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October 27, 1999

Commission Members
Commission on State Mandates
1300 I Street, Suite 950
Sacramento, California 95814

Dear Commission Members:

At the commission's September 15, 1999 meeting, commission members requested information on the legislative intent regarding Chapter 797, Statutes of 1980 (SB 1970, Rodda). After reviewing the materials submitted by the claimants and the Department of Finance (DOF), we concluded that we—as the Legislature's chief fiscal advisor—had additional information which would be helpful to the commission. On October 13, 1999, my office prepared a document summarizing the special education mandate's funding and legislative history.¹ We delivered the document to the Commission on State Mandates (COSM) and faxed it to the parties on the mailing list.

In the supplemental analysis prepared for your October 28, 1999 meeting, your staff summarizes our document and reaches a different conclusion as to the Legislature's intent. In addition, Supplemental Claimants, Riverside County Superintendent of Schools, and Long Beach Unified School District each provided the commission responses to our document on or about October 25th or 26th.

In this letter, we outline our concerns with the COSM staff supplemental analysis. Given that we received two of the school district responses less than 24 hours before the

¹ See Volume VII, Bates p. 2977.

deadline for submitting comments to your staff, however, this letter includes only very limited comments on the matters raised by the claimants.²

Legislative Analyst's Office's (LAO's) Response to Supplemental Analysis

In general, we find that your staff compiled a extensive historical record for the special education mandate, and highlighted many relevant records. This significant staff effort, accomplished under a short time line, is commendable. Our review of the commission staff analysis, however, indicates that there are three major areas in which the historical record is summarized incorrectly, or where unsubstantiated conclusions are presented. We outline these areas of concerns below.

Local "Freeze" and "Fully Funding" Should Not Be Linked

Throughout the analysis, the staff links two fiscal concepts: "freezing the local general fund contribution" and "fully funding the Master Plan." While the staff cites authoritative sources supporting the Legislature's intent to freeze the local general fund contribution (LGFC), the concept of *fully funding* the Master Plan is left unsupported. Instead, the reader is left to infer from the Legislature's actions to (1) freeze the LGFC and (2) prepare a first-year spending plan that did not identify other local costs, that the Legislature intended to guarantee full state funding for any remaining nonfederal program costs forever after. Such an inference, however, is not consistent with the historical record.

In order to understand the purpose of freezing the LGFC, some brief background is needed. As we discussed in our earlier document, during the late 1970s, the Legislature began offering funding to a limited number of districts under an "early-Master Plan" model. Districts funded under the early-Master Plan model usually enjoyed much greater state support than other school districts—and paid a significantly lower portion of program costs from local funds. Thus, at the time Chapter 797 was being considered, there were large differences in the level of local costs borne by school districts.³ These

² Long Beach mailed us their response—we received it October 25th. Supplemental Claimants and Riverside did not include the LAO on their facsimile distribution list. Other parties provided us with copies of their response during the morning of October 26th. The COSM staff requested that the LAO rebuttal be delivered by 10 A.M., October 27th.

³ See, for example, the *Report of the Auditor General, Special Education Financing Warrants Review, 1979, Appendix A*, pp. 4-5; or any DOF bill analysis of Chapter 797, such as the description of the LGFC on Bates p. 3311.

fiscal differences stemmed primarily from variations in prior state funding formulas, not local choices or state policy, and were considered undesirable. During the early legislative history of Chapter 797, there were numerous efforts to reduce these local cost disparities. Various options to promote local cost “equalization” were considered, but rejected for cost or other reasons.⁴

Instead of equalizing this uneven fiscal playing field, the Legislature agreed in Chapter 797 to *freeze* these local costs at their 1979 amounts, without adjustment for enrollment or inflation. Henceforth, the only increase in local costs would stem from local costs which exceed a *uniform* state funding model—not whether the district was fortunate to have been included in an early-Master Plan. Accordingly, freezing LGFC at their 1979 amounts is synonymous with freezing the uneven fiscal landscape of 1979. The freeze does not mean, as we discussed in our previous document and we discuss below, that the Legislature agreed to *fully fund* the Master Plan for Special Education. Instead, the fiscal model enacted in Chapter 797 always assumed that there could be additional local costs beyond the frozen LGFC.⁵

Purpose of Deficit Factor and Enrollment Cap Ignored

Given the prominence afforded to discussion of the special education deficit factor and enrollment cap in our previous document—as well as the DOF bill analyses of

⁴ The earliest versions of Chapter 797, for example, did not include a provision to freeze the LGFC, but equalized local contributions across the state. In a May 6, 1980 progress report memo to the bill’s author, the Senate Office of Research wrote that the bill’s recent amendments removed the equalization provisions, and provided the freeze. The memo states “In sum, the bill is less redistributive than it was before . . . We have made it clear to the parties involved that further discussions are required on the issue of equalizing encroachment. This is a major equity issue as older Master Plan entities are in a favored financial position relative to non-Master Plan entities.” This memo is included as an enclosure.

⁵ We note, for example, that the *California Master Plan for Special Education 1980-81 Fiscal Report*, prepared by the California Department of Education (page 11) that defines state entitlements under Chapter 797 as follows “Entitlements are the amounts of special education costs of a local agency which are recognized by the state for the provision of state aid.”

Chapter 797—we are perplexed by staff’s exclusion of any discussion of these matters in their analysis.⁶

As we discuss in our previous document, the Legislature’s decisions to include a deficit factor in the special education funding model demonstrates the Legislature’s refusal to commit to any specified level of state expenditures for special education. Under the clear terms of Chapter 797, no level of state aid to local education agencies was guaranteed. In any year in which state appropriations were insufficient to pay all local claims, state aid was to be prorated and local education agencies paid the remaining costs. Under the very terms of Chapter 797, there was no state commitment to *fully fund* the master plan.

Similarly (and also discussed in our previous document), the Legislature enacted a funding model which limited any single local education agency’s reimbursement from the state. For example, the Legislature specified that it would *not* reimburse a Local Education Agency’s costs to provide special education services for more than 10 percent of their general student population. This reimbursement percentage was set at a level that was knowingly (1) *lower* than the federal reimbursement percentage, (2) *lower* than the percentage of special education students some school agencies were currently serving, and (3) *lower* than the state percentage cap set forth under the early-Master Plan program.⁷ The DOF bill analyses refers to this percentage cap as “one of the most significant fiscal aspects” of Chapter 797.⁸ The clear purpose of the percentage cap is to *limit* state costs, not to guarantee that the state would reimburse all local expenditures.

Our review indicates that there is no analytic way to reconcile the existence of the deficit factor and the enrollment cap with staff’s conclusion that the Legislature intended to fully fund the Master Plan. If the Legislature intended to fully fund the Master Plan, there is no purpose for a deficit factor or an enrollment cap. Conversely, if the

⁶ Similarly, while staff provides Bates page references to the part of Chapter 797 that freezes the LGFC, there are no citations for the sections of Chapter 797 that outline the deficit factor and the enrollment cap. The deficit factor is in Education Code Sections 56790 to 56792. The enrollment caps are in Education Code Sections 56760 and 56762.

⁷ Virtually all DOF bill analyses include this information. See, for example, Bates pp. 3280-3281 and 3312. In addition, the LAO’s July 1, 1980 bill analyses discusses the change to lower the state’s enrollment cap. See Bates p. 3293.

⁸ This statement is included in virtually all DOF bill analyses, including the ones listed in the above footnote.

state's funding model had a deficit factor and enrollment cap, there was no state commitment to fully fund the Master Plan.

Failure to Increase LGFC Misconstrued

The staff analysis erroneously cites the Legislature's decision not to increase the LGFC as an indication that the Legislature wished to fully fund the Master Plan. As explained earlier in this document, the LGFC represents a frozen artifact of state special education funding formulas from the 1970s. The Legislature knew that the variation among LGFC requirements had no fiscal policy rationale. To increase the LGFC as a way of reducing state special education costs would be to exacerbate these fiscal inequalities. Instead, the Legislature acted to reduce its costs by enacting program changes and limitations on state funding reimbursements—and by implementing the deficit factor set forth in Chapter 797. These alternative ways of minimizing state costs were more desirable from a policy standpoint than modifying the LGFC.

RESPONSE TO SUPPLEMENTAL CLAIMANTS, RIVERSIDE, AND LONG BEACH

As we discussed earlier in this document, we very recently received three responses from claimants and have not reviewed their papers in detail. Accordingly, we offer only the following summary comments.

No Explanation for Deficit Factor or Enrollment Cap

None of the respondents offer any commentary on the deficit factor or enrollment cap. Instead, the respondents ignore these key elements of the fiscal model and simply assert that the state was responsible for funding all local costs in excess of federal reimbursements and the frozen LGFC. Claimants continue to miss the obvious point. If Chapter 797 set forth a funding scheme that guaranteed that the state would *fully fund* the Master Plan, then why do local school districts have costs in addition to their frozen LGFC? The clear answer is that no such guarantee to fully fund the Master Plan was ever provided in Chapter 797. Instead, local school district special education costs are the simple result of a state funding system that always included (1) a deficit factor and (2) cost control mechanisms, such as the enrollment cap.

No Alternative Explanation of Legislative Intent

Given the evidence that the Legislature and administration were fully aware that some procedural elements of Chapter 797 created a state-mandated local program⁹, it is

⁹ See for example, the LAO bill analyses on Bates p. 3295, and DOF bill analyses on Bates p. 3316.

difficult to imagine that the state had any higher priority use for its resources than funding its constitutional obligations. The Legislature and administration's attention to this constitutional obligation is evident in the bill analyses prepared by their fiscal staff. As we discuss in our previous document, these bill analyses consistently comment on the sufficiency of the funding in Chapter 797 to pay for the cost of the state mandates. In their responses, none of the claimants offer any argument as to why the state—at a time that it was facing severe fiscal pressures due to Proposition 13 and a slowing economy—would voluntarily chose to fund a federal mandate over its own.

Our intent in providing this letter and our previous document is to offer the COSM information and perspective from the Legislature's chief fiscal advisor. In developing our material, we relied primarily on the voluminous record already developed for the mandate. To the extent any party needs additional information as to the source of our references or conclusions, we would be happy to assist them. At this point, we note for the record, that we have not received a single inquiry for such information from COSM staff or the claimants.

I hope this information will be helpful . Should you have any questions, or wish additional information, please contact my staff directly: Marianne O'Malley or Stuart Marshall (445-6442). In addition, Ms. O'Malley and Mr. Marshall will attend your October 28th hearing.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

Enclosure