, this data would give the Legislature and the general public a sense of the investment that is made in higher education faculty. In addition, it would facilitate comparisons between UC and CSU faculty compensation, as well as tracking of increases in compensation funding over time.

Broad Comparisons Would Provide Context and Facilitate Policy Choices. In order to provide context for the UC and CSU faculty compensation data, we also recommend that CPEC be directed to collect the same information for selected other institutions. However, we do not recommend that a new group of comparison institutions be established. Judging from past experience, we expect that such an attempt would generate considerable controversy and would be unlikely to result in a consensus. Even if possible, the outcome would not necessarily be desirable. In our opinion, CPEC's past approach of calculating a "parity" number based on a single set of comparison institutions improperly implies a precise compensation target.

Instead, we recommend that CPEC calculate compensation for broad ranges of institutions (both public and private) that reflect the spectrum of campuses within the UC and CSU systems. The intent would not be to develop a close match of the UC and CSU systems, but rather to reflect the breadth of institutional characteristics (such as selectivity) within those systems. For example, in a variety of indices of the top 100 research institutions, UC's eight general campuses (excluding Merced) are typically spread throughout the rankings. Therefore, a measure of faculty compensation for, say, each decile or quintile of the top 100 research universities would provide valuable contextual information for thinking about UC faculty compensation. A similar range of masters-level institutions could be used for CSU.

Such information would allow interested parties (including the Legislature, Governor, and stakeholders within the universities) to draw their own conclusions about the adequacy of faculty compensation. For example, the Legislature might adopt an expectation that UC or CSU faculty be compensated at some percentile level of the range measured by CPEC. On the other hand, it might not set a target at all, and instead simply use the information as one factor in considering what level of funding to appropriate for the systems each year. University officials might use the information as they recruit and make offers to new faculty. At the same time, this information would not preclude the systems and their campuses from using available funding to make whatever compensation decisions they felt would best serve their needs.

UNIVERSITY OF CALIFORNIA (6440)

The University of California (UC) consists of nine general campuses and one health science campus. The Governor's budget includes about \$19 billion for UC from all fund sources—including the state General Fund, student fee revenue, federal funds, and other funds. This is an increase of about \$831 million, or 4.5 percent, from the revised current-year amount. The budget proposes General Fund spending of about \$3.3 billion for the segment in 2007-08. This is an increase of \$192 million, or 6.2 percent, from the revised 2006-07 budget.

Major General Fund Proposals

Figure 1 summarizes the Governor's proposed General Fund changes for the current and budget years. For 2007-08, the Governor proposes \$192 million in various General Fund augmentations, a \$25.3 million General Fund reduction to UC's outreach programs (also known as academic preparation programs) and labor research institute, and a \$24.9 million net increase for baseline and technical adjustments. We discuss the proposed augmentations in further detail below.

Base Budget Increase. The Governor's budget provides UC with a 4 percent General Fund base increase of \$117 million that is not designated for specific purposes. The university indicates that it would apply most of these funds to support salary and benefit increases for faculty and staff.

Enrollment Growth. In addition to the base increase, the budget includes a \$54.4 million General Fund augmentation for enrollment growth at UC. This would fund an increase in state-supported enrollment of 5,000 full-time equivalent (FTE) students, or 2.6 percent, above the current-year level. The proposed augmentation assumes a marginal General Fund cost of \$10,876 per additional student, reflecting a new methodology proposed by the Governor for calculating the marginal cost of serving an additional student.

Figure 1	
University of California	
General Fund Budget Proposal	
<i>(Dollars in Millions)</i>	
2006-07 Budget Act	\$3,076.7
Lease purchase adjustments	\$1.3
2006-07 Revised Budget	\$3,078.0
Baseline and Technical Adjustments	\$24.9
Proposed Increases	
Base increase (4 percent)	\$116.7
Enrollment growth (2.6 percent)	54.4
Augmentation for institutes of science and innovation	15.0
Funding for Petascale supercomputer	5.0
Other increases	1.3
Subtotal	(\$192.4)
Proposed Reductions	
Reduce General Fund support for outreach programs	-\$19.3
Eliminate General Fund support for labor research institute	-6.0
Subtotal	(\$25.3)
2007-08 Proposed Budget	\$3,270.1
Change From 2006-07 Revised Budget	
Amount	\$192.1
Percent	6.2%

Research Initiative. The Governor's budget proposes a \$20 million General Fund augmentation as part of an overall research initiative on technological innovation. This amount includes (1) \$15 million for the expansion of the California Institutes for Science and Innovation and (2) \$5 million to support UC's bid in a national competition to build a new \$200 million Petascale computer (named for the high speed at which it can process information) funded by the National Science Foundation.

Other General Fund Augmentations. The Governor's budget proposal includes \$757,000 in new funding to support additional students in UC's master's nursing programs. In addition, the budget includes a \$570,000 augmentation to expand enrollment in UC's Program in Medical Education (PRIME), which is intended to train physicians specifically to serve underserved communities. The proposed budget also includes another

\$14 million in one-time funds (the same as the current year) for start-up costs to support the UC campus in Merced, which opened in fall 2005.

Student Fee Increases

For 2007-08, the Governor's budget assumes student fee increases of 7 percent for undergraduates, graduate students, and most professional school students and 10 percent for those in certain law and business school programs. (Student fees at UC are established by the UC Board of Regents.) The assumed fee increases are expected to provide an additional \$105 million in student fee revenue. The Governor's proposal would provide UC full discretion in deciding how to spend the additional revenue.

The Governor's budget also assumes that the university will receive new student fee revenue resulting from two actions recently taken by the UC Board of Regents. Specifically, the Regents approved (1) a 5 percent increase in the tuition surcharge for nonresident undergraduate students and (2) a \$60 temporary surcharge for all students to cover a revenue shortfall resulting from a preliminary injunction against the university in a pending student fee lawsuit. Below, we review the various fee levels for the budget year.

Undergraduate and Graduate Systemwide Fees. Figure 2 summarizes the Governor's proposed increases in undergraduate and graduate systemwide fees. As the figure shows, the budget assumes an increase of 7 percent in the systemwide fee (educational and registration fees) for undergraduate and graduate students. When combined with average campus-based fees and the \$60 temporary surcharge discussed above, the proposed total student fee for a full-time student in 2007-08 would be \$7,347 for undergraduates and \$9,481 for graduates. In addition to paying systemwide and campus-based fees, professional school students and nonresident students also pay supplementary fees, as we discuss below.

Figure 2

UC Systemwide Fees^a Resident Full-Time Students

	2006-07	Proposed 2007-08 ^b	Change From 2006-07	
			Amount	Percent
Undergraduate students	\$6,141	\$6,571	\$430	7%
Graduate students	6,897	7,380	483	7

^a Excludes campus-based fees.

^b Excludes a \$60 temporary surcharge recently approved by the Regents to cover a revenue shortfall from a preliminary injunction against the university in a pending student fee lawsuit.

Professional School Fees. The Governor's budget assumes \$4.7 million in additional revenue from a 7 percent increase in most professional schools fees, with certain law and business school fees increasing by 10 percent. Currently, professional school fees vary by program. For 2007-08, the professional school fee is planned to range from a low of \$3,444 for students in nursing programs to a high of \$19,107 for students enrolled in certain business/management programs.

Nonresident Tuition. The proposed budget assumes a planned 5 percent increase in the tuition surcharge imposed on nonresident undergraduate students, as recently approved by the UC Board of Regents. Specifically, this surcharge would increase from \$18,168 to \$19,068. This increase in nonresident tuition for undergraduates is expected to provide about \$5.5 million in additional fee revenue in the budget year. The budget assumes that nonresident tuition for graduate students would remain at \$14,694.

INTERSEGMENTAL ISSUES INVOLVING UC

In the "Intersegmental" write-ups earlier in this chapter, we address several issues relating to UC. For each of these issues, we offer an alternative to the Governor's proposal. We summarize our main findings and recommendations below.

Consider Different Approaches for Funding and Evaluating Outreach Programs. For the fourth year in a row, the Governor's budget proposes to reduce General Fund support for UC's outreach programs, for savings of \$19.3 million. (The UC's budget would still contain \$12 million for these programs.) In the "UC and CSU Outreach Programs" write-up in this chapter, we withhold recommendation on the proposed reduction, pending our review of the evaluation of the programs to be submitted in the spring. If the Legislature wishes to restore funding for these programs, we recommend requiring an external evaluation of UC's outreach programs, rather than continue the practice of asking the university to evaluate the effectiveness of its own programs. We also recommend the Legislature consider an alternative approach for funding and delivering outreach services—a College Preparation Block Grant targeted at K-12 schools with very low college participation rates.

Fund Enrollment Growth Consistent With Demographic Projections and Legislative Marginal Cost Methodology. The Governor's budget provides \$54.4 million to fund 2.6 percent enrollment growth at a marginal General Fund cost of \$10,876 per additional FTE student, based on his proposal for a new marginal cost methodology. The Governor essentially uses the same methodology that he used last year in his 2006-07 budget

proposal, which the Legislature rejected. In the “UC and CSU Enrollment Growth and Funding,” write-up, we recommend two modifications to the Governor’s enrollment proposal. First, based on our demographic projections, we recommend the Legislature provide funding for enrollment growth at a rate of 2 percent. Our proposal would allow the university to accommodate enrollment growth next year due to increases in population, as well as modest increases in college participation rates.

Second, we recommend the Legislature once again reject the Governor’s proposed marginal cost methodology. We find the marginal cost methodology that the Legislature developed and approved as part of the 2006-07 budget more appropriately funds the increased costs associated with enrollment growth and preserves legislative prerogatives. Using this legislatively determined marginal cost methodology, we recommend reducing the Governor’s proposed UC student funding rate from \$10,876 to \$10,586. Accordingly, we recommend a General Fund reduction of \$13.4 million to reflect our enrollment growth and marginal cost recommendations for UC.

Assume Lower Fee Increase to Maintain Students’ Share of Cost at Current-Year Levels. The proposed budget assumes student fee increases of 7 percent for undergraduates, graduate students, and most professional school students. (Certain UC law and business program fees would increase by 10 percent.) In the “Student Fees” Intersegmental write-up, we recommend that, absent an explicit student fee policy, the current share of educational costs borne by students through fees be maintained in 2007-08. We estimate that this would entail a modest fee increase of 2.4 percent, which is our projection of inflation for the budget year. For a full-time UC undergraduate, this equates to an annual increase of \$147.

Standardize Approach for Funding Enrollment in Nursing Programs. The proposed budget includes provisional language requiring UC to increase nursing program enrollment by 57 FTE students. However, in contrast to how nursing enrollment is treated in the California State University (CSU) and California Community College’s budget, the Governor’s proposal does not include this enrollment as part of UC’s overall enrollment growth of 5,000 FTE students. As a result, the new nursing enrollment would not receive marginal cost funding, and the Governor’s budget instead provides the full cost of serving these students as a separate augmentation beyond the regular enrollment growth. In the “Higher Education Nursing Proposals” write-up, we recommend a standardized approach to funding enrollment growth in nursing programs at all three segments. For UC, we recommend the 57 FTE nursing students be counted as part of UC’s overall enrollment growth. This would allow the segment to allocate marginal cost funding to support these particular students. As a result, a separate augmentation for the full cost of these nursing students

would no longer be needed. Accordingly, we recommend reducing UC's appropriation for these students by \$621,000. This would leave \$136,000 in recognition of the unusually high costs (above the marginal cost) imposed by nursing enrollment.

GENERAL FUND BASE INCREASE

Given our projection of inflation for 2007-08, we recommend the Legislature provide a 2.4 percent General Fund base increase, or cost-of-living adjustment, to the University of California (UC). Given the Governor's budget funds a 4 percent base increase, we recommend deleting \$46.7 million from the \$116.7 million General Fund augmentation requested in the budget for UC. (Reduce Item 6440-00-0001 by \$46.7 million.)

In order to offset the effects of inflation, which erodes the purchasing power of a fixed appropriation over time, the annual state budget typically includes funding to provide price or cost-of-living adjustments (COLAs) for many state programs. It is from these adjustments that programs generally pay for employee salary and wage increases, as well as increased prices for goods and services. In other words, these adjustments are not intended to fund increased workload (such as the expansion of existing services or the establishment of new services), but rather are meant to help pay for existing workload whose costs have increased due to inflation. Although COLAs have customarily been provided to UC in most years, there is no statutory requirement for these payments.

Governor's Budget Proposes 4 Percent COLA. For 2007-08, the Governor proposes a 4 percent General Fund base increase (effectively a discretionary COLA) of \$117 million for UC. At this time, we project inflation in 2007-08 to be 2.4 percent (based on our estimate of the change in the U.S. state and local deflator from 2006-07 to 2007-08). We therefore believe the Governor's 4 percent General Fund base increase, combined with increased fee revenue, would provide the university with funding well above what is needed to pay for the higher cost of meeting *existing* workload. For example, UC plans to use some of the new funding to increase salaries beyond inflation, expand research and aid opportunities for graduate students (such as fellowships and research assistantships), and reduce the student-faculty ratio at campuses (meaning offer smaller classes).

Recommend Funding 2.4 Percent COLA. In view of our estimate of inflation for the budget year, we recommend the Legislature provide a 2.4 percent COLA to UC, rather than the Governor's proposed 4 percent. An adjustment tied to inflation would cost \$70 million. Thus, we recommend the Legislature reduce the Governor's proposed base increase for

UC from \$116.7 million to \$70 million, resulting in General Fund savings of \$46.7 million. Under our proposal, the university would still receive sufficient general purpose funding to compensate for increased costs. At the same time, the Legislature could use our identified General Fund savings of \$46.7 million (in addition to the savings from our enrollment growth recommendations) to address the budgetary situation or other priorities in higher education or elsewhere.

PRIME

We withhold recommendation on the proposed \$570,000 augmentation for the University of California's Program in Medical Education pending receipt and review of additional information.

The 2006-07 Budget Act included \$480,000 in General Fund support for 32 medical students in PRIME at UC Irvine. The purpose of PRIME is to train physicians specifically to practice in underserved communities. The Governor's budget proposes a \$570,000 General Fund augmentation for the program to enroll an additional 38 medical students at the Irvine, Davis, San Diego, and San Francisco campuses—more than doubling the number of students currently in the program. Effectively, this would provide a \$15,000 supplement—above the marginal General Fund cost amount provided for all additional students regardless of education level or academic program—for each additional PRIME student. (We further discuss the issue of marginal cost funding in our "UC and CSU Enrollment Growth and Funding" write-up.) According to the university, this supplement is to account for the higher cost of serving medical students. At the time this analysis was being prepared, neither the university nor the administration could provide adequate information to justify the \$15,000 per student amount. As a result, we withhold recommendation on the proposed augmentation pending further detail about the request.

RESEARCH INITIATIVES ON TECHNOLOGICAL INNOVATION

The state's Master Plan for Higher Education specifies that the University of California (UC) is the primary state-supported academic agency for research. In support of this mission, the state provides funding to UC for various research projects undertaken by university faculty. For 2007-08, the Governor's budget proposes a \$20 million General Fund augmentation for new research initiatives focused on technological innovation. Specifically, the budget includes \$15 million to expand the California Institutes for Science and Innovation and \$5 million to support UC's bid to build a supercomputer. In this section, we provide

an overview of research funding at UC and analyze the Governor's proposed augmentations.

Overview of UC Research Funding

The UC is designated as the state's primary research institution. The research undertaken by UC faculty satisfies both academic and societal needs, as well as generates substantial revenue for the university. For example, UC has received more patents for inventions than any other university in the world. The UC's research programs, which periodically change depending on priorities and available resources, can range from industrial and agricultural productivity to advances in health care. As we discuss below, some areas of research are in part determined by the sponsor of the research (such as the federal government or a private company), while others are based on the state's or the university's own priorities.

Each year, the university receives research funding from the state, the federal government, not-for profit institutions, and for-profit companies. In 2006-07, UC received about \$3.4 billion for research from all fund sources, as shown in Figure 3 (see next page). This amount consists of the following:

- **General Fund (\$283 Million).** The 2006-07 budget included \$283 million from the General Fund to support UC's research programs. Most of these funds are considered general purpose research funding that the university can allocate based on its priorities. Only a small amount (\$32 million) is restricted by budget act language for certain research institutes (such as the Medical Investigation of Neurodevelopmental Disorders Institute).
- **State Special Funds (\$30 Million).** The state also provides research funding to UC from special fund sources—mainly revenue generated from special taxes on certain goods. For example, the university recently received about \$13 million for breast cancer research from the proceeds of a special tax on tobacco products.
- **Federal Funds (\$1.8 Billion).** Federal funds are the university's single largest source of support for research, which totals \$1.8 billion in the current year. About 80 percent of these funds comes from two federal agencies—Health and Human Services and the National Science Foundation (NSF). The \$1.8 billion total does not include the operational funding for the three Department of Energy laboratories managed by UC, which currently totals about \$2 billion.
- **Other Funds (\$1.3 Billion).** The university also receives a significant amount of funding each year from private individuals,

foundations, and private businesses to mainly conduct research in areas of particular interest to the provider of the funds.

Figure 3	
UC Research Funding	
<i>2006-07</i> <i>(In Millions)</i>	
	Amount
General Fund	\$283
State special funds	30
Federal funds ^a	1,800
Other funds	1,287
Total	\$3,400
^a Does not include funding received for the operation of the three Department of Energy laboratories managed by UC.	

In addition to the above \$3.4 billion specifically designated for research, a significant portion of funding for instruction (such as equipment and faculty salaries) also supports faculty research activities.

General Fund Supports Numerous Research Programs and Units. As discussed above, the 2006-07 budget provided a total of \$283 million from the General Fund for research at UC. Roughly one-third of this funding is allocated to agricultural research that is coordinated through the Division of Agriculture and Natural Resources at the UC Office of the President (UCOP). Most of the remaining funds are used to support a large number of formal research programs and units that operate on either a (1) systemwide or multicampus level (meaning they serve the entire university system and involve faculty from more than one campus) or (2) campus-specific level (meaning they serve the particular campus at which they are located). Figure 4 identifies some of the major systemwide research programs, as well as various multicampus research units at the university. In addition, the figure also includes a select list of about 80 research units at the individual UC campuses. Although this is not a complete list, it does illustrate the vast array of research units at UC. Figure 4 (see page 232) also illustrates that a number of the different research programs and institutes focus on similar topics and areas of study.

UC Often Adjusts Its Research Priorities. According to the university, an inherent difficulty it frequently faces in allocating research funding is balancing the need to accommodate initiatives in new and

promising research areas with the need to maintain support for existing research programs that it believes are important. In an attempt to achieve such a balance, UC states that it periodically reviews its existing portfolio of research programs to determine if any adjustments in the allocation of research funding are needed to accommodate changing priorities. This has sometimes resulted in the merger, creation, or elimination of particular research units and programs, as well as the redirection of the research endeavors within an existing unit or program.

Governor's Research Proposals

The Governor's budget proposes a \$20 million General Fund augmentation as part of an overall research initiative on technological innovation. This amount consists of two General Fund augmentations:

- \$15 million for the California Institutes for Science and Innovation.
- \$5 million to enhance UC's chances of winning a national competition for a Petascale supercomputer funded by NSF.

Below, we make recommendations regarding each of these proposals.

California Institutes for Science and Innovation

We recommend the Legislature reject the \$15 million proposed augmentation for the California Institutes for Science and Innovation, because (1) neither the administration nor the University of California could provide adequate justification for the additional funds and (2) existing research funds could be redirected to expand these institutes. (Reduce Item 6440-005-0001 by \$15 million.)

For the current year, the 2006-07 Budget Act provided a total of \$4.8 million in General Fund support to UC for the operation of four California Institutes for Science and Innovation. These institutes enable UC faculty to work directly with private companies on such issues as information technology, biomedical research, nanotechnology, health care, and traffic congestion. For the budget year, the Governor proposes a \$15 million increase in base funding for the institutes, for a total of \$19.8 million—a quadrupling in the level of funding. According to the administration, the proposed augmentation is intended to fund advanced technology infrastructure, personnel, and “seed money” to build new research teams.

At the time of this analysis was prepared, the administration and the university were unable to provide adequate information to justify the additional funds for the California Institutes for Science and Innovation. The university simply stated that the institutes are currently underfunded and that the proposed augmentation would move each institute toward a more

Figure 4**Selected UC Research Program and Units**

Systemwide Research Programs	
AIDS Research	Institute for International Studies
Biotechnology Research	Institute for European Studies
Chicano/Latino Policy Research	Institute for Personality and Social Research
Environmental Research	Institute for Urban and Regional Development
Toxic Substance Research	Space Sciences Laboratory
Academic Geriatric Resource Program	Survey Research Center
Pacific Rim Research	Davis
Labor Research	Bodega Marine Laboratory
California Policy Research Center	Biotechnology Program
Multicampus Research Units	Crocker Nuclear Laboratory
Mexico Research/UC Mexus	Institute of Governmental Affairs
Energy Institute	John Muir Institute of the Environment
Geophysics and Planetary Physics	Toxicology and Environmental Health
Observatories	Institute for Data Analysis
Humanities Research	Irvine
Linguistic Minority	Cancer Research Institute
Berkeley	Critical Theory Institute
Archeological Research Facility	Developmental Biology Center
Cancer Research Laboratory	Institute for Brain Aging and Dementia
Center for African Studies	Institute for Software Research
Center for Atmospheric Studies	Los Angeles
Center for Environmental Design Research	American Indian Studies Center
Center for Latin American Studies	Asian American Studies Center
Center for Pure and Applied Mathematics	Brain Research Center
Center for South Asia Studies	Center for 17th and 18th Century Studies
Center for Southeast Asian Studies	Center for African American Studies
Center for the Study of Sexual Culture	Center for Chinese Studies
Earl Warren Legal Center	Center for European and Russian Studies
Earthquake Engineering Research Center	Center for Medieval and Renaissance Studies
Electronics Research Laboratory	Center for the Study of Women
Environmental Sciences Policy and Management	Chicano Studies Research Center
Functional Genomics Laboratory	Cotsen Institute for Archeology
Institute for Environmental Science	Institute for Social Science Research
Institute for Business and Economic research	Institute of Industrial Relations
Institute for East Asian Studies	Ralph J. Bunch Center for African Studies
Institute for Governmental Studies	Center for Southeast Asian Studies
Institute for Human Development	Center for Japanese Studies
	Latin American Studies

Continued

Molecular Biology Institute	Scripps Institute of Oceanography
Riverside	San Francisco
Air Pollution Research Center	Cancer Research Institute
Center for Ideas and Society	Cardiovascular Research Institute
Center for Social and Behavioral Science	Hormone Research Laboratory
Presley Center for Crime and Justice	Metabolic Research Unit
San Diego	Santa Barbara
Biology Center	Center for Ecological Analysis
Cancer Center	Center for Chicano Studies
Center for Astrophysics and Space Science	Marine Science Institute
Center for Energy and Combustion Research	Santa Cruz
Center for Research in Computing and the Arts	Institute of Marine Sciences
Center for US-Mexican Studies	Humanities Research
Institute for Global Conflict	Santa Cruz Institute for Particle Physics

fully funded operating budget. As a result, we cannot find a compelling rationale for the \$15 million augmentation. More importantly, we believe that if UC considers expanding the operations of the institutes to be a high research priority, then the university can redirect funding from existing research programs that it deems are of a lower priority. (The Governor's budget essentially maintains UC's base General Fund research budget at its current-year level of about \$283 million.) For these reasons, we recommend the Legislature reject the \$15 million proposed augmentation for the California Institutes for Science and Innovation.

Petascale Supercomputer

We recommend the Legislature reject the proposed \$5 million General Fund expenditure to enhance the University of California's bid for a Petascale supercomputer, due to the lack of adequate justification for the proposal and the availability of existing research funds that could be redirected for this purpose. (Reduce Item 6440-001-0001 by \$5 million.)

The NSF has recently launched a national bidding process for the design and management of a Petascale supercomputer, which is named for the high speed at which it can process information. Specifically, the foundation plans to invest \$200 million for the development of the supercomputer and an additional \$100 million over a five-year period for its operation, which is scheduled to begin in 2011. In response to NSF's announcement, UC—including the federal energy laboratories that it manages—has formed a consortium with the Georgia Institute of Technology and IBM to prepare and submit a proposal to NSF. This consortium is formally called the National Petascale Applications Resource (NPAR). If NPAR is successful in its bid, the Petascale supercomputer would be located at the Lawrence

Livermore National Laboratory. (The UC currently operates a different type of supercomputer at its San Diego campus.) The university expects that the outcome of its proposal will be known sometime this summer or fall.

Although NSF does not require a direct match from states as part of the bidding process for the Petascale supercomputer, the Governor's budget requests a \$5 million General Fund augmentation to UC's research budget to enhance the NPAR proposal. According to the Department of Finance, the administration intends to provide the university with \$5 million each year for the next ten years, for a total of \$50 million. Although the language in the proposed budget bill does not specifically state that the funds would revert to the General Fund if the university is unsuccessful in its bid, the administration indicates that this is its intent.

Details of Proposal Not Forthcoming. At the time of this analysis, the administration and the university were unable to provide adequate information to justify the proposed \$5 million for the Petascale supercomputer. The UC tells us it is not disclosing details of its NPAR proposal in order to remain competitive. As a result, the Legislature will not have an opportunity to review the details of the project it is being asked to fund. Without a proposal to review, we cannot determine the amount of funds that other NPAR members (such as IBM) will contribute from their own resources towards the operation of the supercomputer. More importantly, we do not know what future state funding would be committed by the proposal. Finally, we do not have adequate information to determine if \$5 million is the correct amount of support needed.

Existing Research Funds Could Be Reallocated. As previously discussed, the annual state budget provides general purpose research funding that the university allocates among competing priorities. This approach provides significant flexibility and autonomy for UC to pursue research in areas that it considers promising and competitive. In some instances, this may result in reconfiguring existing research programs. In other instances, this may mean eliminating or consolidating existing programs that focus on similar research areas in order to "free up" funds for new initiatives (such as the proposed Petascale supercomputer). We also note that some research projects operate on a specific time frame (a five-year contract, for example), which periodically frees up funds for other research projects.

Given the lack of justification for the proposal and the availability of existing research funds, we recommend the Legislature reject the proposed \$5 million in new funding for UC to enhance the NPAR proposal to build a Petascale supercomputer. This would not prevent UC from going forward with its bid.

IMPROVING UC'S LONG RANGE DEVELOPMENT PLANNING PROCESS

*Each campus and medical center of the University of California (UC) periodically develops a Long Range Development Plan (LRDP) that guides its physical development—based on academic goals and projected student enrollment levels—for an established time horizon. In a recent report, **A Review of UC's Long Range Development Planning Process**, we reviewed the current process used to prepare LRDPs and proposed steps to make the process more transparent and effective. We present the major findings and recommendations of our report below.*

The state's *Master Plan for Higher Education* essentially promises eligible students—primarily the top one-eighth of public high school graduates—access to UC. As a result, growth in enrollment demand (due to increases in the number of eligible high school graduates, for example) puts pressure on UC to increase enrollment and expand infrastructure to accommodate the additional students. Each campus plans for growth are identified in its Long Range Development Plan (LRDP), which sets upper limits for broad campus parameters—such as the number of students and employees—for 10 years to 15 years into the future. The LRDP may also identify special infrastructure that might be required, such as parking garages, faculty and student housing, and nature reserves.

In developing LRDPs, campuses consult surrounding communities in an attempt to achieve a mutually agreeable plan. In recent years, such agreement has sometimes been elusive, with differences of opinions over traffic, housing, and other potential impacts of planned campus growth. In view of these disputes, our office analyzed whether UC's LRDP process adequately addresses the impacts that campus growth has on surrounding communities.

What Is an LRDP?

An LRDP, which requires approval by the UC Board of Regents, is a land use plan that guides the physical development of a UC campus. (Although each UC medical center also has an LRDP, our report focused on campus-level LRDPs.) The initial establishment of a campus is guided by an initial LRDP. Subsequent LRDPs for the campus are essentially updates to this initial plan. Campuses prepare LRDPs based on their academic goals and projected student enrollment levels. Thus, an LRDP is an important policy document that outlines a campus's priorities.

In order to assist campuses in developing an LRDP, UCOP provides general guidelines regarding the organization and components to be included in such a plan. The plan should (1) provide guidance for future structure placement, (2) identify areas of open space, (3) show how people move through the site, and (4) discuss how campus systems for various utilities will accommodate the projected campus population. Beyond these guidelines, UCOP does not impose specific requirements for the content or longevity of an LRDP. As a result, the organization of an LRDP and the process used to develop it often varies across campuses.

Not Subject to Local Land Use Control. As a state institution, UC is constitutionally exempt from local land use control. This means that local government does not have the jurisdiction to reject or oppose a campus's LRDP or a specific capital outlay project on the campus. In addition, state agencies typically do not review or approve a UC campus's LRDP. Currently, the Legislature does not provide any formal guidance or oversight regarding the development or implementation of an LRDP.

LRDPs Are Periodically Updated. Although each LRDP has an established time horizon, it does not automatically expire at the end of that horizon. A campus's plan remains in effect until the Regents approve an updated LRDP for that campus. Figure 5 summarizes the status of each UC campus and medical center's LRDP. As indicated in the figure, campuses tend to have different time horizon years based on their particular priorities and objectives. The entire LRDP process (from the time a campus begins to develop an LRDP to when it is approved by the Regents) typically takes two to three years.

Environmental Impact Report (EIR) Required for Each LRDP. The California Environmental Quality Act (CEQA) requires that a comprehensive EIR be prepared specifically for the LRDP of a public higher education campus or medical center. The EIR must (1) provide detailed information about a project's likely effect on the environment (such as traffic), (2) identify measures to mitigate significant environmental effects (such as mitigating traffic impacts by constructing physical improvements like traffic signals or roundabouts), and (3) examine reasonable alternatives to the project. In developing an EIR, CEQA requires UC first to prepare a preliminary EIR for public review and allow at least 30 days for public comment. The UC must evaluate all comments and prepare written responses to them, which must be included in the final EIR. Under CEQA, the Regents—as the “lead agency”—must certify the EIR before approving an LRDP.

Figure 5**University of California
Long Range Development Plan (LRDP) Status**

Campus/Medical Center	Approval Date	Horizon Year
Recently Updated LRDPs		
Berkeley	January 2005	2020
Davis	November 2003	2015
Irvine Medical Center	January 2003	2020
Los Angeles ^a	March 2003	2010
Merced	January 2002	2015/2025 ^b
Riverside	November 2005	2015
San Diego	September 2004	2020
San Francisco ^a	January 1997	2011
Santa Cruz	September 2006	2020
Developing Updated LRDPs		
Davis Medical Center	2007 ^c	TBD ^d
Irvine	2007 ^c	TBD
San Diego Medical Center	TBD	TBD
Santa Barbara	2007 ^c	2025
<p>^a All sites, including the medical center.</p> <p>^b Phased development because Merced is a new campus.</p> <p>^c Anticipated approval date.</p> <p>^d To be determined.</p>		

Concerns With Growth Levels and Off-Campus Impacts

In recent years, some communities surrounding UC campuses have expressed concern about the impacts of planned enrollment growth. Specifically, they question (1) how much campuses should grow and (2) how much UC should pay for the impacts related to that growth. Below, we examine each of these issues.

How Much Does Each UC Campus Plan to Grow?

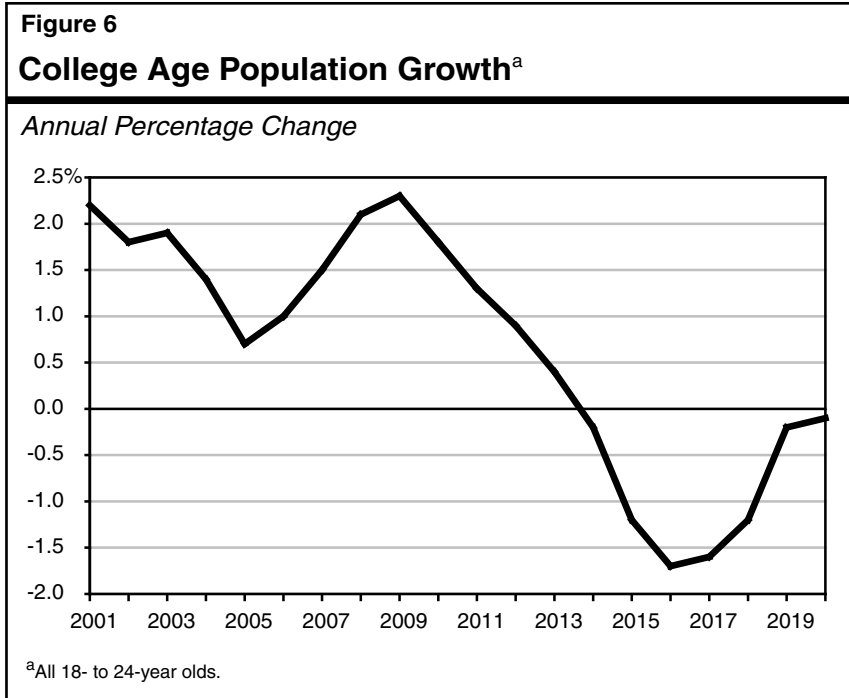
Future student enrollment is one of the main drivers of a campus's LRDP. For example, the number of new academic facilities and housing units depends upon how many additional students enroll at the campus.

Thus, a campus will develop an LRDP by first projecting the number of additional students it plans to enroll in future years.

Both Demographic Changes and Policy Choices Affect Campus Growth. Unlike enrollment in compulsory programs such as elementary and secondary schools, which corresponds almost exclusively with changes in the school-age population, enrollment in higher education responds to a variety of factors. Some factors, such as population growth, are largely beyond the control of the state. Others, such as the creation of new graduate education programs, stem directly from policy choices. In general, enrollment growth corresponds to:

- ***Demographics—Population Growth.*** Other things being equal, an increase in the state's college-age population causes a proportionate increase in those who are eligible to enroll in each of the state's higher education segments. Enrollment projections, particularly for UC, are heavily affected by estimates of growth in the college-age "pool" (18-to 24-year old population). This population has grown modestly in recent years (see Figure 6). Annual growth rates will peak around 2009, and will slow thereafter. In fact, between 2014 and 2020, the state's college-age population will decline each year.
- ***Policy Choices and Priorities—Participation Rates.*** For any subgroup of the general population, the percentage of individuals enrolled in college is that subgroup's college participation rate. However, projecting future participation rates is difficult because students' interest in attending college could be influenced by various factors (including availability of financial aid and the attractiveness of job opportunities). In addition, actions to create or expand particular academic programs would increase overall participation.

UC's Enrollment Plan—Campuses Sometimes Make Their Own Projections. In 1999, UCOP independently developed systemwide enrollment projections through 2010-11 to help guide the university's academic planning efforts. (The actual enrollment at UC depends largely on particular levels of funding from the Legislature, which may fund a different level of enrollment growth than UC requests.) The UCOP's 1999 enrollment projections assume that the percentage of recent California high school graduates enrolled at UC will generally remain constant throughout the forecast period. However, the projections also assume that the percentage of adults participating in graduate education programs will increase enough to fulfill the university's planned expansion of existing and new graduate programs.



Specifically, UC's plan is that systemwide enrollment—excluding health science students—will increase by 48 percent (or 71,000 additional FTE students) from 1998-99 to 2010-11. Based on these projections, each campus is assigned a long-range enrollment target that forms the basis of its LRDP. However, many of the recently approved campus LRDPs are based on a time horizon that goes beyond the 2010-11 time horizon of the 1999 enrollment plan. For example, UC Riverside's current LRDP is based on enrollment projections through 2015. For those years after 2010-11, an individual campus—in consultation with UCOP—essentially projects its enrollment based on its own priorities. In other words, the university currently has not made systemwide projections beyond 2010-11. According to UCOP, the university has initiated a process for developing enrollment projections to at least 2015-16.

Year-Round Operations—Accommodating Growth With Existing Facilities. Student enrollment increases do not necessarily require a proportionate expansion of facilities. This is because campuses have unused capacity that can accommodate additional students. For example, operating campuses on a year-round schedule—which more fully utilizes the summer term—is an efficient strategy for serving more students while reducing out-year costs associated with constructing new classrooms.

Accordingly, the Legislature has encouraged both UC and CSU to serve more students during the summer term.

In recent years, UC's summer enrollment has increased. For example, between summer 2000 and summer 2005, summer enrollment at UC campuses almost doubled. However, despite this increase, the summer term at UC serves only one-fifth the number of students as the fall term. In other words, UC's campuses operate in summer at only 20 percent of their fall levels. Thus, UC could serve tens of thousands of additional students without necessarily expanding its physical development.

Who Pays for Off-Campus Impacts Related to Growth?

When a campus's enrollment and facilities expand, it can sometimes negatively affect the surrounding environment (such as through increased pollution). Under CEQA, the campus is required to identify and implement measures to mitigate such adverse impacts. As previously mentioned, campuses and their surrounding communities sometimes disagree about the responsibility for impacts occurring outside of the university's jurisdiction. For example, although a new signal light in the city could manage traffic from campus expansion, the city and campus might disagree about how the cost of that signal light should be shared.

UC's "Fair Share" Policy. Since 2002, each EIR prepared for an LRDP includes a general statement that the campus will work with the appropriate jurisdiction and contribute its fair share of the improvements needed to mitigate the identified impacts. For example, if the campus is responsible for 80 percent of the traffic on a particular street, then it may decide to contribute 80 percent of the cost for a new traffic signal. However, a campus will only pay its fair share if the responsible jurisdiction (such as a city or county) has (1) established and implemented an appropriate mechanism for identifying and collecting fair share payments from UC and any other developers that contribute to the identified impacts, (2) built the identified improvements, and (3) reached an agreement with UC on a "trigger" point (such as an off-campus intersection reaching a certain level of congestion) when UC will contribute its fair share payment. This means that the responsible jurisdiction must first pay the upfront costs of any such improvements.

Although the university has been including the above fair share payment language in its EIRs since 2002, no UC campus at this time has reached a fair share agreement with a neighboring jurisdiction in accordance to that policy. (This is not to say that campuses have never made any monetary payments to local governments in years past.) As we discuss below, a recent court case increases the need for the state's public universities to work with local municipalities in paying their share of off-campus impacts.

City of Marina v. CSU Board of Trustees. In 1994, CSU agreed to establish a Monterey campus on a portion of the former Fort Ord military base as part of the Fort Ord Reuse Authority (FORA) Act. (The state Legislature created FORA—which includes Monterey County and the Cities of Monterey, Salinas, Carmel, Marina, and Pacific Grove—to manage the transition of the base from military to civilian use.) The CSU Board of Trustees in 1998 certified a master plan for the new campus and an accompanying EIR, which identified significant environmental impacts to various public resources. Although the Trustees agreed to mitigate those impacts that would occur on campus, they asserted that the mitigation of off-campus impacts was not within their jurisdiction, but rather within the jurisdiction of FORA. Accordingly, the Trustees declined to fund off-campus mitigation measures.

In response, FORA and the City of Marina challenged the Trustees' decision to certify the EIR (despite the unmitigated effects) as a violation of CEQA. In July 2006, the California Supreme Court reversed an earlier Court of Appeal's decision by concluding that the Trustees had abused their discretion and thus their approval of the EIR was not valid. Specifically, the Supreme Court ruled that:

- ***Off-Campus Impacts Must Be Mitigated.*** The CEQA does not limit the CSU Trustees' obligation to mitigate or void significant environmental effects occurring only on the university's own property. Rather the Trustees are required to mitigate a project's significant effects on the environment.
- ***Voluntary Payments Are a Feasible Form of Mitigation.*** If the Trustees cannot adequately mitigate off-campus environmental impacts with actions on campus, then a voluntary payment to a third party (such as FORA) to perform the necessary acts off campus is a feasible form of mitigation.

LRDP Process Lacks Accountability, Standardization, and Clarity

In our review of the process used by UC to prepare and implement LRDPs (as well as the accompanying EIRs) for its campuses and medical centers, we generally found a lack of accountability, standardization, and clarity. This creates unnecessary tension between the university and local communities regarding how much campuses should grow and the mitigation of the environmental impacts related to that growth. Figure 7 (see next page) summarizes our major findings, which we discuss in further detail below.

Figure 7**Summary of Major LAO Findings**

- ✓ ***Lack of State Accountability and Oversight.*** Generally, the state neither approves a Long Range Development Plan (LRDP) nor monitors the implementation of the mitigation measures identified in the accompanying Environmental Impact Report.
- ✓ ***Lack of Standardization in Public Participation.*** The University of California (UC) Office of the President does not provide campuses with specific requirements for how local communities should be involved in the LRDP process. As a result, the degree to which local communities are involved in the planning process can vary across campuses.
- ✓ ***Minimal Systemwide Coordination in Projecting Enrollment for Recent LRDPs.*** In 1999, UC developed systemwide enrollment projections through 2010-11, which were used to develop an enrollment plan for each campus. However, when a campus prepares an LRDP that goes beyond 2010-11, it independently develops its own enrollment projections for those subsequent years.
- ✓ ***Campuses Want to Primarily Expand Graduate Enrollment.*** Much of the projected enrollment growth at UC will not be due to increases in freshman enrollment, but rather because of a desire to expand and create new graduate programs (such as in law and public policy). This is because the number of California public high school graduates is expected to decline.
- ✓ ***Lack of Clarity in the California Environmental Quality Act (CEQA).*** The CEQA process can often be costly and time consuming for both the public and private sectors. In part, this is because there are a number of provisions in CEQA where definitions and requirements are unclear or imprecise.
- ✓ ***No UC Campus Has Reached a “Fair Share” Agreement.*** Although UC has a policy for campuses to work with local public agencies to contribute its fair share payments to mitigate off-campus impacts, no UC campus has been able to reach such an agreement with a neighboring jurisdiction.

Lack of State Accountability and Oversight

As previously mentioned, UC is constitutionally exempt from local land use regulations. Unlike the case with private developers and universities, local government does not have any jurisdiction over a UC LRDP. In addition, no other state agency approves an LRDP and EIR, unless it serves as a responsible agency (such as the California Coastal Commission) for environmental compliance. Moreover, the state does not review or monitor UC's implementation of the LRDP and the mitigation measures identified in the accompanying EIR. As a result there is very little state oversight over the LRDP process and the actual plan, and there is no formal process for ensuring that UC mitigates significant environmental impacts resulting from campus growth.

Although the Legislature considers funding requests for individual capital outlay projects as part of the state's annual budget process, it does not directly review LRDPs to determine whether they are aligned to its fiscal and policy priorities from a statewide perspective. (As mentioned earlier in this chapter, the Governor's budget proposes \$503 million in bond funds authorized by Proposition 1D (2006) for 26 capital outlay projects at UC. The budget also includes \$70 million in lease-revenue bonds for new research facilities.) This is particularly important given that an LRDP serves as an important policy document that outlines the enrollment and academic goals of a UC campus and lays out the framework and rationale for future capital outlay projects.

Lack of Standardization in Public Participation

Since UCOP does not have specific requirements regarding what shall be included in the LRDP process, there is often a lack of standardization in the degree to which local communities are involved in the planning process. For example, while some campuses (such as UC Santa Cruz and UC Riverside) developed an LRDP committee that included community representatives and local government officials, other campuses (such as UC Davis) did not. We also found that the number of public workshops held during the LRDP process can vary across campuses. In the process of updating their respective LRDPs, the Davis campus held 17 public workshops and the Santa Cruz campus held 5 public workshops. These workshops generally allow a campus to inform the local community on its development of an updated LRDP—such as the different land use options that the campus is considering—and to solicit their feedback.

Minimal Systemwide Coordination in Projecting Enrollment for Recent LRDPs

Some UC campuses have recently updated their LRDP based on a time horizon beyond 2010-11 (the time horizon of the university's most recent systemwide enrollment plan developed in 1999). For those years after 2010-11, an individual campus essentially develops its enrollment projections based on its own academic goals and locally determined demographic trend rather than systemwide needs. As a result, the campus's enrollment projections beyond 2010-11 are not coordinated with the other campuses. This is particularly important given that the Master Plan provides admission and enrollment guidelines on a statewide basis. For example, the Master Plan calls for UC (as a whole) to draw its students from the top 12.5 percent of public high school graduates in the entire state (not a particular region).

Campuses Want to Primarily Expand Graduate Enrollment

Campuses generally acknowledge that undergraduate enrollment demand will level out in a few years because of an anticipated reduction in the number of California high school graduates. According to the Department of Finance's Demographic Research Unit, growth in the number of high school graduates in the state will peak in a couple of years, and then rapidly decline to the point of going negative in 2012-13. Much of the projected growth identified in recent LRDPs is based on campus desires to expand and create new graduate and professional school programs. For example, the Santa Cruz campus is considering creating professional schools in the areas of management, education, public policy, and public media. In general, LRDPs do not explain the rationale for the proposed professional school from a statewide perspective and why it must be established at that particular campus (versus establishing it at another UC campus or expanding an existing program at another campus).

Lack of Clarity in CEQA

In our 1997 report *CEQA: Making It Work Better*, we examined the entire CEQA process and made recommendations to make the process more efficient and therefore less costly and time consuming for both project developers and public agencies. We found a number of provisions in CEQA where definitions and requirements are unclear, and thus subject to conflicting interpretations. For example, an EIR must include an analysis of the environmental impact for a range of reasonable project alternatives. However, CEQA provides few guidelines as to the kinds of alternatives that must be considered and the level of detail required for each alternative. This has led to analyses of alternatives that contribute little to the decision

making of public agencies. For instance, an alternative examined may not be feasible, such as the case where the alternative is development on a site not owned (or that cannot practically be purchased) by the developer.

Under CEQA, an EIR is required when a lead agency finds that a project may have “significant” adverse environmental impacts. While CEQA guidelines provide some guidance as to the circumstances under which a project would normally have a significant effect on the environment, we found that more detailed guidance is needed to provide greater certainty in the application of this concept. In view of the above, several host communities have filed lawsuits claiming that certain UC campuses have not adequately analyzed all possible alternatives or clarified all mitigation measures. For example, a neighborhood group in West Davis argued that the Davis campus violated CEQA by not considering reasonable alternatives to a proposed housing project.

No UC Campus Has Reached a Fair Share Agreement

The UC’s policy calls for payment of its fair share of costs to implement mitigation measures for off-campus impacts. However, as discussed earlier, no UC campus has made a payment to another public agency based on a fair share agreement developed in accordance to this policy. For example, although the Davis campus is in the process of beginning some of the development projects outlined in its 2004 LRDP, it still has not reached an agreement with the City of Davis for its fair share payments.

LAO Recommendations

Based on our review and findings, we recommend (1) increasing legislative oversight over UC’s LRDPs, (2) developing a more standard approach for soliciting public input, (3) projecting enrollment growth based on statewide goals, (4) making better use of the summer term, (5) clarifying and improving CEQA, and (6) requiring a report on UC’s efforts to reach fair share agreements with neighboring jurisdictions.

Greater Legislative Oversight

We recommend greater legislative oversight over the University of California’s (UC) Long Range Development Plans, in order to ensure that campuses’ long-term goals are aligned with statewide priorities. Specifically, we recommend UC provide copies of draft plans to the Legislature as they are made available for public review.

Given that an LRDP plans for the accommodation of long-term enrollment and academic goals, we recommend greater legislative oversight over

the development of UC's LRDPs. Specifically, we recommend UC provide the Legislature with copies of draft LRDPs that are submitted for public review. (Before the UC Regents can approve an LRDP and accompanying EIR, a campus must allow time for the public to review and comment on these documents.) At its discretion, the Legislature could hold hearings to review certain aspects of these draft plans. Moreover, the Legislature could express any concerns about the draft LRDP before it became final. (This, however, would not preclude the Legislature from expressing concerns in the future when the university requests funding for specific projects related to the LRDP.) This process would allow the university to amend the plan as needed to accommodate any legislative concerns.

Some of the relevant issues that the Legislature could examine in its review are:

- How much is the campus or medical center projected to grow and what type of growth is anticipated (such as in new or expanded graduate and professional school programs)?
- What is the rationale for the expected growth? How did the campus or medical center project the anticipated level of growth? Could the additional students be accommodated through better use of the summer term?
- To what extent were local communities involved in the development of the draft LRDP?
- What significant environmental impacts (if any) will the plan have on nonuniversity property? How does the university plan to mitigate such impacts?

We believe that legislative oversight would help ensure that the university's long-term goals are aligned with the state's priorities.

Develop Standard Approach for Soliciting Public Input

We recommend the University of California provide campuses and medical centers with more specific requirements regarding the level of public involvement in the long range development planning process, in order to increase the transparency of the process.

As noted earlier, there is a lack of standardization across UC campuses regarding the degree to which local communities are involved in the LRDP process. This can sometimes make it difficult for certain communities to provide input in the development of a campus's LRDP. Accordingly, we recommend UC provide more specific requirements and guidance to campuses developing LRDPs. For example, the university could require that a certain number of public workshops be held before the Regents review a

final LRDP. Moreover, UC could require that prior to developing the LRDP, each campus or medical center hold a series of public meetings regarding its academic and enrollment goals. Such an approach could increase the relevance of public input in the LRDP decision making process. Finally, the university could require that each LRDP planning committee include a certain number of community representatives and local government officials.

Project Enrollment Growth on Systemwide Basis

We recommend the Legislature require the University of California to use systemwide enrollment projections to determine the enrollment levels assumed in each Long Range Development Plan.

We recommend the Legislature require that the enrollment projections outlined in each LRDP be based on a systemwide enrollment plan, rather than the independent projections of an individual campus. In other words, in any given year the sum of the campus enrollment targets should equal the enrollment target for the entire university system (which in turn should be based on statewide goals and priorities). As noted earlier, UC is currently in the process of developing a new enrollment plan. Accordingly, we recommend the Legislature direct UC to provide systemwide enrollment projections through 2020 at budget hearings this spring. In order for the plan to be a useful planning tool for the Legislature, we believe that it is important for the university to explain and justify the assumptions and data used to calculate the projections.

A systemwide enrollment plan would also assist the Legislature in assessing proposals to fund specific enrollment growth levels at UC as part of the annual state budget process. For example, the Legislature may take issue with parts of UC's enrollment plan and instead find that growth is needed in different programs in order to meet the state's research and workforce needs (such as nursing) rather than in areas identified by UC. For example, at its November 2006 meeting, the Regents approved the development of a medical school at UC Riverside and a law school at UC Irvine. These plans may not be aligned with legislative priorities, given limited resources.

Better Use of Summer Term

We recommend the University of California campuses make better use of the summer term as a means to accommodate an anticipated increase in the number of students without having to construct new classrooms.

Given the large unused capacity at UC during the summer term, we believe the Legislature and the university should continue to explore ways to increase enrollment during the summer term. This is because better utilization of the summer term is a more cost-effective strategy for accommodating new enrollment growth than building new facilities. In addition, such a strategy helps reduce the significant environmental impacts associated with the construction of facilities. As we discussed in our *Analysis of the 2006-07 Budget Bill*, steps that campuses could take to increase summer enrollment include (1) offering financial incentives (such as charging *lower* fees for the summer term and somewhat *higher* fees for other terms), (2) requiring some summer enrollment at high-demand campuses, and (3) offering courses in the summer that typically fill up quickly during the other academic terms.

Streamline CEQA Process by Clarifying Guidelines

We recommend the Legislature improve the California Environmental Quality Act by clarifying language, improving definitions, and providing better guidelines on what constitutes feasible mitigation measures and alternatives.

As concluded above, CEQA currently provides lead agencies (such as UC) considerable discretion in the EIR process when it fails to provide clear definitions and requirements. For example, the act does not specify the kinds of alternatives that must be considered and the level of detail required for each alternative. Consequently, we recommend the Legislature clarify the terms and requirements of CEQA. For example, we recommend clarifying the scope of the alternative analyses in EIRs, including the reasonable number of alternatives to be considered and the level of detail in the analysis. We also recommend the Legislature provide better guidelines on what constitutes a significant impact and a feasible mitigation measure. (We originally made these recommendations—along with many others—in our 1997 CEQA report in order to make the CEQA process less costly and time-consuming to project developers and public agencies.) Such clarification would help ease some of the tension between UC campuses and their surrounding communities.

Report on Fair Share Agreements

In view of the recent court decision in City of Marina v. California State University Board of Trustees, we recommend the University of California report to the Legislature on what steps it will take to reach agreements with local public agencies regarding the mitigation of its fair share of environmental impacts.

The most contentious issue between campuses and their surrounding communities concerns the mitigation of off-campus impacts. Although UC's current policy is to work with communities in reaching an agreement for paying its fair share contribution, no campus currently has entered into such an agreement in accordance to this policy. In view of the recent court decision in *City of Marina v. CSU Board of Trustees*, however, the university has an obligation to negotiate with local public agencies regarding the mitigation of its fair share of environmental impacts. Thus, we recommend the Legislature require UC to report on what additional steps it will take, including changes to the current three-step policy, to ensure that fair share agreements are in fact developed with the appropriate jurisdictions.

We believe it is important for the Legislature to have assurance that there is resolution on the mitigation of off-campus impacts prior to considering related UC capital outlay projects. Depending on the outcome of UC's report, the Legislature could decide not to approve funding for a UC capital outlay project until the appropriate campus has entered into a memorandum of understanding with the appropriate jurisdictions regarding the mitigation of off-campus impacts associated with that project.

UC CAPITAL OUTLAY

The budget proposes to spend \$573.2 million in bond funds on UC capital projects in the budget year. (Almost all this amount—\$503.2 million—would be from Proposition 1D, the bond approved by voters in November 2006.) Proposed spending would support new phases of 15 projects previously funded by the state, at a cost of \$216.9 million. (These projects have future costs to complete them of \$158.1 million.) The budget also proposes 13 new projects, costing \$356.3 million in 2007-08 and \$95.5 million in future costs.

Proposition 1D allocated \$890 million in funds to UC. After accounting for the monies appropriated in the current year and proposed to be spent in the budget year, there would be \$46.9 million remaining. This amount is not adequate to cover the future costs of all projects already authorized and those proposed by the Governor in the budget.

New Projects. Of the 13 new projects, the costliest are for telemedicine/medical education facilities and two energy research facilities, which we discuss later.

Telemedicine Facilities

We recommend deletion of \$59 million from the administration's telemedicine proposal as: (1) the university has not yet presented a specific facility proposal to the Legislature for the Los Angeles campus and (2) the budget includes an unneeded contingency reserve of \$24 million. (Reduce Item 6440-304-6048 by \$59 million.) We further recommend that the remaining four projects be scheduled and that accompanying provisional language be amended similar to other items.

Proposition 1D, approved by the voters in November 2006, provided \$200 million to UC for telemedicine/medical education facilities. The budget proposes to spend virtually all this amount (\$199 million) in 2007-08 for five projects—one at each of the system's five medical schools (Davis, Irvine, Los Angeles, San Diego, and San Francisco). The state would contribute \$35 million to each project, with the campuses supplementing these funds in some cases.

As required by Proposition 1D, the proposed projects would “expand and enhance medical education programs with an emphasis on telemedicine.” (Telemedicine basically involves teleconferencing so that medical diagnostic services—particularly by specialists—can be provided to underserved areas.) The budget proposes to expand PRIME, currently at the Irvine campus, to three of the other four campuses with medical schools. The program is geared primarily towards training primary care physicians to work in underserved areas of the state.

The facilities request would renovate existing space and add new space to permit the expansion of the state's medical education programs and telemedicine capability. The segment has provided specific proposals for four of the campuses, and we recommend approval of those four projects. For Los Angeles, however, there is no proposal. The university has indicated that a proposal may be coming later this spring or early summer. Without a specific capital outlay proposal, the Legislature has no idea what it is buying in terms of the scope or cost of the project. Furthermore, the segment was unable to offer any reason for the project needing to go forward at this time that justified bypassing the normal capital outlay process. For these reasons, we recommend deletion of \$35 million proposed for the Los Angeles campus.

In addition, the item which appropriates the \$199 million for these projects: (1) includes \$24 million in contingency funding, (2) does not schedule the individual projects, and (3) provides the university with more authority over changes to projects than is the case with all its other projects. We recommend the deletion of \$24 million in contingency funding and that the four projects be scheduled in the item. We further recommend that the proposed budget bill language be modified to limit the university's

authority over project changes, similar to language included for other higher education capital outlay items.

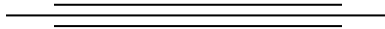
Alternative Energy Research Proposals

We recommend deletion of the Governor's request for \$70 million in lease-revenue bond proceeds to fund two alternative energy research projects, as the administration has not yet presented specific capital facilities proposals. (Eliminate Item 6440-301-0660.)

The budget proposal includes funding for two alternative energy research projects that would be funded with \$70 million in lease-revenue bond proceeds:

- **Helios Project.** The Helios Project would receive \$30 million as the state's share toward construction of a new, \$100 million energy building at the Berkeley campus. (The remaining funding would come from the federal government and private sources.) The Helios project seeks to develop new solar energy technologies.
- **Energy Biosciences Institute.** The Governor's budget seeks another \$40 million in funding from lease-revenue bonds toward the development and operation of an Energy Biosciences Institute at UC Berkeley. This funding would supplement a \$500 million grant that was awarded to the university in January 2007. The Institute would focus on converting biomass materials into fuels and developing other alternative energy technologies. Budget bill language specifies that the scope and cost of this project would be defined by the State Public Works Board.

Recommend Deletion of Funds. While the administration has requested funds for those two projects, it has not presented the Legislature with specific facility requests. That is, the university has not prepared capital outlay budget change proposals which define the scope and costs of the project. As such, the request for funds is premature and we therefore recommend deletion of the funds.



CALIFORNIA STATE UNIVERSITY (6610)

The California State University (CSU) consists of 23 campuses. The Governor's budget includes about \$6.8 billion for CSU from all fund sources—including state General Fund, student fee revenue, federal funds, and other funds. The budget proposes General Fund spending of about \$3 billion for the segment in 2007-08. This is an increase of \$165 million, or 5.9 percent, from the revised 2006-07 budget.

Major General Fund Proposals

Figure 1 summarizes the Governor's proposed General Fund changes for the current and budget year. For 2007-08, the Governor proposes \$176.3 million in various General Fund augmentations, a \$7 million General Fund reduction to CSU's outreach programs, and a \$4.4 million net reduction for baseline and technical adjustments. We discuss the proposed augmentations in further detail below.

Base Budget Increase. The Governor's budget provides CSU with a 4 percent General Fund base increase of \$108.9 million that is not designated for specific purposes. The university indicates that it would apply most of these funds to support salary and benefit increases for faculty and staff.

Enrollment Growth. In addition to the base increase, the budget includes a \$65.5 million General Fund augmentation for enrollment growth at CSU. This would increase the university's state-supported enrollment by 8,355 full-time equivalent (FTE) students, or 2.5 percent, above the current-year level. The proposed augmentation assumes a marginal General Fund cost of \$7,837 per additional student, reflecting a new methodology proposed by the Governor for calculating the marginal cost of serving an additional student.

Figure 1	
California State University	
General Fund Budget Proposal	
<i>(Dollars in Millions)</i>	
2006-07 Budget Act	\$2,788.9
Public Employees' Retirement System rate increase	\$23.3
Carryover/reappropriation	1.2
Other technical adjustments	-2.0
Revised 2006-07 Budget	\$2,811.4
Baseline and Technical Adjustments	-\$4.4
Proposed Increases	
Base increase (4 percent)	\$108.9
Enrollment growth (2.5 percent)	65.5
Expand science and math teacher initiative	2.0
Subtotal	(\$176.3)
Proposed Reductions	
Reduce General Fund support for outreach programs	-\$7.0
2007-08 Proposed Budget	\$2,976.3
Change From 2006-07 Revised Budget	
Amount	\$165.0
Percent	5.9%

Science and Math Teacher Initiative. The budget provides \$2 million in new funding for the expansion of the Governor's science and math teacher initiative, which is intended to increase the number of science and math teachers trained at CSU. The proposed augmentation is intended to enable the university to establish three regional science and math teacher recruitment centers.

Student Fee Increases

For 2007-08, the Governor's budget assumes student fee increases of 10 percent for undergraduates, graduate students, and teacher credential candidates. (Student fees at CSU are established by the CSU Board of Trustees.) The assumed fee increases are expected to provide an additional \$97.8 million in student fee revenue. The Governor's proposal would provide CSU full discretion in deciding how to spend the additional revenue. Below, we review the various fee levels for the budget year.

Systemwide Fees for Undergraduate, Graduate, and Teacher Credential Program Students. Figure 2 summarizes the Governor's proposed increases in systemwide fees. As the figure shows, the budget assumes an increase of 10 percent in the systemwide fee for undergraduate and graduate students, including those enrolled in a teacher credential program (who pay a different fee than students enrolled in other graduate programs). When combined with campus based fees, the proposed total student fee for a full-time student in 2007-08 would be \$3,451 for undergraduates, \$3,895 for teacher credential students, and \$4,093 for all other graduate students.

Figure 2
CSU Systemwide Fees^a
Resident Full-Time Students

	2006-07	Proposed 2007-08	Change From 2006-07	
			Amount	Percent
Undergraduate students	\$2,520	\$2,772	\$252	10%
Teacher credential students	2,922	3,216	294	10
Graduate students ^b	3,102	3,414	312	10

^a Amounts do not include campus-based fees.
^b Excludes students enrolled in teacher credential programs.

Nonresident Tuition. In addition to paying systemwide and campus-based fees, nonresident students also pay a supplementary fee (commonly known as nonresident tuition). The budget assumes that the surcharge for nonresident students—both undergraduates and graduates—would remain unchanged at \$10,170.

INTERSEGMENTAL ISSUES INVOLVING CSU

In the "Intersegmental" write-ups earlier in this chapter, we address several issues relating to CSU. For each of these issues, we offer an alternative to the Governor's proposal. We summarize our main findings and recommendations below.

Consider Different Approaches for Funding and Evaluating Outreach Programs. For the fourth year in a row, the Governor's budget proposes to reduce General Fund support for CSU's outreach programs, for savings of \$7 million. (The CSU budget would still contain \$45 million

for these programs.) In the “UC and CSU Outreach Programs” write-up in this chapter, we withhold recommendation on the proposed reduction, pending our review of the evaluation of the programs to be submitted in the spring. If the Legislature wishes to restore funding for these programs, we recommend requiring an external evaluation of CSU’s outreach programs, rather than continue the practice of asking the university to evaluate the effectiveness of its own programs. We also recommend the Legislature consider an alternative approach for funding and delivering outreach services—a College Preparation Block Grant targeted at K-12 schools with very low college participation rates.

Fund Enrollment Growth Consistent With Demographic Projections and Legislative Marginal Cost Methodology. The Governor’s budget provides \$65.5 million to fund 2.5 percent enrollment growth at a marginal General Fund cost of \$7,837 per additional FTE student, based on his proposal for a new marginal cost methodology. The Governor essentially uses the same methodology that he used last year in his 2006-07 budget proposal, which the Legislature rejected. In the “UC and CSU Enrollment Growth and Funding” write-up, we recommend two modifications to the Governor’s enrollment proposal. First, based on our demographic projections, we recommend the Legislature provide funding for enrollment growth at a rate of 2 percent. Our proposal would allow the university to accommodate enrollment growth next year due to increases in population, as well as modest increases in college participation rates.

Second, we recommend the Legislature once again reject the Governor’s proposed marginal cost methodology. We find the marginal cost methodology that the Legislature developed and approved as part of the 2006-07 budget more appropriately funds the increased costs associated with enrollment growth and preserves legislative prerogatives. Using this legislatively determined marginal cost methodology, we recommend reducing the Governor’s proposed CSU student funding rate from \$7,837 to \$7,710. Accordingly, we recommend a General Fund reduction of \$13.9 million to reflect our enrollment growth and marginal cost recommendations for CSU.

Assume Lower Fee Increase to Maintain Students’ Share of Cost at Current-Year Levels. The proposed budget assumes a 10 percent increase in the systemwide fees for undergraduates, graduate students, and teacher credential candidates at CSU. In the “Student Fees” write-up, we recommend that, absent an explicit student fee policy, the current share of educational costs borne by students through fees be maintained in 2007-08. We estimate that this would entail a modest systemwide fee increase of 2.4 percent, which is our projection of inflation for the budget year. For a full-time CSU undergraduate, this equates to an annual increase of \$147.

Standardize Approach for Funding Enrollment in Nursing Programs. The proposed budget includes provisional language requiring CSU to increase its enrollment in its nursing programs by 340 FTE students. However, in contrast to how nursing enrollment is treated elsewhere in CSU's budget (as well as in the University of California's [UC's] and the California Community College's budget), the Governor's proposal does not provide supplemental funding in recognition of the higher cost of serving these students. In the "Higher Education Nursing Proposals" write-up, we recommend a standardized approach to funding enrollment growth in nursing programs at all three segments. For CSU, we recommend an augmentation of \$939,000 to recognize the higher costs (above normal marginal cost funding) imposed by the additional nursing students.

GENERAL FUND BASE INCREASE

Given our projection of inflation for 2007-08, we recommend the Legislature provide a 2.4 percent General Fund base increase, or cost-of-living adjustment, to the California State University (CSU). Given the Governor's budget funds a 4 percent base increase, we recommend deleting \$43.6 million from the \$108.9 million General Fund augmentation requested in the budget for CSU. (Reduce Item 6610-001-0001 by \$43.6 million.)

In order to offset the effects of inflation, which erodes the purchasing power of a fixed appropriation over time, the annual state budget typically includes funding to provide price or cost-of-living adjustments (COLAs) for many state programs. It is from these adjustments that programs generally pay for employee salary and wage increases, as well as increased prices of goods and services. In other words, these adjustments are not intended to fund increased workload (such as the expansion of existing services or the establishment of new services), but rather are meant to help pay for existing workload whose costs have increased due to inflation. Although COLAs have customarily been provided to CSU in most years, there is no statutory requirement for these payments.

Governor's Budget Proposes 4 Percent COLA. For 2007-08, the Governor proposes a 4 percent General Fund base increase (effectively a discretionary COLA) of \$108.9 million for CSU. At this time, we project inflation in 2007-08 to be 2.4 percent (based on our estimate of the change in the U.S. state and local deflator from 2006-07 to 2007-08). We therefore believe the Governor's proposed 4 percent General Fund base increase, combined with increased fee revenue, would provide the university with funding well above what is needed to pay for the higher cost of meeting *existing* workload. For example, CSU plans to use some of the new funding

to increase salaries beyond inflation, as well as to support new academic technology initiatives. (We further discuss the issue of faculty salaries in the “California Postsecondary Education Commission” section of this chapter.)

Recommend Funding 2.4 Percent COLA. In view of our estimate of inflation for the budget year, we recommend the Legislature provide a 2.4 percent COLA to CSU, rather than the Governor’s proposed 4 percent. An adjustment tied to inflation would cost \$65.3 million. Thus, we recommend the Legislature reduce the Governor’s proposed base increase for CSU from \$108.9 million to \$65.3 million, resulting in General Fund savings of \$43.6 million.

Under our proposal, the university would still receive sufficient general purpose funding to compensate for increased costs. At the same time, the Legislature could use our identified General Fund savings of \$43.6 million (in addition to the savings from our enrollment growth recommendations) to address other priorities in higher education or elsewhere.

SCIENCE AND MATH TEACHER INITIATIVE

We withhold recommendation on the proposed \$2 million General Fund augmentation in base funding for the Governor’s science and math teacher initiative, pending our review of the California State University’s progress report on the initiative to be submitted in April.

For the current year, the *2006-07 Budget Act* includes a total of \$1.4 million in General Fund support for the Governor’s science and math teacher initiative. This initiative, which was initially funded in the 2005-06 budget, is intended to increase the number of science and math teachers trained at CSU. The current-year amount consists of \$715,000 in base funding and a one-time increase of \$652,000. For the budget year, the Governor proposes a \$2 million increase in base funding for the science and math teacher initiative, for a total of \$2.7 million. (The Governor’s budget also includes \$3.8 million to support the same initiative at UC.) The proposed augmentation is intended to enable CSU to expand its current efforts and establish additional regional science and math teacher recruitment centers.

As part of the *2006-07 Budget Act*, the Legislature adopted provisional language to ensure oversight of CSU’s use of the science and math teacher initiative funding. Specifically, the 2006-07 budget requires that CSU report to the Legislature by April 1, 2007, on its progress toward increasing the quality and supply of science and math teachers. We withhold recommendation on the proposed augmentation to the science and math teacher initiative until we have had an opportunity to review this report.

LONG RANGE PLANNING ISSUES

In a recent report, *A Review of UC's Long Range Development Planning Process*, we reviewed the current process used by UC to prepare land use plans (also referred to at UC as long range development plans) that guide the physical development of its campuses. We recommended steps the Legislature could take to make the process more transparent and effective. (The "University of California" write-up earlier in this chapter includes a summary of our report.) Although the report focused exclusively on UC, we believe that many of our recommendations also apply to CSU, as we discuss below.

Each CSU Campus Prepares a Physical Master Plan

Currently, CSU uses a long range planning process somewhat similar to UC's. Each of the 23 CSU campuses periodically develops a physical master plan that is supposed to guide the future development of its facilities—based on academic goals and projected student enrollment levels—for an established time horizon (usually about ten years). Since CSU is a state institution, such a plan is not subject to local land use regulations. This means that local government does not have the jurisdiction to reject or oppose a campus's physical master plan or a specific capital outlay project on the campus. In addition, state agencies typically do not review or approve a CSU campus's master plan. Moreover, the Legislature currently does not provide any formal guidance or oversight regarding the development or implementation of such a plan.

As with UC, the California Environmental Quality Act (CEQA) requires CSU campuses to complete an Environmental Impact Report (EIR) for each plan. The EIR must (1) provide detailed information about a project's likely effect on the environment (such as traffic), (2) identify measures to mitigate significant environmental effects (such as mitigating traffic impacts by constructing physical improvements like signals or roundabouts), and (3) examine reasonable alternatives to the project. Under CEQA, the CSU Board of Trustees must certify an EIR before approving a campus's physical master plan.

In developing physical master plans and the accompanying EIRs, campuses typically consult surrounding communities in an attempt to achieve mutually agreeable plans. In recent years, however, campuses and communities have sometimes disagreed about the responsibility for environmental impacts that occur outside of the university's jurisdiction. For example, although a new signal light in the city could manage traffic from campus expansion, the city and campus might disagree about how the cost of that signal light should be shared. As we discuss below, a re-

cent court decision involving CSU helps clarify the responsibility of the university to help mitigate off-campus impacts.

City of Marina v. CSU Board of Trustees

In 1994, CSU agreed to establish a Monterey campus on a portion of the former Fort Ord military base as part of the Fort Ord Reuse Authority (FORA) Act. (The state Legislature created FORA—which includes Monterey County and the Cities of Monterey, Salinas, Carmel, Marina, and Pacific Grove—to manage the transition of the base from military to civilian use.) The CSU Board of Trustees in 1998 certified a master plan for the new campus and an accompanying EIR, which identified significant environmental impacts to various public resources. Although the Trustees agreed to mitigate those impacts that would occur on campus, they determined that the mitigation of off-campus impacts was not within their jurisdiction, but rather within the jurisdiction of FORA. Accordingly, the Trustees declined to fund off-campus mitigation measures.

In response, FORA and the City of Marina challenged the Trustees' decision to certify the EIR (despite the unmitigated effects) as a violation of CEQA. In July 2006, the California Supreme Court reversed an earlier Court of Appeal's decision by concluding that the Trustees had abused their discretion and thus their approval of the EIR was not valid. Specifically, the Supreme Court ruled that:

- ***Off-Campus Impacts Must Be Mitigated.*** The CEQA does not restrict the CSU Trustees' obligation to mitigate or void significant environmental effects occurring only on the university's own property. Rather the trustees are required to mitigate a project's significant effects on the environment.
- ***Voluntary Payments Are a Feasible Form of Mitigation.*** If the trustees cannot adequately mitigate off-campus environmental impacts with actions on campus, then a voluntary payment to a third party (such as FORA) to perform the necessary acts off campus is a feasible form of mitigation.

LAO Recommendations

As previously discussed, many of the recommendations in our recent report on UC's long range development planning process could also apply to CSU. For example, we believe the Legislature should (1) provide greater oversight over CSU's physical master plans (including the enrollment projections that they are based on) and (2) have the university report on its efforts to mitigate off-campus impacts.

Greater Legislative Oversight

We recommend greater legislative oversight over the California State University's (CSU) physical master plans, in order to ensure that campuses' long-term goals are aligned with statewide priorities. Specifically, we recommend CSU provide copies of draft plans to the Legislature before they are approved by the CSU Board of Trustees. Since future student enrollment levels are the main drivers of a campus's physical master plan, we further recommend requiring CSU to provide systemwide projections through 2020 at budget hearings this spring.

Given that a campus's physical master plan serves as an important policy document that outlines the enrollment and academic goals of a CSU campus and lays out the framework and rationale for future capital outlay projects, we recommend greater legislative oversight over their development. Specifically, we recommend CSU provide the Legislature with copies of draft master plans before they are approved by the CSU Trustees. At its discretion, the Legislature could hold hearings to review certain aspects of these draft plans. Moreover, the Legislature could express any concerns about the draft plan before it became final. (This, however, would not preclude the Legislature from expressing concerns in the future when the university requests funding for specific projects related to a campus master plan.) This process would allow the university to amend the plan as needed to accommodate any legislative concerns.

Since future student enrollment levels are the main drivers of a campus's physical master plan, we also recommend greater oversight regarding CSU's long-term enrollment projections. Specifically, we recommend the Legislature direct CSU to provide an enrollment plan that includes systemwide projections through 2020 at budget hearings this spring. In order for the plan to be useful planning tool for the Legislature, we believe it is important for the university to explain and justify the assumptions and data used to calculate the enrollment projections. A systemwide enrollment plan would also assist the Legislature in assessing proposals to fund specific enrollment growth levels at CSU as part of the annual state budget process.

Update on Mitigation of Off-Campus Impacts

In view of the recent court decision in City of Marina v. California State University (CSU) Board of Trustees, we recommend CSU report to the Legislature on what steps it will take to reach agreements with local public agencies regarding the mitigation of off-campus environmental impacts.

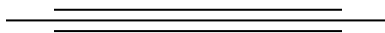
As mentioned above, the recent court decision in *City of Marina v. CSU Board of Trustees* clarifies the need for the university to negotiate with local public agencies regarding the mitigation of the environmental impacts caused by its projects. Thus, we recommend the Legislature require CSU to report on its policies for reaching such agreements with the appropriate jurisdictions. We believe it is important for the Legislature to have assurance that there is resolution on the mitigation of off-campus impacts prior to considering related CSU capital outlay projects. Depending on the outcome of CSU's report, the Legislature could decide not to approve funding for a CSU capital outlay project until the appropriate campus has entered into a memorandum of understanding with the appropriate jurisdictions regarding the mitigation of off-campus impacts associated with that project.

CSU CAPITAL OUTLAY

The budget proposes to spend \$346 million in bond funds on 27 CSU capital projects in the budget year. (Almost all this amount—\$326 million—would be from Proposition 1D, the bond approved by voters in November 2006.) Most of the proposed spending would go for new phases of 19 projects previously funded by the state. (These projects have future costs to complete them of about \$115 million.) The budget also proposes eight new projects, costing \$54 million in 2007-08 and \$134.6 million in future costs.

Proposition 1D allocated \$690 million in funds to CSU. After accounting for the monies appropriated in the current year and proposed to be spent in the budget year, there would be \$30 million remaining in 2008-09. This amount is not adequate to cover the future costs of all projects currently in the works and those proposed by the Governor in the budget.

New Projects. Most of new projects proposed in the budget involve renovation or replacement of existing facilities. Given the high average age of CSU's facilities, it is appropriate for the segment to focus a large proportion of its annual capital budget on these types of projects. The new projects would have little impact on instructional space. In fact, the loss of space in one classroom renovation results in a small net loss of instructional space for the segment as a whole. We raise no issues with CSU's capital outlay budget.



CALIFORNIA COMMUNITY COLLEGES (6870)

California Community Colleges (CCC) provide instruction to about 1.6 million students (fall headcount enrollment) at 109 colleges operated by 72 locally governed districts throughout the state. The state's *Master Plan for Higher Education* and existing statute charge the community colleges with carrying out a number of educational missions. The system offers academic and occupational programs at the lower division (freshman and sophomore) level, as well as recreational courses and precollegiate basic skills instruction. Based on agreements with local school districts, some college districts also offer a variety of adult education programs. In addition, pursuant to state law, many colleges have established programs intended to promote regional economic development.

CCC BUDGET OVERVIEW

Funding Increases Proposed. As shown in Figure 1, the Governor's proposal would increase total Proposition 98 funding (General Fund and local property taxes) for CCC by \$377 million, or 6.4 percent, over the revised current-year estimate. This augmentation funds a cost-of-living adjustment (COLA) of 4.04 percent, enrollment growth of 2 percent, a fee-reduction backfill, and several program expansions. Counting all fund sources—including student fee revenue and federal and local funds—CCC's budget would total \$8.6 billion in 2007-08.

CCC's Share of Proposition 98 Funding. As shown in Figure 1, the Governor's budget includes \$6.3 billion in Proposition 98 funding for CCC in 2007-08. This is almost three-quarters of total community college funding. Overall, Proposition 98 provides funding of approximately \$57 billion in support of K-12 education, CCC, and several state agencies. As proposed by the Governor, CCC would receive 11 percent of total Proposition 98 funding. This is slightly higher than its statutory share, which is 10.9 percent of total Proposition 98 appropriations. In recent years, this provision

has been suspended in the annual budget act and CCC's share of Proposition 98 funding has been somewhat *lower* than 10.9 percent. (The CCC's share of Proposition 98 funding in the current year is 10.7 percent.) In order to provide an amount different from the 10.9 percent specified in statute, the administration proposes again to suspend this provision.

Figure 1**Community College Budget Summary***(Dollars in Millions)*

	Actual 2005-06	Estimated 2006-07	Proposed 2007-08	Change From 2006-07	
				Amount	Percent
Community College Proposition 98					
General Fund	\$3,669.7	\$4,039.6	\$4,223.6	\$184.0	4.6%
Local property tax	1,802.7	1,857.4	2,050.5	193.1	10.4
Subtotals, Proposition 98	(\$5,472.4)	(\$5,897.0)	(\$6,274.1)	(\$377.1)	(6.4%)
Other Funds					
General Fund	(\$264.8)	(\$293.3)	(\$278.6)	(-\$14.7)	(-5.0%)
Proposition 98 Reversion Account	35.6	22.3	—	-22.3	-100.0
State operations	9.2	9.7	9.9	0.2	2.1
Teachers' retirement	82.2	83.0	82.0	-1.0	-1.2
Bond payments	137.8	148.3	187.3	39.0	26.3
Loan for Compton CCD ^a	—	30.0	—	-30.0	-100.0
Compton CCD ^a Loan Payback	—	—	-0.6	-0.6	—
State lottery funds	177.9	173.9	173.9	—	—
Other state funds	13.3	13.9	13.7	-0.2	-1.4
Student fees	344.9	321.7	281.9	-39.8	-12.4
Federal funds	249.8	267.0	267.0	—	—
Other local funds	1,241.7	1,326.9	1,326.9	—	—
Subtotals, other funds	(\$2,292.4)	(\$2,396.7)	(\$2,342.0)	(-\$54.7)	(-2.3%)
Grand Totals	\$7,764.8	\$8,293.7	\$8,616.1	\$322.4	3.9%

^a Community college district.
Detail may not total due to rounding.

Major Budget Changes

Figure 2 (see next page) shows the changes proposed for community college Proposition 98 spending in the current and budget years. Major base increases in 2007-08 include \$225 million for a COLA of 4.04 percent and

Figure 2
California Community Colleges
Governor's Budget Proposal

Proposition 98 Spending
(In Millions)

2006-07 (Enacted)	\$5,885.0
Increase for nursing education programs	\$9.0
Increase for California Partnership for Achieving Student Success	1.0
Local property tax adjustment	4.0
Lease-purchase payment reduction	-2.0
2006-07 (Estimated)	\$5,897.0
Proposed Budget-Year Augmentations	
Cost-of-living adjustment (COLA) for apportionments	\$224.9
Enrollment growth for apportionments	109.1
COLA and enrollment growth for categorical programs	19.6
Current year fee reduction backfill	33.2
Fiscal Crisis Management Assistance Team	0.3
Subtotal	(\$387.1)
Proposed Budget-Year Reductions	
Lease-purchase payments	-\$2.5
Adjustment for revised fee estimates	-1.3
Technical adjustments	-6.2
Subtotal	(-\$10.0)
2007-08 (Proposed)	\$6,274.1
Change From 2006-07 (Estimated):	
Amount	\$377.1
Percent	6.4%

\$109 million for enrollment growth of 2 percent. (Following longstanding practice, the Governor proposes that CCC receive the same statutory COLA as K-12 schools. The statutory COLA is based on an estimate of inflation that will not be finalized until April.) The administration also proposes to continue the student fee reduction that went into effect halfway through the current fiscal year. The budget proposes an additional \$33 million to backfill the full-year effect of this fee reduction (from \$26 per unit to \$20 per unit). In addition to these base adjustments, the Governor proposes program expansions for career technical and nursing education. (We discuss the career technical education proposal earlier in the "Crosscut-

ting Issues” section of this chapter, and the nursing proposal in the “Intersegmental” section.) The Governor’s budget proposes to permanently redirect \$33 million from CCC basic skills enrollment funding to a new “student success” initiative that expands counseling, tutoring, and other support services for students. (We discuss the “student success” initiative later in this chapter.)

Proposition 98 Spending by Major Program

Figure 3 (see next page) shows Proposition 98 expenditures for community college programs. As shown in the figure, apportionment funding (available to districts to spend on general purposes such as salaries, equipment, and supplies) accounts for \$5.6 billion in 2007-08, an increase of \$360 million, or 6.9 percent, from the current year. Apportionment funding in the budget year accounts for about 89 percent of CCC’s total Proposition 98 expenditures.

Categorical programs (whose funding is earmarked for specific purposes) also are shown in Figure 3. These programs support a wide range of activities—from services to disabled students to part-time faculty health insurance. The Governor’s student success initiative would eliminate \$33.1 million from the basic skills overcap categorical program and augment the matriculation categorical by the same amount. In addition, the Governor’s budget proposes increases of approximately 6 percent for matriculation and two other categoricals to fund a COLA and enrollment growth. For most other programs, he proposes no changes.

Student Fees

Effective January 2007, student fees on credit courses decreased from \$26 to \$20 per unit. (There continues to be no fee charged for *noncredit* courses.) The Governor proposes no change to the student fee level in the budget year. Under the Governor’s budget, student fee revenue would account for 3.3 percent of total CCC funding, down from 3.9 percent of CCC funding in 2006-07. (We discuss the fee reduction in more detail in our “Intersegmental” section of this chapter.)

ENROLLMENT LEVELS AND FUNDING

The state’s community college system is the nation’s largest system of higher education and accounts for about 22 percent of all community college students in the country. Three out of four public postsecondary students in the state are enrolled in a California community college.

Figure 3
Major Community College Programs
Funded by Proposition 98^a

(Dollars in Millions)

	Estimated 2006-07	Proposed 2007-08	Change	
			Amount	Percent
Apportionments				
General Fund	\$3,347.4	\$3,513.8	\$166.4	5.0%
Local property tax revenue	1,857.4	2,050.5	193.1	10.4
Subtotals	(\$5,204.8)	(\$5,564.3)	(\$359.5)	(6.9%)
Categorical Programs				
Basic skills overcap ^b	\$33.1	—	-\$33.1	-100.0%
Matriculation ^b	95.5	\$134.4	38.9	40.7
Career technical education	20.0	20.0	—	—
Nursing	25.9	25.9	—	—
Extended Opportunity Programs and Services	112.9	119.8	6.9	6.1
Disabled Students	107.9	114.5	6.6	6.1
Apprenticeships	15.2	15.2	—	—
Services for CalWORKs ^c recipients	43.6	43.6	—	—
Part-time faculty compensation	50.8	50.8	—	—
Part-time faculty office hours	7.2	7.2	—	—
Part-time faculty health insurance	1.0	1.0	—	—
Physical plant and instructional support	27.3	27.3	—	—
Economic development program	46.8	46.8	—	—
Telecommunications and technology services	26.2	26.2	—	—
Financial aid/outreach	52.6	51.3	-1.3	-2.5
Child care funds for students	6.5	6.8	0.3	4.0
Foster Parent Training Program	4.8	4.8	—	—
Fund for Student Success	6.2	6.2	—	—
Other programs	8.7	8.0	-0.7	-8.0
Subtotals, categorical programs	(\$692.2)	(\$709.8)	(\$17.6)	(2.5%)
Totals	\$5,897.0	\$6,274.1	\$377.1	6.4%
<p>^a Excludes available funding appropriated in prior fiscal years.</p> <p>^b Governor proposes to permanently redirect basic skills overcap funding to matriculation in 2007-08 as part of his "student success initiative."</p> <p>^c California Work Opportunity and Responsibility to Kids.</p>				

Recent Trends

What Influences Enrollment at CCC? Many factors affect the number of students that attend a community college. Changes in the state's population, particularly the college-age population, can be a major factor affecting enrollment levels. Fluctuations in participation rates affect enrollment at California's community colleges as well, but these are much more difficult to project. Factors such as state educational policies—relating to fees and financial aid, for example—and personal choices of potential students help determine participation rates. Additionally, factors such as the availability of certain classes, local economic conditions, and the perceived value of the education to potential students also affect participation rates.

Enrollment Levels Up and Down. As shown in Figure 4 (see next page), headcount enrollment (the number of individual part-time and full-time students attending a community college) is about 200,000 students higher than a decade ago. Growth has been uneven, fluctuating on a year-to-year basis. Enrollment peaked in fall 2002, but since then has declined by about 8 percent (140,000 students). During the same period, the college-age population (18- to 24-year olds) has grown by 5 percent, and the adult population (aged 25 to 64) has grown by 7 percent. As we discussed in our *2006-07 Analysis of the Budget Bill* (page E-250), several factors may be contributing to this recent decline, including students opting for employment as a result of an improving state economy. A census survey of community colleges in November 2006 suggests that fall 2006 enrollment may be slightly higher than fall 2005. A final headcount for fall 2006 will not be available until the spring.

Enrollment Growth Overfunded in Past Four Years. Each year the CCC budget includes an augmentation to accommodate additional students. In some years, funding has been insufficient to cover actual growth. For example, enrollment significantly exceeded funding in 2001-02, due in part to individuals returning to attend college at the time of a tight job market. Since the enrollment peak of a few years ago, however, the state budget has provided more funding for enrollment growth than community colleges could use. Figure 5 (see next page) compares budgeted and actual enrollment increases since 2001-02. As the figure shows, budgeted enrollment funding has grown faster than actual enrollment (measured as full-time equivalent [FTE] students) for the past four years. For example, the community colleges were funded for enrollment growth of almost 4 percent in 2004-05, but actual enrollment levels increased by less than 1.5 percent. In 2005-06, the community colleges were funded for enrollment growth of slightly more than 1.1 percent, but FTE enrollment levels actually *declined* by 1.3 percent.

Figure 4

CCC Headcount Has Declined Since Peaking in 2002

Fall Headcount Enrollment, in Millions

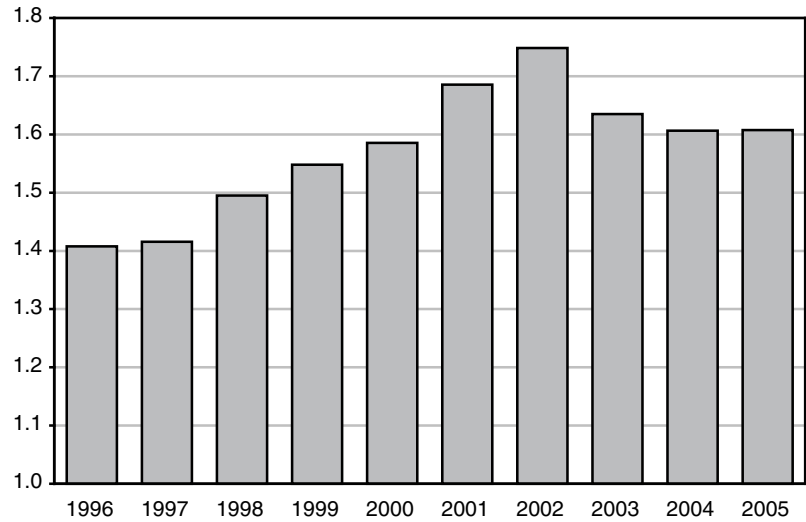
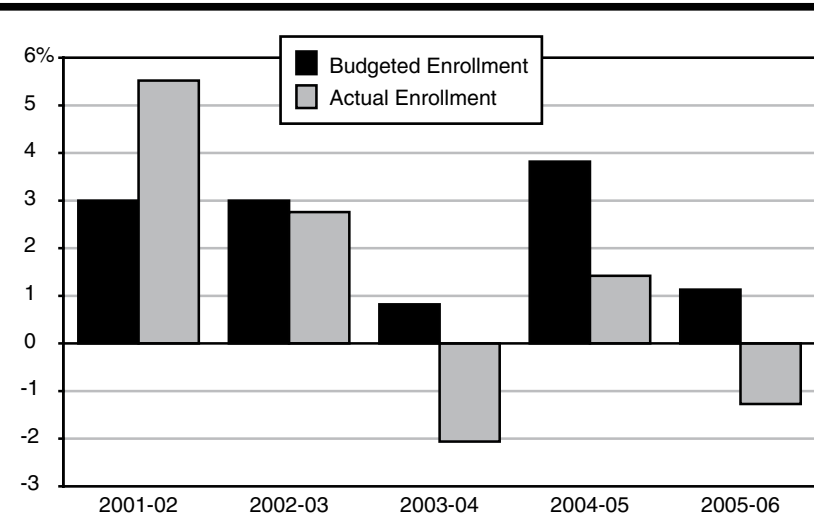


Figure 5

Funding for Enrollment Growth Has Exceeded Actual Enrollment in Recent Years



^aBased on full-time equivalent students.

Current-Year Enrollment Funding

Recent annual budgets have provided community colleges with more enrollment funding than they have been able to use. We recommend that the Legislature reduce the CCC's current-year Proposition 98 appropriation to account for unused enrollment funding in 2006-07. This will help address the state's budgetary problem, with no impact on the segment's ability to accommodate actual enrollment growth.

As a result of the state's recent overfunding of community college enrollment growth, a large amount of enrollment funding is available to the community colleges in the current year. Below, we discuss the two types of enrollment funding available to accommodate growth in 2006-07: (1) enrollment restoration funding for slots that became vacant in past years, and (2) new enrollment growth funding.

Enrollment Restoration Funding

In recent years, over half of community college districts have experienced declining enrollment. State law allows these districts to retain enrollment funding for vacant slots in the year they become vacant in order to cushion district budgets from year-to-year enrollment volatility. However, districts *lose* enrollment funds from their base for slots that remain vacant for a second year. Although individual districts lose funding in these cases, the same amount of funding remains in the overall CCC base budget for three years. These funds are available to "restore" the enrollment base of districts that regain lost enrollment within that three-year period. At the end of each year, any of this funding not used for restoration is available for one-time purposes. Regulations developed by the Chancellor's Office permit use for one-time purposes such as covering shortfalls in student fee revenue and providing general apportionments to districts.

Enrollment Restoration Funds Exceed \$160 Million

Figure 6 (see next page) shows the amount of funding that was reduced from district budgets as a result of declining enrollment over the past three years. The figure shows that these districts are entitled to "earn back" up to \$161 million in enrollment restoration funding to the extent that new students fill the vacant slots in the current year.

Most Districts Unlikely to Restore Enrollment in Current Year; Recommend Reducing CCC's Proposition 98 Appropriation. Based on our discussions with CCC officials and our demographic projections, we expect that only a portion of the \$161 million in enrollment funding will be restored to districts in the current year. The remaining funds would

be freed up for other one-time purposes in the current year. At the time this *Analysis* was being prepared, the exact amount of unused funding was not clear. Our preliminary estimate is that roughly one-half of the enrollment restoration funds (approximately \$80 million) could be freed up. We expect to have a reliable estimate by the time of the May Revision. We therefore recommend the Legislature at that time reduce on a one-time basis CCC's current-year appropriation of Proposition 98 funding by the amount of unused enrollment restoration funding that remains.

Figure 6
Significant Restoration Funding Available to Districts in Current Year

(Dollars in Millions)

Year of Decline	Enrollment Restoration Funds Available	Vacant Slots^a
2003-04	\$2.5	1,282
2004-05	16.3	4,985
2005-06	142.6	41,222
Total Available in 2006-07	\$161.4	47,489

^a Full-time equivalent students.

As we discuss earlier in this chapter (see "Proposition 98 Priorities for 2007-08"), our revenue forecast suggests that the state's current-year spending level for Proposition 98 is about \$600 million higher than the minimum guarantee. For this reason, a reduction in Proposition 98 spending would generate a like amount of General Fund savings. This would also reduce the 2006-07 Proposition 98 base, from which the 2007-08 Proposition 98 guarantee is calculated. Our recommendation would accomplish all this without affecting the ability of the segment to address student enrollment demand.

2006-07 Enrollment Growth Funding

Districts Unlikely to Use All Current-Year Enrollment Growth Funding; Recommend Reducing CCC's Proposition 98 Appropriation. The CCC also has \$97.5 million in current-year funding for new enrollment. Based on our demographic projections and anecdotal information from districts, we expect districts will again not be able to use all of this funding.

We therefore recommend that the Legislature reduce the 2006-07 appropriation for CCC enrollment growth. Although a better estimate will not be known until the May Revision, even if the Legislature reverted only one-half of the budgeted enrollment growth funding, current-year spending would be reduced by almost \$50 million. This recommendation would also generate General Fund savings for the current year, thus improving the state's carry-in balance for 2007-08. It would also reduce the Proposition 98 minimum guarantee for 2007-08 by roughly the same amount, thus facilitating further savings in the budget year.

2007-08 Enrollment Growth Funding

The Governor's budget proposes an augmentation of \$109 million to fund 2 percent enrollment growth at the California Community Colleges. This level of enrollment growth exceeds the statutory growth guideline of 1.65 percent. We recommend the Legislature fund 1.65 percent enrollment growth, for a savings of \$19 million. (Reduce Item 6870-101-0001 by \$19 Million.)

The budget proposal provides an increase of \$109 million for enrollment growth in 2007-08 to fund about 23,000 additional FTE students (a 2 percent increase). With this augmentation, the Governor's budget proposes funding a total of about 1.2 million FTE students in 2007-08.

Chapter 631, Statutes of 2006 (SB 361, Scott), requires CCC's annual budget request to include funding for enrollment growth at least as large as the average growth rate of two state population groups (19- to 24-year olds and 25- to 65-year olds), as determined by the Department of Finance (DOF). The DOF projects that these groups will increase by a combined average of 1.65 percent in 2007-08. This growth rate would translate into about 19,000 additional FTE students, at a cost of \$90 million.

We feel the growth rate derived from the new statutory guideline would easily allow CCC to accommodate all projected enrollment demand. This is because we project that demographically driven enrollment in the community colleges (which accounts for growth rates in the underlying population and assumes constant participation rates) will increase by about 1.1 percent in the budget year. It is not yet known the extent to which the fee reduction—which went into effect in January 2007—will affect participation rates among students. However, our recommendation would accommodate modest increases in participation rates.

Recommend 1.65 Percent Enrollment Growth Funding. For 2007-08, we recommend the Legislature provide funding for 1.65 percent enrollment growth. The Master Plan calls on CCC to be open to all adults who can benefit from instruction, and DOF estimates that this eligibility pool

will grow by 1.65 percent. We believe that this amount would easily fund all anticipated increased enrollment demand at the community colleges. If the amount of funding for growth were reduced to our recommended level of \$90 million, there would be \$19 million in Proposition 98 savings. Depending on the minimum spending requirement in 2007-08, these funds would be available either for General Fund savings or for redirection within Proposition 98 for other K-14 priorities.

PERFORMANCE MEASUREMENT AND ACCOUNTABILITY

The CCC system serves over one and one-half million students (fall headcount) enrolled at 109 campuses operated by 72 locally governed districts, and spends over \$8 billion in public funds annually. For such a large and decentralized system, oversight and accountability measures are critical for ensuring that public resources are being spent efficiently and effectively. The CCC's Board of Governors (BOG) and Chancellor's Office are generally charged with oversight responsibilities. In recent years, system accountability has come into question. Recent reports have highlighted concerns with CCC performance, such as low student completion rates. In response, the Legislature and Governor have sought more formalized oversight and accountability provisions in statute.

“Partnership for Excellence” Had Limited Success

In 1998, the Legislature and Governor established the Partnership for Excellence (PFE) program through Chapter 330, Statutes of 1998 (SB 1564, Schiff). In general, the PFE provided additional funding to community colleges in exchange for their commitment to improve performance in five specified areas, such as the percentage of students that complete courses. A key accountability provision of the PFE called for district- and system-level performance in these specified areas to be reported annually. This information was to inform state-level budgeting, and could be used (if the BOG so chose) to influence the allocation of funding among districts. The BOG chose not to pursue this linking of funding to performance. The system made some very modest gains in some of the specified areas, such as workforce development, although toward the end of the program, performance again declined and most of those gains were lost. The PFE was allowed to sunset in January 2005.

New Reporting System Developed

Anticipating the sunset of PFE, the Legislature and Governor enacted Chapter 581, Statutes of 2004 (AB 1417, Pacheco), which required BOG to develop “a workable structure for the annual evaluation of district-

level performance in meeting statewide educational outcome priorities,” including transfer, basic skills, and vocational education. Pursuant to statutory direction, the BOG consulted with our office, DOF, and various other higher education experts and interested parties as it developed its proposal. The final proposal was adopted as part of the 2005-06 budget package in Chapter 73, Statutes of 2005 (SB 63, Committee on Budget and Fiscal Review). Chapter 73 requires community college districts to report specified data to the CCC Chancellor’s Office, which in turn is to submit an annual report to the Legislature and Governor.

While Chapter 73 established several major types of outcomes to be measured (such as student transfers), it did not specify what specific data was to be used to measure outcomes. For example, transfer rates can be measured using various definitions of the pool of potential transfer students. To resolve these kinds of measurement questions, the Chancellor’s Office established a “Technical Advisory Workgroup.” In addition to staff from the Chancellor’s Office, the workgroup includes research and analysis experts from the community college districts and other agencies, including DOF and LAO. The workgroup developed the measures for the project, known as Accountability Reporting for the Community Colleges (ARCC).

Drafts of the first annual report were released in October 2006 and January 2007 for districts and colleges to review for accuracy. The final version will be released publicly in March 2007. (Please see nearby box for a summary of the ARCC accountability measures.)

Draft Report Points to Both Positive and Negative Trends. Although the final report will not be released until March 2007, the January 2007 draft report suggests a mixture of good and bad news about the community college system. For example, although the total number of student transfers from a community college to a four-year institution has generally increased in the past few years, the number of basic-skills students advancing in their coursework has declined. The data also reveal a wide performance disparity among colleges. For example, students’ basic skills course completion rates range from about 40 percent at some colleges to 80 percent at others.

Reports Should Help Legislature in a Number of Ways. The CCC’s accountability reports should be helpful for a number of different purposes. For example, they can assist the Legislature in its oversight function, depicting overall system performance and effectiveness in carrying out CCC’s educational missions. The reports may also inform budgeting and policy decisions by the Legislature and Governor, helping to identify results from budget investments and issues that require attention. In addition, the re-

Accountability Reporting for the Community Colleges

Using data provided primarily by the community colleges, the Chancellor's Office is to submit an annual report that provides an assessment of the community college system. Reports will include system- and college-level performance and demographic data over multiple years in several categories:

- Total degrees and certificates earned by community college students, and student transfers to four-year institutions.
- Completion and persistence rates for community college students.
- Income trends of students earning a vocational degree or certificate.
- Student progress and achievement in basic skills and English as a second language courses.
- Demographic makeup (such as age and ethnicity) of students at each college.
- A comparison of students' performance at each college with those of comparable "peer" colleges in the system.

The March 2007 report will evaluate the performance of students in credit courses only; reports in subsequent years will include an assessment of noncredit courses as well. In addition, each annual report will include a brief self-assessment of each college's performance, including mitigating factors that might account for certain outcomes.

ports should be useful to local residents in holding their local community college governing boards accountable for district performance.

CCC Funding Reforms Should Enhance Accountability

Equalization Achieved. For years the amount of general purpose or "apportionment" funding the state provided for each credit FTE student varied considerably by district. This was due to tax base differences that predate Proposition 13 in 1978, coupled with complex district allocation formulas. In 2003-04, for example, districts' funding per credit FTE student ranged from \$3,500 to \$8,200 (most districts, however, had levels within a few hundred dollars of the state median of about \$4,000). Beginning in 2004-05, the Legislature providing funding toward the goal of "equalizing" community college district funding within three years. The 2006-07

Budget Act included the final installment of monies to fully achieve the state's equalization goal, that at least 90 percent of statewide community college enrollment receive the same level of funding per credit FTE student. (Funding for *noncredit* students has not been an equalization issue because all districts have received the same amount for each noncredit FTE student.)

Elimination of Program-Based Funding. Along with providing funds to equalize districts, the Legislature recently enacted legislation that changes the method for allocating apportionment monies to districts. Chapter 631, Statutes of 2006 (SB 361, Scott), ensures that district funding remains equalized in subsequent years. Chapter 631 replaced the program-based funding system that had attempted to account for the different costs that different districts experience. Under program-based funding, districts did not receive equal funding rates on a per-FTE student basis. Instead, district allocations were influenced by headcount enrollment, total square footage of district facilities, and other factors. As such, program-based funding worked at cross purposes from the goal of funding statutory equalization targets, and would have eroded the state's equalization efforts over time. By contrast, Chapter 631 promotes and maintains equalization goals by providing virtually all CCC districts with apportionment funding at the same amount per credit FTE student (\$4,367 in 2007-08).

Equalization Funding and New Statute Should Enhance Accountability. The state's *Master Plan for Higher Education* and state law assign to community colleges a number of educational missions. The state also has called on the community colleges to improve in a number of areas, including preparing students to transfer to a four-year institution, awarding degrees and certificates, and improving course completion rates. Generally, it is more difficult to hold all districts accountable for their performance when the amount of funding provided per student varies significantly from district to district. With equalized funding, districts now have comparable levels of resources and the state is in a better position to evaluate performance outcomes across community college districts.

Recent Reports Focus on Accountability and Community College Performance

National Discussion on Outcome Measures and Accountability. The ARCC project and recent CCC funding reforms coincide with a new national focus on higher education accountability. For example, a recent study commissioned by the United States Department of Education suggests that institutions of higher education lack adequate accountability systems for measuring performance and recommended that the federal government provide incentives for states and institutions to implement

performance-based systems that track and report student outcomes (such as graduation rates). Similarly, a National Conference on State Legislatures commission has called on state legislators to exert stronger leadership in higher education public policy by defining clear goals and expectations for two- and four-year institutions, and holding them accountable for their performance.

Studies Find Low Student Success in CCC System. The spotlight on higher education accountability comes at a time in which several new reports have focused on the performance of California's community colleges. In particular, these reports have highlighted the relatively low persistence and completion rates of CCC students. According to the National Center for Public Policy and Higher Education, for example, while the college participation rate of working-age adults in California is among the highest in the country (due primarily to the state's large community college system), *persistence* rates are below the national average. In fact, researchers report that less than one-half of first-year, full-time CCC students return their second year, which is about 10 percent below the national average. Another study (by the National Center for Higher Education Management Systems) finds that the CCC system ranked 45th among states in the ratio of FTE students to the number of degrees awarded in 2004-05.

The California State University—Sacramento's Institute for Higher Education Leadership and Policy (IHELP) recently analyzed a cohort of CCC students who first enrolled in 1999-00. The study found that less than one-quarter of degree- or transfer-seeking CCC students actually earned an associate's degree or certificate and/or transferred to a four-year institution within six years of their initial enrollment. The completion rates were low for students in all racial/ethnic groups, but particularly for black and Latino students. A study released by the Public Policy Institute of California in fall 2006 found similarly low graduation and transfer rates among community college students it identified as degree- or transfer-seeking.

Various Policies Cited as Contributing to Low Completion Rates. The IHELP cites several policies that can contribute to the community college's low completion rates. For instance, the amount of funding a district receives from the state depends largely on the number of students enrolled at a point early in the semester. This funding policy creates incentives to get students "in the seats" early on, but provides no strong incentive to help students pass or even complete their courses.

Recommend State Focus on Improving Student Completions; Provide Locals Flexibility to Achieve Results

In general, we share the concern that current CCC funding mechanisms and related policies can unintentionally create incentives for com-

munity colleges and students to behave in ways that can inhibit student completions. In the following section, we illustrate a way the Legislature could move toward a system that fosters higher completion rates by giving local colleges more decision-making authority, rewarding improvements, and holding community colleges accountable for results. We propose to do this by redirecting funds from the basic skills overcap categorical to a block grant that targets a select group of community colleges.

MAKING BETTER USE OF BASIC SKILLS “OVERCAP” FUNDING

The Governor proposes to permanently redirect \$33.1 million in base funding for basic skills “overcap” enrollment to enhance counseling and other support services at the community colleges. While we find merit with the Governor’s plan to eliminate the basic skills overcap categorical program, we recommend the Legislature use the freed-up funding as needed to reduce Proposition 98 spending in the budget year. If the Legislature desires to retain the money in the California Community Colleges’ budget, however, we recommend it provide the funding as block grants to a targeted group of community colleges, with the funds used to improve student achievement and completion rates. (We also recommend the deletion of unused overcap funds in the current year.)

Current-Year Basic Skills Initiative

The budget for the community college system includes a specified amount of funding for enrollment growth. Growing districts use this funding to accommodate additional students (above their previous year’s level). Using an allocation formula, the Chancellor’s Office determines the amount of growth funding available to each district. This “growth cap” sets the ceiling for how many students the state will fund in the district in a given year. In recent years, districts that enrolled above this cap level risked not receiving funding for those students. An exception was created for districts with overcap growth in basic skills courses. (Basic skills courses include precollegiate classes such as elementary mathematics and English.) Districts meeting certain requirements qualify for basic skills overcap funding. This categorical program was created to fund additional basic skills students.

Reappropriated Overcap Funds Used in Current Year for “Basic Skills Initiative.” Given that no district enrollment is any longer above cap, no basic skills overcap funds have been “earned” since 2003-04. As a result, the Legislature has redirected this funding for other purposes.

Specifically, the 2006-07 *Budget Act* includes \$30.7 million in reappropriated overcap funds from 2005-06 for a basic skills initiative that augments the amount of spending on each basic skills student.

Under the basic skills initiative, funds are allocated to districts on a one-time basis in proportion to their share of statewide basic skills enrollment. Districts may use funds for activities and services such as curriculum development, additional counseling and tutoring, and the purchase of instructional equipment for basic skills classes. A portion of the funds (\$750,000) is for the Chancellor's Office to facilitate statewide research on improving basic skills education in the community colleges.

Low Success Rates for Basic Skills Students. According to the Chancellor's Office, about 75 percent of incoming community college students arrive unprepared for college-level English, and about 90 percent arrive unprepared for college-level math. Moreover, of those students that enroll in basic skills courses, only about 60 percent successfully complete (receive a grade of "C" or better) a basic skills English course, while just 50 percent of students successfully complete a basic skills math course. In addition, only a small percentage (under 15 percent) of community college students that begin at basic skills level English and math eventually advance to and successfully complete transfer (college) level English and math courses.

Program Double Funded in Current Year

In addition to the reappropriated basic skills funding from the prior year, the current-year budget also includes \$33.1 million in base funding for overcap basic skills enrollment. Provisional language redirects any funds not needed for overcap enrollment to basic skills enhancements—essentially the same purpose as the basic skills initiative. Given that no districts are expected to be over cap in the current year, these monies will essentially double the basic skills initiative funding. It is not clear that the Legislature expected to fund the basic skills initiative at this level.

Recommend Reducing CCC's Proposition 98 Appropriation. We recommend the Legislature reduce on a one-time basis CCC's current-year appropriation of Proposition 98 funding by \$33.1 million. This action would avoid double funding the basic skills initiative and would have no effect on the number of basic skills students served. In addition, it would provide General Fund relief. As we discuss earlier in this chapter (see "Proposition 98 Priorities for 2007-08"), our revenue forecast suggests that the state's current-year spending level for Proposition 98 is about \$600 million higher than the minimum guarantee. For this reason, a reduction in Proposition 98 spending would generate a like amount of General Fund savings. This would also reduce the 2006-07 Proposition 98 base, from

which the 2007-08 Proposition 98 guarantee is calculated, allowing additional savings in the budget year.

Governor Proposes to Redirect Budget-Year Overcap Funds for Matriculation

The Governor proposes to permanently redirect the basic skills overcap funds in 2007-08 for a new “student success initiative.” Specifically, the \$33.1 million in base funding previously set aside for basic skills overcap funds would be added to categorical funding for matriculation programs. Matriculation programs include orientation, skills assessment, counseling, tutoring, and related student support services. The majority of funding (\$19.1 million) would be provided to districts to provide tutoring and academic and career counseling to students identified by the community colleges as most in need of these services (particularly recent high school graduates). The remaining \$14 million would be made available to districts to provide additional matriculation services to the general student body.

Basic Skills Overcap Categorical Has Not Served Intended Purpose. We agree with the Governor’s proposal to abolish the basic skills overcap categorical. The intended purpose of the categorical was to reduce the risk of basic skills students being turned away if a district exceeded its growth cap and experienced unfunded FTE students. We believe that the categorical has been problematic for two reasons. First, the Chancellor’s Office does not have a way to determine if basic skills students are the ones that pushed a district “over cap.” Therefore, districts that go over cap become eligible for this categorical funding regardless of the whether they increased their enrollment in basic skills. Second, since there is no requirement for districts to spend these funds on basic skills education, funding from this categorical has not necessarily helped basic skills students.

Legislature Should Put Freed Up Funding to Best Use

Given the state’s General Fund situation, we recommend spending no more than the Proposition 98 minimum guarantee on K-14 programs in 2007-08. To the extent this requires additional reductions beyond what we have already identified, we would recommend the Legislature use the money freed up from the basic skills overcap categorical for General Fund savings. If, however, the Legislature chooses to keep this funding in CCC’s base, we recommend an alternative approach to the Governor’s proposed student success initiative.

Increase Local Flexibility, Emphasize Outcomes. We think that the Governor’s proposal has merit insofar as it focuses resources on improving student outcomes. It recognizes and seeks to address concerns with low

student achievement. However, California's 109 community colleges have different student populations, local resources, and job environments, and thus the causes of student performance issues can vary. For example, some community colleges may have a relatively high need for matriculation services, while others may have a greater need for funding to enhance the quality of instruction in the classroom. Certain colleges may recognize the need to improve their basic skills curriculum, while others may be more in need of additional programs in vocational education. By requiring districts to spend the funds for a specific purpose (matriculation), however, the proposal limits local flexibility to direct funding in ways that address student needs most effectively.

In our view, a more effective approach would be to allow local officials to decide how these funds are spent. Community colleges would then be able to develop their own creative and targeted responses to local educational needs. In addition, we believe that a reduced emphasis on *inputs* (what kind of activities locals fund) should be accompanied with a renewed emphasis on *outcomes* (how students perform). By increasing local autonomy over the use of funds and instead focusing on results, the state—as well as students—will benefit.

Target Community Colleges Serving the Least Prepared Students. With these principles in mind, we recommend that the Legislature redirect base funding for basic skills overcap enrollment to block grants to districts to increase student achievement and completion rates. We recommend the Legislature target this funding to a small number of community colleges that have the least prepared incoming students. Recipients could be identified by, for example, the Academic Performance Index of the community colleges' feeder high schools. These colleges would be permitted to use the grants to address local needs and priorities with enhanced educational services of their choosing. While colleges could employ different strategies, they would share the goal of increasing student performance.

In order to allow CCC time to implement a plan and measure results, we recommend providing this additional funding for a two- to three-year period. Continued funding in subsequent years would be contingent on demonstrated improvements in student outcomes. Colleges' progress could be tracked using CCC's forthcoming accountability reporting system (discussed earlier in this chapter), which includes multiple measures of achievement and completion for all campuses.

Consider Temporarily Waiving Certain Restrictive Policies. As we discuss earlier in our write-up on accountability, there are several laws and regulations in place that limit how community colleges can allocate resources. For example, current policies require a certain ratio of full-time faculty to part-time faculty employed by a district and limit the number

of terms temporary faculty can teach within a three-year period. In past *Analyses* (see, for example, “Part-time Faculty Issues: Changing the Focus to Education Outputs,” *2001-02 Analysis of the Budget Bill* [pages E-210 to E-216]), we found no evidence that these policies improve student outcomes. Indeed, recent studies suggest that policies such as these can impede the ability of community colleges to improve student performance. To further enhance local flexibility and accountability, we recommend the Legislature adopt budget bill language to exempt spending of student-success block grants from these restrictions. This could also provide an opportunity for the Legislature to reevaluate the usefulness of these policies more broadly.

NEWLY IDENTIFIED MANDATE REVIEW

Chapter 1124, Statutes of 2002 (AB 3000, Budget Committee), requires the LAO to review each mandate included in the Commission on State Mandates’ (CSM) annual report of newly identified mandates. In compliance with this requirement, this analysis reviews the mandate entitled “Integrated Waste Management.”

Integrated Waste Management Mandate

Chapter 764, Statutes of 1999 (AB 75, Strom-Martin), requires state agencies (defined to include locally governed CCC districts) to divert from landfills at least 25 percent of generated solid waste by January 2002, and at least 50 percent by January 2004 through reduction, recycling, and composting activities. State agencies must develop an integrated waste management plan and report annually to the California Integrated Waste Management Board (CIWMB) on their ability to meet solid waste-diversion goals.

In March 2004, CSM determined that these activities constitute a state-reimbursable mandate for community college districts. In March 2005, CSM adopted “parameters and guidelines,” which determine the methodology for reimbursing the mandate. Based on the determinations in the parameters and guidelines, CSM estimated in October 2006 the statewide cost of this mandate to be \$10.8 million (for total costs incurred by 27 community college districts from 1999-00 through 2007-08). The estimate is based primarily on the salary and benefit costs of the employees performing activities on behalf of the waste-reduction program, as well as other costs such as developing and maintaining an accounting system to track reduction, recycling, and composting activities. Since only about one-third of districts submitted a claim for this mandate, the long-term cost could be considerably higher. The Governor’s budget does not propose any funding to pay for this mandate.

Savings and Revenues Cannot Be Considered Offsets to Program Costs

While waste-diversion programs can entail costs (such as training staff on recycling requirements and tracking performance), they can also result in increased savings and revenues. For example, savings can be realized to the extent that recycling activities reduce solid-waste disposal costs. In addition, revenues can be generated from the sale of recyclable materials such as glass bottles and aluminum cans.

In reviewing the integrated waste management mandate, however, CSM found that savings and revenues generated by community college districts could not be used to offset districts' cost claims. This is due to CSM's interpretation of a provision in Chapter 764 which states that:

Any cost savings realized as a result of the state agency integrated waste management plan shall, to the extent feasible, be redirected to the agency's integrated waste management plan to fund plan implementation and administration costs, in accordance with Sections 12167 and 12167.1 of the Public Contract Code.

The CSM found that the term "cost savings" did not refer to savings from such activities as avoiding disposal fees. This is because the codes cited in the statute (Public Contract Code sections 12167 and 12167.1) refer only to *revenues* from the sale of recyclable materials. As a result, disposal-related cost reductions are not considered offsetting savings.

The CSM also found that revenues from the sale of recyclable materials are generally not considered offsets to waste diversion-related program costs. This is for two reasons. First, the commission determined Chapter 764's phrase "to the extent feasible" to mean that the Legislature did not intend revenues to be a *mandatory* offset. Instead, CSM interpreted it to mean that districts had discretion to redirect these revenues for other purposes should they decide that using them to offset recycling program costs is not "feasible." Second, Public Contract Code 12167.1, which is referenced in the statute, states that revenues that do not exceed \$2,000 annually are continuously appropriated for expenditure by state agencies (interpreted by CSM to include community college districts) to offset recycling program costs. Revenues above \$2,000, however, are available to districts as offsets only when appropriated by the Legislature. Since appropriations are discretionary acts of the Legislature, CSM found that only the revenue up to \$2,000 can be considered as offset, and then only "to the extent feasible" for districts.

Options to Reduce Program Costs

The Legislature has several options to reduce or eliminate the state cost of this mandate. We recommend, at a minimum, that the Legislature amend statute to ensure that community college districts take into account offsetting savings and revenues in calculating net program costs.

The Legislature has several options to reduce or eliminate the costs from this mandate:

- One option would be to treat community college districts similarly to other local governments, which are authorized to charge fees to cover program costs. This would eliminate future mandate claims.
- Second, the Legislature could treat community colleges the same as K-12 school districts, which are encouraged—but not required—to comply with diversion goals. This would also eliminate future mandate claims.
- Finally, if the Legislature chooses to continue requiring community college districts to achieve statutory diversion rates, and does not want to authorize fees, we recommend it amend statute to require community college districts to apply savings and revenues to offset diversion-program costs. This could be achieved through simple changes to current law. While this option would not eliminate the state mandate, it would eliminate (or greatly reduce) future state reimbursements. This is because the community colleges experience significant offsetting savings and revenues. For instance, CIWMB estimates that the total value of collected recyclables by community college districts from 2001 to 2005 was approximately \$23 million. In addition, CIWMB estimates that districts saved roughly \$20 million between 2001 and 2005 in disposal costs. If the Legislature chooses this option, we further recommend the Legislature direct CSM to amend the “parameters and guidelines” to reflect this change in law.

CCC CAPITAL OUTLAY

The budget proposes to spend \$546.6 million in bond funds on 67 CCC capital projects in the budget year. (Most of this amount—\$479.4 million—would be from Proposition 1D, the bond approved by voters in November 2006.) The proposed funding would support new phases of 32 projects previously funded by the state and 35 new projects.

Proposition 1D allocated \$1.5 billion in funds to CCC. After accounting for the costs to complete all projects proposed by the budget, there would be just over \$100 million in 2006 bond funds remaining to support additional projects in the future.

New Projects. The new proposals cover a wide variety of projects—new classroom, laboratory, and library space; renovations and replacement; campus infrastructure; and seismic-related improvements. While we do not raise questions with specific proposals in this year’s budget, we do have a concern about how the segment calculates districts’ needs for new space, which we discuss below.

Chancellor’s Office Should Recalculate Capacity Factors

We recommend that the Chancellor’s Office, in calculating future district requests for new instructional space, take into account the capacity available with year-round operation.

While community college districts are responsible for building and maintaining their capital facilities, the state has historically played an important role in the funding of those facilities. (State funds have typically been provided through voter approval of general obligation bonds.) Districts submit capital outlay proposals to the Chancellor’s Office, which must then decide how to allocate available funding among the districts. In performing this allocation, the office has developed a comprehensive project rating system to help it assess the relative priorities among the proposals. For example, it gives a higher ranking to a project that addresses a fire and life deficiency or a seismic problem. It also gives more points to a project based on the level of local funding contribution.

While we think the office’s system is a reasonable way to balance the varied demands of the districts, it has one significant weakness. In assessing districts’ requests for new instructional space, the office uses what it calls “capacity load factors.” Simply put, these factors ensure that the state does not fund new space until the district is using its existing space to its full capacity. (This is done through the application of long-established space and utilization standards.) The problem is that the office assumes that the district’s space is available for use only nine months of the year.

For many years, our office has advocated more intensive, year-round use of the state’s higher education facilities. In so doing, the state would not only avoid major costs in building new facilities, but also provide important benefits to students and faculty. The Legislature has taken several actions in recent years—both funding and policy decisions—to increase year-round use. Despite these actions, the California State University (CSU) is using

about 10 percent of its summer capacity, the University of California (UC) is using about 20 percent, and CCC is using about 30 percent.

Year-round operation is particularly important for the community colleges. Whereas UC and CSU—as statewide and regional systems—can accommodate the relatively moderate enrollment growth projected over the next decade without adding much new instructional space, the community colleges will have many districts in growing areas of California experiencing increased enrollments that will have to be addressed. If these districts are assumed to operate on a year-round basis, their instructional space requests will be considerably smaller than would otherwise be the case.

Consequently, we recommend the Chancellor’s Office, in calculating future district requests for new instructional space, take into account the capacity available for year-round operation. This would require adjustments to their capacity load factors to account for facility utilization throughout the 12-month year. (It is important to note that such a change would not *require* any district to change the way it operated in the summer. It would simply ensure that the state did not provide funding for increased instructional space until the district’s enrollment exceeded its year-round capacity.)

STUDENT AID COMMISSION (7980)

The California Student Aid Commission (CSAC) provides financial aid to students through a variety of grant and loan programs. The proposed 2007-08 budget for the commission includes state and federal funds totaling \$1.7 billion. Of this amount, \$892 million is General Fund support—all of which is used for direct student aid for higher education. A special fund covers the commission's operating costs.

Below we summarize the Governor's major budget proposals. We then discuss the Assumption Program of Loans for Education (APLE), including the Governor's proposal to set aside 600 APLE awards for certain University of California (UC) and California State University (CSU) students, as well as several other proposals. We then discuss the Cal Grant programs, including recent legislative efforts, and recommend a funding reduction that corresponds to our recommendation for lower UC and CSU fee increases discussed elsewhere. Finally, we review CSAC's efforts to address operational issues with regard to its auxiliary, EdFund.

Major Budget Proposals

Figure 1 compares the commission's revised 2006-07 budget with the proposal for 2007-08. As the figure shows, funding for state financial aid programs would increase by \$64 million, or 7.7 percent, from the current year. This increase is primarily due to additional costs associated with the Cal Grant programs (\$61 million) and APLE program (\$2.9 million). In contrast to some past years, no funding from the Student Loan Operating Fund would be redirected to support Cal Grant costs.

Cal Grant Programs. As Figure 1 shows, the Governor's budget would increase funding for the Cal Grant Entitlement programs by \$59 million, or 8.9 percent, and Cal Grant competitive programs by \$3.1 million, or 2.7 percent.

Figure 1**Student Aid Commission Budget Summary^a***(Dollars in Millions)*

	2006-07 Revised	2007-08 Proposed	Change	
			Amount	Percent
Expenditures				
Cal Grant Programs				
Entitlement	\$666.5	\$725.6	\$59.1	8.9%
Competitive	114.2	117.3	3.1	2.7
Pre-Chapter 403/00 ^b	1.4	0.2	-1.2	-86.6
Cal Grant C	8.9	9.2	0.3	3.2
Subtotals—Cal Grant	(\$790.9)	(\$852.2)	(\$61.3)	(7.8%)
APLE ^c	\$46.3	\$49.3	\$2.9	6.3%
Graduate APLE	0.4	0.4	—	—
National Guard APLE	—	0.2	0.2	N/A
Law enforcement scholarships	0.1	0.1	—	—
Totals	\$837.8	\$902.2	\$64.4	7.7%
Funding Sources				
General Fund	\$827.2	\$891.6	\$64.4	7.8%
Federal Trust Fund ^d	10.7	10.7	—	—
<p>^a In addition to the programs listed, the commission administers the Byrd Scholarship, Child Development Teacher and Supervisor Grant, and California Chafee programs—all of which are supported entirely with federal funds. It also administers the Student Opportunity and Access program, a state outreach program supported entirely with Student Loan Operating Fund monies.</p> <p>^b These programs predate the Cal Grant Entitlement programs and are being phased out.</p> <p>^c Assumption Program of Loans for Education.</p> <p>^d These monies pay for Cal Grant costs.</p>				

The Governor's budget funds approximately 900 new High School Entitlement awards. This reflects growth of 2 percent, consistent with the projected growth in high school graduates for 2006-07. It also funds 880 new Transfer Entitlement awards, which reflects a 15 percent increase over the current year. (In part, the increase in entitlement awards is due to recent legislation that expands eligibility. We discuss this later in this write-up.) The Governor's budget includes no funding to increase the number of new Competitive awards because the commission already issues the maximum number allowable under statute (22,500).

The budget proposal includes augmentations to increase the fee coverage portion of Cal Grant awards for UC and CSU students to match

proposed fee increases at those segments. The maximum Cal Grant award for needy students at private institutions would remain unchanged from the current-year level of \$9,708.

ASSUMPTION PROGRAM OF LOANS FOR EDUCATION

The APLE is designed to increase the number of qualified teachers in disadvantaged schools and in high-priority subject areas. Toward that goal, the program pays off (“forgives”) student loans, up to specified amounts, for individuals who teach in either:

- A school that has a high proportion of low-income students, low-performing students, or uncredentialed teachers; or
- A subject area which the California Department of Education has determined to have a critical shortage of teachers.

The program forgives up to \$11,000 of college loan debt for a person who teaches for four consecutive years in a qualifying school or subject area. Additional loan forgiveness is provided for those who teach in the lowest-performing schools (in the first two deciles as measured by the Academic Performance Index) and for those who teach mathematics, science, or special education.

Not All Authorized Awards Being Used

Each year CSAC allocates all authorized APLE slots among qualified teacher education institutions in proportion to their production of teachers. If an institution is not able to use all the APLE awards allocated to it, CSAC redirects the unused awards to other institutions that can use them. Even with this redirection, however, a portion of the APLE awards authorized in the annual budget act has gone unclaimed in each of the past several years. As Figure 2 shows, 708 APLE awards were not used in 2004-05, and 861 were not used in 2005-06. As of January 2007, about 6,175 awards remained unissued for 2006-07, but typically many applications for these awards are received in March and April.

Legislature Rejected Earlier Proposals to Restrict Some Warrants. Despite the state’s historic inability to grant all authorized awards, in 2005-06 and 2006-07 the Governor proposed to *restrict* 600 of the total number of authorized APLE warrants for exclusive use by UC and CSU students that are participating in the Governor’s Math and Science Initiative. Seeing no point in further restricting a program that already had more slots than participants, the Legislature rejected the Governor’s proposal both times. In the current year, the Governor responded by vetoing 600 of the 8,000 APLE awards the Legislature authorized in the budget bill.

Figure 2**Hundreds of APLE^a Awards Unclaimed Each Year***Number of APLE Warrants*

	2004-05	2005-06	2006-07 ^b
Authorized	7,700	8,000	7,400
Used	6,992	7,139	1,225
Unused	708 (9.2%)	861 (10.8%)	6,175 (83.4%)

^a Assumption Program of Loans for Education.

^b As of January 2007. According to the California Student Aid Commission, the majority of applications for these awards are received in March and April.

Governor Again Seeks to Restrict Program. For 2007-08, the Governor proposes to authorize a total of 8,000 new APLE awards, but again seeks to restrict 600 of them to UC and CSU students participating in the Governor's Math and Science Initiative. The language would also require CSAC to "consult" with UC and CSU in setting criteria for the 600 awards. (These new awards would not create General Fund costs until future years, after the recipients completed their credential programs and their student loans became due. There is, therefore, no funding proposed for these awards, although the budget does include funding to cover loan forgiveness from previously issued awards that will require payment in 2007-08.)

Legislature Should Again Reject Governor's Proposal

We recommend the Legislature once again reject the Governor's proposal to restrict 600 Assumption Program of Loans for Education (APLE) awards to the University of California and the California State University students participating in his Math and Science Initiative. (Amend Item 7980-101-0001, Provision 1[d].) We also recommend that the Legislature not approve a proposed staffing augmentation until the commission provides long overdue performance information on APLE.

Because authorized awards have gone unclaimed in recent years, we see no reason to further restrict this program. This is particularly the case given that the Governor proposes to authorize 600 more awards than were authorized in the current year. The administration has provided no evidence that students in the Governor's Math and Science Initiative experience any difficulty in receiving an APLE warrant. Further, even if the number of students seeking APLE warrants began to exceed the number

of authorized awards, statute already directs CSAC to give priority to students seeking mathematics or science credentials.

For these reasons, we recommend that the Legislature reject the Governor's proposal to restrict 600 APLE awards to UC and CSU Math and Science program participants. Specifically, we recommend that Item 7980-101-0001, Provision 1 (d) be amended as follows:

(d) The purchase of loan assumption warrants under Article 5 (commencing with Section 69612) of Chapter 2 of Part 42 of the Education Code. The Student Aid Commission shall issue 8,000 new warrants. ~~Of this amount, and notwithstanding any other provision of law, the commission shall allocate a total of 600 new warrants to the University of California and the California State University as determined in consultation with those segments, to be awarded to participants in the Science and Math Teacher Initiative. Expenditures associated with these warrants shall not count towards the maximum expenditures specified in Education Code Section 69613.8(c).~~

Greater Oversight Needed. The underutilization of APLE awards raises questions about how awards are allocated among institutions, about the appropriate number of awards that should be authorized annually, about how the program is promoted, and other concerns. For example, given that APLE participation already is lower than envisioned in recent budget acts, the Legislature might wish to consider ways to increase participation to the levels it envisioned when enacting the budget.

State law requires the commission to annually provide a report on various aspects of APLE that could help the Legislature consider these and other related questions. For example, the commission is required to report annually on the age, sex, and ethnicity of program participants in various categories, such as those who teach in schools serving rural areas and those from out of state. The last such report provided by the commission was for the 2002-03 fiscal year. The CSAC informs us it is currently working to provide an updated report.

Staffing Augmentations Should Depend on Responsiveness of Agency. The CSAC's budget request includes \$175,000 for two new positions to perform institutional audits. While we do not take issue with the proposed positions themselves, we do not believe the Legislature should act on the proposed augmentation until CSAC fulfills its statutory reporting responsibilities. Information on the performance of programs such as APLE is critical to legislative oversight and is necessary for considering proposals such as the Governor's request to restrict some APLE warrants. For these reasons, we recommend that the Legislature not approve the two proposed new positions until the agency provides the APLE report called for in statute.

National Guard APLE (NG-APLE)

As established in 2003 and amended in 2004, NG-APLE offers loan forgiveness as an incentive for more individuals to enlist or re-enlist in the National Guard, State Military Reserve, and Naval Militia. Specifically, qualifying members have a portion of their education loans forgiven after each year of military service up to four years, for a maximum of \$11,000. The *2006-07 Budget Act* authorizes the commission to issue up to 100 National Guard warrants. The CSAC still has not adopted regulations for this program, though CSAC staff informs us they still expect to adopt regulations and issue the 100 warrants authorized in 2006-07. The Governor's 2007-08 budget proposal includes \$200,000 to pay costs associated with those warrants.

Extension of Sunset, but No New Warrants Proposed. Statutory authorization for the program will sunset on July 1, 2007. The Governor is proposing to extend the sunset date to 2012, but does not include authorization for any additional NG-APLE warrants (beyond the 100 authorized for the current year).

Similar New Program Proposed Under Military Department. As we describe in the "General Government" chapter of this *Analysis*, the Governor proposes that a new Tuition Assistance Program (TAP) be established in the Military Department. The TAP is aimed at prospective and current National Guard members as an incentive to join or reenlist. The annual cost of the program would be \$3.3 million.

No Need to Establish New Program. In our analysis of TAP, we recommend the Legislature reject the proposal. If the Legislature wishes to continue to provide student financial aid as a way to help recruit National Guard members, we would advise renewing NG-APLE and authorizing additional awards. This program is superior to TAP in at least three ways. First, NG-APLE is easier to administer. As a loan forgiveness program, it only pays benefits once the student has completed his or her military commitment. In contrast, TAP would provide payment up front, and thus it would be necessary for the state to try to collect those funds from the student if he or she fails to complete the military commitment. Second, NG-APLE is structured similar to other programs already administered by CSAC. The TAP would create a new program to be administered by the Military Department, which has less experience in administering student financial aid programs. And third, NG-APLE is established in statute, while the Governor's proposal for TAP would give full discretion to the Military Department regarding the allocation of awards. For these reasons, we believe the TAP proposal would be difficult to administer, inefficient, and lacking in accountability.

State Nursing APLE and State Facilities Nursing APLE

The CSAC is authorized to issue awards for two additional APLE programs. The State Nursing APLE forgives up to \$25,000 in student loans for nursing program graduates who teach for three years in a California college or university. The current-year budget authorizes the commission to issue 100 new warrants for this program.

The State Facilities Nursing APLE was created last year by Chapter 837, Statutes of 2006 (SB 1309, Scott). It provides up to \$20,000 in loan forgiveness to nursing program graduates who work for four years in a state nursing facility with a vacancy rate that exceeds 10 percent. The current-year budget includes \$30,000 in base funding for the commission to implement the program, and authorizes the commission to issue up to 40 awards.

At the time this analysis was prepared, the commission had issued no awards for either of these programs. The Governor's 2007-08 budget proposal does not authorize the commission to issue any additional awards under these programs.

CAL GRANT PROGRAMS

The Governor proposes augmentations in the Cal Grant programs to cover higher costs due to increased participation and increased fees at the University of California and the California State University. In this section, we discuss two recent statutory changes to the Cal Grant programs, and recommend an adjustment that corresponds with our recommendation for smaller fee increases.

Recent Statutory Changes

The state's Cal Grant programs generally cover fees, tuition, and some living expenses. After the enactment of Chapter 403, Statutes of 2000 (SB 1644, Ortiz), all needy students are entitled to receive a Cal Grant so long as they meet certain age, income, and other criteria.

Cal Grant Entitlement Expanded. Chapter 822, Statutes of 2006 (AB 2813, De La Torre), expanded eligibility for the Transfer Cal Grant Entitlement. Prior to enactment of this bill, qualified students who were transferring from a community college to a four-year university were entitled to a Cal Grant if (among other requirements) they had not yet reached 24 years of age. Chapter 822 raised the age threshold to 28 years of age. This change is estimated to result in several hundred additional students receiving the entitlement each year, with a fiscal impact of about \$2 million in the budget year.

Private Cal Grant Funding Restored, but Still No Policy. As called for in state law, students attending a public university segment have the cost of their fees covered through Cal Grants. Because of the wide variation in tuition charges among the many private and independent colleges in the state, the value of the Cal Grant for students attending such institutions varies, though a maximum amount is established by the annual budget act. As shown in Figure 3, this maximum amount was *reduced* in 2004-05 in order to relieve pressure on the General Fund. That reduction was restored in the current year.

Figure 3	
Private and Independent College Cal Grant	
<i>Maximum Award Amount</i>	
2001-02	\$9,708
2002-03	9,708
2003-04	9,708
2004-05	8,322
2005-06	8,322
2006-07	9,708
2007-08	9,708

In recent years, we have recommended the Legislature establish in statute a policy that would link the value of the Cal Grant for needy students at *nonpublic* institutions to the General Fund subsidy the state provides for needy students at *public* institutions. (See, for example, our *Analysis of the 2006-07 Budget Bill*, page E-268.) We believe that, without a specific policy, Cal Grant decisions can appear arbitrary, unpredictable, and inconsistent.

Last year the Legislature passed legislation (AB 358, Liu) that would have set the private Cal Grant at 90 percent of the average General Fund subsidy provided to needy UC and CSU students. This bill was vetoed by the Governor. For 2007-08, the Governor proposes to leave the maximum private Cal Grant award unchanged at \$9,708, which we estimate to be about \$1,300 lower than the parity target sought by AB 358.

Cal Grant Funding for 2007-08

The Governor's budget proposes an augmentation of \$61.3 million to accommodate growth in Cal Grant participation and to cover the fee increases he proposes for the University of California and the California State University. We recommend an adjustment that corresponds with our recommended lower fee level. (Reduce Item 7980-101-0001 by \$20 million.)

The Governor proposes an augmentation of \$61.3 million to cover increased costs of the Cal Grant program, including a 1.6 percent increase in student participation and an 8 percent increase in the value of the average award. About \$28.7 million of the proposed increase in the average Cal Grant award is due to the cost of covering UC and CSU student fees, which the Governor has proposed to increase by 7 percent and 10 percent, respectively.

In the "Student Fees" Intersegmental write-up in this chapter, we note that the state currently has no explicit fee policy to guide annual changes to fee levels. We recommend that, absent a fee policy, the Legislature simply maintain the share of education cost that fees currently represent. Under our recommended UC and CSU budgets, this would require fee increases of about 2.4 percent at UC and CSU. Covering these fee increases with Cal Grants would require about \$8.6 million, or about \$20 million less than proposed by the Governor. Accordingly, we recommend Item 7980-101-0001 be reduced by this amount.

RESTRUCTURE STATE ADMINISTRATION OF GRANT AND LOAN PROGRAMS

For the past couple of years, the California Student Aid Commission (CSAC) and its auxiliary organization, EdFund, have been the focus of attention concerning issues of inadequate oversight and interagency tension. Given the apparent inability of CSAC to resolve these issues through a revised operating agreement, we continue to recommend that the Legislature replace the current two-agency structure for administering higher education grant and loan programs with a single-agency structure.

Background

In 2005-06, members of the education and budget committees expressed concern with the organizational relationship between CSAC and EdFund. Responding to a legislative directive, our office issued a report in January 2006 that examined this relationship and identified options for restructuring it (*California's Options for Administering the Federal Family*

Education Loan Program). Since that time, the California State Auditor has also released a report that identified tensions between CSAC and EdFund, and documented inadequate oversight that may have hampered monetary collections and programmatic expansion. The auditor made a number of recommendations, generally calling for CSAC to better monitor EdFund operations and consider certain changes to how various roles and responsibilities are divided between CSAC and EdFund.

CSAC Has Not Been Able to Revise Operating Agreement

State law requires that the operations of EdFund (including its roles and responsibilities) be specified in an “operating agreement” that is approved by CSAC and periodically updated. The last substantive update of the agreement was in 2002-03. Any meaningful attempt to address the operational issues raised by the Legislature, our office, and the State Auditor would likely require a substantial revision to the operating agreement, if not more fundamental changes.

Earlier Extension of Operating Agreement Did Not Achieve Promised Results. The CSAC committed to the Auditor and the Legislature that it would modify its operating agreement with EdFund in response to expressed concerns. When it became clear that CSAC would not be able to approve a new operating agreement before the existing agreement was set to expire on September 30, 2006, CSAC sought an extension until January 31, 2007. In notifying the Legislature of this extension, CSAC and EdFund assured the Legislature that the extension would allow sufficient time to develop a new agreement with appropriate revisions. In late 2006, however, CSAC once again informed the Legislature that it could not meet the sunset deadline, and sought another extension until June 30, 2007—again assuring the Legislature that it will have a new agreement in place before the extension expires. The Joint Legislative Budget Committee agreed to the extension, but emphasized that the Legislature may need to take measures to resolve the underlying issues of the CSAC-EdFund relationship itself if CSAC were unable to resolve them through the operating agreement by June 30, 2007.

Structural Reform Needed

We recommend the Legislature enact legislation that would restructure how the state administers grant and loan programs. Specifically, we recommend the Legislature authorize a single agency, with a single board and Executive Director, to administer both state grant and federal loan programs.

As we described in our January 2006 report, we believe the existing organizational arrangement between CSAC and EdFund suffers from three

main shortcomings: (1) the existence of two separate governing bodies (the CSAC commission and the EdFund board) creates tension among the leadership; (2) state law does not adequately delineate which agency is responsible for which operational functions; and (3) CSAC and EdFund have conflicting incentive structures. While some of these shortcomings could be ameliorated through revisions to the CSAC-EdFund operating agreement, the continuing inability of CSAC to identify and approve such revisions suggests that underlying statutory and structural factors need to be addressed by the Legislature.

Accordingly, we continue to recommend the Legislature replace the current two-agency structure for administering grant and loan programs with a single agency that has a unified leadership. The single agency could be a state agency or a nonprofit agency. While both models have been used successfully in other states, we think a nonprofit public benefit corporation would have greater flexibility to adapt to changes in loan programs and loan competitors. At the same time, a nonprofit organization would need to be subject to adequate accountability requirements to ensure that it is meeting legislative intent and providing students with excellent service.

Single-Agency Structure Most Likely to Overcome Existing Problems. Compared to a two-agency, shared-control structure, a single-agency structure has certain inherent advantages. Tension is less likely to develop among organizational leadership in a single agency with a single board and executive director, and confusion about roles and responsibilities is likely to be more easily and quickly resolved.

Greater Autonomy Should Be Coupled With Greater Accountability. Increasing the agency's autonomy over its daily administrative activities should be coupled with increased attention to accountability. Toward this end, the Legislature could establish accountability requirements such as annual audits and outcomes reporting to ensure the agency is meeting legislative intent.

New Structure Could Accommodate Broader Reform. We think another distinct advantage of our recommendation is that it creates a structure within which other reforms could easily be accommodated. As a single agency, it would be better situated to integrate grant and loan information and services. As such, the Legislature could consider a variety of other reforms related to financial aid administration. For example, the new agency could assume responsibility for the state's savings and scholarship programs (currently administered by the Scholarshare Investment Board). This would unify all state-level financial aid administration in one umbrella agency and create a single point for state-level financial aid information.

FINDINGS AND RECOMMENDATIONS

Education

Analysis

Page

Proposition 98 Update

- E-16 ■ **Updated Revenue Forecast Leads to Different Estimates for Proposition 98 Minimum Guarantee in Both the Current and Budget Years.** Because of lower estimates for General Fund revenues, our forecast suggests the minimum guarantee is \$609 million lower in 2006-07 and \$261 million higher in 2007-08, as compared to the administration's estimates.
- E-19 ■ **For the First Time, Proposition 98 Funding Level Will Be Adjusted Downward to Reflect Declining Attendance.** After two years of being held harmless for statewide declines in student population, in 2007-08 the Proposition 98 minimum guarantee will be calculated using the actual change in K-12 average daily attendance (-0.4 percent). Overall Proposition 98 funding still increases compared to the current year.
- E-22 ■ **Forecast Suggests Test 1 Factor Could Become Operative in Near Future.** Healthy growth in General Fund and local property tax revenues coupled with declining K-12 attendance result in a shrinking share of the General Fund going to Proposition 98. Our forecast suggests the Test 1 requirement—roughly 40 percent of all General Fund spending—could become operative as early as 2009-10.

Analysis**Page****Proposition 98 Priorities**

- E-25 ■ **Proposition 98 Priorities.** Recommend Legislature reduce current-year Proposition 98 spending by \$609 million, which would reduce the 2007-08 minimum guarantee by \$634 million. These actions would help the state address its General Fund budgetary problem.
- E-31 ■ **Maintain Priority on Reducing Debt.** Recommend Legislature use any additional Proposition 98 funds that materialize this year to pay for the ongoing cost of state-mandated local programs and reduce the states “credit card” debt.

A Proposition 98 Roadmap

- E-33 ■ **A Proposition 98 Roadmap.** A long-term roadmap could strengthen the Legislature’s role in the annual budget process, increase its ability to pay for its high-priority policy initiatives, and help school and community college districts implement state initiatives more effectively.
- E-39 ■ **Major Components of a K-12 Spending Roadmap.** Our roadmap includes two priorities goals: (1) investing in child development programs and supplemental funding programs for the major subgroups of K-12 students who perform well below state standards, and (2) helping districts address the long-term financial threat posed by retiree health insurance costs.
- E-43 ■ **Implementing the Roadmap’s K-12 Priorities.** Invest new discretionary Proposition 98 funds in three program areas: (1) child development programs, (2) existing programs that support supplementary services to low-performing and at-risk students, and (3) “fiscal solvency” block grants that would assist districts to pay for retiree health benefits.

Analysis**Page**

- E-48 ■ **Major Components of a California Community Roadmap.** Recommend using new discretionary Proposition 98 funds to (1) pay off districts' outstanding liabilities through fiscal solvency block grants, and (2) improve completion rates through student success block grants.

Career Technical Education (CTE)

- E-53 ■ **Governor's Proposal.** Proposes \$52 million in grants to strengthen secondary and post-secondary vocational education programs.
- E-56 ■ **Program Needs a Long-Term Foundation.** Lack of a long-term goals of the program and a reliance competitive grants raise significant questions about the state's approach to implementing SB 70 and the budget-year plan.
- E-61 ■ **\$400 Million Is Enough to Improve CTE Statewide.** Recommend legislation that directs most of the \$52 million proposed for SB 70 to pay for the first year of a seven-year grant program that would support a comprehensive program of improvement at the county or regional level.

California Education Network

- E-67 ■ **Provide \$12.6 Million for the High Speed Network (HSN).** Recommend Legislature provide \$12.6 million Proposition 98 for the HSN project. This would fund a baseline budget as well as implementation of the first phase of a technology refresh plan.
- E-72 ■ **Enact Legislation to Further Protect State Interests.** Recommend Legislature enact legislation requiring contracts between higher education and the Corporation for Education Network Initiatives in California (CENIC) include the contractual provisions required in Chapter 552 for the K-12 system.

Analysis**Page**

- E-72 ■ **Request CENIC Provide Asset and Fee Information As Required in the 2006-07 Budget Act.** Recommend Legislature require CENIC to provide previously requested information, by April 1, 2007, on its assets and fee structure.

Home-to-School Transportation

- E-87 ■ **Reject Governor's School Transportation Proposals.** Recommend Legislature reject the Governor's proposals to fund the Home-to-School Transportation program from the Public Transportation Account (PTA) and rebench the Proposition 98 guarantee by a like amount.
- E-89 ■ **Use PTA to Generate Savings Without the Risk.** Recommend Legislature use roughly \$300 million in PTA monies on a one-time basis in the current year to support the Home-to-School Transportation program. Using PTA monies in such a way could produce substantial savings in both the current and budget years.

Child Care and Development

- E-95 ■ **Governor's Proposal to Increase State Share of Stage 2 Child Care.** Assuming the Governor's fiscal outlook, recommend Legislature adopt the Governor's proposed change to the federal and state shares of Stage 2 child care funding. In contrast, if the situation worsens, recommend Legislature take a series of other actions, including not doing Stage 2 shift in 2007-08.
- E-99 ■ **Accept Governor's Proposal to Add \$5 Million to the Base for Wrap Around Child Care but Remove Restrictions.** Recommend Legislature approve \$5 million in new ongoing monies but designate the funding for the standard wrap around child care program.

Analysis**Page**

- E-103 ■ **Require the California Department of Education (CDE) to Provide Suggestions for Making the Child Care Facilities Revolving Fund (CCFRF) Fully Operational.** Recommend Legislature direct CDE to report at spring budget hearings on the status of the CCFRF major renovation and repair loan program. Specifically, recommend CDE explain why the program has not yet been implemented and present options for expediting it. As one of these options, recommend Legislature consider shifting program administration back to the School Facilities Division.
- E-106 ■ **Convene a Working Group to Create a Strategic Child Care and Development Quality Plan by March 1, 2008.** Recommend Legislature convene a working group to (1) define quality levels and standards, (2) develop a method for measuring quality and publicizing the results, (3) create incentives for providers to improve quality, and (4) recommend ways to improve the effectiveness of quality improvement monies.

Quality Education Investment Act (QEIA)

- E-118 ■ **Small Changes Could Yield Significant Benefits.** Recommend Legislature run QEIA as a pilot program and allow schools to self-select themselves into one of three reform groups. Recommend funding an independent evaluator to assess the performance of the groups over the seven-year life of the program.
- E-120 ■ **Make Accounting of QEIA Monies More Transparent.** Recommend Legislature reflect QEIA payments in the annual education trailer bill to make the payments easier for all parties to track.

English Learners (EL)

- E-130 ■ **Adopt a More Strategic Approach to Funding EL Students.** Recommend Legislature determine an explicit “weight” at which EL students should be funded.

Analysis**Page**

- E-135 ■ **Fund Best Practices Study.** Recommend Legislature provide between \$500,000 and \$800,000 in one-time monies for an evaluation of the recently established best practices pilot program. Recommend evaluation focus on identifying effective instructional approaches, instructional materials, and professional development programs designed to enhance EL student achievement.
- E-139 ■ **Fund Teacher Preparation Program Study.** Recommend Legislature provide between \$250,000 and \$500,000 in one-time monies to evaluate the effectiveness of teacher preparation programs at improving EL student achievement.
- E-142 ■ **Modify State Assessments to Measure Student Progress.** Recommend Legislature require the California Department of Education to contract for a report on the feasibility of vertically scaling the state's assessment system and report back by April 1, 2008.

Soledad Enrichment Action Charter School

- E-144 ■ **Soledad Enrichment Action Charter School.** Recommend extending its authority for two years to operate as a community day school.

Intersegmental: UC and CSU Outreach Programs

- E-171 ■ **Withhold Recommendation Pending Forthcoming Evaluations.** Withhold recommendations on the proposed General Fund reductions to the University of California and the California State University's outreach programs, pending review of the universities' evaluation reports to be submitted this spring.
- E-172 ■ **Different Approaches for Evaluating and Funding Outreach.** If the Legislature rejects the Governor's proposed reductions to outreach programs, we recommend it require an external evaluation of these programs. Also, as an alternative approach

Analysis**Page**

for funding and delivering outreach services, the Legislature could establish a College Preparation Block Grant targeted at K-12 schools with very low college participation rates.

Intersegmental: UC and CSU Enrollment Growth And Funding

- E-178 ■ **Reduce Budgeted Enrollment Growth at the University of California (UC) and the California State University (CSU).** Based on our demographic projections, we recommend the Legislature fund budgeted enrollment growth of 2 percent for UC and CSU.
- E-180 ■ **Plan for State’s Long-Term Higher Education Priorities.** In view of the projected decline in the state’s college-age population, we believe that the Legislature has a special opportunity to determine and fund its long-term higher education priorities.
- E-190 ■ **Fund 2 Percent Enrollment Growth Based on Legislative Methodology for Marginal Cost. Reduce Item 6440-001-0001 by \$13.4 Million and Item 6610-001-0001 by \$13.9 Million.** Using the marginal cost methodology recently approved by the Legislature and our proposed 2 percent enrollment growth, we recommend reducing the Governor’s proposed funding rates for each additional student at UC (from \$10,876 to \$10,586) and CSU (from \$7,837 to \$7,710). Further recommend Legislature (1) amend proposed budget bill language to reflect our proposed marginal cost and enrollment growth rates and (2) adopt supplemental report language specifying that enrollment growth funding provided in future budgets be based on the legislative methodology.

Intersegmental: Student Fees

- E-194 ■ **Explicit Fee Policy Needed.** We recommend that the Legislature adopt a fee policy that bases student fees at the three segments on fixed shares of total educational costs. This would promote access, equity, and accountability in the higher education systems.

Analysis**Page**

- E-195 ■ **Absent Fee Policy, Maintain Shares of Cost at Current Levels.** Until the Legislature makes a policy choice about the percentage of cost that students should pay at the three segments, we recommend that student fees be adjusted to ensure that the share of cost paid by students remain unchanged in the budget year. This would require 2.4 percent increases at the University of California and the California State University, generating \$36 million and \$23.5 million, respectively, in new revenue.
- E-199 ■ **No Need for Fee Buyout.** Whatever level of student fees the Legislature envisions, there is no need to “buy out” any portion of the Governor’s fee proposal. The notion of buying out fees confuses the role of fees and undermines the Legislature’s role in budgeting.

Intersegmental: Higher Education Nursing Proposals

- E-210 ■ **Standardize Approach for Funding Nursing. Reduce Item 6440-001-0001 by \$621,000 and Increase Item 6610-001-0001 by \$939,000.** Recommend the Legislature fund nursing enrollment within regular enrollment growth. Given rapid increases in nursing enrollment, we recommend the Legislature provide the University of California (UC) and California State University (CSU) with additional funding above the normal marginal cost rate. The combined effect of these two recommendations would reduce UC’s augmentation and increase CSU’s funding.
- E-211 ■ **Reject \$9 Million in Current-Year Appropriations for Community Colleges.** Recommend the Legislature reject the Governor’s \$9 million current-year request to establish new nursing programs and simulation laboratories, as the need for these proposals have not been justified.
- E-212 ■ **Approve New Support Services for Community College Nursing Students.** Recommend the Legislature approve the Governor’s \$5.2 million request to expand support services to nursing students.

Analysis**Page**

- E-213 ■ **Reject Proposal for Special Funding of Prerequisite Courses. Reduce Item 6870-101-0001 by \$3,786,000.** Recommend the Legislature reject the proposal to allocate \$3.8 million in additional funds to community college districts for science prerequisite courses. This additional funding is not justified and the intended outcome would not help nursing programs.
- E-213 ■ **Assess Admissions Policies.** Recommend the Legislature direct the community college Chancellor's Office to report at budget hearings on improving the selectivity of nursing-program admissions processes in order to promote fairness and student success.

California Postsecondary Education Commission (CPEC)

- E-217 ■ **CPEC Should Focus on Coordination and Data Management Roles.** We agree with the general approach in proposed budget bill language that assigns priority to CPEC's responsibilities concerning reviewing the need for new institutions and programs. We recommend, however, the Legislature also include as a priority CPEC's data management responsibilities.
- E-217 ■ **New Approach to Faculty Compensation Needed.** We find that CPEC's faculty salary surveys for the University of California (UC) and the California State University (CSU) are flawed and misleading, and recommend instead that the Legislature direct CPEC to produce faculty compensation surveys that (1) include all forms of compensation and (2) compare UC and CSU faculty compensation to that of a broad range of institutions.

University of California (UC)

- E-227 ■ **General Fund Base Increase. Reduce Item 6440-001-0001 by \$46.7 Million.** Based on our projection of inflation for 2007-08, we recommend the Legislature reduce the General Fund base increase proposed by the Governor for UC from 4 percent to 2.4 percent. Accordingly, we recommend deleting \$46.7 million from the \$116.7 million proposed General Fund augmentation.

Analysis**Page**

- E-228 ■ **Program in Medical Education (PRIME).** Withhold recommendation on the proposed \$570,000 augmentation for UC's PRIME, pending receipt and review of additional information.
- E-231 ■ **California Institutes for Science and Innovation. Reduce Item 6440-005-0001 by \$15 Million.** Recommend the Legislature reject the \$15 million proposed augmentation for California Institutes for Science and Innovation, because (1) neither the administration nor UC could provide adequate justification for the additional funds and (2) existing research funds could be redirected to expand these institutes.
- E-233 ■ **Petascale Supercomputer. Reduce Item 6440-001-0001 by \$5 Million.** Recommend the Legislature reject the proposed \$5 million General Fund expenditure to enhance UC's bid for a Petascale supercomputer, due to the lack of adequate justification for the proposal and the availability of existing research funds that could be redirected for this purpose.
- E-235 ■ **Improving UC's Long Range Development Planning Process.** Based on our review of the process used by UC to prepare a Long Range Development Plan (LRDP) for each campus and medical center, we recommend (1) increasing legislative oversight over UC's LRDPs, (2) developing a more standard approach for soliciting public input, (3) having UC provide systemwide enrollment projections through 2020 at budget hearings, (4) making better use of the summer term to accommodate additional students, (5) clarifying and improving the California Environmental Quality Act, and (6) requiring a report on UC's efforts to reach fair share agreements with neighboring jurisdictions.
- E-250 ■ **Telemedicine Facilities. Reduce Item 6440-304-6048 by \$59 Million.** Recommend deletion of \$59 million from the Governor's telemedicine proposal as: (1) UC has not yet presented a specific facility proposal for the Los Angeles campus and (2) the proposed budget includes an unneeded contingency reserve of \$24 million. Further recommend that the remaining four projects be scheduled and that accompanying provisional language be amended to similar items.

Analysis**Page**

- E-251 ■ **Alternative Energy Research Proposals. Eliminate Item 6440-301-0660.** Recommend deletion of the Governor's request for \$70 million in lease-revenue bond proceeds to fund two alternative energy research proposals, as the administration has not yet presented specific capital facilities proposals.

California State University (CSU)

- E-256 ■ **General Fund Base Increase. Reduce Item 6610-001-0001 by \$43.6 Million.** Based on our projection of inflation for 2007-08, we recommend the Legislature reduce the General Fund base increase proposed by the Governor for CSU from 4 percent to 2.4 percent. Accordingly, we recommend deleting \$43.6 million from the \$108.9 million proposed General Fund augmentation.
- E-256 ■ **Science and Math Teacher Initiative.** Withhold recommendation on the proposed \$2 million General Fund augmentation to the Governor's science and math teacher initiative, pending review of the university's progress report to be submitted in April.
- E-258 ■ **Long Range Planning Issues.** Recommend CSU provide draft copies of its physical master plans to the Legislature before they are approved by the CSU Board of Trustees. Since future student enrollment levels are the main drivers of these plans, we further recommend CSU provide systemwide projections through 2020 at budget hearings. Finally, we recommend CSU report on what steps it will take to mitigate off-campus impacts as a result of campus growth.

California Community Colleges (CCC)

- E-269 ■ **Reduce Current-Year Enrollment Restoration Funding.** We estimate that community college districts will only use a portion of over \$160 million in enrollment restoration funds, which are available in the current year to districts that fill slots that became vacant in recent years. When a reliable estimate of unused funds

Analysis**Page**

is known at the time of the May Revision, we recommend the Legislature delete these unused funds on a one-time basis.

- E-270 ■ **Reduce Current-Year Appropriation by Amount of Unused Enrollment Growth Funding.** We expect that community college districts will not be able to use all \$97.5 million in current-year enrollment growth funds. In order to address the state's budgetary problem, we recommend the Legislature reduce CCC's current-year Proposition 98 appropriation for CCC enrollment growth. A clearer estimate of this amount should be known at the time of the May Revision.
- E-271 ■ **Fund 1.65 Percent Enrollment Growth in Budget Year. Reduce Item 6870-101-0001 by \$19 Million.** Recommend the Legislature fund 1.65 percent enrollment growth in the budget year, consistent with the statutory growth guideline. Funding at this level would save \$19 million relative to the Governor's proposal. Depending on the minimum spending requirement for Proposition 98 in 2007-08, this funding would be available for General Fund savings or for redirection to other K-14 priorities.
- E-272 ■ **Accountability Update.** We provide an update on the implementation of a new segment- and college-level accountability system for CCC, as well as a review of several new studies on performance deficiencies at the community colleges.
- E-278 ■ **Reduce Current-Year Proposition 98 Appropriation by \$33.1 Million.** Recommend the Legislature delete unused basic skills overcap funds in current year to achieve General Fund savings.
- E-279 ■ **Eliminate Basic Skills Overcap Categorical, but Put Freed-Up Funds to Best Use.** Recommend the Legislature approve the Governor's proposal to abolish the basic skills overcap categorical program, as the categorical has not served its intended purpose. Depending on the minimum spending requirement for Proposition 98 in 2007-08, we recommend using free-up funds either for General Fund savings or a block grant for community colleges to improve student achievement.

Analysis**Page**

- E-283 ■ **Amend Integrated Waste Management Mandate.** The Legislature has several options to reduce or eliminate the costs from this mandate. Recommend, at a minimum, the Legislature reduce future state reimbursements by amending statute to ensure that community college districts apply savings and revenues to offset waste-diversion program costs.
- E-284 ■ **Factor in Year-Round Facility Use.** Recommend the Chancellor's Office, in calculating future district requests for instructional space, take into account the capacity available with year-round operation.

Student Aid Commission

- E-289 ■ **Legislature Should Reject Proposal to Restrict the Assumption Program of Loans for Education (APLE) Awards. Amend Item 7980-101-0001, Provision 1(d).** We recommend the Legislature again reject the Governor's proposal to restrict 600 APLE awards to University of California and the California State University students participating in the Governor's Math and Science Initiative. The program is already underutilized, and further restrictions could drive participation rates down even further.
- E-290 ■ **Commission Should Provide Statutorily Required Reports.** For the past several years the commission has not provided statutorily required reports on participation in the APLE program. We recommend the Legislature not approve a proposed staffing augmentation until the commission provides this information.
- E-294 ■ **Cal Grant Program Costs Would Be Lower With Lower Fee Increases. Reduce Item 7980-101-0001 by \$20 Million.** Our recommendation of lower fee increases than those proposed by the Governor would result in lower Cal Grant costs (relative to the Governor's proposed level). We therefore recommend a corresponding reduction in Cal Grant funding.

Analysis**Page**

- E-295 ■ **Restructure State Administration of Grant and Loan Programs.** For the past couple of years, the relationship between the California Student Aid Commission (CSAC) and its auxiliary organization, EdFund, has shown increasing evidence of organizational tension and inadequate oversight. Given the evident inability of CSAC to resolve these issues through a revised operating agreement, we continue to recommend that the Legislature replace the current two-agency structure for administering higher education grant and loan programs with a single-agency structure.

