LAO

The 2017-18 Budget:
Analysis of the May Revision Education Proposals

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Executive Summary

In this report, we analyze the May Revision education proposals. This year, the May Revision departs notably from prior years in that it funds above the required Proposition 98 levels—providing $1.6 billion more than required over the 2015-16 through 2017-18 period. This augmentation, coupled with another $594 million in higher Proposition 98 General Fund support that primarily covers lower property tax estimates, results in schools and community colleges reaping nearly all of the benefit under the May Revision. We analyze this approach and present alternative approaches in the first section of our report. We then analyze other key aspects of the May Revision, including the additional funding provided to accelerate implementation of the Local Control Funding Formula and unpause implementation of the budget agreement on child care and preschool. In the report, we also discuss many other proposals, including those related to community colleges, tuition increases at the universities, Cal Grant award increases, and the recent audit of the University of California.

CONTENTS

INTRODUCTION

In this brief, we analyze the Governor's May Revision education proposals. In the first section, we review changes in the overall Proposition 98 funding level. In the subsequent sections, we describe and assess the Governor's major proposals for K-12 education, child care and preschool, the California Community Colleges, the California State University, the University of California, and student financial aid.

PROPOSITION 98 OVERVIEW

Below, we explain, assess, and offer alternatives to the May Revision Proposition 98 budget package.

Major Changes

Relative to Governor's Budget, May Revision Increases Proposition 98 Funding by $1.5 Billion Over the Period. Figure 1 compares Proposition 98 funding under the Governor's January budget and May Revision. Compared with January, the May Revision proposes $1.5 billion in additional funding across the 2015-16 through 2017-18 period ($433 million in 2015-16, $22 million in 2016-17, and $1.1 billion in 2017-18). Under the May Revision, total Proposition 98 funding in 2017-18 is $74.6 billion, a $3.2 billion (4.5 percent) increase over the revised 2016-17 level. The May Revision also lowers local property tax estimates by a total of $664 million across the period, due primarily to secured property tax collections lagging expectations. Proposition 98 General Fund spending, by contrast, increases $2.2 billion across the period.

Administration Proposes to Fund Higher Than the Minimum Guarantee Each Year of Period. In most years, the state sets Proposition 98 funding equal to the minimum guarantee. The top part of Figure 2 displays our estimate of the minimum guarantee under the administration's May revenue projections. If the administration had funded at these levels, Proposition 98 funding compared with January would have been approximately $70 million lower across the period. (Specifically, funding would have been $558 million lower in 2016-17 and $489 million higher in 2017-18.) The

Figure 1

May Revision Increases Proposition 98 Funding Across the Period

(In Millions)

	2015-16	2016-17	2017-18
Governor's Budget			
General Fund	$48,989	$50,330	$51,351
Local property tax	19,681	21,038	22,160
Totals	**$68,671**	**$71,368**	**$73,511**
May Revision			
General Fund	$49,424	$50,602	$52,852
Local property tax	19,679	20,787	21,749
Totals	**$69,103**	**$71,390**	**$74,601**
Change			
General Fund	$435	$273	$1,500
Local property tax	-2	-251	-411
Totals	**$433**	**$22**	**$1,090**

Governor, however, proposes to provide $1.6 billion more than required across the period. As shown in the bottom of Figure 2, the May Revision funding level is $433 million above the 2015-16 guarantee, $580 million above the 2016-17 guarantee, and $601 million above the 2017-18 guarantee.

Figure 2

May Revision Funds Above the Minimum Guarantee Each Year of Period

(In Millions)

	2015-16	2016-17	2017-18
Estimated Minimum Guarantee[a]			
General Fund	$48,991	$50,023	$52,251
Local property tax	19,679	20,787	21,749
Totals	**$68,671**	**$70,810**	**$74,000**
May Revision Proposed Funding			
General Fund	$49,424	$50,602	$52,852
Local property tax	19,679	20,787	21,749
Totals	**$69,103**	**$71,390**	**$74,601**
Difference			
General Fund	$433	$580	$601
Local property tax	—	—	—
Totals	**$433**	**$580**	**$601**

[a] Assumes the state funds at the level required to meet the minimum guarantee each year. Reflects May Revision estimates of General Fund revenue, local property tax revenue, and other Proposition 98 inputs.

Funding Above Minimum Guarantee Accelerates Maintenance Factor Payment. In January, the administration estimated the state would end 2017-18 with an outstanding maintenance factor obligation of $1.6 billion. Under the May Revision, the administration estimates this amount at $822 million, a decrease of $805 million from the January level. The main factor explaining this decrease is the proposed increase in ongoing funding provided by the end of 2017-18. This additional funding effectively accelerates maintenance factor payments.

Administration Proposes Not Making Statutory Supplemental Appropriation Through 2020-21. A law enacted in 1990 requires the state to provide a supplemental appropriation when Test 3 is operative and the minimum guarantee otherwise would grow less quickly than the rest of the state budget. To date, the state has provided this supplemental appropriation six times, with the amount ranging from $68 million (in 1990-91) to $1.4 billion (in 2001-02). It has notwithstood the otherwise required appropriation once (in 1993-94). The May Revision proposes to not make this supplemental appropriation from 2016-17 through 2020-21. In the first two years of this period, the proposal does not have any direct effect on school funding. In 2016-17, the law would have required a supplemental appropriation of $347 million, but the May Revision funding level already exceeds this amount by $132 million. In 2017-18, the law requiring the supplemental appropriation would not be applicable because Test 2 rather than Test 3 is operative. In the latter three years of the period, the administration estimates that the proposal would reduce required Proposition 98 spending by $450 million in 2018-19, $290 million in 2019-20, and $110 million in 2020-21.

May Revision Eliminates Accounting Shift and Payment Deferral. The Governor's January budget included several proposals to reduce Proposition 98 spending in 2015-16 and 2016-17. The largest of these proposals involved (1) scoring $324 million in spending toward 2016-17 instead of 2015-16 and (2) deferring an $859 million payment for the Local Control Funding Formula (LCFF) from 2016-17 to 2017-18. The May Revision rescinds both of these proposals. For 2015-16, the result, when combined with several smaller adjustments, is a $433 million increase in spending relative to the January budget. For 2016-17, spending is $859 million higher because the state no longer defers the LCFF payment but $324 million lower because costs are no longer shifted from 2015-16—for a $535 million net increase. The May Revision, however, includes a new proposal to reduce spending that counts toward the guarantee. This proposal is to cover $513 million in LCFF costs with a one-time settle-up payment (we describe other changes to the Governor's settle-up proposal in the next paragraph). By making this designation, the state is able to cover the spending with Proposition 2 funds. Due to these savings, Proposition 98 spending in 2016-17 is only $22 million above the level included in the January budget.

Revises Settle-Up Proposal. The state currently owes $1 billion related to meeting the 2009-10, 2011-12, and 2013-14 minimum guarantees. In January, the administration proposed making an associated $400 million settle-up payment. The Governor's budget designated the funds primarily for one-time discretionary grants, with smaller amounts for the Career Technical Education (CTE) Incentive Grant program and community college deferred maintenance. The May Revision increases the proposed settle-up payment to $603 million. Of this amount, the administration designates $513 million for covering LCFF costs in 2016-17, with the remainder allocated for the CTE Incentive Grant and guided pathways initiative. (Currently, the available trailer legislation reflects the allocations for LCFF and the CTE program but not guided pathways.) The administration still funds community college deferred maintenance and one-time discretionary grants but intends to do so using Proposition 98 funds that count toward the 2017-18 minimum guarantee, as discussed below.

Sets Aside $1.1 Billion Until May 2019 When State Finalizes 2017-18 Guarantee. The Governor proposes to make $1.1 billion of the funding included in the May Revision contingent on the 2017-18 minimum guarantee meeting projections. The specific allocations affected by this proposal include $1 billion in one-time K-12 discretionary funding and $124 million in one-time funding for community college deferred maintenance. The Governor proposes to delay the release of the entire $1.1 billion until May 2019, at which time the state will finalize its estimate of the 2017-18 guarantee. The funding for the two specified programs would be reduced automatically to the extent the guarantee falls below the administration's May Revision projections. Although trailer bill language is not yet available, we understand that approximately 89 percent of any reduction would be applied to the K-12 discretionary grants and 11 percent to community college deferred maintenance.

Includes Two Major Ongoing Spending Priorities. The May Revision provides a $642 million increase for LCFF, bringing the total LCFF augmentation up from $744 million to $1.4 billion. As described later in this brief, the administration estimates that this augmentation would allow the state to fund 97 percent of the formula's target level. The May Revision also includes an additional $160 million in unallocated base funding for the community colleges, bringing the total unallocated apportionment increase up from $24 million to $184 million.

Assessment

Increase in Proposition 98 General Fund Nearly Equals Increase in State Tax Revenue. As mentioned above, compared with the Governor's January budget, the May Revision increases Proposition 98 General Fund spending by $2.2 billion across the period. By comparison, it increases its estimate of General Fund tax revenue by $2.4 billion over the period. That is, the increase in Proposition 98 General Fund spending is nearly equal to the increase in state revenue.

Funding Above Minimum Guarantee Increases Future Funding Requirements. Under the May Revision, Proposition 98 funding by the end of the period is $601 million higher than if the state had funded at the minimum guarantee each year. Under Proposition 98, the formulas for calculating the minimum guarantee generally build upon the level of funding provided in the previous year. As a result, the May Revision commits the state to a higher funding level not only in the budget period, but also in subsequent years. Higher minimum guarantees in the out-years would tend to make the state budget more difficult to balance, especially during economic slowdowns and recessions. Higher Proposition 98 guarantees also reduce funding available for the state's non-Proposition 98 priorities.

Contingency Proposal Helps Protect Against Downside Risk in 2017-18. In developing its estimate of the 2017-18 guarantee, the administration assumed that per capita General Fund revenue would grow 4.7 percent. Compared with the administration, our revenue estimates are about $1 billion higher in 2016-17 but $160 million lower in 2017-18, yielding a growth rate of 3.9 percent. Using the lower growth rate, the 2017-18 minimum guarantee is roughly $500 million lower than the administration's estimate. Under the administration's contingency proposal, the state automatically would reduce K-12 discretionary funding by about $450 million and community college deferred maintenance funding by about $50 million to align Proposition 98 funding with the lower minimum guarantee.

Proposal Is One Reasonable Planning Option. The administration's contingency proposal is one way the state can provide a cushion in the event of an economic slowdown or downturn, allowing the state to adjust reserved school funding without making reductions to LCFF or other ongoing school programs. We think this is a particularly important issue for 2017-18, as our revenue estimates already have the guarantee below the May Revision estimate. One benefit of reserving a small portion of Proposition 98 funding is that it sends a clear signal to schools about how the state is likely to respond in the event that revenues do not match budget projections. In some prior years, the state has dealt with revenue declines through a range of mid-year actions including deferrals, fund swaps, cuts to specific programs, cuts across the board, and other actions, sometimes on relatively short notice. The contingency proposal reduces the likelihood that the state needs to make retroactive adjustments. We also note that many variations of the Governor's basic proposal could be considered. For example, the state could change the amount of funding subject to the contingency proposal as well as the date on which it releases funds.

Not Automatically Providing Statutory Supplemental Appropriation Provides Legislature With More Budget Flexibility in Future Years. Not providing the supplemental appropriation could lead to somewhat slower growth in school funding in future years. Under the Governor's multiyear estimates, Test 3 is operative from 2018-19 through 2020-21 and supplemental payments are required all three years. Though supplemental payments otherwise would be required under the administration's May revenue projections, many other economic scenarios are possible and some have different implications. For example, if state revenue were to come in higher than projected, Test 2 might become operative and the Test 3 supplemental appropriation would be irrelevant. On the other hand, if the state entered a recession, the size of the supplemental payment otherwise required could be even larger. For state budgeting purposes, not automatically providing the supplemental appropriation could provide some additional flexibility, which would be particularly helpful during tight fiscal times. Such an approach would give the Legislature more options for balancing the budget while still preserving its ability to provide any amount of funding on top of the minimum guarantee.

LAO Estimates of Property Tax Revenue Slightly Above May Revision Estimates. Compared with the administration's estimates of property tax revenue, our estimates are $96 million (0.5 percent) higher in 2016-17 and $169 million (0.8 percent) higher in 2017-18. Differing assumptions about the revenue associated with the dissolution of redevelopment agencies explain most of this difference. Specifically, we assume that a somewhat larger share of the revenue allocated to these former agencies is available for distribution to schools, colleges, and other local governments, whereas the administration assumes that debts and other obligations will erode more of the available revenue. In 2017-18, an additional difference is our assumption about assessed property values. Whereas we estimate that assessed values will grow by 5.6 percent, the administration estimates growth of 5.3 percent.

Alternatives

Weighing Proposition 98 and Non-Proposition 98 Priorities Typically Starting Point in Building Overall Budget Package. Every year the Legislature decides how to weigh its Proposition 98 and non-Proposition 98 budget priorities. Most years the administration and the Legislature use the Proposition 98 minimum guarantee as their starting point in making this decision. This May Revision is unusual because it proposes to fund a total of $1.6 billion above the minimum guarantees across the 2015-16 through 2017-18 period, providing schools with most of the increase identified in state revenue. In building its budget, the Legislature may prefer to fund at a level different from what the Governor proposes. Below, we first discuss the trade-offs involved in funding at or above the minimum guarantee. Next, we discuss an alternative that would free up funding for other state priorities. Under the alternative, school funding would be above the minimum guarantee but below the May Revision Proposition 98 level. Lastly, we review two key budget dynamics that will affect the Legislature's decisions.

Funding at Minimum Guarantee Would Free Up General Fund but Require Accounting Adjustments. One alternative is for the Legislature to fund at the revised estimates of the minimum guarantee each year, consistent with its traditional budgetary practice. Since the minimum guarantee across the entire period is similar to January estimates, this approach would result in schools receiving about the same funding as in the Governor's January budget. It would require the Legislature to adopt some accounting changes, potentially using more settle-up funding (which we discuss further below), shifting costs from an accounting perspective among years, and/or reinstating a deferral. Such retroactive adjustments are relatively common budget practice. Since 1988, the state has revised Proposition 98 funding downward after the adoption of the budget act about half of the time and upward half of the time. The downward revisions have involved myriad actions, including payment deferrals, accounting shifts, fund swaps, and mid-year cuts. Funding at the minimum guarantees across the period would free up $1.6 billion General Fund for non-Proposition 98 programs and/or higher discretionary state reserves.

Other Alternative Could Free Up Funding for Rest of Budget While Still Funding Schools Above the Guarantee. If the Legislature wanted to fund above the minimum guarantee but lower than the May Revision Proposition 98 level, one budget option would be to make a larger school settle-up payment. Under such an approach, the state could score some spending in 2015-16 and 2016-17 that exceeds the minimum guarantees as settle-up payments. It would count the higher settle-up payments toward its Proposition 2 debt payments, and replace a like amount of other Proposition 2 debt payments included in the May Revision. From the state's perspective, using settle-up payments has the benefit of reducing dollar-for-dollar its ongoing Proposition 98 costs. From a Proposition 2 perspective, the state continues to pay down the same amount of debt, though the higher settle-up payment means that some other debt must be paid down less quickly. Relative to the May Revision proposal, we estimate that the state could use settle-up payments to free up as much as $1 billion for its priorities across the period (about half of this amount would be one-time and half would be ongoing). From schools' perspective, only the accounting of the money would change in 2016-17, with no effect on their programs or their cash situation. Lowering the amount that counts toward the minimum guarantee in 2016-17, however, would lower the 2017-18 guarantee. If the entire $1 billion in settle-up were used in 2016-17, we estimate the 2017-18 the minimum guarantee would be about $500 million lower than the May Revision Proposition 98 funding level. The state also could consider using settle-up payments to free up any lesser amount of funding for the rest of the budget, thereby keeping total Proposition 98 funding closer to the May Revision level.

Key Budget Dynamics to Consider. As the Legislature goes about evaluating various options for funding Proposition 98, we encourage it to keep two specific factors in mind:

- ***Decisions About Funding Levels in 2015-16 and 2016-17 Have Cumulative Effects.*** Given that the minimum guarantee generally builds upon the level of funding provided in the prior year, a decision to fund above the minimum guarantee in 2015-16 could be magnified three-fold across the period. That is, to the extent the state funds above the 2015-16 guarantee, it also increases the guarantees for 2016-17 and 2017-18. Similarly, funding above the 2016-17 guarantee increases the 2017-18 guarantee by a roughly similar amount.

- ***The 2017-18 Funding Level Affects Future Budgets.*** Looking beyond the immediate budget period, the 2017-18 spending level determines the state's ongoing Proposition 98 commitment, affecting the state's ability to balance the budget in the future.

K-12 EDUCATION

K-12 Proposition 98 Funding Up $1.3 Billion Across Period. Figure 3 (see next page) compares total K-12 funding under the Governor's January budget with the May Revision. The May Revision provides an additional $1.3 billion in Proposition 98 funding for K-12 education across the 2015-16 through 2017-18 period. Under the May Revision, total Proposition 98 funding for K-12 education in 2017-18 is $66 billion, reflecting an increase of $2.9 billion (4.4 percent) over the revised 2016-17 level. Proposition 98 funding per student is $11,080, an increase of $490 (4.4 percent) over the revised 2016-17 level. Below, we describe and assess the May Revision proposals for K-12

Figure 3

Comparing K-12 Proposition 98 Funding Under Governor's Budget and May Revision

(Total Funding in Millions)

	2015-16	2016-17	2017-18
January Budget			
General Fund	$43,686	$44,887	$45,886
Local property tax	17,052	18,236	19,200
Totals	**$60,738**	**$63,122**	**$65,087**
Students[a]	5,971,343	5,958,933	5,958,288
Dollars per student	$10,171	$10,593	$10,924
May Revision			
General Fund	$44,040	$45,114	$47,178
Local property tax	17,048	18,035	18,858
Totals	**$61,088**	**$63,148**	**$66,036**
Students	5,971,790	5,962,962	5,960,101
Dollars per student	$10,229	$10,590	$11,080
Change			
General Fund	$354	$227	$1,292
Local property tax	-4	-201	-343
Totals	**$350**	**$26**	**$949**
Students	447	4,029	1,813
Dollars per student	$58	-$3	$156

[a] Reflects average daily attendance.

education. We discuss preschool changes in the next section.

Major Spending Changes

Figure 4 summarizes May Revision spending changes for K-12 education in 2017-18. Below, we describe the most notable of these changes.

Increases One-Time Discretionary Funding by $725 Million. The Governor's January budget included $283 million for one-time discretionary per-student grants to schools. The May Revision provides an additional $725 million, bringing total one-time discretionary funding up to $1 billion. Consistent with the January proposal, the administration proposes to distribute the $1 billion based on student attendance, with the rate increasing to $169 per student (up from $48 per student in January). The administration indicates the funding would not be allocated to local education agencies (LEAs) until May 15, 2019. At that time, the administration would only allocate the amount required to meet the revised estimate of the 2017-18 minimum guarantee. As proposed in January, LEAs could use the funds for any education purpose, but the administration encourages the funds be used for deferred maintenance, professional development, and implementation of the Common Core State Standards, among other priorities. If an LEA has outstanding mandate backlog claims, the funding would be scored against those claims.

Increases LCFF Funding by $642 Million. This increase brings the total LCFF augmentation to $1.4 billion. Under the May Revision, LCFF is funded at 97 percent of the full implementation cost. By comparison, the January budget funded 96 percent of the full implementation cost. (The full implementation cost of LCFF has increased by $73 million since January—the net effect of the inflation rate increasing from 1.48 percent to 1.56 percent, partly offset by a slight decline in projected attendance.)

Other Changes

Requires K-12 High Speed Network (HSN) to Fund Operations From Grant Balance, Allows It to Spend Down Reserve on Internet Upgrades. The state contracts with Imperial County Office of Education to administer HSN, which coordinates

Figure 4

2017-18 K-12 Proposition 98 Changes

(In Millions)

	Governor's Budget	May Revision	Change
2016-17 Revised Spending	**$63,122**	**$63,148**	**$26**
Technical Adjustments			
Make LCFF adjustments	$65	$157	$92
Make other adjustments	190	135	-55
Adjust categorical programs for changes in attendance	-9	-6	2
Revise estimate of energy efficiency funds	24	-23	-47
Subtotals	($270)	($263)	(-$8)
Policy Adjustments			
Increase LCFF funding	$744	$1,387	$642
Provide discretionary one-time funding	—	1,012	1,012
Augment State Preschool Program	24	151	128
Provide COLA for select categorical programs[a]	58	61	3
Add mandated reporter training to mandates block grant	8	8	—
Support SCROC	—	4	4
Develop electronic LCAP template[b]	—	—	—
Defer payments from June to July 2017	859	—	-859
Subtotals	($1,694)	($2,624)	($931)
Total Changes	**$1,964**	**$2,887**	**$923**
2017-18 Proposed Spending	**$65,087**	**$66,036**	**$949**

[a] Applies to special education, child nutrition, services for foster youth, adults in correctional facilities, and American Indian education. COLA increased from 1.48 percent under the Governor's Budget to 1.56 percent under the May Revision.

[b] May Revision includes $350,000 for this purpose.

LCFF = Local Control Funding Formula; COLA = cost-of-living adjustment; SCROC = Southern California Regional Occupational Center; and LCAP = Local Control and Accountability Plan.

Internet services to schools. The Governor proposes to replace $8 million in ongoing Proposition 98 funding for HSN in 2017-18 with $8 million from the Broadband Infrastructure Improvement Grant (BIIG) fund balance. (The *2015-16 Budget Act* included $50 million for HSN to administer BIIG, a program designed to help schools upgrade their Internet infrastructure such that they could administer online tests.) The Governor also adds expenditure authority to allow HSN to spend $2.5 million of its operating reserve for Internet infrastructure upgrades at certain county offices of education that could benefit from faster speeds.

Provides $10 Million Over Four Years to Southern California Regional Occupational Center (SCROC). The SCROC is an education center in Torrance that provides CTE and education toward a diploma to high school students and adults. The Governor proposes to provide $10 million over four years to SCROC—$4 million in 2017-18, $3 million in 2018-19, $2 million in 2019-20, and $1 million in 2020-21. The administration indicates that the allocation is to aid the center as it "transitions" to a fee-supported model under the LCFF. The administration indicates the proposed augmentation in 2017-18 is intended to return SCROC's budget to its 2012-13 level. The budget bill language places no restrictions or conditions on the funds.

Adds New Mandate to K-12 Mandates Block Grant With No Additional Funding. The May Revision adds the California Assessment of Student Performance and Progress (CAASPP) mandate to the K-12 mandates block grant, with no associated increase in funding. The Commission on State Mandates determined that compliance with the minimum technology requirements of new statewide exams constituted a reimbursable mandate. This includes the costs of purchasing new devices, maintaining sufficient Internet speeds, and conducting related administrative tasks. LEAs participating in the block grant would no longer be able to submit claims for reimbursement of the CAASPP mandate.

Creates Competitive Grant Program for Educator Recruitment and Support. The May Revision repurposes $11 million in federal Title II local assistance funding for a new competitive grant program that would assist LEAs with attracting and supporting the development of educators in high-need subjects and schools. The program would be administered by the Commission on Teacher Credentialing (CTC) and the California Center on Teaching Careers, an entity created by the state in 2016-17 to conduct a statewide teacher recruitment campaign.

Increases Maximum Charter School Facility Grant. The Governor's January budget included $112 million for the Charter School Facility Grant program, which helps certain charter schools cover the costs of renting or leasing instructional facilities. The May Revision makes no change to funding for the program but proposes trailer bill language increasing the maximum grant amount. Currently, qualifying charter schools can receive grants equating to either $750 per student or 75 percent of their annual facilities costs, whichever is lower. The $750 per-student amount has not been updated since the program was created in 2001. The Governor proposes to increase the per-student amount to $1,236 in 2017-18, an increase the administration considers commensurate with inflation since 2001. The Governor also proposes to apply the statutory K-12 cost-of-living adjustment (COLA) to the maximum per-student grant amount in subsequent years.

Assessment and Recommendations

Below, we assess the May Revision proposals for K-12 education and provide associated recommendations. Figure 5 summarizes these recommendations.

Consider Balance of One-Time and Ongoing Spending. In recent years, the state has dedicated most new ongoing Proposition 98 funds to furthering implementation of LCFF, while still dedicating some funds to one-time initiatives. The May Revision takes a somewhat similar approach but places even more emphasis on one-time spending—dedicating more than $1 billion for one-time discretionary grants for schools. In developing its final budget package, the Legislature likely will want to consider the trade-offs of dedicating increases to one-time grants versus LCFF. Whereas increasing LCFF funding particularly helps schools serving a large share of disadvantaged students and accelerates progress toward full implementation, providing one-time per-pupil grants benefits all schools equally. Such an approach can be particularly beneficial as all districts are experiencing increases in their pension costs. The one-time grants, if linked to a contingency plan, also would better position the state to accommodate a drop in the 2017-18 minimum guarantee.

Use One-Time Funding to Strategically Retire Mandate Backlog. Regardless of the exact amount the final budget package dedicates to one-time funding, we continue to recommend the state link such funding to a strategic plan to retire the K-12 mandate backlog. Even though the May Revision proposes considerable one-time funding, it does not take such an approach. By distributing discretionary funding purely based on attendance, we estimate less than 30 percent ($298 million) of the $1 billion included in the May Revision would reduce the mandate backlog. This is because more than half of LEAs have no outstanding claims and the claims for other LEAs vary widely on a per-student basis. We estimate continuing to use a per-student approach to retire the entire backlog would cost $173 billion—nearly 200 times more than the backlog. We recommend the Legislature use one-time funding to more strategically retire the mandate backlog. Under our recommended approach, all districts could receive funding but districts with outstanding claims would need to agree to write off their existing claims.

Adopt HSN May Revision Proposal but Consider Legislative Role in Infrastructure Upgrades Moving Forward. We recommend the Legislature adopt the May Revision proposal requiring HSN to fund operations out of the remaining BIIG fund balance because virtually all schools can administer online tests and $20 million still remains in the fund. We also recommend the Legislature adopt the May Revision proposal allowing HSN to spend down

Figure 5

Summary of K-12 Education Recommendations

Program	May Revision Proposal	LAO Recommendation
K-12 discretionary funding/ mandates backlog	Increases by $725 million one time (raising total increase to $1 billion).	***Modify.*** Link additional one-time discretionary grants to a strategic plan to pay off remainder of K-12 mandates backlog.
LCFF for school districts	Increases by $642 million ongoing (raising total increase to $1.4 billion).	***Adopt.*** Additional funding accelerates LCFF implementation.
K-12 High Speed Network (HSN)	Removes $8 million in ongoing Proposition 98 funding for HSN's operations and requires program to fund operations from Broadband Infrastructure Improvement Grant (BIIG) fund balance. Allows HSN to spend $2.5 million of operational reserves toward Internet infrastructure upgrade projects.	***Adopt.*** $20 million remains in BIIG fund balance and virtually all schools now can administer online tests. Moving forward, the Legislature may wish to consider whether it wants a more active role in reviewing and approving infrastructure projects.
Southern California Regional Occupational Center (SCROC)	Provides SCROC $10 million Proposition 98 General Fund over four years: $4 million in 2017-18, $3 million in 2018-19, $2 million in 2019-20, and $1 million in 2020-21.	***Reject.*** Like all other career technical education programs, SCROC has had four years to transition to new funding model. SCROC already has committed to maintaining career technical education programming until 2020-21.
CAASPP Mandate	Adds mandate to K-12 mandates block grant with no additional funding.	***Modify.*** Add mandate and $25 million to block grant. Shift $12.8 million from assessments item into block grant.
Educator recruitment and support grants	Repurposes $11 million in Title II funds for a new competitive grant program.	***Modify.*** Adopt funding level but narrow the scope of grants and award to appropriate agency.
Charter School Facility Grant Program	Increases grant amount from $750 to $1,236 per student and applies COLA to amount in subsequent years. Recipients receive lesser of this amount or 75 percent of their facilities cost.	***Modify.*** If desire is to use K-12 COLA, change per-student grant to $1,117 (rather than $1,236). Could explore using another inflationary index.
LCAP electronic template	Provides $350,000 to develop an electronic LCAP template for school districts to use in developing and sharing their LCAPs.	***Adopt.*** Electronic template would streamline process for districts to develop and publish LCAPs.

LCFF = Local Control Funding Formula; CAASPP = California Assessment of Student Performance and Progress; and LCAP = Local Control and Accountability Plan; and COLA = cost-of-living adjustment.

part of its operating reserve on planned Internet infrastructure upgrades. We recommend, however, that the Legislature consider whether it would like a more active role in reviewing and approving infrastructure projects in the future.

Special Treatment for SCROC Problematic, Recommend Rejecting Proposal. In 2015-16, SCROC enrolled roughly 2,000 high school students and 1,000 adults and its operating budget was $5 million. Of this amount, 50 percent came from six school districts who pay fees for their high school students to take SCROC classes, 30 percent came from the CTE Incentive Grant, 15 percent came from fees it charged adult students, and the remaining 5 percent came from other sources. Like all other CTE programs, SCROC has had four years to negotiate with the districts it serves to transition to a fee-supported model, and half of its budget already comes from K-12 fees. At this point, we see no statewide benefit for providing a special state appropriation to help SCROC return to its funding level from more than five years ago. Moreover, as a condition of receiving CTE Incentive Grant funds, SCROC committed to maintaining K-12 CTE programming until 2020-21 and having a plan to sustain its program once the grant funds expired. For these reasons, we recommend the Legislature reject the proposal and instead require SCROC and its member districts to manage their program locally and honor their commitment to maintain their CTE programs.

Add CAASPP Mandate and $25 Million, Along With Shifting Associated Apportionment Funding, Into the K-12 Mandates Block Grant. As we discussed in *The 2017-18 Budget: Proposition 98 Education Analysis*, we recommend adding the CAASPP mandate into the K-12 mandates block grant. However, we also recommend increasing block grant funding by $37.8 million. This amount includes our estimate of the mandate's annual costs ($25 million) as well as a shift into the mandates block grant of apportionment funding ($12.8 million) currently provided to cover other administrative costs related to these exams.

Concerns With Educator Recruitment and Support Grant Proposal. Although state spending on educator recruitment and support could have benefits, the May Revision proposal lacks detail and fails to identify a specific policy problem or objective. If the Legislature wishes to repurpose existing federal Title II monies, we recommend it identify a specific problem and clear associated program objectives, operate the program through the agency that conducts similar activities, and develop ways to measure and monitor the outcomes of the program.

Recommend Adjusting Charter School Facility Grant Amount. We think an award equal to 75 percent of a charter school's facility costs represents a sensible balance between providing state support while still ensuring these schools have an incentive to keep their costs low (as they must pay the remaining costs). We also think capping support at a specified dollar amount is sensible, as it prevents the state from subsidizing even 75 percent of unnecessarily expensive facilities. Given the state has not adjusted per-student rates since 2001, we think raising them is reasonable. The May Revision, however, miscalculates the increase to the per-student grant if the intent is to update it using the statutory K-12 COLA (as indicated in trailer bill language). Using that index, the per-student grant would be $1,117—$119 lower than the May Revision level. If the Legislature desired to update the index using the statutory K-12 COLA, we recommend it set the new rate at $1,117. Alternatively, the Legislature could explore using another inflationary index that better reflects increases in leasing costs.

CHILD CARE AND PRESCHOOL

Child Care and Preschool Funding Up Notably From Governor's January Budget. Compared to the Governor's January budget, the May Revision includes $198 million in additional funding for subsidized child care and preschool programs. Of this amount, $151 million is from Proposition 98 General Fund and $54 million is from non-Proposition 98 General Fund. These increases are offset by an $8 million reduction in federal funding. The May Revision augmentation brings total 2017-18 funding for child care and preschool programs to $4 billion, reflecting a 7 percent increase from the revised 2016-17 level. In this section, we describe and assess the May Revision proposals for child care and preschool programs, including the California Work Opportunity and Responsibility to Kids (CalWORKs) child care programs, non-CalWORKs programs, the California State Preschool Program, and Transitional Kindergarten.

Major Changes

As Figure 6 shows, when combined with the increase included in the Governor's January budget,

Figure 6

2017-18 Child Care and Preschool Changes

(In Millions)

	Governor's Budget	May Revision	Change
Reimbursement Rates			
Increases Standard Reimbursement Rate (SRR) 6 percent starting July 1, 2017	—	$93	$93
Increases SRR to cover full-year cost of rate increase adopted in 2016-17	—	68	68
Annualizes Regional Market Rate (RMR) increase initiated January 1, 2017	$57	57	—
Increases RMR to the 75th percentile of the 2016 regional market survey starting January 1, 2018[a]	—	42	42
Annualizes 5 percent license-exempt rate increase initiated January 1, 2017	11	11	—
Subtotals	($68)	($270)	($202)
Preschool Slots			
Annualizes State Preschool slots initiated April 1, 2017	$24	$24	—
Provides 2,959 full-day State Preschool slots at LEAs starting April 1, 2018	—	8	$8
Subtotals	($24)	($31)	($8)
Caseload Changes			
Adjusts Transitional Kindergarten for changes in attendance and LCFF rates	$8	$31	$23
Makes statutory adjustment to non-CalWORKs slots[b]	-7	-7	—
Makes CalWORKs caseload and average cost of care adjustments	-11	-76	-64
Subtotals	(-$11)	(-$52)	(-$41)
Other Adjustments			
Provides 1.56 percent COLA to certain child care and preschool programs	—	$29	$29
Removes one-time funding	-$7	-7	—
Subtotals	(-$7)	($21)	($29)
Totals	**$73**	**$271**	**$198**

[a] Includes a temporary hold harmless provision so that no provider receives less in 2017-18 than it received in 2016-17.

[b] Reflects 0.4 percent decrease in the birth-through-four population.

LEA = local education agency; LCFF = Local Control Funding Formula; and COLA = cost-of-living-adjustment.

the May Revision designates $271 million for additional child care and preschool spending. Below, we describe the most notable May Revision changes.

Adds $210 Million Above January Level to Implement Components of Multiyear Budget Agreement. For 2017-18, the multiyear child care and preschool budget agreement assumed (1) annualization of the rate and slot increases initiated part way through 2016-17, (2) an additional 2,959 State Preschool slots, and (3) an $86 million increase in rates. The January budget included funding to implement a portion of the first component of the agreement—annualizing some rate increases and preschool slots. The May Revision includes the following actions to implement the remaining components of the deal:

- ***Increases Standard Reimbursement Rate (SRR) 11 Percent Above Effective 2016-17 Rate.*** The May Revision provides $68 million to increase the SRR by 5 percent. (Even though the intent of this proposal is to annualize the cost of a rate increase approved in 2016-17, the augmentation effectively results in a 5 percent year-over-year rate increase due to how last year's rate increase was implemented.) On top of this 5 percent increase, the May Revision includes $93 million for an additional 6 percent SRR increase.

- ***Increases Regional Market Rate (RMR) to 75th Percentile of 2016 Market Rate Survey Beginning January 1, 2018.*** The May Revision includes $42 million to increase the RMR and hold child care providers harmless if the new rates are lower than current levels. The hold harmless provision would be effective until January 1, 2019. (The 2016-17 budget plan increased rates to the 75th percentile of the 2014 survey beginning January 1, 2017. This earlier action also included a hold harmless provision, effective until July 1, 2018, that ensured no providers received rates below 2015-16 levels.)

- ***Adds 2,959 LEA State Preschool Slots Starting April 1, 2018.*** The May Revision includes $8 million Proposition 98 General Fund for this purpose.

Includes $29 Million to Provide 1.56 Percent COLA to Non-CalWORKs Child Care Programs. Whereas the Governor's January budget included no COLA for any child care or preschool programs, the May Revision funds the statutory COLA for most programs. Of the associated $29 million augmentation, $24 million is to further increase the SRR (which applies to State Preschool and General Child Care programs), $4 million is for the Alternative Payment program, and $346,000 is for Resource and Referral agencies and Local Planning Councils.

Reduces CalWORKs Child Care Spending by $64 Million From January Level to Reflect Revised Caseload and Average Cost of Care Estimates. The May Revision is based on updated data regarding CalWORKs child care caseload and the types of care families select. (Changes in types of care used affect the average cost of care, independent from the rate increases described above.) Of this amount, $44.8 million is due to a net decrease of 4,866 cases across all three CalWORKs stages. (Stage 1 and Stage 2 are down a combined 4,928 cases, with Stage 3 up by 62 cases.) The remaining $19.6 million reduction is due to lower average cost of care estimates.

Modifies Proposals to Align State Preschool and Transitional Kindergarten. The May Revision modifies two of the Governor's January proposals intended to help align the state's developmental programs for four-year olds. In January, the Governor proposed to exempt any State Preschool program operating in facilities constructed according to the state's K-12 building standards from the state's preschool licensing requirements. The May Revision delays implementation of this proposal until 2018-19. In January, the Governor also proposed allowing State Preschool classrooms taught by a teacher with a Multiple Subject Teaching Credential to operate with an adult-to-child ratio of 1:12 (rather than the 1:8 ratio currently required). Under the revised proposal, these teachers also would be required to have completed 24 units of early education coursework or comparable experience.

Assessment and Recommendations

Below, we assess the May Revision child care and preschool proposals and provide associated recommendations. Figure 7 summarizes these recommendations.

No Major Concerns With SRR and COLA Proposals. We have no concerns with the May Revision SRR proposal, as it adheres to the multiyear budget agreement. We also have no major concerns with funding the statutory COLA for most child care and preschool programs.

Hold Harmless Provision Continues to Disconnect Rates From Child Care Market. Hold harmless provisions (1) allow some families to access a larger share of the child care market than others and (2) reimburse some child care providers at rates higher than the 75th percentile of their regional markets. By adding a new hold harmless provision (in addition to the existing hold harmless provisions), the Governor's proposal exacerbates

Figure 7

Summary of Child Care and Preschool Recommendations

Issue	May Revision Proposal	LAO Recommendation
Standard Reimbursement Rate (SRR)	Provides $161 million to increase SRR by total of 11 percent beginning July 1, 2017.	***Adopt.*** May Revision proposal implements budget agreement.
Regional Market Rate (RMR)	Provides $42 million to increase RMR to the 75th percentile of the 2016 regional market survey beginning January 1, 2018. Includes hold harmless provision.	***Modify.*** Reject hold harmless provision. With freed up funding, consider adding new slots or increasing all rates to a higher percentile of the 2016 regional market survey.
Cost-of-Living Adjustment (COLA)	Includes $29 million to provide COLA for non-CalWORKs child care and preschool programs.	***Adopt.*** May Revision proposal funds statutory COLA.
State Preschool Slots	Provides $8 million for 2,959 full-day State Preschool slots at LEAs, beginning April 1, 2018.	***Modify.*** Allow both LEAs and non-LEAs to apply for additional full-day State Preschool slots.
CalWORKs Child Care	Reduces funding by $64 million due to changes in caseload and average cost of care.	***Modify.*** Adopt LAO caseload and average cost of care estimates for CalWORKs Stage 2. Results in $15 million non-Proposition 98 General Fund savings.
Quality Improvement Activities	Does not include sufficient funding to meet federal spending requirement on quality improvement activities.	***Modify.*** Increase quality improvement spending by $7 million to meet federal requirement. Add to recommended county-level quality improvement block grant.
State Preschool and Transitional Kindergarten Alignment	Makes modest changes to January preschool alignment proposals.	***Reject.*** Take holistic rather than piecemeal approach to fixing poorly designed system.

LEA = local education agency.

the inequities in access and reimbursement rates across the state. We recommend the Legislature adopt a rate policy that does not include additional hold harmless provisions.

Consider Other Options for Promoting Access. At the 75th percentile of the most recent survey, families in all areas of the state would have access to the vast majority of child care providers in their area. Rather than giving families in a few areas even more access by adopting a new hold harmless provision, the Legislature could consider various other options for expanding access more rationally throughout the state. One option that would cost the same as the May Revision hold harmless provision would be to fund about 2,000 additional Alternative Payment slots and distribute them based upon each region's share of the unserved eligible population. Alternatively, if the Legislature is interested in dedicating all additional funding to rate increases, it could increase the RMR to a higher percentile of the regional market survey. We estimate increasing the RMR to the 77th percentile of the 2016 survey without a hold harmless provision would cost roughly the same as the May Revision proposal. Both alternatives would remove existing inequities and ensure families across the state have access to the same share of their local child care providers.

New Preschool Slots at LEAs Likely to Go Unused. The Legislature has authorized an additional 8,789 full-day State Preschool slots for LEAs over the last two years—5,830 in 2015-16 and 2,959 in 2016-17. Based on the most recent information provided by the California Department of Education (CDE), only 2,714 of these slots have been awarded for full-day programs at LEAs. The remaining funding has been awarded to LEAs and non-LEAs for part-day slots or remains unallocated. We recommend the Legislature make funds available to all State Preschool providers, not only LEAs, to ensure slots are used as intended. Authorizing slots to non-LEAs, however, would increase the state's non-Proposition 98 General Fund costs, if implemented the same as in the past few years. Based on current practice, the cost of full-day programs at LEAs is entirely funded within Proposition 98, whereas 38 percent of the cost of full-day programs at non-LEAs is covered by non-Proposition 98 General Fund. (Part-day slots for LEAs and non-LEAs are funded entirely within Proposition 98.)

Governor Likely Overestimates Cost of CalWORKs Stage 2. The May Revision assumes 52,913 cases in CalWORKs Stage 2 in 2017-18, about 3 percent above CDE's most recent 2016-17 estimates. We estimate Stage 2 caseload in 2017-18 to be 1,200 below the administration's estimate, roughly flat compared to CDE's most recent 2016-17 estimates. Our projection is based on recent data showing the number of families entering Stage 2 is roughly the same as the number of families exiting the program. We also estimate the average annual Stage 2 cost of care will be $9,431—$71 less per case than the Governor assumes in the May Revision. As a result of our caseload and cost of care estimates, we project CalWORKs Stage 2 child care costs to total $488 million—$15 million lower than the May Revision estimates. Recognizing these savings would free up non-Proposition 98 General Fund spending that could be used to fund full-day State Preschool slots at non-LEAs, other legislative priorities, or an increase in the state's discretionary reserves.

May Revision Does Not Include Sufficient Funding to Meet Federal Spending Requirement for Quality Improvement Activities. As a condition of receiving federal funds for child care and preschool, California is required to spend a certain percentage of federal funds and a state match on activities to improve quality. Based on the most recent information from the federal government, we estimate California will be required to spend

$85 million on quality improvement activities in 2017-18. The May Revision includes $78 million for these activities—$7 million less than the federal requirement. To remain compliant with the federal rules, we recommend the Legislature increase spending on quality improvement activities by $7 million. As we discussed in our March report, *The 2017-18 Budget: Analysis of Child Care and Preschool Proposals*, we recommend the Legislature combine seven of the state's existing quality improvement programs into a county-level block grant that could be used for a variety of improvement activities. We recommend the $7 million augmentation be added to the county-level block grant (bringing the size of the total block grant under our recommendation up to $28 million).

Continue to Have Overarching Concerns With Preschool Alignment Proposals. As we discussed in our March report, we have concerns that the Governor's alignment proposals add greater complexity to the existing system without providing substantial alignment between State Preschool and Transitional Kindergarten. The May Revision makes minor improvements to these proposals but does not address our core concerns. We continue to recommend the Legislature not take time to tweak a poorly designed system but instead take a more holistic approach to aligning State Preschool and Transitional Kindergarten.

COMMUNITY COLLEGES

Community College Funding Up $219 Million Across Period. Figure 8 compares total funding for the California Community Colleges (CCC) under the Governor's January budget with the May Revision. The May Revision provides an additional $219 million in Proposition 98 funding for community colleges across the 2015-16 through 2017-18 period. Under the May Revision, total Proposition 98 funding for community colleges in 2017-18 is $8.6 billion, reflecting an increase of $324 million (4 percent) over the revised 2016-17 level. Proposition 98 funding per full-time

Figure 8

Comparing CCC Proposition 98 Funding Under Governor's Budget and May Revision

(Total Funding in Millions)

	2015-16	2016-17	2017-18
Governor's Budget			
General Fund	$5,304	$5,443	$5,465
Local property tax	2,630	2,803	2,959
Totals	**$7,933**	**$8,246**	**$8,424**
FTE students	1,145,637	1,156,810	1,168,379
Dollars per FTE student	$6,925	$7,128	$7,210
May Revision			
General Fund	$5,384	$5,489	$5,674
Local property tax	2,631	2,753	2,891
Totals	**$8,016**	**$8,242**	**$8,565**
FTE students	1,137,619	1,152,708	1,154,917
Dollars per FTE student	$7,046	$7,150	$7,416
Change			
General Fund	$81	$46	$209
Local property tax	2	-50	-68
Totals	**$83**	**-$4**	**$141**
FTE students	-8,018	-4,102	-13,462
Dollars per FTE student	$121	$22	$206

FTE = full-time equivalent.

equivalent (FTE) student is $7,416, an increase of $267 (4 percent) over the revised 2016-17 level. Below, we describe and assess the May Revision proposals for community colleges.

Major Spending Changes

Figure 9 summarizes 2017-18 spending changes for the community colleges. The three major May Revision changes are: (1) providing a larger unallocated base increase, (2) increasing deferred maintenance funding, and (3) reducing enrollment growth funding.

Provides Additional $160 Million Unallocated Base Increase. Together with the $24 million proposed in January, the unallocated apportionment funding increase would total $184 million. The Governor proposes the augmentation in recognition of increased operating expenses for retirement benefits, facility maintenance, professional development, full-time faculty, and other general expenses. Colleges could use these funds for any purpose.

Provides Additional $92 Million for Deferred Maintenance. Of this amount, $49.5 million comes from Proposition 98 funds and $42.6 million from settle-up funds. (The Governor's budget already had included $43.7 million in settle-up funds for deferred maintenance, bringing total associated settle-up funds to $86.3 million. Since release of the May Revision, the administration has indicated its intent to use the $86.3 million in settle-up funds for a portion of the guided pathways initiative and to fund deferred maintenance entirely from within the 2017-18 Proposition 98 minimum guarantee. The administration indicates this shift is necessary to implement its Proposition 98 contingency proposal.

Figure 9

2017-18 CCC Proposition 98 Changes

(In Millions)

	Governor's Budget	May Revision	Change
2016-17 Revised Spending	**$8,246**	**$8,242**	**-$4**
Technical Adjustments			
Remove one-time spending	-$177	-$177	—
Other technical adjustments	-35	-84	-$49
Subtotals	(-$212)	(-$260)	(-$49)
Policy Adjustments			
Provide unallocated base increase	$24	$184	$160
Fund guided pathways initiative (one time)	150	150	—
Increase COLA from 1.48 percent to 1.56 percent[a]	98	102	4
Reduce enrollment growth from 1.34 percent to 1 percent	79	58	-22
Fund deferred maintenance (one time)	—	50	50
Fund Innovation Awards (one time)	20	20	—
Augment Online Education Initiative	10	10	—
Fund integrated library system (one time)	6	6	—
Increase Full-Time Student Success Grant	3	5	2
Subtotals	($390)	($584)	($194)
Total Changes	**$179**	**$324**	**$145**
2017-18 Spending	**$8,424**	**$8,565**	**$141**

[a] Applied to appportionments, Extended Opportunity Programs and Services, Disabled Students Programs and Services, CalWORKs student services, and support for certain campus child care centers.

COLA = cost-of-living adjustment.

Under that proposal, the bulk of these funds would be set aside as a reserve to be allocated in May 2019 after determining the revised 2017-18 Proposition 98 minimum guarantee.) The funding provided for deferred maintenance could be used for facility maintenance and repairs, water conservation projects, and replacement of instructional equipment and library materials. The Chancellor would allocate these funds to colleges on the basis of FTE enrollment.

Reduces Enrollment Growth Estimate for 2017-18 by $22 Million. The May Revision reduces enrollment growth in 2017-18 from 1.34 percent to 1 percent, for savings of $22 million relative to the Governor's budget. The proposed reduction stems from recent attendance reports showing systemwide enrollment has slowed in 2016-17. Despite this slowing, the May Revision does not reduce 2016-17 enrollment growth funding. The May Revision includes new provisional language to permit the Chancellor's Office to allocate unused 2017-18 growth funding to backfill any unanticipated shortfalls in apportionments (such as a shortfall due to lower-than-expected local revenues).

Other Spending Changes

Provides $3.7 Million to Cover Higher COLA. The May Revision increases the COLA for apportionments and select categorical programs from 1.48 percent to 1.56 percent based on updated data.

Provides $1.9 Million Net Increase to Full-Time Student Success Grant Program. The May Revision increases funding for supplemental awards for full-time community college students who are Cal Grant B or C recipients. The proposal raises the maximum annual award amount from $600 to $700. The administration expects that the increase in the *maximum* award would raise the *average* award from $515 to $600. The average annual award is less than the maximum award because some grant recipients end up qualifying for the award in only one term. Were the maximum award not to be increased, the administration estimates that the program would yield notable savings from its current budgeted funding level. The May Revision also makes a small upward adjustment to expected participation in 2017-18.

Adjusts 2015-16 Apportionment Funding. The May Revision makes two notable changes to 2015-16 apportionment funding:

- ***Adjusts Unused Prior-Year Enrollment Growth.*** In January, the administration estimated $56 million in unused 2015-16 growth and reduced funding accordingly. Final attendance reports indicate only $30 million went unused. The May Revision adds back $26 million.

- ***Increases General Fund Support to Reach Target Proposition 98 Spending Level.*** For 2015-16, the May Revision has an overall Proposition 98 spending level that is notably above the Governor's January budget. To help reach the higher spending level, the May Revision provides an additional $32 million in General Fund support previously associated with a property tax backfill. It also provides an additional $23 million in General Fund support formerly associated with adjustments of $16 million to property tax revenue and $7 million to student fee revenue. The combined General Fund increase of $55 million is to be distributed to colleges on a FTE student basis for any locally determined, one-time purpose.

Provides Additional State Operations Funding. The May Revision rescinds the Governor's January proposal to provide an additional $378,000 non-Proposition 98 General Fund and authority for two new vice chancellor positions.

It replaces this proposal with an increase of $618,000 non-Proposition 98 General Fund, $454,000 in reimbursements, and authority for six new positions. The General Fund portion would support two additional information technology specialists and an administrator to oversee guided pathways implementation. In addition, it would provide funding to fill an existing vacant executive position to serve as a second deputy chancellor. The reimbursement authority would support two research specialists and an attorney. All three of these staff would provide fee-based services to colleges, districts, and external researchers.

Provides $1.8 Million for Equal Employment Opportunity. The May Revision provides $1.8 million from a special fund to promote equal opportunity in hiring and promotion at community college districts.

Changes to Guided Pathways Proposal

In January, the Governor proposed a one-time $150 million program to help community colleges develop a "guided pathways" approach to improving student outcomes. The May Revision maintains the same level of funding but proposes several changes to specific components of the original proposal.

Authorizes Expenditure Over Five Years. The May Revision includes provisional language authorizing the expenditure of funds until June 30, 2022.

Clarifies Definition of Guided Pathways and Suggested Use of Funds. The administration modifies its proposed trailer bill language to include a more specific definition of a guided pathways program based on the definition in use by the California Guided Pathways Project, a privately funded initiative administered by the CCC Foundation. The modified language also suggests how colleges could use state funds provided for the program.

Authorizes Chancellor's Office to Require Additional Information From Colleges. The proposed trailer bill language authorizes the Chancellor's Office to develop an application for the program or require a college to submit information to assess the college's commitment to guided pathways. It also authorizes the Chancellor's Office to set criteria for releasing funding in stages based on a participating college's progress toward implementing guided pathways.

Clarifies Reporting Requirements. The proposed trailer bill language requires the Chancellor's Office to develop indicators for measuring early outcomes of guided pathways. It also requires that a summary of each participating college's progress based on these indicators be included in the final annual report (due 2022).

Other Policy Changes

Gives Colleges More Time to Use Innovative Apprenticeship Grants. The May Revision would extend by two years the encumbrance and expenditure period for grants awarded in 2015-16 and 2016-17 under the California Apprenticeship Initiative. Typically, state agencies have a total of three years to encumber and spend appropriations. Under the May Revision, the period would be extended to five years for this program. The Department of Finance has indicated that it likely would continue this practice for apprenticeship grants in the future through provisional language in the budget. The purpose of this change is to allow more time to implement and pilot new apprenticeship programs, which may require complex agreements among employers and education providers.

Creates Exemption From Competitive Bidding Rules. Sometimes the Chancellor's Office contracts with a community college district to perform certain services on behalf of the CCC system. The

May Revision exempts the Chancellor's Office from competitively bidding new district contracts of $20 million or less, as well as all district renewal contracts. Nearly all existing district contracts fall under the $20 million threshold and thus would be affected by the proposal. Under the May Revision proposal, the Board of Governors would continue to review and approve all CCC contracts.

Assessment and Recommendations

Below, we assess the May Revision proposals for community colleges and provide associated recommendations. Figure 10 (see next page) summarizes these recommendations.

Recommend Designating Portion of Additional Funding for Apportionments. Given cost pressures on community college districts and the availability of additional Proposition 98 funding at the May Revision, we think providing additional funding for apportionments is reasonable. Providing more general purpose funding would increase budget flexibility for districts as they work to meet state and local priorities.

Recommend Funding Deferred Maintenance. Given CCC has a substantial backlog of deferred maintenance, we recommend providing additional funding to reduce the backlog.

Recommend Lowering Enrollment Growth Estimate for 2017-18. Based on updated attendance reports, we believe a systemwide enrollment growth target of 1 percent is more reasonable than the higher January proposal of 1.34 percent. Attendance data show roughly two-thirds of districts have been experiencing enrollment declines in recent years, with roughly one-third of districts still continuing to grow.

Recommend Reducing 2016-17 Enrollment Funding. Based on recent attendance reports, we estimate the state will have at least $50 million in unused enrollment growth funding for the current year. The Legislature could redirect this funding to deferred maintenance or other one-time Proposition 98 priorities. (We have no concerns with the administration's enrollment funding adjustment for 2015-16, as it aligns with final attendance reports.)

Recommend Approving Increase in Full-Time Student Success Grant. As noted in our recent report, *Creating a Debt Free College Program*, many community college students have considerable unmet financial need. Receiving more financial aid could allow some students to reduce the number of hours they work per week, thereby making full-time enrollment more manageable. Full-time enrollment is associated with better student outcomes, including higher completion rates and less time to degree. For these reasons, we recommend approving the proposed augmentation. Given the proposed increase in the maximum annual award is small ($100), the impact on student behavior, however, also is likely to be small.

Revenue-Related Adjustments to 2015-16 Should Conform to Overall Proposition 98 Package. The May Revision proposals to restore the local revenue backfill and rescind January adjustments for higher revenue from property taxes and student fees are unrelated to changes in revenue estimates. Instead, they are related to the Governor's Proposition 98 funding target for 2015-16. Whether to approve these adjustments will depend on the Legislature's overall decision about its target Proposition 98 funding level in 2015-16.

Recommend Modifying Guided Pathways Language. We believe the May Revision modifications to the guided pathways initiative are modest improvements from the Governor's January proposal. In particular, we believe the addition of a more specific definition of guided pathways, early outcome indicators, and authorization to use the funds over five years are constructive changes. The proposal does not, however, go far enough toward increasing the likelihood that funding results in the desired improvements. As discussed below, we have several remaining concerns and recommend certain associated changes.

Figure 10

Summary of CCC Recommendations

Program	May Revision Proposal	LAO Recommendation
General purpose apportionment funding	Increases by $160 million ongoing.	***Adopt.*** Colleges can use flexible funds to meet highest priorities.
Deferred maintenance and instructional equipment	Provides additional $92 million one time, bringing total to $136 million one time.	***Adopt.*** Addressing CCC's deferred maintenance backlog is a high state priority for one-time funding.
Enrollment growth	Lowers 2017-18 growth rate from 1.34 percent to 1 percent and reduces by $22 million. Authorizes allocation of unused amount to backfill apportionment shortfalls.	***Adopt.*** Based on recent attendance reports, 1 percent is a more reasonable estimate.
	Makes no change to 2016-17.	***Modify.*** Reduce funding by $50 million to reflect updated attendance reports and redirect funds to deferred maintenance or other high one-time priorities.
	Revises 2015-16 upward by $26 million to reflect smaller enrollment decline than expected.	***Adopt.*** Reflects updated attendance reports.
Full-Time Student Success Grants	Increases by $1.9 million to raise award by $100 per year (for new maximum award of $700) and increases caseload estimate.	***Adopt.*** Community college students have significant unmet financial need.
2015-16 apportionment increases	Increases 2015-16 funding by a total of $55 million to reach higher Proposition 98 spending level.	***Conform to Proposition 98 Package.*** Spending level in 2015-16 will need to conform to overall budget package. No major underlying programmatic issues.
Guided pathways	Makes various policy changes.	***Modify.*** Adopt proposed changes but increase amount designated for state-directed technical assistance to participating colleges and strengthen accountability requirements.
State operations	Provides additional state operations funding and positions.	***Adopt.*** CCC and DOF staffing review indicates additional data, technology, research, institutional effectiveness, and legal services support warranted.
Equal Employment Opportunity (EEO)	Provides $1.8 million from EEO Fund (one time).	***Adopt.*** Uses special fund balance for authorized purposes.
Apprenticeships	Provides colleges two additional years to use 2015-16 and 2016-17 California Apprenticeship Initiative grants.	***Adopt.*** We have no concerns about this proposal.
Contracts	Exempts certain contracts from competitive bidding. Applies only to contracts between Chancellor's Office and colleges.	***Modify.*** Exempt contract renewals, but not new contracts.

- ***Decentralized Approach.*** As we noted in *The 2017-18 Budget: Higher Education Analysis*, existing large-scale guided pathways initiatives in other states have retained all funding centrally to provide expertise, professional development, and technical assistance to colleges. They have not funded colleges directly. The Governor's January and May proposals, in contrast, give at least 90 percent of the funding to colleges and set aside only up to 10 percent for centralized support. Such a decentralized approach risks shortchanging colleges on the professional development and technical assistance component. We think setting aside at least 35 percent of the funding for centrally coordinated technical assistance teams would very likely improve implementation efforts. The central funds also could be used for collecting and monitoring of data on early outcome indicators, as well as providing feedback and support to colleges.

- ***Scope of Implementation for Participating Colleges.*** The proposal continues to lack clarity as to whether a participating college must work toward creating pathways for all entering students, or could instead create a more limited program for a subset of students.

- ***Use of Funds.*** Although the proposed list of potential uses for program funds is a good start, we recommend adding that these one-time funds may not be used to provide direct services to students or fund other ongoing operational costs. The state already provides significant funding for these other purposes. The aim of guided pathways is to make strategic changes ensuring those ongoing efforts are as effective as possible.

- ***Applicant Screening and Award Payments.*** The May Revision *authorizes* but does not *require* that the Chancellor conduct more thorough screening of applicants and set progress criteria for releasing funds. We recommend these components be made requirements.

Recommend Approving New State Operations Proposal. The May Revision proposal stems from a comprehensive organizational review of the Chancellor's Office conducted over several months by its staff and the Department of Finance. The review indicates additional staffing is warranted in the Technology, Research, and Information Systems Division and the Office of the General Counsel. In addition, if the Legislature approves the Governor's guided pathways proposal, the additional position in the Institutional Effectiveness Division also will be warranted. Given identified workload and existing staffing, we believe the proposed allocation of General Fund support for three new positions and an existing vacant position, supplemented by reimbursement authority for three additional positions, is reasonable.

Other Recommendations. We have no concerns about the Governor's Equal Employment Opportunity funding proposal. It uses special funds for authorized purposes. We also have no concerns about the Governor's proposal to give apprenticeship grant recipients additional time to use funding. Finally, we recommend modifying the May Revision proposal on district contracts to exempt only contract *renewals* from competitive bidding requirements.

CALIFORNIA STATE UNIVERSITY

California State University (CSU) Funding Up From January Levels by $121 Million, Primarily Due to Recognizing Tuition Increase. The top part of Figure 11 compares state General Fund and tuition revenue for CSU under the Governor's January budget and May Revision. Under the May Revision, combined CSU funding from the two sources is $121 million (2 percent) higher than in the Governor's January budget. This consists of $135 million in higher tuition revenue offset by a $15 million decline in state General Fund support. As compared with the revised 2016-17 level, CSU funding in 2017-18 is $247 million (4 percent) higher. Under the May Revision, CSU's combined General Fund and tuition revenue reaches $6.8 billion in 2017-18. Below, we describe and assess the May Revision proposals for CSU.

Spending Changes

Revises Base General Fund Increase Downward by $15 Million. As Figure 12 shows, this reduction results from two adjustments. Under the May Revision, CSU receives an unrestricted base increase of $153 million rather than $157 million. (This $4 million drop could be framed in many ways, including being conveyed as an adjustment to reflect higher Cal Grant costs due to CSU's tuition increase. The administration, however, links the drop to its proposal to keep private Cal Grant awards at their current level rather than cutting them as previously scheduled.) The May Revision also adjusts CSU's General Fund support downward by $11 million to reflect recently revised state contribution rates for CSU pensions.

Provides $2 Million From Transportation Special Fund. Pursuant to Chapter 5 of 2017 (SB 1, Beall), the May Revision appropriates $2 million from the State Transportation Fund to CSU for transportation research and transportation-related workforce training and education.

Figure 11

Changes in General Fund and Tuition Revenue for the Universities

(In Millions)

	2015-16 Revised	2016-17 Revised	2017-18 Governor's Budget	2017-18 May Revision	2017-18 Change	Year-to-Year Change at May Revision
California State University						
General Fund						
Ongoing	$3,271	$3,479	$3,714	$3,699	-$15	$220
One time	5	110	1	1	—	-109
Subtotals	($3,276)	($3,589)	($3,715)	($3,700)	(-$15)	($112)
Tuition and fees	$3,022	$2,963	$2,963	$3,098	$135	$135
Totals	**$6,298**	**$6,552**	**$6,678**	**$6,799**	**$121**	**$247**
University of California						
General Fund						
Ongoing	$3,135	$3,279	$3,362	$3,358	-$4	$79
One time	124	262	169	169	—	-93
Subtotals	($3,259)	($3,541)	($3,531)	($3,527)	(-$4)	(-$14)
Tuition and fees	$4,087	$4,393	$4,548	$4,623	$74	$229
Totals	**$7,346**	**$7,934**	**$8,079**	**$8,150**	**$70**	**$216**

Figure 12

2017-18 California State University General Fund Changes

(In Millions)

	Governor's Budget	May Revision	Change
Unrestricted base increases (ongoing)			
Funding per Governor's original long-term plan	$131	$127	-$4
Redirected savings from Middle Class Scholarship modifications	26	26	—
Subtotals	($157)	($153)	(-$4)
Pension adjustment (ongoing)	$50	$39	-$11
Retiree health benefits adjustment (ongoing)	23	23	—
Lease-revenue bond debt service adjustment (ongoing)	5	5	—
Remove one-time funding provided in prior year	-87	-87	—
Other adjustments	-22	-22	—
Total Changes	**$126**	**$112**	**-$15**

Assessment and Recommendations

The top part of Figure 13 (see next page) summarizes our recommendations for CSU, which we discuss below.

Under May Revision, CSU Has Sizeable Unrestricted Base Increase. In March 2017, the CSU Board of Trustees approved a tuition increase for resident and nonresident students. This increase, which is scheduled to take effect in fall 2017, will generate net revenue of about $95 million in 2017-18 ($135 million in gross revenue less about $40 million that CSU intends to use for tuition discounts and waivers for certain students). When combined with the $153 million unallocated ongoing General Fund augmentation included in the May Revision, CSU would have $248 million (4 percent) in additional unrestricted base resources in 2017-18 compared with the current year.

Administration Does Not Earmark Any of Increase for Enrollment Growth. CSU has indicated that it intends to use the additional unrestricted monies to address a number of its priorities, including using (1) $139 million to fund collective bargaining agreements that were approved by the Board of Trustees last spring, (2) $26 million to cover basic cost increases (such as higher health care premiums for employees), and (3) $75 million for the system's Graduation Initiative (primarily to make available more courses to current students). CSU has indicated that without additional funding from the state (beyond the amount proposed in the May Revision), it does not intend to fund enrollment growth in 2017-18.

Recommend Approving May Revision Funding Level but Setting Expectation for Enrollment Growth. In *The 2017-18 Budget: Higher Education Analysis*, we note that CSU has reported denying admission in recent years to some eligible transfer students. Given this development, together with statute that requires CSU to prioritize transfer applicants, we continue to recommend the Legislature signal to CSU that increasing transfer enrollment is a priority. The Legislature could send this signal by adopting provisional language that sets an enrollment target for new transfer students. An expectation of 2 percent enrollment growth in the budget year would result in about 7,200 more FTE transfer students being served, which we estimate would allow CSU to accommodate all or virtually all transfer applicants in 2017-18. Under our recommendation, costs for CSU to serve these students, which we estimate

Figure 13

Summary of University Recommendations

Issue	May Revision Proposal	LAO Recommendation
California State University		
Unrestricted base increase	Reduces General Fund base increase from $157 million to $153 million. Recognizes 5 percent tuition increase. Places no conditions on funding.	***Modify.*** Approve May Revision base increase. Coupled with tuition increase, funding sufficient to cover core costs. Add budget bill language specifying enrollment target for new transfer students.
Transportation research	Provides $2 million from transportation special fund for transportation research.	***Adopt.*** Implements recently chaptered legislation.
University of California		
Unrestricted base increase	Reduces General Fund base increase from $81 million to $77 million. Recognizes 2.5 percent tuition increase.	***Modify.*** Approve May Revision base increase. Coupled with tuition increase, funding sufficient to cover core costs. Add budget bill language specifying 2018-19 enrollment target.
Conditions placed on portion of base increase	Makes $50 million of UC's base increase contingent on implementing recommendations made by the State Auditor, increasing transfer enrollment, and piloting activity-based costing at three campuses.	***Modify.*** Adopt specified conditions but conduct additional legislative oversight of UC's budget.
Transportation research	Provides $5 million from transportation special fund for transportation research.	***Adopt.*** Implements recently chaptered legislation.
Breast cancer research	Increases January proposal by $2.1 million from breast cancer research special fund.	***Adopt.*** Reflects updated revenue estimates.
Tobacco disease-related research	Increases proposed Proposition 56 funding by $1.2 million and Proposition 99 funding by $3,000.	***Adopt.*** Reflects updated revenue estimates.

at about $60 million (after factoring in about $20 million in net tuition revenue generated by the additional students), likely would come at the expense of CSU's Graduation Initiative. Given the opportunities we have identified for CSU to reform its assessment practices and make available more course slots by reducing excess units, we believe CSU can make significant progress on improving student outcomes without funding set aside for the Graduation Initiative in the budget year.

UNIVERSITY OF CALIFORNIA

Funding for the University of California (UC) Higher Than January Level by $70 Million. The bottom part of Figure 11 (page 24) compares state General Fund and tuition revenue for UC under the Governor's January budget and May Revision. Under the May Revision, combined UC funding from the two sources is $70 million (1 percent) higher than reflected in the Governor's budget. This amount consists of $74 million in higher gross tuition revenue, offset by a $4 million decline in state General Fund support. As compared with the revised 2016-17 level, UC funding in 2017-18 is $216 million (3 percent) higher. Under the May Revision, UC's combined General Fund and tuition revenue reaches $8.2 billion in 2017-18. Below, we describe and assess the May Revision proposals for UC.

Spending Changes

Revises Base General Fund Increase Downward by $4 Million. As Figure 14 shows, the May Revision includes an unrestricted base increase for UC of $77 million rather than $81 million proposed in January. (As we note in the "California State University" section, the administration links this drop to its private Cal Grant award proposal, though the decrease could be framed in many other ways.) In addition to the $77 million base increase, the Governor continues his January expectation regarding Proposition 56 funding. Under his proposal, he would use $50 million in Proposition 56 monies designated for graduate medical education to free up a like amount of General Fund that UC currently spends for those purposes. Taken together, these actions would effectively provide the university system with a total base General Fund increase of $127 million.

Conditions a Portion of State Funding on UC Meeting Three Expectations. The May Revision conditions $50 million of the base General Fund increase on UC meeting three expectations, as described below. If the Department of Finance deems UC to have met the conditions, it would release the $50 million in May 2018.

- ***State Auditor Recommendations.*** In an April 2017 report, the State Auditor identified a number of problems with the UC Office of the President (UCOP), including the office's staffing size and costs, spending on systemwide programs, and overall budget. The Auditor's report included dozens of recommendations designed to enhance transparency, operational performance, and state oversight. The Auditor called for these recommendations to be implemented over a three-year period (between April 2018 and April 2020). The May Revision would link budget-year funding with UC's implementation of the April 2018 recommendations.

- ***Transfer Enrollment.*** The May Revision also expects all but two campuses (Merced and San Francisco) to enroll at least one new transfer student for every two new freshman students for the 2018-19 academic year. That is, at least one-third of

Figure 14

2017-18 University of California General Fund Changes

(In Millions)

	Governor's Budget	May Revision	Change
Pay down unfunded pension liability (one time)	$169	$169	$0
Unrestricted base increase (ongoing)	81	77	-4
Resume funding for medical education program (ongoing)	2	2	—
Remove one-time funding provided in prior year	-262	-262	—
Total Changes	**-$10**	**-$14**	**-$4**

each campus's new resident undergraduate enrollment would need to be transfer students. This target is intended to align with policies called for in the 1960 *Master Plan for Higher Education*. In 2015-16, 31 percent of UC's incoming resident undergraduates were transfer students.

- ***Activity-Based Costing.*** The May Revision's final condition is for UC to pilot activity-based costing at three campuses. The purpose of activity-based costing is to identify program- and course-level costs of providing instruction and other services to students. Currently, one pilot is underway at the Riverside campus, and two campuses (Merced and Davis) have completed scoping studies for pilot programs.

While the first expectation reflects the State Auditor's recent findings, the other two expectations (transfer enrollment and activity-based costing) reflect goals UC previously committed to achieve in a May 2015 agreement with the Governor.

Recognizes Tuition Increase. In late January, the UC Regents adopted a tuition level of $11,502, a $282 (2.5 percent) increase over the 2016-17 level. UC estimates this increase will generate $74 million in additional revenue, of which $26 million will be redirected for financial aid. The May Revision recognizes this increase. (UC also adopted 5 percent increases in the Student Services Fee and nonresident supplemental tuition, which the Governor's January budget recognized.)

Includes Several Special Fund Revisions. The May Revision includes the following special fund revenue adjustments: (1) a $2.1 million adjustment for breast cancer research, for total funding of $7.2 million, and (2) a $1.2 million combined increase in Proposition 56 and Proposition 99 funding for tobacco-related disease research, for total combined funding of $92 million. The proposals reflect updated revenue estimates in each fund. Additionally, pursuant to Chapter 5 of 2017 (SB 1, Beall), the Governor proposes appropriating $5 million from the State Transportation Fund to UC for transportation research.

Assessment and Recommendations

The bottom part of Figure 13 (page 26) summarizes our recommendations for UC, which we discuss below.

May Revision Funding Sufficient to Cover UC's Core Costs. As we noted in *The 2017-18 Budget: Higher Education Analysis*, the Governor's January proposal, coupled with UC's adopted tuition increases and other sources of new revenue, sufficiently covers UC's core costs in the budget year. Because overall proposed funding for the university system is virtually unchanged from January, we do not have concerns with the May Revision funding level. We continue to recommend, however, that the Legislature adopt resident enrollment targets in the budget act for the 2018-19 academic year. (The state already has funded enrollment growth for the 2017-18 academic year, and we recommend it wait to fund 2018-19 enrollment until 2018-19.)

Shared Interest in Implementing Auditor's Recommendations. The State Auditor's April 2017 report includes a number of recommendations designed to improve transparency and accountability at UCOP, including (1) developing a budget display that shows all actual and planned spending, (2) adopting a formal reserve policy, and (3) developing a comprehensive list of systemwide initiatives. We share the administration's goals of ensuring UC meaningfully implements these recommendations.

Recommend Legislature Adopt May Revision Conditions of Funding and Conduct Oversight Hearings. Given the general concerns regarding the recent audit and UC's previous commitments to attain specified transfer ratios and implement activity-based costing, we think the Governor's proposed conditions are reasonable. We note, however, that the language gives the Governor authority to determine whether UC has satisfied each expectation. To ensure UC also is responsive to legislative priorities, we recommend the Legislature conduct oversight hearings throughout next year on key issues of interest. For example, it might hold an oversight hearing to learn more about UCOP's staffing size and costs. To the extent UC does not meet legislative expectations, the Legislature will have the opportunity to respond through the budget process next year.

STUDENT FINANCIAL AID

Student Financial Aid Funding Up Under May Revision. Figure 15 compares total funding for the California Student Aid Commission (CSAC) under the Governor's January budget and May Revision. Funding in 2017-18 is up $114 million compared with the Governor's budget. Under the May Revision, total funding for CSAC in 2017-18 is $2.2 billion, reflecting an increase of $109 million (5 percent) over the revised 2016-17 level. Below, we describe and assess the May Revision proposals for CSAC.

Figure 15

California Student Aid Commission Budget

(In Millions)

	2015-16 Revised	2016-17 Revised	2017-18 Governor's Budget	2017-18 May Revision	2017-18 Change	Year-to-Year Change at May Revision
Expenditures						
Local Assistance						
Cal Grants	$1,861	$1,986	$1,986	$2,109	$123	$124
Middle Class Scholarships	44	74	74	64	-10	-10
Assumption Program of Loans for Education	14	10	7	7	1	-3
Chafee Foster Youth Program	11	14	14	14	—	—
Student Opportunity and Access Program	8	8	8	8	—	—
National Guard Education Assistance Awards	2	2	2	2	—	—
Other Programs[a]	1	1	1	1	—	—
Subtotals	($1,941)	($2,095)	($2,093)	($2,206)	($113)	($111)
State Operations	$14	$17	$14	$15	$1	-$2
Totals	**$1,955**	**$2,112**	**$2,107**	**$2,221**	**$114**	**$109**
Funding						
General Fund	$1,419	$1,163	$1,153	$1,078	-$75	-$85
Federal TANF	521	926	926	1,120	194	194
Other[b]	16	23	29	23	-6	—

[a] Includes Cash for College, Child Development Teacher and Supervisor Grants, Graduate Assumption Program of Loans for Education, John R. Justice Program, Law Enforcement Personnel Dependents Scholarships, and State Nursing Assumption Program of Loans for Education for Nursing Faculty.

[b] Includes College Access Tax Credit Fund, Student Loan Authority Fund, and other federal funds.

TANF = Temporary Assistance to Needy Families.

Spending Changes

Adjusts Cal Grant Funding Based on Updated Participation Estimates. The May Revision decreases Cal Grant funding by $56 million in 2015-16 and increases it by $33 million in 2016-17 and $72 million in 2017-18 to reflect updated Cal Grant participation estimates.

Increases Cal Grant Award Amounts for Students Attending CSU and UC. The May Revision includes $49 million for higher Cal Grant costs for students attending CSU ($28 million) and UC ($21 million). These changes conform to CSU's and UC's scheduled tuition increases (5 percent and 2.5 percent, respectively). Cal Grant awards cover full tuition costs at CSU and UC (with the exception of some first-year students).

Maintains Cal Grant Award Amount for Private, Nonprofit Schools but Establishes Conditions. The Governor's January budget scored savings due to a statutorily scheduled decrease in the Cal Grant award for low-income students attending private, nonprofit schools. Specifically, the award is set to decrease from $9,084 to $8,056, beginning in 2017-18. The May Revision provides $8 million relative to the Governor's budget to maintain the award at its existing level. The administration proposes to eliminate any future scheduled reduction in the award. As a condition of receiving the $1,028 differential, however, the Governor proposes that institutions benefitting from the award enroll more low-income students, enroll more transfer students, and offer more online courses.

Reduces Cal Grant B Supplement. The May Revision adjusts funding for the Cal Grant B supplement downward by $5.6 million. The supplement provides additional funding to all Cal Grant B recipients based on the amount of funds annually deposited in the College Access Tax Credit Fund. The reduction lowers the per-award supplement from $49 to $24—a decrease of $25. The reduction conforms to updated estimates of the resources available in the special fund.

Provides CSAC With Authority to Offer More Initial Competitive Cal Grant Awards. The May Revision proposes to allow CSAC to make 35,000 initial competitive Cal Grant award offers in 2017-18. It makes no changes, however, to funding or to the maximum authorized number of new paid awards (25,750). The proposal maintains the current-law requirement that CSAC make half of its award offers in March and the other half in September. CSAC reports that the competitive Cal Grant has a utilization rate of 96 percent annually. The administration indicates that to use 100 percent of funding and allow more students to receive awards earlier in the year, CSAC would like a statutory change explicitly allowing it to make a larger number of additional initial Cal Grant offers.

Decreases Middle Class Scholarship Funding Based on Updated Participation Estimates. The May Revision reduces funding for Middle Class Scholarships in 2017-18 by $10 million (bringing total funding down from $74 million to $64 million). The reduction reflects a decline in participation estimates. In addition, the Governor reduces the scholarship by $4.5 million in 2015-16 to conform with updated participation estimates (bringing the total down from $48 million to $44 million in that year). The May Revision makes no change to the Governor's January proposal to phase out the Middle Class Scholarship over the next four years.

Small Adjustments to Other Financial Aid Programs. The May Revision makes small adjustments in participation and award amounts to several other financial aid programs, including the Assumption Program of Loans for Education (APLE), the State Nursing Assumption Program of Loans for Education (SNAPLE), the Child Development Teacher and Supervisor Grant Program, the John R. Justice Loan Assumption

Program, and the Law Enforcement Personnel Dependent Grant Program.

Provides Funding for IT Project Planning. The May Revision includes $546,000 in one-time funding for CSAC to continue working on replacing its online grant delivery system. CSAC uses its grant delivery system to process financial aid applications, make aid offers, and process payments. The project currently is moving through the California Department of Technology's "Project Approval Lifecycle" process. Most state IT projects are required to go through this four-stage planning process. The CSAC project currently is in stage two of the process. Of the proposed $546,000, $296,000 is to allow CSAC to continue contracting with an external project management team and $250,000 is for required contracting with the Department of Technology.

Increases Temporary Assistance for Needy Families (TANF) Support, Decreases General Fund Support Accordingly. The May Revision increases federal TANF support by $194 million and decreases state General Fund by that amount. This fund swap has no programmatic effect.

Assessment and Recommendations

As Figure 16 shows (see next page), we recommend adopting most of the financial aid proposals in the May Revision. Below, we assess and provide recommendations for two proposals for which we have concerns.

Recommend Maintaining Private, Nonprofit Cal Grant Award at Existing Level but Rejecting Proposed Conditions as Part of Budget Closeout. We continue to recommend that the Legislature establish a statutory policy for private Cal Grant awards similar to the one in effect prior to 2000. This policy linked the private award to costs and tuition at UC and CSU. If the Legislature were to adopt the same policy as back then, we calculate the private, nonprofit Cal Grant award amount (or aspirational goal) would be $16,510. By not lowering the award amount, as proposed in the May Revision, the award amount would be closer to this aspirational goal. Though we think setting the award amount no lower than its existing rate is reasonable, we have concerns with placing conditions on the awards. To date, the state has not placed unique conditions on private, nonprofit Cal Grant awards (apart from institutional eligibility criteria relating to graduation rates and student loan default rates, which also apply to UC and CSU campuses). Adding such conditions therefore would reflect a substantial policy change. If the Legislature wishes to place special stipulations on private, nonprofit Cal Grant awards, we believe this is better done as part of a broader policy making process, whereby clear objectives, performance measures, and enforcement mechanisms could be established.

Reject Proposal to Provide CSAC With Authority to Offer More Initial Competitive Cal Grant Awards. Current law places no cap on the number of awards CSAC may offer annually. Thus, CSAC does not need legal authority to offer more awards. If the Legislature is concerned that a 96 percent utilization rate is too low or that some students are receiving awards too late in the year, it could explore policy responses to those specific problems. For example, to increase the utilization rate, the Legislature could establish a process for allowing CSAC to run a deficiency request if it paid out slightly more than the maximum allowable number of new awards. Under this approach, the Legislature might set a cushion of 2 percent, thereby allowing CSAC to run over the cap by about 500 awards and still be funded for those awards.

Figure 16

Summary of Financial Aid Recommendations

Program	May Revision Proposal	LAO Recommendation
Cal Grants		
Participation	Decreases by $56 million in 2015-16, increases by $33 million in 2016-17, and increases by $72 million in 2017-18.	***Adopt.*** Conforms with updated participation estimates.
Awards for students at UC and CSU	Increases by $49 million ($21 million UC and $28 million CSU).	***Adopt.*** Conforms with UC and CSU tuition increases.
Awards for students at private, nonprofit schools[a]	Provides $8 million to maintain award at $9,084 (rather than reducing to $8,056 as previously scheduled). Links the $1,028 difference in award amount to three conditions (enrolling more low-income students, enrolling more transfer students, and offering more online courses).	***Modify.*** Adopt funding level but reject conditions without prejudice. Could consider any new conditions as part of developing a statutory policy on private, nonprofit awards.
Cal Grant B supplement from College Access Tax Credit Fund	Decreases by $5.6 million (reducing the award supplement from $49 to $24).	***Adopt.*** Conforms with updated estimates of available resources.
Initial offers for competitive awards	Provides CSAC authority to make 35,000 initial award offers in 2017-18 but continues to fund 25,750 new awards.	***Reject.*** Does not address root issue.
Other		
Middle Class Scholarships	Decreases by $4.5 million in 2015-16. Decreases by $10 million in 2017-18.	***Adopt.*** Conforms with updated participation estimates.
Grant Delivery System Modernization Project	Provides $546,000.	***Adopt.*** Allows CSAC to continue IT project planning.
Temporary Assistance for Needy Families (TANF)	Increases federal TANF support by $194 million, with a corresponding decrease in General Fund support of that amount.	***Adopt.*** Reflects fund swap and has no programmatic effect.
Other financial aid programs[b]	Adjusts for changes in participation and award amounts.	***Adopt.*** Conforms with updated estimates.

[a] Also applies to for-profit institutions that are accredited by the Western Association of Schools and Colleges.

[b] Applies to Assumption Program of Loans for Education (APLE), State Nursing Assumption Program of Loans for Education (SNAPLE), Child Development Teacher and Supervisor Grant Program, John R. Justice Loan Assumption Program, and Law Enforcement Personnel Dependent Grant Program.

CSAC = California Student Aid Commission and IT = information technology.

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