# HIGHER EDUCATION

## MAJOR ISSUES

**▌*The University of California (UC) and California State University (CSU).*** The budget proposes General Fund support for the UC and the CSU of $3.8 billion in 1996-97. This is the result of an increase of $124 million, or 6.5 percent, for UC and an increase of $96 million, or 5 percent, for CSU compared with estimated current-year expenditures. The proposed General Fund increase is sufficient to eliminate the need for undergraduate student fee increases proposed by both segments for 1996-97. As a result, the budget assumes no undergraduate student fee increase in the budget year. (See page F-6.)

**▌*California Community Colleges (CCC) Funding Options.*** In both 1995-96 and 1996-97, the options available to the Legislature depend on the projected level of General Fund tax revenues and whether the Governor's proposed tax cut is adopted.

- ***Budget Revenue Projection, With Tax Cut.*** To fully fund growth and COLA for categorical programs, we recommend redirecting funding from discretionary spending for enrollment growth.

- ***LAO Revenue Projection.*** Under the LAO projections, there would be more than enough Proposition 98 monies to fund all budget proposals for the CCCs. We recommend the Legislature use the remaining funds—up to $78 million in 1996-97—for maintenance and operations, instructional equipment and library materials, additional enrollment growth, and equalizing district funding. (See page F-40.)

***Eliminate Deferred Maintenance Over Several Years.*** The budget proposes total spending of $45.8 million for deferred maintenance for the UC, CSU, and CCC. We recommend the Legislature, instead, take a more comprehensive approach to the system's maintenance problems—deferred and regular—by initiating a state-segment partnership to:

- ***Increase Funding for Regular Maintenance***. Funding regular maintenance at an adequate level would prevent future deferral of maintenance projects.
- ***Hold the Segments Accountable for Adequate Spending on Maintenance.*** This would prohibit the addition of new projects to existing deferred maintenance backlogs.
- ***Eliminate Deferred Maintenance Backlogs***. We recommend the Legislature develop a program to eliminate existing deferred maintenance over a five- to ten-year period. (See page F-13.)

***Cal Grant Increase Proposed.*** The budget proposes $10 million to increase the maximum Cal Grant award level for recipients who attend non-public postsecondary institutions. The long-term cost of this proposal would reach about $30 million annually by 1999-2000. The $10 million may be needed to backfill federal spending reductions for student financial aid. If federal spending is maintained, and if the Legislature is willing to commit to a long-run cost of about $30 million, we recommend the Legislature spend $5 million to increase the maximum award level for recipients at nonpublic institutions and $5 million to increase the annual number of new Cal Grant awards. (See page F-59.)

# HIGHER EDUCATION

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# HIGHER EDUCATION

## OVERVIEW

***The budget proposes modest increases in state spending for all higher education segments, and no increases in undergraduate student fees.***

The budget proposes General Fund expenditures of $5.9 billion for higher education in 1996-97. This is $358 million, or 6.5 percent, more than estimated expenditures in the current year. Including local property tax revenues assumed for community colleges, the budget proposes spending of $7.2 billion, which is $367 million, or 5.4 percent, more than estimated expenditures in the current year.

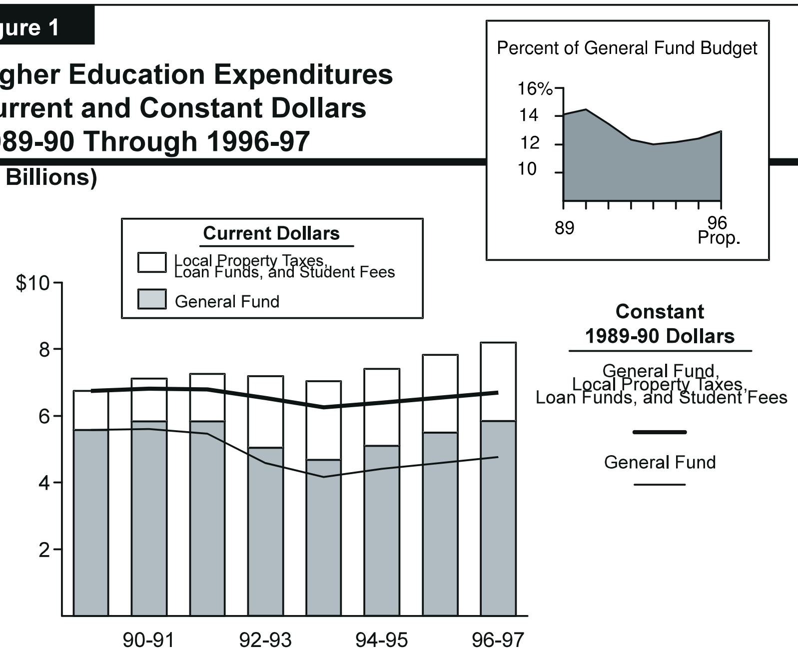
Figure 1 (see next page) shows that higher education expenditures from the General Fund have increased by $275 million since 1989-90, representing an average annual increase of 0.7 percent. When these expenditures are adjusted for inflation, General Fund spending decreased over this time period by an average of 2.2 percent annually.

The share of General Fund spending allocated to higher education has declined from 14 percent to 13 percent over this period. Including increased student fees (net of financial aid), local property taxes, and loan funds, higher education expenditures have increased by $1.5 billion over the period, an average annual increase of 3 percent. Adjusted for inflation, spending has decreased slightly, by less than 0.5 percent annually.

**Figure 1**

**Higher Education Expenditures Current and Constant Dollars 1989-90 Through 1996-97**

**(In Billions)**




# SPENDING BY MAJOR PROGRAMS

Figure 2 shows spending from the General Fund, local taxes, and student fee revenues (net of financial aid) in detail.

For the University of California (UC) and the California State University (CSU), the budget proposes General Fund increases of $124.1 million (6.5 percent) and $95.5 million (5.7 percent), respectively. (The CSU figure understates actual budget-year growth, because 1995-96 expenditures include $20 million in one-time spending.)

The budget proposes no undergraduate fee increases for the UC or CSU. Increased fees for UC professional programs and enrollment changes account for the increases in student fee revenues shown in Figure 2. Based on these fee proposals, total revenues would increase by $141 million (5.9 percent) at the UC and by $99 million (4.7 percent) at the CSU.

For the California Community Colleges (CCC), the budget proposes to increase support from the General Fund in 1996-97 by $86.7 million (6.3 percent). Combined support from the General Fund, property tax

$94.4 million (3.3 percent). (The CCC figure understates actual budget-year growth, because the 1995-96 expenditures include $79 million in one-time expenditures.) The budget proposes to leave CCC fees at their existing level of $13 per credit unit.

**Figure 2**

**Higher Education Budget Summary Selected Funds Sources[a] 1994-95 Through 1996-97**

**(Dollars in Millions)**

| | Actual 1994-95 | Estimated 1995-96 | Proposed 1996-97 | Change From 1995-96 Amount | Change From 1995-96 Percent |
|---|---|---|---|---|---|
| **University of California** | | | | | |
| General Fund | $1,825.4 | $1,917.7 | $2,041.8 | $124.1 | 6.5% |
| 1996 higher education capital outlay bond fund | — | — | 10.0 | 10.0 | —[b] |
| Student fee revenues | 456.6 | 476.3 | 483.3 | 7.0 | 1.5 |
| **Totals** | **$2,282.0** | **$2,394.0** | **$2,535.1** | **$141.1** | **5.9%** |
| **California State University** | | | | | |
| General Fund | $1,578.1 | $1,673.8 | $1,769.3 | $95.5 | 5.7% |
| Student fee revenues | 341.6 | 343.6 | 347.2 | 3.6 | 1.1 |
| **Totals** | **$1,919.7** | **$2,017.4** | **$2,116.5** | **$99.1** | **4.7%** |
| **California Community Colleges—local assistance** | | | | | |
| General Fund (Proposition 98) | $1,182.2 | $1,373.2 | $1,459.9 | $86.7 | 6.3% |
| General Fund (non-Proposition 98) | 3.1 | 0.2 | — | -0.2 | -100.0 |
| Local property taxes | 1,332.0 | 1,348.1 | 1,356.9 | 8.8 | 0.7 |
| Student fee revenues | 174.9 | 164.6 | 163.7 | -0.9 | -0.5 |
| **Totals** | **$2,692.2** | **$2,886.1** | **$2,980.6** | **$94.4** | **3.3%** |
| **Student Aid Commission —local assistance** | | | | | |
| General Fund | **$222.9** | **$234.4** | **$245.9** | **$11.4** | **4.9%** |

[a] Student fee revenues are net of financial aid. For 1996-97, selected bond funds for UC that are proposed to support deferred maintenance are displayed to allow for comparison with CSU and the community colleges, where deferred maintenance is supported through the General Fund.

[b] Not a meaningful figure.

# MAJOR BUDGET CHANGES

Figure 3 presents the major budget changes in General Fund spending for higher education. The budget proposes $270 million for increases in employee compensation and prices ($100 million at UC, $68 million at CSU, and $92 million at the CCCs). An additional $59 million is proposed to increase the level of funded enrollment in the three segments ($9 million at UC, $12 million at CSU, and $48 million at CCCs). Funding for debt service costs on previously authorized lease-payment bonds also accounts for a significant portion of the General Fund increase—$42 million ($13 million at UC, $11 million at CSU, and $18 million at CCCs).

The budget proposes increased deferred maintenance funding for all three segments. However, Figure 3 shows only the proposed General Fund expenditures in 1996-97—$9.6 million for CSU. The budget also proposes to allocate other funds for deferred maintenance, as follows:

- UC: $10 million of the $150 million in proposed general obligation bonds for UC capital outlay projects.
- CCC: $17.5 million in one-time 1995-96 Proposition 98 funds.

Finally, the budget proposes a $10 million increase in Cal Grant funding to raise the maximum grant level for new students at nonpublic institutions from $5,250 to $7,200. This proposal has a long-run annual cost of about $40 million.

# ENROLLMENT

Figure 4 (see page 10) shows student enrollment at each of the segments. It shows that the UC's full-time-equivalent (FTE) enrollment will remain essentially steady from 1993-94 through 1995-96. The CSU's FTE enrollment is expected to increase from 247,866 in 1993-94 to an estimated 253,100 in 1995-96, growing by 5,234 students, or 2.1 percent. The CCCs' resident FTE enrollment declined from 864,014 in 1993-94 to an estimated 854,138 in 1995-96, a decrease of 9,876 students, or 1.1 percent. This decline is probably due to a number of factors, including fee increases and efforts to limit enrollment in response to the fiscal uncertainties of 1993-94 and 1994-95.

**Figure 3**

**Higher Education**
**Proposed Major General Fund Changes for 1996-97**

| | | |
|---|---|---|
| **University of California** | **Requested: $2 billion** | |
| | **Increase: $124 million** | **(+6.5%)** |

+
- $100 million for employee compensation and price increases
- $13 million for added debt costs on lease-payment bonds
- $9 million for increased enrollment

| | | |
|---|---|---|
| **California State University** | **Requested: $1.8 billion** | |
| | **Increase: $95 million** | **(+5.7%)** |

+
- $68 million for employee compensation and price increases
- $13 million for deferred maintenance ($9.6 million) and continued campus development ($3.5 million)
- $12 million for increased enrollment
- $11 million added for debt costs on lease-payment bonds

−
- $20 million to eliminate one-time carryover funds in 1995-96

| | | |
|---|---|---|
| **California Community Colleges—Local Assistance** | **Requested: $1.5 billion** | |
| | **Increase: $87 million** | **(+6.3%)** |

+
- $92 million for a 3.45 percent COLA for general-purpose spending and categorical spending for remedial education
- $48 million for enrollment growth
- $18 million added for debt costs on lease-payment bonds
- $13 million to backfill property tax and fee revenue shortfalls

−
- $84 million to eliminate one-time spending proposed for 1995-96

**Other Programs**

+
- $10 million to the Student Aid Commission to increase the maximum Cal Grant award for new enrollees at independent and proprietary colleges

The budget estimates that actual FTE enrollment levels at the UC and the CSU will increase slightly in 1996-97—less than 1 percent in both cases. These budget estimates are somewhat lower than recent enrollment projections by the demographics unit of the Department of Finance (DOF), which show headcount enrollments increasing by about 1.2 percent for UC and by about 1.4 percent for CSU from fall 1995 to fall 1996. However, given recent variations in enrollment at the two systems (particularly in the proportions of full-time and part-time students at CSU, which are important in comparing headcount to FTE enrollment), it appears that the budget estimates of 1996-97 FTE enrollments for the two systems are within a reasonable range.

**Figure 4**

**Higher Education**
**Full-Time Equivalent Students[a]**
**1993-94 Through 1996-97**

| | 1993-94 | 1994-95 | Estimated 1995-96 | Proposed 1996-97 |
|---|---|---|---|---|
| **University of California** | | | | |
| Undergraduate | 112,970 | 113,356 | 114,700 | 114,900 |
| Postbaccalaureate | 578 | 513 | 400 | 400 |
| Graduate | 25,930 | 25,546 | 25,400 | 25,700 |
| Health sciences | 12,823 | 12,635 | 12,500 | 12,500 |
| **Totals** | **152,301** | **152,050** | **153,000** | **153,500** |
| **California State University** | | | | |
| Undergraduate | 213,632 | 213,389 | 220,640 | 221,786 |
| Postbaccalaureate | 14,357 | 13,563 | 12,276 | 12,338 |
| Graduate | 19,877 | 20,160 | 20,184 | 20,276 |
| **Totals** | **247,866** | **247,112** | **253,100** | **254,400** |
| **California Community Colleges** | | | | |
| Resident | 864,014 | 854,628 | 854,138 | 878,439 |
| Nonresident | 27,246 | 25,738 | 25,717 | 26,448 |
| **Totals** | **891,203** | **880,581** | **879,855** | **904,887** |
| **Hastings College of the Law** | **1,268** | **1,257** | **1,220** | **1,220** |

[a] Total enrollments including nonresidents for all segments. Nonresidents are separately identified for community colleges to allow comparison with the Governor's Budget, which identifies resident students only.

For the CCCs, the budget proposes enrollments of 878,439 resident FTE in 1996-97, an increase of 24,301 students, or 2.9 percent. This is the cumulative effect of three proposals: (1) an increase of 12,428 students due to adult population growth of 1.46 percent, (2) an increase of 3,332 students at recently constructed CCC education centers, and (3) an increase of 8,541 students funded from 1995-96 growth funding that will not be allocated to colleges until 1996-97. We provide a detailed discussion of CCC growth funding in our analysis of the CCC budget.

## STUDENT FEES

Figure 5 presents student fee levels from 1993-94 through 1996-97. The budget proposes to provide increased General Fund support in lieu of the revenues that UC and CSU proposed to raise through 1996-97 undergraduate fee increases ($27 million for UC and $30.2 million for CSU). Accordingly, Figure 5 shows no increase in undergraduate fees for UC and CSU in 1996-97. Fee increases are proposed for UC

**Figure 5**

**Higher Education Student Fees Per Full-Time Student 1993-94 Through 1996-97**

| | 1993-94 | 1994-95 | 1995-96 | Proposed 1996-97 |
|---|---|---|---|---|
| **University of California** | | | | |
| Undergraduate/graduate | $3,454 | $3,799 | $3,799 | $3,799 |
| Law[a] | 3,830 | 6,175 | 8,175 | 10,175 |
| Business[a] | 3,454 | 5,799 | 7,799 | 9,799 |
| Medicine[a] | 3,830 | 6,175 | 7,175 | 8,175 |
| Dentistry/Veterinary medicine | 3,454 | 5,799 | 6,799 | 7,799 |
| **California State University** | 1,440 | 1,584 | 1,584 | 1,584 |
| **California Community Colleges[b]** | 390 | 390 | 390 | 390 |
| **Hastings College of the Law[a]** | 3,830 | 6,175 | 8,175 | 10,175 |

[a] Fees charged to new students. Special phasing arrangements have been made for selected business schools.

[b] Excludes BA degree holders, who were charged $50 per credit unit until January 1, 1996.

professional programs—$2,000 per student for Law and Business, and $1,000 per student for Medicine, Dentistry, and Veterinary Medicine. These increases are consistent with legislative intent, as expressed in the *Supplemental Report of the 1994 Budget Act*, that the UC increase fees for students enrolled in selected professional programs over a five-year period to the average of fees charged by comparable public universities. The budget proposes no increase in CCC fees.

Despite large increases in fees since 1989-90, the budget estimates that proposed 1996-97 UC undergraduate resident student fees are $624 less than the current average student fees of the four public universities with which the UC compares itself on faculty salaries. The budget estimates that proposed 1996-97 CSU fees are $1,208 lower than the current average fee of the 15 public universities with which the CSU compares itself on faculty salaries. The budget also shows that California's current community college fees are still the lowest in the nation.

# CROSSCUTTING ISSUES

## RETHINKING THE STATE'S APPROACH TO DEFERRED MAINTENANCE

***The current system of funding ongoing maintenance and deferred maintenance creates counterproductive fiscal incentives that encourage the University of California, the California State University, and the California Community Colleges to defer needed maintenance. We recommend specific steps the Legislature should take to resolve the existing backlogs in deferred maintenance and the underfunding of regular maintenance.***

### BACKGROUND

To keep the state's facilities at the University of California (UC), the California State University (CSU), and the California Community Colleges (CCC) functional for public use, the state and the systems fund both ongoing maintenance and special repair programs.

"Maintenance" includes (1) janitorial and groundskeeping activities and (2) programs to maintain the condition of facilities and infrastructure / utility systems. "Special repair" refers to maintenance projects that are required periodically and are above the level of expenditures needed for routine maintenance. Examples of special repairs include replacing roofs, painting exteriors, and replacing mechanical / electrical equipment.

## Deferred Maintenance: Save Now, Pay More Later

When ongoing maintenance is not sustained at an appropriate level and special repair projects are not accomplished as needed, the result is a backlog of projects termed "deferred maintenance." If repairs to key building and infrastructure components are constantly deferred, facilities can eventually require more expensive investments, such as emergency repairs (when systems break down), capital improvements (such as major rehabilitation), or replacement. Generally, deferral of maintenance projects reduces the useful life of facilities and thus increases future capital outlay needs.

## Reported Deferred Maintenance Backlogs Are Huge

Over the past 10 to 15 years, California's three public higher education systems have been in a state of constant maintenance deferral. As a result, the UC estimates that its deferred maintenance backlog exceeds $480 million, of which about $251 million are priority-one projects. (Priority-one deferred maintenance projects are those requiring immediate action to return a facility to normal operation, stop accelerated deterioration, or correct a cited safety hazard.) The CSU estimates that its deferred maintenance backlog exceeds $325 million, of which about $108 million are priority-one projects. The CCC Chancellor's Office estimates that the statewide community college deferred maintenance backlog is about $90 million.

These figures represent each segment's evaluation of "need." Based on our campus visits, we believe that the total deferred maintenance backlog is in the range of several hundred millions of dollars; however, our review indicates that the specific magnitude of the problem is uncertain for three reasons:

- The project lists—particularly for the CSU—are not up-to-date.
- Some of the specific projects we have reviewed—such as providing technology enhancements for classrooms—are renovations, not deferred maintenance.
- The estimated project costs have not been independently reviewed—actual costs could be considerably more or less than stated.

## Budget History and 1996-97 Proposals

***UC and CSU.*** In 1994-95 and 1995-96, the annual Budget Act and related legislation authorized loan financing for "priority-one" deferred maintenance projects at the UC and CSU that would have an anticipated useful life of at least 15 years. The state provided loans of $17 million to $25 million per segment per year. These loans are being repaid through augmentations to the UC and CSU General Fund budgets.

Although the 1996-97 budget proposes a change in funding source for UC and CSU deferred maintenance—no loans this year—it essentially continues the previous years' approach. That is, it augments the segments' operating budgets by an amount that is small in comparison to the total amount of the deferred maintenance backlog. Specifically, the budget allocates about $10 million each to UC and CSU for high-priority deferred maintenance. The UC amount is from one-time general obligation (GO) debt financing and the CSU amount is from General Fund monies (with the intent that this is a “base” adjustment, which would be available annually).

***Community Colleges.*** For the last several years, the state has provided deferred maintenance funding of $8.7 million annually to the community colleges from Proposition 98 funds. Due to a required dollar-for-dollar local match, this annual appropriation generates about $17 million in deferred maintenance activities.

The budget proposes a total of $26.2 million for community college deferred maintenance in 1996-97. It proposes to spend $17.5 million in one-time 1995-96 Proposition 98 funds for CCC deferred maintenance, and waive the local match requirement for these funds. The budget also proposes the ongoing amount of $8.7 million from 1996-97 funds, but maintains the local match requirement for these funds.

## PROBLEMS WITH THE STATE'S CURRENT APPROACH

Figure 6 (see next page) summarizes the major shortcomings of the state's current approach to deferred maintenance. Most importantly, the state's current approach treats deferred maintenance as an ongoing “program.” The existence of deferred maintenance, however, really represents a maintenance program *failure*. A deferred maintenance project is one that should have been addressed in a prior year under a properly functioning regular maintenance program.

One reason for the failure of the segments' regular maintenance programs is simple—regular, ongoing maintenance has been underfunded. Both the state and the segments have contributed to this underfunding. Moreover, separate funding for deferred maintenance may actually create a fiscal incentive to defer projects rather than deal with them in a more timely manner. Below, we discuss these problems in detail.

**Figure 6**

**Problems in the State's Current Approach to Maintenance**

**The Current Approach:**

Deferred maintenance is a state-funded program. State provides relatively small annual augmentations for this purpose to the systems' base operating budgets.

**Problems:**

- Does not address underlying causes of deferral:
  - State underfunds regular maintenance programs.
  - Segments not held accountable for spending state maintenance funds for that purpose.
- Counterproductive fiscal incentive—makes projects less expensive for systems to address as deferred maintenance than under a regular maintenance program.

***State Funding: Maintenance Has Been a Low Priority.*** Underfunding of maintenance has occurred in part because the state did not budget sufficient funds to maintain both student instruction and maintenance and special repairs. Maintenance has been viewed as a lower priority than the need to maintain the quantity and quality of direct student instruction. It has been seen as more discretionary and, therefore, deferrable. As a result, spending on maintenance has lagged, and facilities have prematurely deteriorated. In the short-run, this policy has mitigated the effect of the recession's low-revenue years on higher education enrollments and the quality of instruction. If pursued in the long-run, however, it would constrain *future* enrollment and quality levels as the state would eventually have to redirect funds otherwise available for these purposes to repair and replace prematurely worn out buildings and infrastructure.

***Segments Not Held Accountable.*** Underfunding of regular maintenance has also occurred in part because the segments redirected funds budgeted by the state for routine maintenance to other activities. This is because there is no framework under which the state holds the systems accountable for the outcomes of their maintenance programs.

The state has the primary responsibility for funding maintenance at the systems. It has little control, however, for determining ongoing maintenance spending at each campus. Although the state has periodically reviewed some specific maintenance and repair-related issues (such as whether the UC and CSU maintenance cost standards are consistent), there are serious gaps in oversight. For example, the UC and CSU maintenance standards have not been reviewed since the mid-1980s, and there is no systematic process for reviewing where actual spending levels stand comparison to the standards. As a result, the UC and CSU have significant flexibility in determining the level of maintenance that actually occurs at each campus. Similarly, state funds are allocated to the CCCs on the basis of maintenance and operation workload, but the colleges have virtually unlimited discretion in determining what kinds of maintenance these funds support—or whether they are used to support maintenance at all.

***Fiscal Incentive to Defer Makes a Bad Situation Worse***. The state's current method of funding deferred maintenance actually provides an incentive for the systems to defer projects. This is because the state has addressed the maintenance problem primarily by adding state monies for deferred maintenance over and above the regular operating budget of the systems. As a result, the current funding arrangement rewards the systems for maintenance deferrals by providing a higher level of funding for deferred maintenance.

For the CCCs, the state provides matching funds under the deferred maintenance program. From the colleges' perspective, therefore, it costs less—in terms of system discretionary funds that must be used—to address a repair under the state-funded deferred maintenance program than it does to address it under a regular maintenance program. Thus, the fiscal incentive offered by the state's approach points in the wrong direction.

## NEW APPROACH NEEDED IN 1996-97

***We recommend that the Legislature: (1) increase funding for ongoing maintenance and hold the systems accountable for better results, (2) prohibit the addition of any new projects to existing deferred maintenance backlogs, and (3) start a process to eliminate the existing backlogs.***

We believe that the improvement in the state’s economic and budgetary situation makes this a good time for the state to begin resolving the maintenance problems at the UC, CSU, and CCC. We recommend the Legislature follow the principles outlined in Figure 7 (see next page) as it considers this issue. Figure 7 also summarizes our recommendations to the Legislature for putting these principles into action. Below, we discuss these recommendations primarily as they apply to the UC and CSU. We present a detailed proposal for the community colleges later in our analysis of the CCC budget.

Figure 7

**Principles and Recommendations for Reform of Higher Education Maintenance Funding**

**Principles:**

- Adequately fund regular, ongoing maintenance.
- Hold the systems accountable for improving regular maintenance efforts.
- Shift fiscal incentives to discourage deferral of projects.

**Recommendations:**

- Augment the segments' maintenance budgets in 1996-97.
- Require a segmental funding match and increased maintenance efforts.
- Require all funds budgeted for maintenance to be spent for that purpose.
- Prohibit adding new projects to existing deferred maintenance backlogs after January 1, 1996.
- Reject debt financing of UC deferred maintenance in 1996-97.
- Develop a plan to eliminate existing deferred maintenance backlogs over time.

## Provide Adequate Maintenance Funding

The first step in correcting the deferred maintenance problem is ensuring the segments adequately fund ongoing maintenance. The segments report that their maintenance budgets are currently underfunded relative to state standards. Specifically, the UC and CSU advise that their building and infrastructure maintenance budgets (which exclude custodial and grounds maintenance) are at least $33 million and $22 million below the standard, respectively.

Given that this shortfall is the responsibility of both the state and the segments, we recommend that the state and the segments share the burden of restoring maintenance funding to adequate levels. Specifically, we recommend:

- The state provide an augmentation for maintenance to the segments.
- The segments match the augmentation from existing resources.
- The state hold the segments accountable for increased maintenance effort.

***State Augmentation.*** We recommend the Legislature provide a General Fund augmentation of $10 million each to the UC and CSU and $25 million for the CCC. We believe the increase in state funding would be a step towards ensuring that the segments provide an adequate level of maintenance, thereby avoiding higher deferred maintenance costs later.

***Segment Match.*** We recommend the Legislature require the segments to match from internal sources the augmentation provided by the state. Thus, the total increase in maintenance funding for each segment would be $20 million for UC and CSU, and $50 million for the CCC, an amount that would move the segments toward sufficient maintenance funding. In order to match state maintenance funds, we recommend the Legislature redirect funding from other priorities, as shown below:

- For the UC, redirect roughly $5 million in federal overhead funds that we recommend not be used for capital outlay purposes (please see the Capital Outlay chapter of this *Analysis*), and redirect a portion of the budget's proposed $124 million General Fund increase.
- For the CSU, redirect the $9.6 million in planned 1996-97 expenditures for deferred maintenance, and a portion of the budget's proposed $96 million General Fund increase.
- For the CCC, redirect $25 million in general-purpose funding from other priorities.

In planning for future budgets, the state and the segments should take further steps to bring ongoing maintenance funding fully up to the standard.

***Accountability.*** The Legislature should require the segments to use all state funding budgeted for maintenance—plus the proposed segment match—solely for the purpose of maintenance. The Legislature should define “maintenance” in this regard as efforts to maintain facilities and infrastructure, as opposed to janitorial services and groundskeeping. While the latter are important, they have no major effect on the length of facilities' useful life. During budget hearings, we will recommend Budget Bill language necessary to accomplish these recommendations.

## Cap the Backlog at Its Current Level

The second step in correcting the deferred maintenance problem is to hold the segments responsible for any new deferred maintenance costs in the future. Given increased funding for regular maintenance, the systems should commit to the proper maintenance of all existing facilities. The Legislature should make it clear that it will not fund projects that are deferred in the future.

This means the state needs to refine the segments' lists of existing deferred maintenance projects to which no new projects could be added. After the Legislature closes the segments' existing lists, it should ensure that state control agencies have an opportunity to review the projects on the list and determine whether they are appropriately classified as deferred maintenance (as opposed to capital renovation, for example).

We therefore recommend the following supplemental report language, which would require the segments to submit their lists of deferred maintenance projects as of January 1, 1996, to the Legislative Analyst's Office (LAO) and the Department of Finance (DOF). The lists would be reviewed and evaluated by the LAO, the DOF, and representatives of the segments:

> The University of California Office of the President, the Chancellor of the California State University System, and the California Community Colleges Chancellor's Office shall submit to the Legislative Analyst's Office (LAO) and the Department of Finance (DOF) upon enactment of the 1996 Budget Act, the list of segment-wide deferred maintenance projects identified as of January 1, 1996. The LAO, DOF, and representatives of the UC, CSU, and CCCs shall review the projects for merit—based on criteria agreed to by the parties. Based on this process, the LAO and the DOF shall jointly present—no later than November 1, 1996—a final list of all existing deferred maintenance projects at California public postsecondary education institutions.
>
> It is the intent of the Legislature to provide deferred maintenance funding in the future only for those projects included on the list presented on November 1, 1996. It is further the intent of the Legislature that the segments shall not defer maintenance in the future. Given the increased level of funding for regular maintenance provided in the Budget Act, and the Legislature's intent to fully fund regular maintenance in future years, the Legislature regards any deferred maintenance project that is not included on the November 1, 1996 list as the fiscal responsibility of the segment, not of the state.

## Reject 1996-97 Debt Financing of UC Deferred Maintenance Projects

We recommend the Legislature reject the proposal to provide $10 million from proposed general obligation bond funds for UC deferred maintenance in 1996-97 (delete Item 6440-001-0658). We believe that the use of debt financing for deferred maintenance projects prior to the thorough review of UC's existing deferred maintenance list (as described above) would be premature. Moreover, this one-time, relatively small, amount of deferred maintenance funding in the budget year leaves future funding for UC's deferred maintenance backlog an open question. Below we discuss some funding sources—including debt financing—that could be used as part of a long-range plan to reduce the backlog of deferred projects identified in the proposed November 1, 1996 report to the Legislature. In 1996-97, the UC should use funds from its regular operating budget to address any urgently needed deferred maintenance.

### Develop a Plan to Eliminate the Existing Deferred Maintenance Backlog

The third step in resolving the deferred maintenance problem is to develop a way to fund the existing deferred maintenance backlog. The Legislature, working with the administration and the systems, should specify a time period—of probably five to ten years—to eliminate the current backlog of projects. The amounts addressed each year should be included in the annual Budget Act—beginning with 1997-98—under a separate deferred maintenance item for each segment.

***Potential Funding Sources.*** To ultimately eliminate the current deferred maintenance backlog, the following sources should be considered:

- State General Fund. For example, the Legislature could set aside for this purpose a portion of tidelands oil revenues, or revenues from the sale of state surplus property.
- Segmental funds.
- Bond funds. We recommended against this source when bonds are proposed as an *ongoing* funding source for deferred maintenance as an ongoing program. However, they are a more appropriate funding source to address a well-defined *one-time* problem.
- Federal overhead funds for the UC.

We think it is appropriate to select a combination of the above (all of which would be temporary in nature) in order to provide as much funding as possible to quickly eliminate the deferred maintenance backlog. Given that the state and the segments each bear some responsibility for the deferral of these projects, we recommend that the Legislature require the segments to match any state funds allocated to reduce the backlog.

## CONCLUSION

A long-run strategy to address maintenance failures at the state's higher education segments is essential to protect the state's investment in higher education buildings and infrastructure. Unless the state acts now to (1) bring the systems' maintenance spending to adequate levels and (2) hold the systems' accountable for addressing their ongoing regular maintenance needs, maintenance will continue to be deferred. As a result, the state will face higher future costs of renovating and replacing prematurely worn out facilities.

We recognize that other state agencies and the K-12 schools also have significant deferred maintenance backlogs. We believe, however, that the state should start by addressing the higher education problem because the size of the deferred maintenance backlog in higher education significantly exceeds the combined total of deferred maintenance needs in other state agencies.

# UC AND CSU FACULTY SALARIES: UPDATE

***Consistent with legislative intent, the California Postsecondary Education Commission staff have consulted with a technical advisory committee regarding the faculty salary methodology and plan to recommend to the commission that the committee's proposed compromise methodology be adopted.***

Every year, pursuant to Senate Concurrent Resolution 51 of 1965, the California Postsecondary Education Commission (CPEC) submits to the Governor and the Legislature an analysis of faculty salaries at the University of California (UC) and the California State University (CSU) compared to the average salaries of specified groups of higher education institutions. The UC and CSU use the average salaries of their respective comparison schools to determine the reasonableness of the faculty salaries they provide. The CPEC's analysis is based on a set of procedures and calculations that are collectively referred to as the "faculty salary methodology."

Figures 8 and 9 (see next page) display the faculty salary comparison institutions for UC and CSU, respectively.

In our *Analysis of the 1995-96 Budget Bill*, we noted that the last comprehensive review of the faculty salary methodology occurred roughly a decade ago. We also found that the existing methodology resulted in the calculation of faculty salary gaps—the amounts that average faculty salaries at UC and CSU fall below the salaries paid at their comparison institutions—that are too large, particularly at the CSU. This was primarily because the methodology did not adequately account for the significantly higher proportion of full professors at the CSU compared to its 20 comparison institutions. The UC's faculty staffing patterns are more in line with its eight comparison institutions.

To address this issue, we recommended the Legislature use a faculty salary methodology based on a comparison of the simple average CSU and UC faculty salaries with the simple average faculty salaries of their respective comparison institutions. We also suggested reviewing CSU's comparison institutions list because it contains at least one major doctoral-granting institution (the University of Southern California). Universities that grant significant numbers of doctoral degrees generally pay higher faculty salaries than institutions with teaching missions that are more similar to the CSU. (Under the state's Master Plan for Higher

Education, the CSU is authorized to offer doctoral degrees only through joint arrangements with the UC or private universities.) For this reason, we questioned whether such schools should be included in CSU's comparison group.

**Figure 8**

**The University of California Comparison Institutions for Faculty Salaries 1996-97**

| Public Institutions: | Private Institutions: |
|---|---|
| University of Illinois (Champaign-Urbana) | Harvard University |
| University of Michigan (Ann Arbor) | Massachusetts Institute of Technology |
| University of Virginia (Charlottesville) | Stanford University |
| State University of New York (Buffalo) | Yale University |

**Figure 9**

**The California State University Comparison Institutions for Faculty Salaries 1996-97**

**Public Institutions:**

- Arizona State University
- Cleveland State University
- George Mason University
- Georgia State University
- Illinois State University
- North Carolina State University
- Rutgers University (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

**Private Institutions:**

- Bucknell University
- Loyola University of Chicago
- Reed College
- Tufts University
- University of Southern California

The Legislature, per our recommendation, specified its intent in the *Supplemental Report of the 1995 Budget Act* that the CPEC, in consultation with a technical advisory committee, make recommendations on the appropriateness of addressing the above issues to the Legislature, the Department of Finance (DOF), and the Legislative Analyst's Office (LAO) by December 1, 1995.

***Group Recommends New Methodology.*** During fall 1995, the CPEC convened a technical advisory group to review the faculty salary methodology composed of representatives from the UC and CSU administration and faculty, the DOF, the LAO, and other interested parties. In addition to the issues noted above, the systems raised two additional concerns:

- First, UC believes the existing methodology does not adequately reflect the fact that UC competes for faculty with both public and private institutions. The existing methodology places greater weight on the salaries at the larger institutions, which tend to be public institutions. Since public universities also pay less, UC feels the salary methodology places them at a competitive disadvantage.
- Second, CSU faculty believes the existing methodology does not reflect the fact that the majority of CSU faculty live in high-cost areas (such as the Los Angeles and San Francisco Bay areas), while the majority of the faculty in the CSU comparison institutions do not. The CSU provided comparison data for the cities in which its campuses and its comparison institutions are located to demonstrate this disparity. The CSU proposed to adjust the methodology to account for this issue.

Ultimately, members of the technical advisory committee developed a compromise faculty salary methodology. Under the compromise, the methodology would be changed to:

- Move half way from the existing weighted staff salary to the simple average salary comparison we recommended in our *Analysis.* This would better recognize the importance of actual staffing patterns at UC and CSU in relation to their respective comparison institutions.
- Adjust the UC calculation to recognize that UC competes for faculty roughly equally with public and private institutions;
- Adjust the CSU calculation to reflect that a higher proportion of CSU faculty are located in high-cost areas, compared to faculty at the CSU's comparison institutions.

The proposed compromise would maintain the existing comparison institutions for the UC and CSU, reflecting a prevailing view that the comparison institution lists appear reasonable when viewed as a whole. The representatives of the technical advisory group also suggested to the CPEC staff that the proposed methodology take effect in 1996-97. The group suggested another review of the methodology in time for consideration of the 1999-2000 budget, which would review the appropriateness of using the simple average faculty salaries to measure the salary gaps at UC and CSU and the appropriateness of the institutions on the CSU's comparison list.

We believe the proposed compromise faculty salary methodology is a reasonable one to use through 1998-99. It is also important, however, to review the methodology periodically to ensure that issues of interest to the Legislature are thoroughly considered. For this reason, we will continue to review the issue of comparability and the use of comparison institutions to set faculty salaries.

Under the existing methodology, the CPEC identified faculty salary gaps of 10.4 percent for the UC and 12.7 percent for the CSU in 1995-96 (before any faculty salary increases). If the proposed compromise methodology is adopted for 1996-97, there would continue to be a 10.4 percent gap for the UC, but the CSU gap would decline to 9.5 percent. At the time of this analysis, the CPEC staff were anticipating that they would recommend to the commission that the suggested compromise be adopted. The commission will act upon its staff recommendations on the faculty salary methodology later in spring 1996.

***No Budget-Year Implications.*** As a practical matter, the issues we discuss above are not likely to have implications for the 1996-97 budget. Specifically, the UC budget proposes a 5 percent general faculty salary increase, plus merit salary adjustments for eligible faculty. The CSU budget proposes an overall 4 percent compensation increase, with specific allocations subject to collective bargaining. Even with these proposed increases, there would still be a faculty salary gap of about 5.4 percent at UC and CSU. (The actual CSU gap would depend on the results of collective bargaining.)

# MARGINAL COST AT UC AND CSU: UPDATE

***Proposed marginal cost calculations for the UC and CSU have recently been developed in line with legislative intent.***

Through 1991-92, the relationship between the budget and enrollment for the University of California (UC) and the California State University (CSU) was clearly defined. As enrollments changed, dollars were added or subtracted from the UC and CSU budgets based on agreed-upon cost calculations (called "marginal cost," as defined below) for serving new students in each of these systems. Beginning in 1992-93, this relationship was suspended. Faced with significant General Fund reductions and student fee increases, the Governor and the Legislature deleted Budget Bill language in the 1992 Budget Act that provided funding adjustments in the event of certain fluctuations (up or down) in enrollment.

In the *Supplemental Report of the 1994 Budget Act*, the Legislature expressed its intent that, beginning with the 1996-97 budget, the state return to the use of marginal cost as the basis for funding enrollment changes and that representatives from the UC, CSU, the Department of Finance (DOF), and the Legislative Analyst's Office (LAO) review the components of the marginal cost calculation and propose any modifications in the development of the 1996-97 budget. The Legislature also readopted the pre-1992 Budget Act language in the 1994 Budget Act to provide funding adjustments if actual enrollments are more than 2 percent above or below the enrollment targets. However, the Governor vetoed the language, stating that adjustments to the UC and CSU funding levels "should be addressed through additional legislative action when compared to other essential financial needs." (As a practical matter, actual UC and CSU enrollments since that time have not varied by more than 2 percent in any one year compared to the Legislature's enrollment targets for these systems, and thus the veto of this language has had no specific budget implications.)

Below, we define "marginal cost" and review recent actions that respond to the Legislature's intent that the calculation be reviewed in time for consideration of the 1996-97 budget.

***What Is "Marginal Cost"?*** "Marginal cost" of a university education is generally used to describe the various per-student costs of serving relatively small blocks of new students (such as 1,000). The marginal cost is often less than the average cost because it reflects what are called "economies of scale"—that is, certain fixed costs (such as for central administration) may change very little as new students are added to an existing campus. The major components of a marginal cost calculation generally include faculty costs, library services, student services (such as counseling and financial aid), and certain other administration costs. The marginal costs of a UC and CSU education are funded by the state General Fund and student fee revenues.

***Issues Related to Prior Marginal Cost Calculation.*** In response to the Legislature's directive, representatives from the UC, CSU, DOF, and LAO reviewed the marginal cost calculations that were in effect in 1991-92 and potential changes to them. The major issues raised about the 1991-92 marginal cost calculations generally fell into the following two categories:

- ***The Data Are Out-of-Date.*** The calculations have not been adjusted over roughly the past five years to reflect increases in actual costs.
- ***More Consistent Treatment of UC and CSU Is Needed.*** Some components of the calculations (such as the allocation of student fees toward marginal cost) need adjustment to reflect consistent treatment of the UC and CSU while still reflecting the systems' differing costs and missions.

The representatives, however, also noted that many parts of the marginal cost calculation continue to be reasonable. These include (1) determining the marginal cost for the budget year based on current-year costs and (2) setting the additional cost of hiring faculty to serve additional students at entry-level, rather than average, salaries.

***Overview of Proposed New Marginal Cost Calculations.*** The four agencies ultimately agreed to specific marginal cost calculations for the UC and CSU. The proposed calculations for each of the systems:

- Include in the marginal cost, half of the average cost of administration and 80 percent of average student services costs. Entry-level faculty salaries continue to be used.
- Update the cost data to reflect estimated costs for 1995-96 and consistent treatment between the UC and CSU.
- Do not "make up" for any past-year underfunding issues. (In some cases—such as in the area of instructional equipment replacement—however, the proposed new calculations appropriately include new costs created by adding new students.)

As was the practice through 1991-92, the marginal cost for each budget year would be updated to reflect estimated current-year expenditures. Finally, the General Fund and student fee revenues would support the total marginal cost in relation to the past year's "split" between the two funding sources (for example, the approximate 1995-96 "split" would be used as the basis for the 1996-97 calculation). The split is needed to calculate the General Fund amount that must be added for the support of new students.

Under the proposed calculations, the marginal cost identified for UC in 1996-97 would total $8,730 ($6,809 from the General Fund and $1,921 from student fee revenues). The marginal cost identified for the CSU for 1996-97 would total $5,917 ($4,734 from the General Fund and $1,183 from student fee revenues).

Given changes in budgeting practices that occurred over time in both segments, it is difficult to compare the proposed marginal costs to those that existed in 1991-92. For the UC, our review of the General Fund portion of the marginal cost indicates that the proposed 1996-97 amount ($6,809) is $809, or about 14 percent above the 1991-92 level of $6,000. This increase is in line with the cumulative impact of inflation over the time period. For the CSU, the total marginal cost in 1992-93 (the most recent year in which a detailed calculation is available) was about $4,500, compared to a total proposed 1996-97 amount of $5,917. However, it is not meaningful to compare the two figures because the 1992-93 figure excluded significant costs, such as costs for some student services.

***Conclusion.*** There is no particular "correct" way to calculate marginal cost. We believe, however, that the marginal cost agreement described above is a reasonable one and it also treats the UC and CSU in a consistent manner. The CSU's proposed 1996-97 budget plan would fund anticipated enrollment increases based on the proposed marginal cost. The UC indicates that it intends to implement the proposed marginal cost as soon as possible, but not later than 1997-98. The systems' plans appear reasonable in light of the Legislature's intent that the state return to the use of marginal cost as the basis for funding enrollment changes.

HIGHER EDUCATION

# DEPARTMENTAL ISSUES

## UNIVERSITY OF CALIFORNIA (6440)

The University of California (UC) includes eight general campuses and one health science campus. The budget proposes General Fund expenditures of $2 billion. This is an increase of $124 million, or 6.5 percent, from estimated current-year expenditures. The General Fund increase is primarily for salary, cost, and enrollment increases and additional costs for lease-payment bonds, as shown in Figure 3 of the higher education overview section. The budget estimates that the UC's full-time-equivalent (FTE) enrollment will be roughly 153,500 in 1996-97. It does not anticipate a general fee increase for undergraduate and graduate students, though it would continue an ongoing multiyear plan to phase in fee increases for students in professional schools (such as law or medicine) to the average of fees charged by comparison public universities.

### Teaching Hospitals Net Gains: Update

***Pursuant to legislative intent, we have reviewed the University of California information on teaching hospital net gains, and find that they are below the 5 percent level we have identified as being needed for hospital equipment and capital outlay purposes. Consequently, we have not identified additional net gains as being available for redirection to the campuses for critical funding needs.***

Over the past two years, we have recommended redirecting the amount of UC teaching hospital net gains that exceeded the 5 percent level we identified as being needed for hospital equipment and capital outlay purposes. Specifically, we recommended that the UC reallocate teaching hospital net gains in excess of 5 percent of net operating revenues from the hospitals to the campuses, and dedicate the funds towards critical campus funding needs in the areas of deferred maintenance, instructional equipment replacement (IER), and library materials.

In 1994-95, the Legislature adopted our recommendation and in the *Supplemental Report of the 1994 Budget Act* provided that $18 million from 1992-93 and 1993-94 be redirected for these purposes in 1994-95. Last year, we identified an additional $9 million in net gains above 5 percent from 1992-93 and 1993-94 that could be redirected for these purposes. The Legislature adopted a compromise that specified legislative intent in the *Supplemental Report of the 1995 Budget Act* that $5.5 million of the $9 million be redirected to the campuses for deferred maintenance. (The language did not specify legislative intent regarding expenditure of the remaining $3.5 million.)

Later, the final 1995 budget package resulted in a $9.5 million funding shortfall for the UC. The UC Office of the President states that based "on discussions with state representatives, the University had been planning to shift $5.5 million of state support from the hospitals to deferred maintenance on a one-time basis—but that was prior to the development of the budget shortfall. Given the changed circumstances, the hospital funds will be utilized to help meet the shortfall (in 1995-96)."

***No Additional Net Gains Above 5 Percent.*** In the *Analysis of the 1995-96 Budget Bill*, we noted that the UC's projections for 1994-95 and for several years thereafter indicated that the UC's teaching hospitals will experience financial difficulty due to a variety of factors, including an expected decline in the number of patient days; a decrease in the rate of reimbursements from Medicare, Medi-Cal, and disproportionate provider payments; and changes expected because of the emerging managed care environment. Consequently, the UC's projections indicated that the UC hospitals will not achieve annual net gains above 5 percent in the near future. The Legislature subsequently specified its intent in the *Supplemental Report of the 1995 Budget Act* that the UC report to the Legislature by December 1, 1995 on the net gains achieved in 1994-95 and that the Legislative Analyst include a review of the University's report in its *Analysis of the 1996-97 Budget Bill*.

Our review of the UC's report indicates that the UC hospitals realized a net gain of 4.9 percent in 1994-95 and are projected to realize a net gain of 2.2 percent in 1995-96. Consistent with our previous analyses, we therefore have not identified any funds that are available for redirection from this source.

## Teaching Hospitals Long-Range Planning Report

***Consistent with legislative intent, the UC has engaged in a consultation process regarding the long-term implications of managed care and other health care changes for support of medical education in teaching hospitals.***

In the *Analysis of the 1995-96 Budget Bill*, we noted that the Legislature needs information on the long-term implications of managed care and potential federal funding changes on the UC teaching hospitals. The Legislature specified its intent in the *Supplemental Report of the 1995 Budget Act* that the UC, in consultation with other hospitals with a significant medical education component, report at hearings on the proposed 1996-97 budget regarding options for addressing the impact of future changes in the health care environment.

***Changes in the Medical Industry Are Already Affecting UC Hospital Practices***. Based on our site visits to UC teaching hospitals and our review of various hospital programmatic and funding information, we find the hospitals have significantly reduced costs and changed medical education practices in response to cost-cutting pressures related to managed care. For example, after an extensive medical consultation and review process, one hospital we visited cut the length of hospital stay required for a particular type of heart surgery almost in half, with no reported adverse effect on patient outcomes. Other common changes include providing cost-benefit information on various prescription drugs and medical tests to medical staff to encourage the use of cost-effective medical practices.

Throughout our visits, however, UC officials voiced concerns that potential reductions in federal Medicare support for medical education and cost pressures related to managed care may eventually result in (1) significant unfunded medical education costs and / or (2) reductions in the level of medical education provided at UC teaching hospitals and other hospitals with significant teaching components. The UC indicates that teaching hospitals have a “competitive cost disadvantage” because they need more resources than other hospitals to accomplish their core teaching mission. For example, medical interns and residents need practice in reviewing various tests and observing the relative impact of various procedures. However, providing sufficient levels of practice can be costly.

***UC Consulted as Requested***. Over the past year, the UC consulted with other educational institutions that operate teaching hospitals (such as Stanford University and the Charles R. Drew University of Medicine and Science) and associations that represent other hospitals with a significant medical education component to address the Legislature's intent. This effort seems timely, given that the U.S. Congress has considered various budget reductions for medical education, particularly in Medicare. (At the time of this analysis, final federal actions on these proposals had not been taken.)

The UC indicates that it will provide a status report on the actions it has taken to address legislative intent and on related federal budget actions during budget hearings. We will comment on the UC's report, as appropriate, during the hearings.

## Progress Report on Faculty Workload

Chapter 776, Statutes of 1993 (SB 506, Hayden) expressed the Legislature's intent that courses required for normal progress to a baccalaureate degree be provided in sufficient numbers at the UC. Chapter 776 requires the Legislative Analyst to review and analyze the annual reports the UC submits on faculty workload. The 1995 report provides trend data indicating that (1) total student credit hours per student increased by 0.8 percent from 1990-91 through 1993-94 and (2) faculty teaching workload, as measured by the number of classes taught and student credit hours per faculty member, increased by 6.5 percent and 6.7 percent, respectively. Compared to historic trends, the change in faculty teaching workload represents a moderate increase in our view.

The report indicates that campus “faculty and administrators believe that the courses necessary for graduation are available to students.” The data presented in the report would tend to support this conclusion. The latest available time-to-degree data for the UC (for freshmen entering in Fall 1986 who graduated within six years) indicate that the average time to degree is just over four years—13.4 quarters.

The UC's 1996 faculty workload report was due to the Legislature by February 1, 1996. We will comment on it, as appropriate, during budget hearings.

# CALIFORNIA STATE UNIVERSITY (6610)

The California State University (CSU) consists of 22 campuses. The budget proposes General Fund expenditures of $1.8 billion, an increase of $96 million, or 5.7 percent, from estimated current-year expenditures. This increase would support salary, price, and enrollment increases and additional costs for lease-payment bonds as shown in Figure 3 of the higher education overview section. The budget estimates that CSU's full-time-equivalent (FTE) enrollment will be about 254,400 in 1996-97. No general student fee increase is proposed.

## Legislative Oversight: Faculty Workload

***We recommend that the Legislature adopt supplemental report language to ensure that a recent contract agreement with the California Faculty Association will not result in a decrease in faculty teaching workload and direct the California State University to report on the actual impact of the contract's faculty workload provisions beginning in 1996-97.***

The CSU's primary mission under the Master Plan for Higher Education is undergraduate instruction and graduate instruction through the master's degree. The CSU is also authorized to (1) offer doctoral programs jointly with the University of California and private universities and (2) support research related to its instructional mission.

The Legislature has expressed considerable interest in the amount of time faculty spend teaching. In 1992-93 and 1993-94, the Legislature adopted language in the *Supplemental Report of the Budget Act* deferring a planned reduction in faculty teaching workload, and expressing legislative intent that courses required for normal progress to a baccalaureate degree not be reduced.

Prior to 1995-96, CSU faculty workload consisted of 12 units of direct instruction and three units of instruction-related responsibilities per semester. Direct instruction is generally defined as four three-unit courses per semester. Instruction-related activities generally include student advising, committee work, and community service.

In October 1995, the CSU trustees and the California Faculty Association (CFA) reached a contract agreement for 1995-96 through 1997-98 that would eliminate the faculty workload standard. The contract instead specifies that each campus department's workload assignments must meet departmental and student needs. The CSU has characterized the change as necessary to give additional flexibility to campus departments to meet student demand for courses. To gauge the impact of this change, the CSU and the CFA have agreed to continue reporting workload in the traditional teaching unit manner.

Some changes in workload standards may be needed to accommodate changes in the way courses are taught. For instance, measuring the teaching workload of distance learning and computer-assisted courses (where the development workload is high) can be difficult.

We have discussed the proposed changes with CSU and it is not clear to us whether the elimination of the teaching unit standards will lead to an increase or a decrease in faculty workload. We are concerned, however, that the contract's workload provisions may result in a decrease in faculty teaching workload. The Legislature has not been presented with the opportunity to review any change in faculty workload and the need for a decrease has not been substantiated. In fact, the *CSU Faculty Workload Study* indicates that in 1988-89 (the last time this information was collected), the total workload (including teaching and research) at CSU and selected public institutions was roughly comparable, although a greater proportion of the workload at CSU was in teaching rather than research. The CSU's higher teaching workload and lower research workload reflects the CSU's mission under the Master Plan for Higher Education.

To address these concerns, we recommend that the Legislature specify its intent that the recent contract agreement with the CFA not result in a decrease in faculty teaching workload. This is consistent with the Legislature's actions in 1992-93 and 1993-94.

We also recommend the Legislature require CSU to report on the effect of the new contract provisions on faculty workload. This information could be made available by aggregating the workload information that CSU collects from each campus department into systemwide and campus totals. Accordingly, we recommend that the Legislature adopt the following supplemental report language:

> It is the intent of the Legislature that faculty teaching workload not decrease at the CSU. It is also the intent of the Legislature that the CSU provide a preliminary report to the legislative fiscal and policy committees, the Joint Legislative Budget Committee, the California Postsecondary Commission, and the Department of Finance by December 1, 1996 summarizing faculty workload indicators systemwide and on each campus (or a representative sample of campuses) in 1995-96 compared to 1994-95. The indicators shall include, but not be limited to, the level of direct faculty instructional workload, independent study, and assigned release

time as measured by weighted teaching units, and the number of student credit units per faculty member. It is further the intent of the Legislature that the CSU provide a final report on these issues, incorporating data from 1996-97, to the agencies cited above by December 1, 1997.

## One-time Carryover Funds: Update

***We find that the California State University has generally observed legislative intent regarding $20 million in one-time carryover funds that are available in the current year. We recommend that the Legislature adopt supplemental report language specifying its priorities regarding how carryover funds are generated and used in 1996-97.***

The proposed budget identifies $20 million (excluding lease-payment bond funds) in one-time carryover funds available in 1995-96. Figure 10 shows CSU's expenditure plan for the funds. Consistent with past practice, the 1995 Budget Act permits CSU to carry over (or "reappropriate") General Fund monies for two years. The language also requires CSU, by September 30 of specified years, to report to the Joint Legislative Budget Committee (JLBC) and the Department of Finance (DOF) on the amounts of funding carried over and the uses of the funds. (The proposed 1996-97 Budget Bill continues the carryover authority and reporting language.)

**Figure 10**

**California State University Expenditure Plan for One-Time Carryover Funds 1995-96[a]**

**(In Millions)**

| | Carryover From | | |
|---|---|---|---|
| **Use** | **1993-94** | **1994-95** | **Total** |
| Discretionary | $0.6 | $0.5 | $1.1 |
| Campuses | 7.1 | 7.2 | 14.3 |
| Systemwide office | 2.3 | 2.2 | 5.5 |
| **Totals** | **$10.1** | **$9.9** | **$20.0** |

[a] Detail may not add to totals due to rounding.

In our *Analysis of the 1995-96 Budget Bill*, we raised a number of issues about the particularly high level of one-time funds carried over from prior years ($41 million). Most importantly, we noted that over half of the funds represented “forced savings” that may have been generated by limiting student access. We recommended that the Legislature establish limits on, and priorities for, the use of one-time carryover funds.

The Legislature adopted language in the *Supplemental Report of the 1995 Budget Act* specifying its intent regarding carryover funds. The language also called for the Legislative Analyst's Office (LAO) to report its findings on whether CSU has observed the Legislature's intent in the *Analysis of the 1996-97 Budget Bill.*

Below, we discuss the Legislature's intent regarding carryover funds and CSU's proposed expenditure plan for the funds. Then, we assess whether CSU has observed the Legislature's intent.

***Legislative Intent.*** The supplemental report language specifies legislative intent that CSU use its existing internal budget consultation process in determining the use of carryover funds. The language also states the Legislature's intent that carryover funds available in 1995-96 shall not be generated by:

- A reduction in the specified enrollment level of 252,000 students (plus roughly 400 students at the California Maritime Academy);
- A reduction in the quality of instruction, including but not limited to student-faculty ratio and time-to-degree;
- Any increase in student fee levels.

***CSU's Proposed Expenditure Plan.*** As Figure 10 shows, most of the one-time carryover funds that are available in 1995-96 were originally allocated to the campuses and the systemwide office. The CSU advises that these funds were reappropriated back to the campuses and the systemwide office (as has been the historic practice). Only $1.1 million of the $20 million represents “discretionary” funds that were not reserved for a particular purpose. The CSU allocated these funds for enrollment growth at certain campuses.

***LAO's Comments.*** Our analysis shows that, in contrast to last year, the $20 million in one-time carryover funds available in 1995-96 falls within a normal amount of carryover for CSU—that is, the savings do not appear to have been “forced.” We also find that, consistent with legislative intent, the carryover did not result from fee increases, reductions in specified enrollment levels, or in the quality of instruction as measured by the student-faculty ratio. (Recent time-to-degree information is not available for analysis.)

It also appears that the use of the “discretionary” portion of the carryover funds was subject to existing internal CSU budget consultation processes. Specifically, CSU staff and a representative of the CFA informed us that the use of these “discretionary” funds was discussed at an October 1995 meeting.

Accordingly, we believe CSU's actions regarding carryover funds have generally been consistent with legislative intent. However, since it is not clear what level of consultation was envisioned by the Legislature, we are unable to assess whether the consultation meeting on the discretionary portion of the carryover funds met the Legislature's expectations.

***Recommendation on 1996-97 Carryover Authority.*** Consistent with legislative actions last year, we recommend the Legislature adopt supplemental report language again for the 1996-97 budget specifying its intent regarding how carryover funds shall be generated. We also recommend the Legislature specify its priorities for the use of the funds. Over the past several years, the Legislature has sought funding for deferred maintenance and instructional equipment replacement at CSU. Given the continuing needs in these areas, we recommend that these priorities be specified by adopting the following supplemental language:

> It is the intent of the Legislature that any funds reappropriated by this item shall not be generated by (1) a reduction in the budgeted 1996-97 enrollment level of 254,400, (2) a reduction in the quality of instruction, as measured by the student-faculty ratio and (if available) time-to-degree, or (3) an increase in systemwide fee levels. It is also the intent of the Legislature that the priorities for use of the funds shall be deferred maintenance and instructional equipment replacement. The use of the funds shall continue to be subject to existing internal CSU budget consultation processes. The CSU shall report to the Department of Finance and the Joint Legislative Budget Committee by September 30, 1996 the amount being reappropriated and the purposes for which the funds will be used. It is the intent of the Legislature that the Legislative Analyst report in its *Analysis of the 1997-98 Budget Bill* if it determines the CSU has not observed legislative intent as stated above.

# CALIFORNIA COMMUNITY COLLEGES (6870)

The California Community Colleges (CCC) provide instruction to about 1.3 million adults at 107 colleges operated by 71 locally governed districts throughout the state. The system offers academic and occupational programs at the lower-division (freshman and sophomore) level, basic skills education, and citizenship instruction.

The proposed 1996-97 CCC budget is $3.4 billion. This is an increase of $109 million, or 3.3 percent, above the amount provided in the current year. Of the proposed $3.4 billion, $1.6 billion is from the General Fund, $1.4 billion is from local property tax revenues, and the remaining support is from student fees, state lottery funds, and federal funds.

## LEGISLATURE'S COMMUNITY COLLEGE FUNDING OPTIONS

The options facing the Legislature for community college funding are complex. The Legislature must determine spending levels and priorities for both the current and the budget year. Current-year spending is an issue because more Proposition 98 funding is available for K-14 programs than was anticipated in the 1995 Budget Act.

The 1996-97 spending level for community colleges depends on the level of the Proposition 98 minimum funding guarantee assumed by the Legislature. This, in turn, depends on (1) General Fund revenue growth in 1996-97 and (2) whether the Legislature adopts the Governor's proposed tax cut. As we discuss in the K-12 priorities section (see Section E of this *Analysis*), the Legislative Analyst's Office's (LAO's) estimate of General Fund tax revenue growth—and therefore our estimate of the Proposition 98 minimum funding guarantee—significantly exceeds the budget's estimate.

To assist the Legislature with its deliberations on community college funding priorities, we developed three alternatives to the administration's spending proposals. The proposals are based on three possible scenarios regarding the level of Proposition 98 funding available to the community colleges. These scenarios are based on:

- Governor's Budget revenue projections.
- The LAO revenue projections, assuming the Legislature approves the proposed tax cut.

- The LAO revenue projections, assuming the Legislature rejects the tax cut.

In each of these alternative proposals, we base our recommendations on the following order of priorities:

- ***Fund Continuing Program Costs.*** Support of the current level of service in K-14 programs should receive the highest priority.
- ***Protect Existing Investment in Facilities and Equipment.*** Funding for maintenance and instructional equipment replacement should have a high priority.
- ***Use Existing Facilities to Capacity.*** The state should provide targeted funding for enrollment growth that enables colleges to use newly constructed state-funded facilities to capacity.
- ***Fund Program Improvement.*** The Legislature should support critical program improvement proposals and provide equalization monies to address historical inter-district funding differences.

Regardless of the revenue assumption adopted, we recommend approval of most of the Governor's Budget proposals for 1995-96 and 1996-97:

- Backfilling CCC student fee and property tax shortfalls and making minor adjustments in the level of funding for administration of fee waivers.
- Providing full enrollment growth and cost-of-living adjustment (COLA) for general purpose spending.
- Funding increased debt service costs related to prior-year use of lease payment bonds to fund construction of new facilities.

With regard to the funds remaining after these priorities have been addressed, recommendations differ somewhat depending on the revenue assumptions adopted by the Legislature.

## *1996-97 Proposition 98 Funds—Budget Revenue Assumptions*

### Fund Continuing Program Costs

***We recommend the Legislature redirect $6.9 million from proposed funding for enrollment growth at new facilities to support growth and cost-of-living adjustment for selected categorical programs.***

The budget proposes $942,000 to support growth and COLA for CCC categorical aid for remedial education. The budget, however, proposes no growth and COLA funding for other CCC categorical programs that have been a high legislative priority: Extended Opportunity Programs (services to socioeconomically disadvantaged students), Disabled Students Program and Services, and matriculation (admissions, assessment, advising). Without funding adjustments for increased costs and for increased numbers of students, these programs would be unable to provide the existing level of services to students in 1996-97. The amount necessary to provide growth and COLA for these three additional categorical programs is $6.9 million.

In order to maintain the existing level of services in these categorical programs, we recommend the Legislature redirect $6.9 million from catch-up funding for enrollment growth at new community college centers. The budget proposes $10 million for this purpose in addition to funding general purpose enrollment growth. The new centers were authorized through a statewide planning process to provide access to community college instruction in underserved areas of the state. Due to the fiscal constraints of the past several years, however, the state has not provided the growth funding necessary to support the number of additional students the centers were designed to serve.

We believe that the budget proposal to fund enrollment growth at new centers has merit. Our proposal would leave $3.1 million to be spent for this purpose. Moreover, we recommend additional funding for this purpose under our revenue scenarios (see below). Under the budget revenue assumptions, however, Proposition 98 funds are not sufficient to fund the proposed $10 million for growth at new centers and maintain the existing level of service in important categorical programs. In our view, continuing the current level of service in existing programs with ongoing demand should take priority over program expansion.

## Protect Existing Investment in Facilities and Equipment

***We recommend the Legislature redirect $8.7 million from deferred maintenance to regular maintenance (eliminate Schedule (o) of Item 6870-101-001, and increase Schedule (a) by $8.7 million).***

This is part of our proposal to provide a permanent solution to the deferred maintenance problem for the public higher education segments. In a later section of this analysis, we discuss the proposal in detail.

## *1996-97 Proposition 98 Funds— Legislative Analyst's Office Revenue Assumptions*

Figure 11 displays our recommended alternative spending plans if the Legislature adopts our higher projections of General Fund tax revenues and the Proposition 98 minimum spending requirement in 1996-97. The figure shows scenarios with and without the Governor's tax reduction proposal. In developing these alternatives, we assumed the community colleges would receive around 10 percent of additional Proposition 98 funds that would be available for K-14 programs under our revenue assumptions. This is roughly the share of total Proposition 98 funds proposed for the community colleges in the budget.

**Figure 11**

**Community College Funding Priorities**
**LAO Recommendations**
**1996-97 Proposition 98 Funds**

**(In Millions)**

| | LAO Compared to Budget | |
|---|---|---|
| | **With Tax Cut** | **With No Tax Cut** |
| **Fund continuing program costs** | | |
| Categorical programs | | |
| Growth and COLA | $7.6 | $7.7 |
| **Protect investment in facilities and equipment** | | |
| Instructional materials | 15.0 | 15.0 |
| Deferred maintenance | -8.7 | -8.7 |
| Maintenance and operations | 20.0 | 25.0 |
| **Use existing facilities to capacity** | | |
| Growth: new centers | 5.0 | 5.0 |
| Growth: other new facilities | 8.0 | 20.0 |
| **Fund program improvement** | | |
| Equalization | — | 14.0 |
| **Totals** | **$46.9** | **$78.0** |

Our alternatives would add $47 million to the budget's proposed level of CCC spending if the Legislature adopts the Governor's tax cut, and a total of $78 million if it does not. Under our alternatives, we recommend approval of all the 1996-97 budget proposals, except the proposed $8.7 million for deferred maintenance. We also recommend the Legislature adopt the plan we present below for spending these additional funds.

## Fund Continuing Program Costs

***We recommend the Legislature provide up to an additional $7.7 million to support growth and cost-of-living adjustment for selected categorical programs.***

As indicated above, we recommend the Legislature fund growth and COLA for CCC categorical programs that have been a high legislative priority. Under the budget revenue assumptions, we recommended an additional $6.9 million for this purpose as discussed earlier. Under the LAO scenarios, we recommend up to an additional $7.7 million. (This amount is slightly larger because other recommendations we make for the use of additional funds would result in a greater number of students.)

## Protect Existing Investment In Facilities and Equipment

***We recommend the Legislature provide augmentations of (1) $15 million for replacement of instructional equipment and library materials and (2) up to $16.3 million for maintenance and operation workload.***

***Instructional Equipment and Library Materials***. The budget proposes substantial *one-time* funding that would partially address existing equipment replacement backlogs. There remains a need, however, to ensure that colleges set aside sufficient funds on an annual basis to adequately address their ongoing needs for repair and maintenance of instructional equipment and library materials.

Recent estimates suggest that the ongoing annual cost of repairing and/or replacing existing CCC instructional equipment and library materials is roughly $100 million. Some of this need is filled by college spending from general purpose funds. There is no definitive information, however, on the amount spent for this purpose statewide. In our visits to colleges—particularly, in our reviews of vocational education programs—funding for this purpose is consistently mentioned as a critical need.

Given the need for replacement of instructional equipment and library materials we have observed in our site visits, we recommend the Legislature provide $15 million in 1996-97 to fund the CCC Instructional Equipment Replacement Program for the ongoing maintenance, replacement, and upgrade of instructional equipment and library materials. We further recommend that the Legislature continue its past practice of requiring districts to match every $3 of state funds provided under this program with $1 of district funds. The $15 million would then fund a $20 million effort.

***Maintenance.*** We recommend the Legislature provide an additional $11.3 million under the tax cut alternative and $16.3 million under the no tax cut alternative to support regular maintenance. This is in addition to redirecting $8.7 million from deferred maintenance to regular maintenance that we recommend above. This is part of our proposal to provide a permanent solution to the deferred maintenance problem for the public higher education segments, which we discuss in a later section of this analysis.

## Use Existing Facilities to Capacity

***We recommend the Legislature provide an additional $5 million for unfunded enrollment growth in new community college centers, and up to $20 million for unfunded enrollment growth in new regular campus facilities***

The budget provides $10 million for unfunded enrollment growth in new community college centers that have opened since 1991-92. The state authorized these centers to provide access to community college instruction in underserved areas. Due to the fiscal constraints of the past several years, however, the state has not provided the growth funding necessary to support the number of new students the centers were designed to serve. State funding of enrollment growth for new facilities on regular college campuses has also lagged.

The Legislature should take steps to ensure that community colleges more fully use the facility capacity that currently exists. The amounts of spending we recommend for this purpose are not sufficient to fully address capacity growth at the CCCs. We are concerned, however, that the colleges would have trouble increasing enrollments to full capacity in a single year. The Legislature could continue to address this enrollment issue in future years as revenues permit. Therefore, we recommend the Legislature:

- Provide a total of $15 million for enrollment growth in new community college centers (this would provide $5 million more than the budget proposal). The Chancellor's Office advises that this would cover half the total underfunding of enrollment capacity at new centers.

- Provide $8 million (under the tax cut alternative) to $20 million (under the no tax cut alternative) for facilities-related enrollment growth that has occurred on regular community college campuses. The Chancellor's Office estimates that total unfunded capacity growth on regular campuses (excluding new centers) is $70 million to $80 million.

### Fund Program Improvement

***Under the no tax cut alternative, we recommend that the Legislature provide $14 million from 1996-97 funds to reduce inter-district funding disparities.***

Given that the community colleges likely cannot absorb more enrollment growth funding in 1996-97 than we would suggest in previous recommendations, we recommend the Legislature use the $14 million that remains under the no tax cut alternative to fund inter-district equalization. Community college districts did not receive the same equalization funding that was provided to K-12 school districts in the 1980s. Consequently, significant funding disparities still exist between community college districts.

Under community colleges regulations, equalization funding is applied first to the district whose funding per standard unit of workload is lowest, until that district's level of funding matches the level of the next lowest district. Any remaining funding is applied to bringing both of these districts to the funding level of the next lowest remaining district, and so on.

At the writing of this analysis, the Chancellor's Office could not determine how many districts would benefit from the proposed level of equalization funding. We recommend that the Chancellor's Office report at budget hearings on the equalizing effects of this proposal.

## *1995-96 Proposition 98 Funds*

Figure 12 shows that the budget proposes $79.4 million in one-time Proposition 98 funding for the community colleges in 1995-96:

- Backfill of estimated 1995-96 shortfall in local property tax revenues ($9.4 million)
- Block grant for education technology, instructional equipment, and library materials ($52.5 million). Funds would be distributed to college districts in proportion to enrollment.
- Deferred maintenance ($17.5 million)

**Figure 12**

**Community College Funding Priorities**
**LAO Recommendations**
**1995-96 One-Time Funds**

**(In Millions)**

| | Budget Proposals | LAO Recommendations: Budget Revenues | LAO Recommendations: LAO Revenues |
|---|---|---|---|
| **Fund continuing program costs** | | | |
| Backfill property tax shortfall | $9.4 | $9.4 | $9.4 |
| **Protect investment in facilities and equipment** | | | |
| Deferred maintenance | 17.5 | 25.0 | 25.0 |
| Block grant | 52.5 | 44.5 | 55.5 |
| **Fund program improvement** | | | |
| Technology planning | — | .5 | .5 |
| **Totals** | **$79.4** | **$79.4** | **$90.4** |
| Difference from budget spending level | | — | $11.0 |

Figure 12 also shows our recommended alternative spending plan for 1995-96 Proposition 98 funds under the budget revenue assumptions and our revenue assumptions. Under either set of assumptions, we make the following recommendations (which are fully discussed in later sections of this *Analysis*):

- ***Fund Technology Planning.*** We recommend the Legislature fund the development of technology standards and planning guidelines that could be adapted for use by any community college.

- ***Increase Deferred Maintenance Funding, Require Local Match.*** We recommend the Legislature increase deferred maintenance funding from $17.5 million to $25 million. We also recommend the Legislature follow its existing practice of requiring community colleges to match state deferred maintenance funds dollar for dollar.

Under our revenue assumptions, the Legislature would have $11 million left to allocate after funding the budget proposals. We recommend the Legislature use these additional funds to fund augmentations for technology planning and deferred maintenance and increase the proposed block grant to $55.5 million. The block grant funds are needed to reduce existing repair and replacement backlogs for instructional equipment and library materials, and to undertake initiatives in education technology.

## DEFERRED MAINTENANCE

***We recommend the Legislature adopt a new policy toward deferred maintenance by (1) increasing funding for ongoing operations and maintenance and (2) using one-time 1995-96 funds to begin eliminating the backlog of deferred maintenance projects.***

The budget proposes $8.7 million for deferred maintenance in 1996-97. The budget also proposes $17.5 million in one-time funds for community college deferred maintenance projects from 1995-96 Proposition 98 settle-up funds. The settle-up monies are funds owed to K-14 education programs in 1995-96 under Proposition 98 due to an increase in the Proposition 98 minimum funding guarantee. These funds would be appropriated in the 1996 education budget trailer bill and, therefore, would not be available to colleges for spending until 1996-97. Thus, a total of $26.2 million in state funds earmarked for community college deferred maintenance projects would be available for spending in 1996-97.

The administration also proposes to waive the local match requirement for the $17.5 million in one-time funds, which would cut in half the program effect of the settle-up funds. (Existing law requires that community college districts provide a dollar-for-dollar match with district funds for any state funds they receive for deferred maintenance.) The budget proposes to keep the local match requirement in place for $8.7 million in ongoing funds.

As we note in our discussion in the higher education crosscutting issues section of this analysis, deferred maintenance has come to be seen as an ongoing program. The community colleges, for example, have received an appropriation for this purpose annually since the early 1980s. However, a deferred maintenance project is one that should have been done earlier under a properly functioning maintenance program. Thus, existence of deferred maintenance really represents a maintenance failure. As a result of this ongoing failure to properly maintain college facilities, the state and the colleges now face higher costs to repair and upgrade facilities.

In our crosscutting issues discussion, we propose a framework for addressing this problem. It involves a state-segment partnership that would:

- Adequately fund ongoing maintenance to ensure that no further maintenance projects are deferred.
- Prohibit adding new projects to existing deferred maintenance backlogs after October 1, 1996.

- Eliminate the backlogs of deferred projects over a period of several years.

Below, we use this framework as a basis for recommendations concerning deferred maintenance and ongoing regular maintenance funding for the community colleges.

## Adequately Fund Ongoing Maintenance

To prevent further deferral of current maintenance projects, the Legislature should ensure an adequate level of maintenance funding for the CCCs. Although it is very difficult to assess the community colleges' actual level of maintenance spending or need for additional maintenance funding, evidence of underfunding exists. The Chancellor's Office, for example, advises that the colleges add about $20 million in new deferred maintenance projects every year. However, this may not represent the full extent of underfunding. It is possible, for example, that colleges add only their most pressing projects, because deferred maintenance funding provided annually by the state is small compared to the size of the already existing backlog.

An alternative measure of the adequacy of maintenance funding is to compare current levels with an objective standard that is based on an "adequate" level of maintenance. Consequently, we measured CCC maintenance funding with the standard used by UC and CSU. Based on this standard, we estimate the amount of local assistance funding allocated by the Chancellor's Office to colleges for maintenance and operations is about $50 million below the "adequate" level.

As a result, we conclude that a $50 million increase in annual spending for maintenance would move CCC funding for maintenance to the standard used by the UC and CSU and prevent further deferral of projects. In keeping with our principle that adequate maintenance funding is a joint state-segment responsibility, we recommend the Legislature allocate up to $25 million in 1996-97 Proposition 98 funds to increase ongoing annual funding for regular CCC operations and maintenance.

We further recommend the Legislature require a dollar-for-dollar increase in local operations and maintenance effort as a condition of receiving these funds. The local match requirement means that up to $50 million in additional maintenance spending would occur as a result of the proposed $25 million increase in state spending.

***Funding Sources.*** In order to provide funding for the state's $25 million share, we recommend the Legislature first redirect $8.7 million from funds budgeted for CCC deferred maintenance in

1996-97 (eliminate Schedule (o) of Item 6870-101-001 and increase Schedule (a) by $8.7 million) to fund regular ongoing maintenance. The annual $8.7 million appropriation for deferred maintenance—with a local dollar-for-dollar match—gives the wrong incentive to districts. From a district perspective, the local cost of a deferred repair is half the cost of performing the repair as regularly scheduled maintenance. Thus, the current approach gives districts a strong fiscal incentive to add to the backlog.

If the Legislature adopts our higher revenue estimates, we recommend that it also allocate up to $16.3 million in Proposition 98 funds for community colleges operations and maintenance. (Increase Schedule (a) of Item 6870-101-0001 by up to $16.3 million.)

***Local Match.*** We further recommend the Legislature adopt the following budget bill language to control the appropriation of up to $25 million for operations and maintenance:

> Of the funds appropriated in Schedule (a) $25,000,000 shall be distributed by the Chancellor's Office to community college districts in proportion to districts' maintenance and operations workload, as defined in Title 5, Division 6, of the California Code of Regulations. As a condition of receiving these funds, a district shall provide to the Chancellor's Office a resolution from the district Board of Trustees indicating that it will increase its operations and maintenance spending from 1995-96 actual levels by the amount of the allocation plus an equal amount to be provided from district discretionary funds. The Chancellor may waive this requirement, case-by-case, based upon a review of a district's financial condition. Compliance with the resolution shall be reviewed under the district annual audit. Any allocation rejected by a district shall be distributed among the remaining districts in proportion to operation and maintenance workload.

## Prohibit Adding New Projects to Existing Backlogs

In our higher education crosscutting issues section, we recommend that the Legislature prohibit the CCCs (along with UC and CSU) from adding new projects to the deferred maintenance backlog. This is because each segment should be held accountable for doing ongoing maintenance—given sufficient funding as proposed above—so that no additional projects are deferred.

In the Crosscutting Issues section, we propose supplemental report language which would require the CCC (along with UC and CSU) to submit their lists of deferred maintenance projects—as they existed on January 1, 1996—to the LAO and the DOF no later than enactment of the 1996 Budget Act. The lists would be reviewed by the LAO, the DOF, and representatives of the segments to determine—based on criteria agreed to by the parties—which projects should be included in the deferred maintenance backlog. The backlog, as defined in this way, would become the target of deferred maintenance funding efforts. The segments would not be permitted to add new projects to this backlog.

### Eliminate the Backlog of Deferred Maintenance Projects

The Chancellor's Office advises that the existing CCC deferred maintenance backlog is about $90 million. The Chancellor's Office also indicates that, given sufficient funding, the community colleges probably have the ability to undertake up to about half of this workload in any given year. Consequently, we recommend the Legislature take steps to eliminate this backlog over a two-year period. For 1996-97, we recommend the Legislature eliminate $50 million of the backlog by providing a total of $25 million in 1995-96 one-time funds for deferred maintenance—$7.5 million more than provided in the budget—to be matched by community college districts on a dollar-for-dollar basis.

***Local Match.*** We recommend the Legislature reject the administration's proposal for an across-the-board waiver of the local match requirement for 1995-96 deferred maintenance funding. The state should maintain the local match requirement in order to encourage the colleges to do their part in addressing this backlog. Moreover, existing law already empowers the Community Colleges Board of Governors to waive the requirement on a case-by-case basis if a district is unable to provide the local match due to fiscal problems.

Consequently, we recommend that the Legislature adopt the following trailer bill language to control appropriation of the $25 million:

> The funds appropriated in this section shall be distributed by the Chancellor's Office to community college districts on a project-by-project basis based on priority of need for the project. Pursuant to Section 84661 of the Education Code, districts shall provide matching funds, unless the Board of Governors of the California Community Colleges waives this requirement in accordance with law.

## OTHER BUDGET ISSUES

### 1995-96 Block Grant: Redirect Funds To Support Community Colleges Technology Planning

***We recommend the Legislature redirect $500,000 in one-time funds from the proposed $52.5 million block grant to develop a standard education technology needs assessment and planning guide for use by community colleges.***

The budget proposes $70 million in one-time spending from 1995-96 Proposition 98 funds for community colleges. This includes a $52.5 million block grant to the colleges for instructional equipment, library materials, and education technology. Block grant funds would be allocated to community college districts in proportion to enrollment. These funds would be appropriated in the 1996 education budget trailer bill, and would not be available for spending by the colleges until 1996-97.

***Education Technology Planning.*** In our visits to community colleges over the past two years, we have observed wide variations in the use of technology. Some colleges have a very sophisticated strategic planning process, and are well along the way of putting technology in place to meet their priorities. Other colleges have only begun to plan. There is currently no formal process by which colleges that are relatively far along in this process can share what they have learned with colleges that have just begun. We believe that production of a planning guide, made available to all districts would help ensure that the state gets the greatest possible benefit from the funding it provides to the community colleges for technology improvements.

Accordingly, we recommend the Legislature redirect $500,000 from the proposed block grant to fund development of standard technology planning guidelines that could be adapted for use by any college. The guidelines should:

- Review the different ways telecommunications and computing technologies can improve instruction, student services, and administration.
- Identify a model technology planning process, from needs assessment to implementation, including facilities planning.
- Establish minimum standards and specifications for computing and telecommunications hardware and software necessary for collaborative inter-college projects.

Funds for this project should be awarded by the Chancellor's Office through a contract on a competitive basis. The Legislature should specify that any subcontracts be awarded on a competitive basis and only after review and approval by the Chancellor's Office.

## Community Colleges Enrollment Falls Despite $61 Million in Growth Funding

***We recommend the Legislature adopt Budget Bill language and supplemental report language to ensure that the CCC Chancellor's***

***Office uses budget-year growth funding to support increased enrollments.***

Under the state's Master Plan for Higher Education, the CCC are charged with being the point of access to higher education for the great majority of Californians. For this reason, preserving access to the CCC has been a major priority of the Legislature. Accordingly, the Legislature provided $32 million to fund CCC enrollment growth in 1994-95 and $29 million in 1995-96. Over the two-year period, this $61 million would have supported enrollment growth of about 3.2 percent. At the time this analysis was prepared, however, the CCC had allocated *none* of this funding to support enrollment growth. In fact, the number of FTES served by the CCC is estimated to have *declined* by about 9,900, or 1.2 percent during the period 1994-95 through 1995-96.

***Growth Funding Diverted to Other Uses or Allocated Late.*** Instead of allocating these funds to increase enrollments, the Chancellor's Office used them in both years to backfill budget reductions, and has held them in reserve to backfill anticipated shortfalls in local property tax revenues (community college general purpose spending is funded in roughly equal parts by the state General Fund and by local property tax revenues) and student revenues. The Chancellor's Office is able to do this because community college funding regulations treat growth funding as a kind of contingency reserve, to be allocated for increased enrollments only if it is not needed to (1) fund the prior year level of funding and (2) provide a COLA.

The Chancellor's Office now advises that it will allocate about $14 million of 1995-96 growth funding in February, because (1) the gap between actual 1995-96 property tax revenues and the budgeted level of property tax revenues is currently estimated to be less than expected earlier in the fiscal year and (2) the budget proposes to fully backfill any 1995-96 gap from the state General Fund (Proposition 98). It appears unlikely, however, that this mid-year allocation will result in any significant increase in 1995-96 enrollment. This is because colleges will already have begun their spring terms with conservative enrollment targets based on earlier advice from the Chancellor's Office that there would be no growth allocation for 1995-96. They have little flexibility at this time to add staff and expand enrollments. Colleges whose level of enrollment has historically exceeded the level funded by the state will be able to use this allocation to close the gap—without producing any increase in the actual number of students served.

***1996-97 Growth Funding Should Be Spent for That Purpose.*** The budget also provides $37.9 million for regular enrollment growth in 1996-97. In order to ensure that the Chancellor's Office allocates this full amount for growth at the beginning of the fiscal year, we recommend the Legislature prevent the Chancellor's Office from allocating growth funds for another purpose. Specifically, we recommend the following actions:

- Separately schedule the $37.9 million provided for growth in 1996-97. This would limit the use of these funds to increasing the number of funded FTES. We also recommend the following Budget Bill language:

  > Notwithstanding any other provision of law, the funds appropriated in Schedule (p) shall be allocated for growth in FTES, on a district-by-district basis as determined by the Chancellor of the California Community Colleges.

- Adopt supplemental report language stating the Legislature's intent concerning the level of FTES enrollment funded by the 1996-97 Budget Act. We will update the level of FTES enrollment during hearings:

  > The level of apportionment and growth funding reflected in Schedules (a) and (p) of this item is provided for a state-funded FTES enrollment level of 874,448 in 1996-97. The California Community Colleges Chancellor's Office shall report to the Legislature by March 1, 1998 on the actual level of state-funded FTES in 1996-97 and the reasons for, and impact of, any adjustments to this FTES level.

## Report on Performance Measures and Standards Not Progressing

***We recommend the Chancellor's Office report at budget hearings on reasons for its lack of progress in preparing a proposal for community colleges performance measures and standards, and provide a detailed plan for completing a satisfactory proposal by November 30, 1996.***

In the *Supplemental Report of the 1995-96 Budget Act*, the Legislature expressed its intent that the Chancellor's Office prepare a report identifying specific outcome measures that can be reliably compiled on an annual basis and a set of standards that define a level of performance that can reasonably be expected of individual colleges and the community colleges system as a whole. The report, due by November 30, 1996, must also identify any anticipated costs of compiling and reporting data related to these outcome measures and standards.

With the 16-month period for preparation of the report half gone, the Chancellor's Office has done no significant work on this project. We are now concerned that the report will not be completed on time, or will not fulfill the requirements laid out in the supplemental language. This report is a critical step in ongoing efforts by the Legislature to get an accurate picture of community college performance and to hold the colleges accountable for well-defined educational outcomes. We presented an in-depth review of community college outcome measures and accountability efforts in the *Analysis of the 1995-96 Budget Bill*, pointing out that the development of performance standards was a crucial first step toward a performance-based budgeting process for the community colleges.

Accordingly, we recommend the Chancellor's Office report at budget hearings on the reasons for its slow start on the report. We also recommend that the Chancellor's Office advise the Legislature of its plan for producing a report that complies with the supplemental language by November 30, 1996. The plan should include an outline of the report, address the level of staff resources devoted to the project, and indicate at what points in the preparation of the report it will consult with the California Postsecondary Education Commission (CPEC) as required by the supplemental report language.

## COMMUNITY COLLEGES CONTRACT EDUCATION

We recently reviewed a contract between the San Joaquin Delta College (Delta College) and the Richard A. McGee Correctional Training Center (the academy) that raises serious issues concerning contract abuses. Specifically, we found that Delta College uses this contract to claim state funding on the basis of instructional services that it does not provide and the academy uses the contract to augment its annual equipment budget without review by the Legislature.

### Background

***The Academy.*** The academy provides basic training for the California Department of Corrections (CDC) correctional officer cadets as well as a more limited amount of advanced training for other CDC personnel. The training is provided by senior correctional officers who are temporarily housed at the academy. The CDC General Fund support budget funds the salaries and operational costs of the academy.

During 1994-95, the CDC provided an estimated $28 million in support of academy operations, including $21 million for cadet compensation, $6 million for staff compensation and operating expenses, and nearly $1 million in expenditures for academy equipment. The CDC anticipates the academy budget in 1995-96 will be at a similar level.

***The Contract.*** The Delta College and academy contract allows correctional officer cadets to receive about 12 college credits for courses in the administration of justice that they receive at the academy. The CDC employees who provide the instruction sign individual instructional agreements with Delta College, and therefore the college views them as college employees. The current contract covers the 1994-95 and 1995-96 fiscal years.

The contract creates a fiscal arrangement that mutually benefits the two organizations. Delta Colleolleenefits because it counts the cadets served in basic training as its own students for the purpose of claiming state funds. The academy benefits because the college purchases equipment that is used at the academy.

In 1994-95, the 2,300 cadets trained at the academy generated 1,356 FTES for which the college claimed state funding. We estimate that Delta College realized a $1.8 million net gain from the contract in 1994-95. The 1994-95 gain did not come from a regular general apportionment of state funds because most of the FTES generated at the academy were in excess of the state's apportionment cap. However, because the college had enrollment over its cap—due to contract-generated FTES—it claimed $2.2 million in state categorical funding. From this $2.2 million, the college spent about $427,000 to purchase instructional equipment that was used at the academy.

## Legislative Action Needed to Curb Contracting Abuses

***We recommend that the California Community Colleges Chancellor's Office report at budget hearings concerning administrative or legislative steps necessary to prevent San Joaquin Delta College—or any other college—from using contracts to claim state funding for instructional services it does not provide.***

This contract raises three serious issues concerning state oversight of the CDC and community college programs. We discuss these issues in detail below.

***Contract Is an Abuse of State Funding System for Community Colleges.*** The Delta College / academy contract creates the fiction that the academy is an instructional program of the college. The college claims state funds because the students are supervised by the CDC instructors who, the college asserts, are Delta College employees. However, the instructors are paid by the academy, not Delta College. Consequently, Delta College receives substantial state funding (a net $1.8 million in

1994-95) in consideration of instructional services that, in reality, are provided by the academy. The academy gets around the state budget process, significantly increasing its annual equipment budget (by $427,000, or 40 percent, in 1994-95) with no legislative review.

We note with concern that Delta College has contracts of an identical nature with three other state agencies for 1995-96 and 1996-97:

- The California Department of Forestry and Fire Protection (CDFFP)—to serve cadets at the CDFFP Fire Academy in Ione.
- The California Department of the Youth Authority (CYA)—to serve trainees at the CYA basic academy at Stockton.
- The Department of Developmental Services (DDS)—to provide psychiatric technician training at the Stockton State Hospital.

Although we are not aware of other community colleges that currently have similar contracts with state agency training programs, we are concerned that staff at Delta College regard the academy contract as one example of a widespread practice.

***Contract May Be Illegal.*** The contract violates the spirit, and perhaps the letter, of CCC regulations that govern the claiming of state funds. Specifically, these regulations state that a community college district may not claim state apportionments for FTES generated by a class if (1) the district receives full compensation for the direct education costs of the class from any public or private agency or (2) attendance in the class is not open to the general public (*California Code of Regulations*, Title 5, Sections 58050(a)(4) and 58051.5).

Our review indicates the academy classes fail one, and perhaps both, of these tests. First, the academy funds the salaries and benefits of its instructors, all operating expenses of its instructional program, and the substantial majority of its equipment expenses. Delta College does provide some equipment funding—$427,000 in 1994-95—that technically could be viewed as supporting direct instructional costs of the academy. We could not determine what proportion of this amount could be considered a "direct" education cost. Delta College, however, received state funding of $1.8 million in excess of the equipment funding for work that it did not perform—work that was already funded once by the state through the CDC.

Second, the academy is not open to anyone but the CDC cadets. The CDC basic training classes are technically community college courses and therefore theoretically open to any student in the college's service area, as required by CCC regulations. In practice, however, a CDC cadet must be in residence at the academy to fully participate in basic training. A student may not be in residence at the academy unless selected by the CDC as a cadet. As a result, we conclude the academy is a CDC operation in every practical respect, and the college has no practical control over who attends it.

***Contract Circumvents Financial Accountability.*** The contract provides no assurance that additional equipment purchases made on behalf of the academy are justified or that the prices being paid for this equipment are reasonable. Community college purchases are exempt from review by the Department of General Services and the DOF. Moreover, the Legislature is not given the opportunity to weigh equipment purchases made on behalf of the academy against the equipment and other expenditure needs of other CDC programs and other state programs.

***Recommendations.*** Delta College should not receive state funding on the basis of instructional services that it does not provide. Moreover, it is contrary to sound budgeting and financial practices for the academy to augment its annual equipment budget by 40 percent without review by the Legislature or oversight by state control agencies.

The Legislature has already directed the Bureau of State Audits to review this contract and determine whether similar contracts exist between other community colleges and state agencies. In addition, we recommend:

- The CCC Chancellor's Office report at budget hearings whether existing regulations permit the CDC, the CDFFP, the Youth Authority, and the DDS personnel trained under contract to be claimed as Delta College students for the purpose of generating state funding. If the Delta College practice is determined to be illegal, we recommend that the Chancellor's Office explain what administrative actions it has taken against Delta College, and what measures it is taking to ensure that this practice is not occurring at other colleges.

- Enactment of legislation to unambiguously prohibit the Delta College practice beginning in 1996-97 if the Chancellor's Office determines that it is allowable under existing regulations.

We discuss further recommendations regarding this issue in our analysis of the Department of Corrections budget (see Section D of this *Analysis*).

# STUDENT AID COMMISSION (7980)

The Student Aid Commission (SAC) provides financial aid to students through a variety of grant, loan, and work-study programs. The proposed 1996-97 SAC budget is $614 million, which represents a $12 million (1.9 percent) increase compared to estimated current-year expenditures. The commission receives about 60 percent of its funding from federal funds. The General Fund provides most of the remaining funding ($252 million), which primarily supports the Cal Grant Program.

## THE CAL GRANT PROGRAM

The budget proposes a $10 million augmentation to raise the maximum annual Cal Grant award level for new grant recipients who choose to attend nonpublic institutions. This would raise the maximum Cal Grant A and Cal Grant B award for these students from the current level of $5,250 to about $7,200, an increase of $1,950 or 37 percent. New students who receive this higher grant level in 1996-97 would continue to receive it in future years as they continue their progress toward a degree until, eventually, all Cal Grant recipients at nonpublic institutions would be eligible for the higher maximum award. As a result, by 1999-2000, the annual cost of this proposal would be about $30 million.

The Cal Grant program has three statutory goals for the use of additional funds: (1) increase access to higher education by increasing the annual number of awards, (2) maintain a maximum award level for students at the University of California (UC) and the California State University (CSU) that covers mandatory fees, and (3) increase the degree of choice between public and nonpublic institutions by increasing the maximum award level for students who attend nonpublic institutions. The budget proposes no increase in the number of new Cal Grant awards. In addition it assumes no increase in student fees for UC or CSU, and therefore proposes no increase in the maximum grant level for recipients who attend either segment. Thus, the budget addresses only the last of these goals.

### Background

Cal Grants are the primary form of state-funded financial aid for students at postsecondary education institutions in California. In

1995-96, the state will spend an estimated $239 million from the General Fund to benefit about 92,000 college and university students. Cal Grants account for just under 6 percent of all financial aid received by students attending higher education institutions in California. Other major sources of student financial aid include Federal Family Education Loans (45 percent of all aid), various federal grant programs (25 percent), and institution-based aid (24 percent).

There are three types of Cal Grants. Figure 13 summarizes the purpose, eligibility, amount of award, and number of new awards granted annually for each type. Generally:

- ***Cal Grant A*** provides a degree of choice among private and public institutions to students who are both financially needy and academically worthy.
- ***Cal Grant B*** provides access to postsecondary education for students with the greatest financial need.
- ***Cal Grant C*** helps financially needy students pay for postsecondary vocational programs.

The Legislature has established in statute the following goals for the Cal Grant program:

- Increase access to postsecondary education by providing enough first-year awards to cover one-quarter of all graduating high school seniors.
- Maintain access to public institutions by providing a maximum award for students attending UC and CSU that covers at least mandatory systemwide and campus-based student fees.
- Ensure a degree of choice between public and nonpublic institutions by setting the maximum award for recipients attending nonpublic institutions at the General Fund cost of educating a student at public four-year postsecondary institutions. This standard is defined as the average CSU cost of instruction and academic support, plus the average of UC and CSU systemwide and campus-based student fees.

Full achievement of these goals would cost hundreds of millions of dollars. In the discussion that follows, however, we use them as a yardstick to show where the Cal Grant program currently stands relative to the Legislature's policy goals, and to compare the effects of the budget proposal with the effects of alternative approaches to expanding the program.

**Figure 13**

## Comparison of Cal Grant Programs 1995-96

| Cal Grant A | Cal Grant B | Cal Grant C |
|---|---|---|
| | **Purpose** | |
| Choice—based on financial need and academic performance | Access—based primarily on financial need, preference for initial attendance at community college | Vocational—based on financial need |
| | **Eligibility** | |
| Income ceiling: $52,200 for dependent student with five family members | Income ceiling: $32,249 for dependent student with five or more family members | Income ceiling: Same as Cal Grant A |
| Asset ceiling: $42,000 | Asset ceiling: $42,000 | Asset ceiling: $42,000 |
| Freshman GPA cutoff:<br>UC/CSU: 3.47<br>CCC: 3.19 | Applicants ranked based on family income, family size, GPA, family education background, and marital status of parents | Applicants ranked based on work experience, educational performance, and recommendations |
| Plan to enroll at least two years at UC, CSU, or nonpublic institution | Plan to enroll at least one year at a college | Plan to enroll at least four months at community college, independent college, or vocational school |
| | **Average Family Income of New Recipients (1994-95)** | |
| $28,656 | $9,678 | $23,561 |
| | **Maximum Award** | |
| Tuition and fees:<br>Nonpublic: $5,250<br>UC: $3,799<br>CSU: $1,584 | Tuition and fees:<br>No award in the first year, then same as Cal Grant A | Tuition and fees:<br>Nonpublic: $2,360<br>UC: $2,360<br>CSU: $1,584 |
| Other costs: None | Other costs: Up to $1,410 | Other costs: Up to $350 |
| | **Number of New Awards Annually** | |
| 17,400 | 12,250 | 1,570 |
| | **Cost (in millions)** | |
| $165.5 | $71.7 | $1.7 |

Figure 14 compares actual numbers and levels of Cal Grant awards to these statutory goals for certain years (1980-81, 1990-91 and 1995-96). The Cal Grant program has never come close to providing the number of first-year awards referenced in the statutory goals. In the current year, the actual number of new awards is about half of the statutory target. Maximum Cal Grant A and B awards, however, have nearly kept up with student fee increases at UC and CSU. Currently, the maximum grant levels cover systemwide student fees at UC and CSU, but not mandatory campus-based fees.

**Figure 14**

**Cal Grants**
**Statutory Goals Compared to Actual Awards**
**1980-81, 1990-91, and 1995-96**

| | 1980-81 | 1990-91 | 1995-96 |
|---|---|---|---|
| **Goal: Number of awards** | | | |
| 25 percent of high school graduates | 60,543 | 58,541 | 65,095 |
| Actual number of new awards | 23,232 | 31,220 | 31,220 |
| Percent of goal | 38% | 53% | 48% |
| **Goal: Cover UC and CSU fees**[a] | | | |
| **UC** | | | |
| Weighted average tuition and fees | $776 | $1,820 | $4,123 |
| Maximum award | 774 | 1,820 | 3,799 |
| Percent of goal | 100% | 100% | 92% |
| **CSU** | | | |
| Weighted average tuition and fees | $226 | $920 | $1,878 |
| Maximum award | 225 | 920 | 1,584 |
| Percent of goal | 100% | 100% | 84% |
| **Goal: Support private institution recipients at level of public institution funding** | | | |
| Specified costs and fees at public institutions | $3,417 | $6,289 | $8,829 |
| Maximum award | 3,200 | 5,250 | 5,250 |
| Percent of goal | 94% | 83% | 59% |

[a] Cal Grant A and B.

Growth in maximum Cal Grant A and B awards for students at nonpublic institutions has not kept pace with growth in the statutory benchmark. Figure 14 shows that the proportion of the statutory goal covered by the maximum award fell from 94 percent in 1980-81 to 59 percent in 1995-96. Figure 15 shows that the proportion of Cal Grant A recipients who attended independent colleges and universities (ICU) decreased as the maximum Cal Grant A award covered a smaller share of ICU tuition and fees. (We use Cal Grant A for this illustration because the program accounts for about 90 percent of Cal Grants used at nonpublic institutions.)

**Figure 15**

**Cal Grant A Fee Coverage and Use Decline At Independent Colleges and Universities (ICU)**

| | 1980-81 | 1990-91 | 1995-96 | 1996-97 Proposed |
|---|---|---|---|---|
| ICU weighted average tuition and fees | $4,610 | $11,662 | $15,098 | $15,702 |
| Maximum Cal Grant award | 3,200 | 5,250 | 5,250 | 7,200 |
| Tuition and fees covered by Cal Grant | 69% | 45% | 35% | 46% |
| Proportion of Cal Grants used at ICUs | 43% | 31% | 29% | Unknown |

## Evaluation of the Budget Proposal

***We recommend the Legislature base its decision on the proposed $10 million augmentation on (1) the need to backfill federal cuts in financial aid and (2) the Legislature's willingness to commit to a $30 million long-term increase in the cost of the Cal Grant program.***

The budget proposal would narrow the gap between the maximum Cal Grant award and tuition and fees at California nonpublic postsecondary institutions. We have several concerns about it, however, that we address in detail below.

***Funds May Be Needed to Backfill Federal Spending Cuts.*** The state currently receives $9.7 million in federal funds through the State Student Incentive Grant (SSIG) program. The SAC uses these funds to maintain the Cal Grant program's number and level of awards. The fate of the SSIG program is uncertain, pending completion of federal budget negotiations. It seems likely, however, that program funds will be reduced by at least half (the President's and the Senate's proposal). The House proposes to eliminate the program.

***Proposal Will Have Little Influence on Students' Choice of Schools.*** In the budget year, it is unlikely that the Governor's proposal will influence very many students to attend a private institution instead of a UC or CSU campus. This is because students have already applied to colleges for the fall of 1996, and will have decided where to attend before enactment of the 1996-97 budget. Thus, an increase in Cal Grant award levels would be a one-time windfall either to (1) students who would have attended nonpublic institutions in any case, or (2) nonpublic institutions, if they adjust their institution-based aid packages lower to offset the Cal Grant increases. We have no data to determine the extent to which the higher Cal Grant awards would offset institutional aid.

We also find it unlikely that the proposal will influence very many students to attend a nonpublic institution in future years. Figure 15 shows that the budget proposal would increase Cal Grant coverage of tuition and fees at ICUs from 35 percent in 1995-96 to 46 percent in 1996-97, which would be about the same percentage as in 1990-91. Over the long-run, we estimate this level of tuition and fee coverage would result in redirection of about 1,100 students from the UC and CSU to ICUs, increasing the number of Cal Grant recipients at ICUs from about 15,000 to about 16,100. Without further increases in the maximum award, however, this effect would erode over time as tuition and fees increase.

***Proposal Addresses Only One of the Legislature's Goals.*** The budget proposal takes a step toward satisfying the statutory goal of using Cal Grants to provide needy students a degree of choice between public and nonpublic institutions. It does not, however, broaden overall student access to Cal Grants by increasing the number of available awards, which has also been a major state goal.

## Cal Grant Policy Alternatives

Given these concerns, we recommend the Legislature consider alternative ways of spending the proposed $10 million increase. Figure 16 shows estimates of the long-term effect of the budget proposal and some alternative budget-year strategies for the Cal Grant program. These options illustrate the consequences of different policies that the Legislature may wish to consider concerning (1) long-term spending increases for Cal Grants and (2) the balance of access and choice. The first set of options in Figure 16 shows three alternatives with a long-run annual cost of about $10 million—the same amount as proposed for 1996-97. The second set of options assume a long-term cost of about $30 million—the long-term cost of the budget proposal.

**Figure 16**

**Cal Grant Augmentation Options**

| Option | Maximum Nonpublic Award | Number of New Awards |
|---|---|---|
| **Long-Run Annual Cost of $10 Million** | | |
| **Backfill SSIG cut (if needed)**<br>Spend $9.7 million and maintain current service level | No change | No change |
| **Emphasize choice**<br>Spend $10 million to increase award (all recipients) | +$660 (13%) | No change |
| **Emphasize access**<br>Spend $3 million to increase number of new awards | No change | +1,150 (4%) |
| **Long-Run Annual Cost of $30 Million** | | |
| **Emphasize choice (budget proposal)**<br>Spend $10 million to increase award level only (new recipients only) | +$1,950 (37%) | No change |
| **Emphasize access**<br>Spend $10 million to increase number of new awards only | No change | +4,660 (15%) |
| **Balance choice and access**<br>Spend $5 million to increase award level (new recipients only)<br>Spend $5 million to increase number of new awards | +$960 (18%) | +2,130 (7%) |

***Limit Long-Run Annual Cost to $10 Million.*** Figure 16 shows that the Legislature can make modest progress toward the Cal Grant programs statutory goals for access or choice if it limits the ongoing annual cost of the 1996-97 augmentation to $10 million. It could use this amount to:

- ***Backfill Lost Federal Funds.*** The ongoing cost of backfilling the potential elimination of federal SSIG funds would be about $10 million. Without a General Fund backfill, the SAC would have to reduce numbers and / or levels of Cal Grant awards.

- ***Emphasize Choice.*** The Legislature could emphasize choice by spending $10 million in 1996-97 to raise the maximum award levels for all new *and existing* Cal Grant recipients at nonpublic institutions. Exercising this option would raise the maximum award level by $660, or 13 percent. An increase of this amount roughly equals the average projected 1996-97 increase in the weighted average tuition and fees at ICUs.

- ***Emphasize Access.*** In order to increase the number of new Cal Grant awards in 1996-97, but limit the long-run increase in Cal Grant spending to $10 million, the Legislature would have to spend less than $10 million for this purpose in 1996-97. Specifically, Figure 16 shows that a $3 million augmentation in 1996-97 devoted solely to increasing the annual number of new Cal Grant awards would have a long-run annual cost of $10 million. Choosing this option would raise the annual number of new Cal Grant awards by 1,150, or 4 percent.

***Accept a $30 Million Increase in Long-Term Annual Cal Grant Costs***. If the Legislature is willing to commit to long-run annual spending increases of $30 million for Cal Grants (the ultimate cost of the budget proposal), there are three options available. The options differ in the relative weight they give to increased access—an increase in the number of Cal Grant awards—and increased choice—an increase in the maximum award level for recipients at nonpublic institutions. One option shown in Figure 16 is the budget proposal, which emphasizes choice. The remaining two options are:

- ***Emphasize Access.*** If the Legislature spent the entire $10 million to increase the number of new Cal Grant awards, and made no change in the existing distribution of new awards among Cal Grants A, B, and C, 4,660 additional new awards could be offered annually, an increase of 15 percent from the current level of 31,220 grants.

- ***Balance Choice and Access.*** The Legislature could achieve a balance between increasing the number of new awards and increasing the maximum grant level for first-time students at nonpublic institutions by spending $5 million for each purpose. Figure 16 shows that this option would increase the maximum grant level for new recipients by $960, or 18 percent, and increase the annual number of new Cal Grant awards by 2,130, or 7 percent. As we indicated in our analysis of the budget proposal, an increase of this magnitude in the maximum grant level would probably have very little long-run effect on student decisions about whether to attend public or nonpublic institutions.

### Recommendation

Our recommendation concerning the proposed $10 million increase in Cal Grant funding depends on (1) federal action on the SSIG program and (2) the level of long-run spending increases the Legislature is willing to make for the Cal Grant program:

- ***Maintain the Existing Level of Service if SSIG Funding Is Eliminated***. If the federal government eliminates funding for the SSIG program, we recommend the Legislature (1) provide a $10 million General Fund augmentation for the Cal Grant program to backfill the loss of federal funds and (2) direct the SAC to maintain the program's existing level of service.
- ***Delete Augmentation if Long-Run Cost of About $30 Million Is Not Acceptable.*** If the Legislature is not willing to commit to long-run increases of about $30 million in the annual costs of the Cal Grant program, we recommend the Legislature reject the proposed $10 million augmentation. As illustrated in our discussion above, little lasting progress can be made toward the statutory goals of the program at a lower level of long-term spending. We believe the Legislature could better use the $10 million to address other program priorities.
- ***Balance Choice and Access if Long-Run Cost of About $30 Million Is Acceptable.*** We recommend that the Legislature provide a $10 million increase in Cal Grant spending only if it finds acceptable long-run increases of about $30 million in the annual cost of the Cal Grant program. In this case, we recommend that the Legislature direct the SAC to designate half of the funds to increase the number of new grants and half to increase the maximum award level for first-time grant recipients in nonpublic institutions. This allocation would allow the state to make balanced progress toward two statutory goals of the Cal Grant program.

## OTHER ISSUES

### The Student Aid Commission Operating Structure Under Review—Budget Proposal for SAC Operations May Be Revised

***We withhold recommendation on proposed augmentations of $138,000 from the General Fund and $2,707,000 from the State Guaranteed Loan Reserve Fund (59.7 personnel years), until ongoing administrative reviews of the SAC's operating structure are complete and any resulting budget revisions have been submitted by the administration.***

The budget proposes to augment SAC operations by 59.7 personnel years in 1996-97 at a cost of $2.8 million—$138,000 from the General Fund and $2,707,000 from the loan fund. The budget also advises that the administration is reviewing the administrative structure of the SAC. When the review is concluded, the administration may propose additional resources for the SAC. The SAC itself has recently completed a revised statement of goals and strategies and will soon publish a work plan to implement them.

***The SAC Operating Structure Is Ripe for Review.*** We see these reviews of SAC's operating structure as positive developments, given the numerous management problems within SAC that have been identified by various state, federal, and private agencies. (The problems have been discussed by various legislative committees over the past two years and are summarized in our *Analysis of the 1995-96 Budget Bill.*)

Moreover, the environment in which the SAC pursues its student loan processing business has become significantly more uncertain and competitive during the last five years. In 1990-91, SAC processed about 87 percent of new guaranteed student loans in California. Competing loan guarantors accounted for the remaining 13 percent. In 1995-96, SAC staff estimate that SAC will process only about 54 percent of all new guaranteed student loans in California. The remaining 46 percent of new student loans will be handled by competing guarantee agencies (20 percent) and through direct lending by colleges and universities (26 percent). While the future of direct lending is the subject of ongoing federal budget negotiations, SAC staff anticipate that competition from out-of-state loan guarantee agencies will continue to sharpen.

Given this newly competitive environment, we believe that the Legislature should consider the following major policy issues as it evaluates the future of the SAC.

- ***Will SAC Continue to Be Viable as a State Agency?*** This issue centers on the question of whether a state agency can achieve the operational flexibility and emphasis on customer relations necessary to maintain sufficient market share and sustain its loan guarantee business. The SAC also would need to improve the automated Financial Aid Processing System to compete.
- ***Should SAC's Loan Guarantee Business Be Privatized?*** If so, how should the Cal Grant Program be administered? A new legal and administrative framework would be needed for SAC. The effect of privatization on state employees would also need to be explored.

- ***What Happens if SAC Goes Out of Business?*** If SAC—either as a state or a private agency—ultimately is driven out of the loan guarantee business by direct lending and out-of-state guarantee agencies, students attending institutions with higher loan default ratios—community colleges and proprietary institutions, for example—could find it more difficult or more expensive to get loans. What might the state do to maintain access to loans for these students?

***Proposed Augmentations Should Be Evaluated After the Administration's Review Is Complete.*** Most of the proposed augmentations for SAC operations appear to be justified on the basis of increased loan and grant processing workloads, given the current operating structure of the SAC. We withhold recommendation on them, however, pending our review of proposals for changes in the SAC's operating structure and revised spending proposals that may emerge this spring as a result of the administration's study of SAC operations. We will make recommendations on these proposals and SAC's overall structure during budget hearings.

## Student Aid Commission Ignores Budget Act Direction

***We recommend that the Student Aid Commission explain at budget hearings why it did not comply with the requirements of the 1995 Budget Act regarding its automated Financial Aid Processing System.***

The automated Financial Aid Processing System (FAPS) has been in operation since May 1990 for the Cal Grants Program and since January 1992 for the federal loan programs. The system is intended to fully automate Cal Grant and federal loan processing through a single state-operated system. It has so far cost about $18 million to develop and currently costs about $11 million annually to operate. Significant problems with FAPS have been major concerns of the Legislature. The Legislature also has expressed concern that a private contractor—Electronic Data Systems (EDS)—retained to operate and maintain FAPS on an “interim” basis in 1990 continues to do so through a series of contract extensions that have occurred without a competitive bidding process.

***State Auditor's Report: FAPS Problems Continue.*** In September 1994, an independent report by Deloitte and Touche identified several major shortcomings of FAPS. It suggested short-term strategies for addressing some of these shortcomings. For the long-term, however, the report indicated that SAC should partially, if not entirely, replace FAPS.

In the 1995 Budget Act, the Legislature directed the Bureau of State Audits to review the extent to which SAC had addressed the concerns and implemented the recommendations of the Deloitte study. The bureau reported on its review of FAPS in December 1995. The report concluded that, while SAC has made some improvements in FAPS, it has not yet addressed fundamental design deficiencies of the system. As a result, FAPS continues to run inefficiently, and still cannot adequately perform significant accounting functions.

***Reprocurement of FAPS Contract Delayed—EDS Contract Extended Again.*** In mid-1995, SAC hired a new executive director. The new director and his management team adopted a FAPS strategy that departs significantly from the plan represented to the Legislature by SAC during spring 1995 budget hearings. Under the prior management, the SAC had decided to stick with FAPS for the short-run, while working on upgrades to improve the system. After several delays, it was set to establish in September 1995 a new contract by competitive bid—referred to as “reprocurement”—for the ongoing operation and maintenance of FAPS.

The new management team, not convinced that continuation of FAPS is the most cost-effective solution to SAC's loan and grant processing problems, cancelled the reprocurement. Instead, SAC extended its existing contract with EDS to operate and maintain FAPS through June 1996 while it completes an analysis of several alternative long-term solutions. The analysis will address at least the following alternatives:

- Maintain and upgrade all existing FAPS systems.
- Abandon the existing FAPS accounting and finance systems and merge the parts of FAPS that work relatively well with a new accounting system.
- Replace FAPS with a system used by another loan guarantee agency.
- Develop new loan and / or grant processing systems from scratch.

The SAC also is negotiating with EDS to obtain a fee-for-service contract to operate and maintain FAPS for up to an additional two years while the SAC implements its preferred alternative.

***Recommendation.*** The Legislature has expressed considerable interest in the problems of FAPS because the success of FAPS is directly related to the ability of SAC to remain a viable guarantor of federal student loans. Moreover, the Legislature adopted language in the 1995 Budget Act requiring competitive bidding of contracts for operation and maintenance of FAPS. Specifically, the language required the SAC to (1) contract with the Bureau of State Audits to ensure that reprocurement of system maintenance provides for competition and (2) ask the vendor community to propose the best ultimate solution to the commission's loan and grant processing needs. By extending the EDS contracts, SAC has ignored the Budget Act language on competitive bidding. Accordingly, we recommend that SAC explain why it did not comply with this requirement. In addition, we recommend SAC report at budget hearings on its progress in determining the future of FAPS and what steps it is taking to ensure that any future reprocurement of FAPS or procurement of an alternative system is fully competitive.

## Legislative Oversight: Federal Audits

***We recommend that the Student Aid Commission report at budget hearings on its progress in resolving significant issues raised in a series of federal audits.***

In a series of audits conducted over the last five years, the U.S. Department of Education (USDE) concluded that SAC owed up to $220 million to the federal government based on various audit findings. Generally, these findings indicate that SAC did not provide sufficient oversight of loans in default or process lender claims and payments to lenders in a timely manner. The SAC has appealed all of these findings, maintaining that the USDE findings are based on small and statistically invalid samples. Moreover, while the SAC acknowledges lapses in its processing of defaulted loans and delays in paying lenders' claims, it argues that lenders and the federal government did not suffer any net monetary losses as a result.

In 1994, USDE rejected SAC's appeal for about $62 million of the total SAC audit liability and requested immediate payment of this amount from the SAC's loan fund. The SAC filed suit in U.S. District Court to prevent the transfer of funds. At the time of this *Analysis*, SAC staff advised that SAC and USDE continue to negotiate over the settlement of the lawsuit and remaining audit findings. They could not share specific information on the nature of the negotiations as a result of confidentiality surrounding the lawsuit. They expressed optimism, however, that the lawsuit and the remaining audits might soon be settled.

We recommend that the SAC report at budget hearings concerning the progress of its negotiations with USDE.

# LIST OF FINDINGS AND RECOMMENDATIONS

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## Crosscutting Issues

| | | |
|---|---|---|
| 1. | **Rethinking Deferred Maintenance.** All of the higher education segments have significant deferred maintenance backlogs. Recommend the Legislature begin a program of eliminating deferred maintenance and holding the segments accountable for providing adequate maintenance by: | F-13 |

- Increasing General Fund support for the segments' ongoing maintenance programs.
- Requiring each segment match the General Fund augmentation with funds already included in the budget.
- Beginning a process for eliminating UC and CSU deferred maintenance backlogs over a five- to ten-year period.

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| 2. | **UC and CSU Faculty Salaries.** Consistent with legislative intent, the California Postsecondary Education Commission staff have consulted with a technical advisory committee and developed a preliminary revised methodology for comparing UC and CSU faculty salaries to other specified higher education institutions. | F-23 |
| 3. | **Marginal Cost at UC and CSU.** Enrollment increases at UC and CSU are funded at the "marginal" cost of providing services to additional students. The updated calculations of marginal costs for both segments are reasonable. | F-27 |

## University of California

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| 4. | **Teaching Hospital Net Gains: Update.** The UC teaching hospital net gains are below 5 percent. Consequently, no funds are available for redirection to the campuses. | F-31 |

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| 5. **Teaching Hospitals Long-Range Planning Report.** Consistent with legislative intent, the UC has engaged in a consultation process regarding the long-term implications of managed care and other health care changes for support of medical education in teaching hospitals. | F-33 |

## California State University

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| 6. **Faculty Workload.** Recommend the Legislature adopt supplemental report language to (1) ensure that a recent contract agreement with the California Faculty Association will not reduce faculty teaching workload and (2) direct the California State University (CSU) to report on the actual impact of the contract's faculty workload provisions beginning in 1996-97. | F-35 |
| 7. **One-Time Carryover Funds.** The CSU has generally observed legislative intent regarding $20 million in one-time carryover funds that are available in the current year. Recommend that the Legislature adopt supplemental report language specifying its priorities regarding how carryover funds are generated and used in 1996-97. | F-37 |

## California Community Colleges

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| 8. **CCC Priorities—Budget Revenue Assumptions for 1996-97.** Under the budget revenue assumptions: | |
| • **Fund Continuing Program Costs.** Recommend redirecting $6.9 million from discretionary enrollment growth funding to support growth and COLA for selected categorical programs. | F-41 |
| • **Protect Existing Investment in Facilities and Equipment.** Recommend redirecting $8.7 million from deferred maintenance to regular maintenance. | F-42 |

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| 9. **CCC Priorities—LAO Revenue Assumptions for 1996-97.** Under LAO revenue assumptions: | |
| • **Fund Continuing Program Costs.** Recommend augmentation of up to $7.7 million to support growth and COLA for selected categorical programs. | F-44 |
| • **Protect Existing Investment in Facilities and Equipment.** Recommend augmentation of (1) $15 million for repair and replacement of instructional material and library materials and (2) up to $16.3 million for regular maintenance. | F-44 |
| • **Use Existing Facilities to Capacity.** Recommend augmentation of up to $25 million to fund enrollment growth in newly constructed community college facilities. | F-45 |
| • **Fund Program Improvement.** Recommend augmentation of up to $14 million to reduce inter-district funding disparities. | F-46 |
| 10. **1995-96 One-Time Funds.** Recommend the Legislature make the following changes to proposed 1995-96 expenditures: | |
| • **Deferred Maintenance.** Recommend $7.5 million augmentation for deferred maintenance and retaining the local match requirement for all deferred maintenance funds. | F-47 |
| • **Block Grant for Technology and Instructional Equipment.** Recommend $11 million augmentation of block grant for technology and instructional equipment under LAO revenue assumptions. | F-47 |
| 11. **Deferred Maintenance**. Recommend the Legislature adopt a new deferred maintenance policy by (1) increasing funding for ongoing operations and maintenance from 1996-97 funds and (2) using one-time 1995-96 funds to begin eliminating existing deferred maintenance backlog. | F-48 |

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| 12. **Technology Planning Needed.** Recommend the Legislature provide $500,000 in one-time funds to develop an education technology needs assessment and planning guide for community colleges. | F-51 |
| 13. **Growth Funding.** Recommend the Legislature adopt Budget Bill language to ensure that the CCC Chancellor's Office uses budget-year growth funding for increased enrollment. | F-52 |
| 14. **Performance Standards Report Not Progressing.** Recommend the Chancellor's Office report at budget hearings on its lack of progress and a detailed plan for completing the report by November 30, 1996. | F-54 |
| 15. **Action Needed to Curb Contracting Abuses.** Recommend the CCC Chancellor's Office report at budget hearings on steps to prevent colleges from using contracts to claim state funding for instructional services that are not provided. | F-56 |

## Student Aid Commission

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| 16. **Cal Grant Funding Increase.** Recommend the Legislature use the $10 million proposed Cal Grant increase to backfill federal spending reductions, if necessary. If not, and the Legislature is willing to commit to long-run annual cost of about $30 million, recommend spending $5 million for increased award level and $5 million for increased number of grants. | F-63 |
| 17. **SAC Operating Budget Under Review.** Withhold recommendation on $138,000 from the General Fund and $2,707,000 from the State Guaranteed Loan Reserve Fund (59.7 personnel years), pending completion of ongoing review of SAC's operating structure and submission of any resulting budget revisions. | F-67 |

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| 18. **Legislative Oversight: FAPS.** Recommend the SAC explain at budget hearings current plans for its automated Financial Aid Processing System (FAPS) and why it did not comply with requirements of the 1995 Budget Act regarding FAPS. | F-69 |
| 19. **Legislative Oversight: Federal Audits.** Recommend the SAC report at budget hearings on progress in resolving significant fiscal and operational issues raised in a series of federal audits. | F-71 |