

State Education Funding Still at Risk Due to Dispute Over Prison Inmate Services

Since 1995, the state of California has been at odds with the U. S. Department of Education (USDE) over special education services for eligible inmates in state prisons. The dispute has threatened receipt of federal funds for special education programs in California's public schools as we indicated in our *Analysis of the 1997-98 Budget Bill* (see page D-89). Despite the recent approval of changes in federal law by the Congress and the President, which Californians believed would resolve the state-federal conflict, the USDE continues to assert that California is out of compliance. This could place more than \$300 million in federal funds for special education in California's public schools at risk.

Background

In 1975, the Congress and President enacted the Individuals with Disabilities Education Act (IDEA) which defines the disabilities that qualify a child for special education and mandates school responsibilities and parental rights. Under current law, individuals between the ages of 3 and 22 who meet the qualifica-

tions are eligible. The federal government provides funds to the state to support special education programs in public schools, including \$306 million in Federal Fiscal Year 1997 (FFY 97).

In 1997, the Congress and President enacted the IDEA Amendments of 1997 to reauthorize and modify the IDEA. Among its provisions, the amendments limit the financial penalties that the USDE may impose on a state if one of the state agencies responsible for providing special education services fails to comply with federal law. The state and federal governments are now in disagreement over how the new law affects the California Department of Corrections (CDC) and inmates in adult prisons.

Governor's Executive Order. The IDEA Amendments of 1997 provide that the Governor "may assign to any public agency in the state the responsibility for carrying out special education provisions in adult prisons." On June 5, 1997, Governor Wilson issued Executive Order W-155-97 designating the CDC as the

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state agency with that responsibility. The executive order also directed the CDC to seek a full exemption in Congress from any requirement to provide special education services to inmates in adult prisons. Finally, the executive order directed the CDC to request that the U.S. Secretary of Education take no action against California due to the state's decision not to establish special education in adult prisons pending the final outcome of California's efforts to obtain a full exemption.

Differing Interpretations Of Federal Law

The Governor has interpreted the 1997 Amendments as allowing the state to withhold services from eligible CDC inmates while risking the loss of only a small portion of the \$306 million in federal special education monies. The Governor has noted that the IDEA Amendments of 1997 state that "any withholding of funds . . . shall be limited to the specific agency responsible" for the decision—in California's case, the CDC—thus holding funding for special education administered by the State Department of Education (SDE) largely immune from any federal penalty.

Nevertheless, the USDE indicates that the CDC *and* the SDE are out of compliance with the requirements of the IDEA and is threatening to require California to repay to the federal government its most recent allocation of \$306 million in special education funding. In a letter to the SDE and the CDC dated July 16, 1997, the USDE indicated that the state "has a

history of unsatisfactory performance and has failed to conform to the terms of previous awards with respect to its obligation to serve individuals with disabilities in state adult correctional facilities."

The USDE contends that there are individuals, adjudicated as minors, who are serving time in CDC facilities. If this were the case, the SDE would be responsible for ensuring that eligible inmates receive special education. However, according to the CDC, there are currently no individuals in the CDC who were adjudicated as minors serving time under its authority. The CDC does have persons eligible for special education in CDC facilities, but asserts that none of them fall under the responsibility of the SDE.

Outlook

Our review suggests that the position taken by the USDE is at odds with the specific policy set by Congress to limit penalties imposed on states. Whether California ultimately must return some small portion of its FFY 97 special education grant, the full \$306 million, or some amount in between is yet to be determined. Should the controversy not be resolved, future allocations for FFY 98 and beyond could also be at risk. Legislation has been introduced in Congress that would fully exempt the state from requirements to provide special education to inmates in adult prisons.

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Recent Economic And Revenue Developments

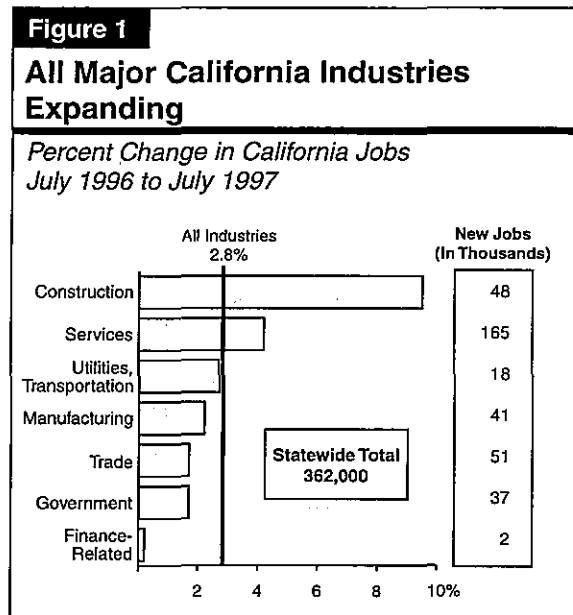
Moderate Economic and Revenue Growth Assumed in 1997-98

The 1997-98 Budget, signed by the Governor on August 18, assumes moderate economic and revenue growth during this fiscal year. General Fund revenues are forecast to total \$52.5 billion, a 6.8 percent increase from 1996-97. Recent economic and revenue developments are generally consistent with—if not slightly stronger than—the budget forecast.

Economic Growth Continues At Healthy Pace

California's broad-based economic expansion is continuing in mid-1997. Wage and salary employment in July was up 362,000 over the prior year, led by healthy gains in the business-related services sector. Every major industry sector is now showing job gains, including aerospace and finance, which until recently had been the state's only industries continuing to lose jobs (see Figure 1).

Real Estate Strengthening. The real estate market is showing convincing signs of improvement. Statewide existing home sales in July were the strongest since 1989, with home prices rising in many regions of the state. Sales and prices are particularly strong in the San Francisco Bay Area, with other coastal areas also showing healthy increases. The improvements in the real estate market are translating into increases in new construction. Permits for new residential building in June were up al-



most 18 percent from their June 1996 level. If sustained, the upturn in new construction would have significant impacts on taxable sales of building-related materials, appliances, and furniture.

General Fund Revenues Slightly More Than Projected

July receipts were up \$94 million from the budget forecast. There were numerous special factors affecting the revenue totals. However, even after adjusting for these factors, the underlying revenue trend appears to be slightly stronger than assumed. In particular, sales taxes and personal income tax withholding payments were up in July, consistent with

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other evidence that California's economy is currently growing at a healthy pace. Preliminary evidence for August indicates that the positive trend in withholding receipts is continuing. Based on data for all but the last two days of the month, it appears that withholding collections exceeded the estimate by more than \$100 million in August.

September A Key Revenue Month

A more definitive picture of the current-revenue trend will likely emerge in September, when more than \$5.7 billion in total collections

are projected. During this month, individuals and the majority of corporate taxpayers will be remitting their third quarterly prepayments toward their estimated 1997 income tax liabilities. These payments have often provided a significant insight into the strength of income tax liabilities for the tax year. Similarly, substantial collections are projected for withholding payments, sales and use taxes, and insurance taxes.

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