

# MAJOR ISSUES

## *K-12 Education*

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### **Legislature's Funding Decisions Need to Balance State and Local Needs**

- The Governor's Budget proposes to direct all new Proposition 98 funding in 1997-98 to support new or expanded K-12 categorical programs. No budget-year increase in general purpose funding is proposed.
- After providing adequate funding to support continuing program costs and other financial commitments, we recommend the Legislature direct about half of any available funds for state-directed purposes and use the remaining funds to increase local general purpose funding (see page E-17).
- We also recommend the Legislature reform the system of K-12 categorical programs by consolidating 21 programs into four categorical block grants. This would increase local flexibility and focus district programs on improving student achievement (see page E-68).

### **Survey on Class Size Reduction Shows Implementation Has Stretched Thin Teacher and Facility Resources**


- A survey of 150 districts showed three major problems with the current program, including (1) the inflexibility of the 20 students to one teacher limit creates substantially higher costs and other problems for districts, (2) teachers hired for the program are less qualified than teachers hired in previous years, and (3) districts appear to be running out of lower cost options for class-size facilities.
  - Our recommendations include (1) providing greater district flexibility over the use of teachers funded under the program, (2) delaying implementation of a fourth grade due to short-
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ages of qualified teachers and facilities, and (3) approving the per-pupil level of class size funding proposed in the budget (see page E-35).

**LAO's Ten-Year Plan for Increasing District Maintenance and Eliminating Deferred Maintenance**

- District deferred maintenance needs totaled about \$2.7 billion in 1995-96. To address this problem, we recommend the state commit \$2 billion in new state funds over ten years to help districts reduce or eliminate their current backlog.
- In return, districts must commit to increasing ongoing maintenance over three years to a level that ensures that districts are no longer deferring needed maintenance. Districts would be eligible for the \$2 billion in deferred maintenance funds only if a commitment to adequate maintenance is made (see page E-82).

**Large Increase in Federal Funds Magnifies the Flaws in the Design of the State's Subsidized Child Care Programs**

- The budget proposes to add significant new federal child care funds in 1997-98 to existing programs in the state Department of Education (SDE). The proposal does little to address significant program problems, however, including (1) undue complexity in the design and administration of the program and (2) inability of the programs to absorb large funding increases.
  - We recommend reducing by \$43.9 million the additional funding for SDE child care programs. These funds could be directed to the Department of Social Services if needed for welfare reform or could be restored to SDE in the future as the programs are able to expand (see page E-91).
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# OVERVIEW

## *K-12 Education*

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**The budget includes an increase in K-12 Proposition 98 funding of \$1.7 billion in the budget year. This is \$190 per student, or 3.9 percent, more than the revised estimate of per-student expenditures in the current year. The budget also proposes to spend \$836.9 million from prior-year Proposition 98 funds in 1997-98.**

Figure 1 (see page 6) shows the budget from all fund sources for K-12 education for the budget year and the two previous years. Proposition 98 funding constitutes about three-fourths of overall K-12 funding. In 1997-98, Proposition 98 funding is projected to increase by \$190 per student to \$5,010. This is a 3.9 percent increase from the revised 1996-97 per-student amount.

The budget also proposes to spend \$836.9 million from prior-year Proposition 98 funds in 1997-98. As a result of increases in the minimum amounts guaranteed to schools in 1995-96 and 1996-97 (due primarily to higher tax revenues and increased ADA), the state owes schools \$629.5 million more for those years (referred to as “settle-up” funds). An additional \$207.4 million results primarily from *unspent* prior-year Proposition 98 funding.

Figure 1 also shows that the budget includes expenditures of \$3.2 billion in federal funds in 1997-98. This is \$478 million, or 18 percent, more than estimated federal expenditures in the current year. Major changes in federal K-12 funding include the following additional amounts: \$226 million for child development, \$95 million for Goals 2000, \$89 million for child nutrition and \$78 million for special education.

***School Districts by Type and Enrollment.*** A total of 5.4 million pupils attended school in California’s 999 school districts in 1995-96. Figure 2 (see page 7) provides enrollment data by size of school district. Enrollment levels vary significantly among school districts. For example, the state’s largest school district, Los Angeles Unified, enrolled 647,600 students in 1995-96, which is more than the combined enrollment of over 600 of the state’s smallest school districts.

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<b>Figure 1</b>					
<b>K-12 Education Budget Summary 1995-96 Through 1997-98</b>					
<b>(Funding in Millions)</b>					
	Actual 1995-96	Estimated 1996-97	Proposed 1997-98	Change From 1996-97	
				Amount	Percent
<b>K-12 Proposition 98</b>					
State (General Fund)					
Cash	\$16,086.8	\$17,542.7	\$18,919.8	\$1,377.1	7.9%
Loan repayment	100.0	150.0	200.0	50.0	33.3
Local property tax revenue	8,574.9	8,727.2	9,027.5	300.3	3.4
Subtotals, Proposition 98	(\$24,761.7)	(\$26,419.9)	(\$28,147.3)	(\$1,727.4)	(6.5%)
<b>Other Funds</b>					
General Fund					
Teachers retirement	\$775.4	\$809.4	\$848.7	\$39.3	4.9%
Bond payments	721.6	762.9	812.1	49.1	6.4
Other programs	106.8	162.4	155.5	-6.9	-4.2
State Lottery funds	691.5	582.0	582.0	—	—
Other state funds	40.4	64.1	57.5	-6.6	-10.2
Federal funds	2,590.8	2,695.0	3,173.1	478.1	17.7
Other local	2,188.2	2,166.4	2,161.8	-4.7	-0.2
<b>Totals</b>	<b>\$31,876.3</b>	<b>\$33,662.2</b>	<b>\$35,938.0</b>	<b>\$2,275.8</b>	<b>6.8%</b>
<b>K-12 Proposition 98</b>					
Average Daily Attendance (ADA)					
	5,320,064	5,450,480	5,578,346	127,866	2.3%
Amount per ADA	\$4,636	\$4,820	\$5,010	\$190	3.9%

**Expenditures per ADA in Comparison to Other States.** Figure 3 compares expenditures per ADA in constant dollars (that is, adjusted for inflation) for selected states, the nation as a whole, and California. The states selected for comparison are the eight largest states, which we refer to as the "Big Eight": Florida, Illinois, Michigan, New Jersey, New York, Ohio, Pennsylvania, and Texas. We also show an average for the "Big Six," which includes the eight states less New Jersey and New York. As shown in Figure 3, including New Jersey and New York in the calculation significantly increases the average. New Jersey and New York spent approximately \$9,900 per ADA in 1995-96.

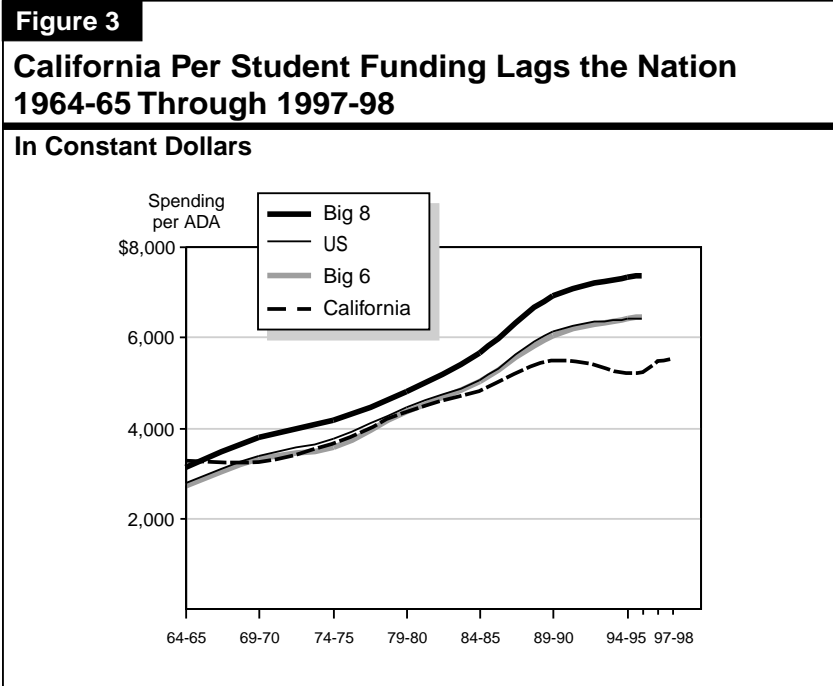
Figure 3 shows expenditures per ADA projected through 1997-98 for California. Data for the other states was available through 1995-96. Be-

**Figure 2**

**Distribution of School Districts by Enrollment  
October 1995**

Enrollment Level	Number of Districts				Enrollment	
	Elem	High		Total	Total	Percent of Total
		School	Unified			
More than 200,000	—	—	1	1	647,612	12.0%
100,000 to 199,999	—	—	1	1	130,360	2.4
50,000 to 99,999	—	—	6	6	373,113	6.9
40,000 to 49,999	—	—	3	3	136,085	2.5
20,000 to 39,999	2	5	33	40	1,093,180	20.2
10,000 to 19,999	21	10	55	86	1,214,070	22.4
5,000 to 9,999	45	17	61	123	877,224	16.2
2,500 to 4,999	65	18	50	133	478,208	8.8
1,000 to 2,499	95	25	50	170	303,237	5.6
500 to 999	89	18	22	129	93,471	1.7
Less than 500	269	11	27	307	63,327	1.2
<b>Totals</b>	<b>586</b>	<b>104</b>	<b>309</b>	<b>999</b>	<b>5,409,887</b>	<b>100.0%</b>

Data exclude county offices of education. Grand total including county offices is 5,467,224.



tween 1964-65 and 1984-85 California's spending per ADA was roughly equal to both the US average and the average for the "Big Six." Starting in about 1985, California's spending began to increase at a slower rate, and it actually fell during the early 1990s. In 1995-96 California's expenditures per ADA began to increase again. Even with this turn-around, California expenditures per ADA are about \$1,000 lower per student than the U.S. and the Big 6 averages.

## PROPOSITION 98

Proposition 98, enacted in 1988 as a voter-approved amendment to the California Constitution (later amended by Proposition 111 in 1990), establishes a minimum funding level for K-12 schools and the California Community Colleges (CCC). Proposition 98 also provides support for direct educational services provided by other agencies, such as the state's special education schools and the California Youth Authority. Proposition 98 funding constitutes about three-fourths of overall K-12 funding.

The minimum funding levels are determined by one of three specified formulas. Figure 4 briefly explains the workings of Proposition 98, its "Tests," and other major funding provisions. The five major factors involved in the calculation of each of the Proposition 98 "Tests" include: (1) General Fund revenues, (2) state population, (3) personal income, (4) local property taxes and (5) K-12 ADA.

Because these factors change during the year, the minimum guarantee under Proposition 98 also changes. Any additional amount needed to fund any *increase* in a previous year's guarantee is referred to as Proposition 98 "settle-up" funding. As noted above, the Governor's budget includes \$629.5 million related to "settle-up" for prior years (\$225.7 million from 1995-96 and \$403.8 million from 1996-97).

Figure 4 shows that currently "Test 1" is equal to 34.5 percent of General Fund revenues plus local property tax revenues. This percentage was originally calculated to be about 40 percent. In recognition of shifts in property taxes to K-14 schools from cities, counties and special districts, the rate was adjusted to the current rate of approximately 34.5 percent.

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**Figure 4**

**Proposition 98 at a Glance**

**Major Provisions of Proposition 98**

Proposition 98 guarantees K-14 school agencies an annual amount of funding equal to the greater of:

- a specified percent of the state’s General Fund revenues (Test 1), or
- the amount provided in the prior year, adjusted for growth in students and inflation (Tests 2 and 3).

This minimum guaranteed amount is determined by the steps below.

**Step 1: Compute “Test 1”**

**Test 1.** Multiply 34.5 percent times state General Fund revenues and add local property taxes.

**Step 2: Compare Inflation Factors**

Compare the annual change in:

- Per capita personal income to
- Per capita General Fund revenues plus 0.5 percent.

The lower of these factors determines which “Test” is compared to Test 1.

**Step 3: Calculate Either Test 2 or Test 3**

If the per capita **personal income** change is lower, calculate Test 2.

**Test 2** = Proposition 98 amount provided in prior year (combined state aid and local property taxes) adjusted for change in K-12 ADA and annual change in per capita personal income. Subtract current-year property taxes to yield the General Fund amount under Test 2.

If the per capita **General Fund** revenue change is lower, calculate Test 3.

**Test 3** = Same as Test 2 except that the inflation factor used is the annual change in per capita General Fund revenues plus 0.5 percent.

**Step 4: Compare Test 1 to Either Test 2 or Test 3**

The higher General Fund amount is the “Test” in effect for that year and is the minimum guaranteed by Proposition 98.

**Other Major Funding Provisions**

**Suspension**

Proposition 98 also includes a provision allowing the state to suspend the minimum funding level for one year through urgency legislation other than the budget bill.

**Restoration (“Maintenance Factor”)**

Proposition 98 includes a provision to restore prior-year funding reductions (due to either suspension or the “Test 3” formula). The overall dollar amount that needs to be restored is referred to as the “maintenance factor.”

### Proposition 98 Allocations by Segments

Figure 5 displays the allocation of Proposition 98 funding by segment. The overall increase for Proposition 98 in the current year is \$452.3 million. As Figure 5 shows, K-12 education's share of this amount is \$403.8 million, the Community College's allocation is \$48.2 million, and other agencies' funding of \$0.3 million accounts for the balance.

The budget proposes \$31.4 billion for Proposition 98 in 1997-98. The shares allocated to the three components remain virtually unchanged from the 1996-97 revised shares. Community College Proposition 98 funding issues are discussed in the Higher Education section of the *Analysis* (please see Section F).

<b>Figure 5</b>					
<b>Proposition 98 Allocations 1996-97 and 1997-98</b>					
<b>(Dollars in Millions)</b>					
	<b>1996-97</b>			<b>1997-98</b>	<b>Change From 1996-97 Revised</b>
	<b>Budget Act</b>	<b>Revised</b>	<b>Change</b>	<b>Proposed</b>	
<b>Proposition 98</b>					
“Test”	Test 3	Test 3	—	Test 3	—
<b>Total Proposition 98</b>	\$29,063.8	\$29,516.1	\$452.3	\$31,428.9	\$1,912.7
<b>K-12 Education</b>					
Amount	\$26,016.1	\$26,419.9	\$403.8	\$28,147.3	\$1,727.4
Share	89.5%	89.5%	—	89.6%	—
<b>Community Colleges</b>					
Amount	\$2,956.5	\$3,004.7	\$48.2	\$3,193.3	\$188.6
Share	10.2%	10.2%	—	10.2%	—
<b>Other Agencies</b>					
Amount	\$91.2	\$91.4	\$0.3	\$88.2	-\$3.3
Share	0.3%	0.3%	—	0.3%	—

### Governor's Budget Proposals for Prior-Year Proposition 98 Funds

As noted earlier, the budget proposes to allocate to K-12 education \$836.9 million in prior-year Proposition 98 funds. Figure 6 shows the major expenditure proposals which include:

<b>Figure 6</b>		
<b>K-12 Education Governor's Budget Proposals For Prior-Year Revenue</b>		
<b>(In Millions)</b>		
<b>Revenue Limits</b>		
Equalization and deficit reduction	\$304.2	
Additional growth in ADA	264.4	
Subtotal		\$568.6
<b>Program Expansions</b>		
Facilities for class size reduction	\$151.0	
CTC alternative credentialing	9.0	
Standardized account code	9.0	
Statewide assessments	6.0	
Single gender schools	5.0	
Oxnard HSD extended year program	3.9	
Other	1.0	
Subtotal		\$184.9
<b>New Programs</b>		
High school technology	\$50.0	
Child care facilities	15.0	
California Student Information System	10.0	
Angel Gate Academy (at-risk students)	6.4	
Kern telecommunications	2.0	
Subtotal		\$83.4
<b>Total</b>		<b>\$836.9</b>
<b>Sources</b>		
<i>Proposition 98 "Settle-Up"</i>		\$629.5
<i>Unspent class size reduction</i>		140.0
<i>Proposition 98 Reversion Account</i>		42.8
<i>Other sources</i>		24.6

- \$304.2 million to be equally divided for revenue limit equalization and deficit reduction. The Legislature provided for this allocation in Chapter 203, Statutes of 1996 (AB 3497, Richter). While this increase is built into the base for 1997-98, Chapter 203 requires that the 1996-97 amount not be released

until February 1998. Thus, there is both a one-time and ongoing effect of these funds in 1997-98.

- \$264.4 million due to revised ADA estimates. This cost continues in 1997-98.
- \$151 million for classroom facilities for the class size reduction (CSR) program. Of this amount, the budget proposes to redirect \$140 million from unspent CSR funds in the current year.
- \$50 million for a new High School Education Technology Incentive Grant Program.

We discuss the proposals shown in Figure 6 later in this *Analysis*.

## 1997-98 BUDGET PROPOSALS

The budget proposes a Proposition 98 funding increase of \$1.7 billion for 1997-98. Figure 7 highlights each of the major changes proposed for K-12 Proposition 98 in the budget year. The major budget proposals include:

- \$530.3 million for enrollment growth, based on a projected ADA increase of 2.35 percent in 1997-98.
- \$628.8 million to provide a 2.53 percent cost-of-living adjustment (COLA).
- \$296.8 million to expand the class size reduction program to a fourth grade.
- \$76.7 million set-aside for special education funding equalization and funding reform legislation.

We discuss the details of these proposals later in this *Analysis*.

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<b>Figure 7</b>		
<b>Governor's K-12 Budget Proposals</b>		
<b>1997-98 Proposition 98</b>		
<b>(In Millions)</b>		
<b>1996-97 (revised)</b>		\$26,419.9
<b>Enrollment Growth</b>		
District revenue limits	\$438.6	
County offices of education	13.5	
Special education growth	74.5	
Summer school growth	3.7	
Subtotal		\$530.3
<b>Cost-of-Living Increases</b>		
Revenue limits	\$490.9	
County limits	12.4	
Special education	76.4	
Other	49.1	
Subtotal		\$628.8
<b>Funding Adjustments</b>		
Class size reduction—base adjustment	\$160.1	
School restructuring	-26.4	
Special education adjustments	-51.9	
Other	-6.7	
Subtotal		\$75.1
<b>Program Expansions</b>		
Child care	\$26.1	
Mandates	14.8	
Volunteer mentor	10.0	
Beginning teacher	10.0	
Assessment	4.4	
Early mental health initiative	3.0	
Subtotal		\$68.3
<b>New Programs</b>		
Class size reduction—additional grade	\$296.8	
Special education reform	76.7	
Ed Tech Center	1.0	
K-12 fiscal data	0.5	
Subtotal		\$375.0
<b>Proposition 98 loan repayment</b>		\$50.0
<b>1997-98 (proposed)</b>		\$28,147.3
<b>Change from 1996-97 (revised)</b>		\$1,727.4

## **PROPOSITION 98 1997-98 SPENDING BY MAJOR PROGRAM**

Figure 8 shows Proposition 98 spending for the major K-12 programs. Revenue limit funding accounts for \$20.2 billion in 1997-98, or about 72 percent of overall Proposition 98 expenditures. The state General Fund supports about 55 percent of revenue limit funding, and local property taxes provide the remaining 45 percent.

Except for revenue limits, the largest K-12 program is special education. Including a proposed General Fund set-aside for funding reform, special education funding is expected to increase by \$180 million in 1997-98. The class size reduction program, started in 1996-97, will be the second largest categorical program in 1997-98, with proposed expenditures of \$1.3 billion. Funding for most other categorical programs remains flat in 1997-98 because the Governor's budget includes neither COLA nor growth funding for these programs.

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<b>Figure 8</b>				
<b>Major K-12 Education Programs Funded by Proposition 98 1996-97 and 1997-98</b>				
<b>(Dollars in Millions)</b>				
	<b>Estimated 1996-97</b>	<b>Proposed 1997-98</b>	<b>Change From 1996-97</b>	
			<b>Amount</b>	<b>Percent</b>
<b>Revenue Limits</b>				
Schools	\$10,558	\$11,201	\$643	6.1%
Counties	174	191	17	9.5
Property tax revenue	8,512	8,808	296	3.5
Subtotals, revenue limits	(\$19,244)	(\$20,199)	(\$955)	(5.0%)
<b>Special Education</b>				
State General Fund	\$1,860	\$1,959	\$99	5.3%
GF set-aside for reform	—	77	77	—
Property tax revenue	215	220	5	2.2
Subtotals, special education	(\$2,075)	(\$2,256)	(\$180)	(8.7%)
<b>Mega-Item— Categorical Programs</b>				
Desegregation	\$546	\$496	-\$49	-9.0%
Economic impact aid	366	416	49	13.5
Home to school transportation	480	478	-2	-0.4
School improvement	360	360	—	—
Instructional materials	157	157	—	—
Other programs	551	534	-17	-3.1
Subtotals, Mega Item	(\$2,461)	(\$2,442)	(\$19)	(-0.8%)
<b>Other Programs</b>				
Class size reduction	\$771	\$1,259	\$488	63.3%
Child development	517	556	40	7.6%
Adult education	452	452	—	—
ROC/P	272	272	—	—
Summer school	155	163	8	4.9
Mandates	105	120	15	14.1
Deferred maintenance	35	35	-1	-2.4
Early mental health	12	15	3	25.0
Volunteer mentor	—	10	10	—
Other programs	170	170	-1	-0.4
Subtotals, other programs	(\$2,489)	(\$3,051)	(\$561)	(22.5%)
<b>Proposition 98 loan repayment</b>	<b>\$150</b>	<b>\$200</b>	<b>\$50</b>	<b>33.3%</b>
<b>Totals</b>	<b>\$26,420</b>	<b>\$28,147</b>	<b>\$1,727</b>	<b>6.5%</b>





# BUDGET ISSUES

## *K-12 Education*

### K-12 PRIORITIES

*The budget proposes to direct all new Proposition 98 funding—and most cost-of-living adjustments (COLA) for existing categorical programs—to support new or expanded state categorical programs. Outside of a COLA, the budget does not propose to increase local general purpose funding, which would increase the ability of school districts to meet local needs.*

The 1997-98 Governor's Budget proposes to spend \$28.1 billion in state and local Proposition 98 support for K-12 education. This represents an increase of \$1.7 billion, or 6.5 percent, from the revised 1996-97 level. The proposed level of funding is sufficient to (1) pay for the 2.35 percent projected growth in the student population, (2) provide a 2.53 percent COLA for many programs, and (3) have \$500 million remaining to support state and local initiatives to improve the K-12 system.

The Governor's budget proposes to reshape K-12 priorities in two ways:

- ***Tax Cut Reduces Proposition 98 Funding.*** The Governor's 10 percent corporate tax rate reduction would result in less Proposition 98 funding available to K-14 education. The impact on Proposition 98 in 1997-98 is about \$58 million.
- ***Significant New Spending on State Categorical Programs.*** The budget proposes to spend \$711 million in Proposition 98 funds to create new or expand existing state categorical programs in 1997-98. Of this amount, \$488 million is for the expanded class size reduction program. An additional \$268 million in one-time fund-

ing from prior-year funds also is earmarked for categorical purposes.

We discuss these issues further below.

### IMPACT OF TAX CUT GROWS IN FUTURE YEARS

The Governor’s budget proposes to reduce the bank and corporation tax rate by 10 percent over two years, reducing the rate by 5 percent in 1998 and another 5 percent in 1999. In 1997-98, the tax cut would reduce General Fund revenues by \$93 million, resulting in a \$58 million reduction in Proposition 98 funds.

The impact of the tax cut would grow significantly in future years, however. Figure 9 displays our estimate of the impact of the Governor’s proposal over a four-year period. By 2000-01, Proposition 98 funding would be about \$307 million less each year than if no tax cut were made. This is about the amount needed to reduce the class size in an additional elementary grade.

<b>Figure 9</b>		
<b>Impact of the Proposed Corporate Tax Reduction 1997-98 to 2000-01</b>		
<b>(In Millions)</b>		
	<b>Reduction in</b>	
	<b>General Fund Revenues</b>	<b>Proposition 98</b>
1997-98	\$93	\$58
1998-99	336	158
1999-00	562	264
2000-01	654	307
<b>Totals</b>	<b>\$1,645</b>	<b>\$787</b>

The impact on Proposition 98 of changes in the state’s tax structure is only one of the fiscal issues the Legislature must address as it considers the Governor’s proposal. How the forgone revenues affect the Legislature’s ability to fund its priorities for other state programs is equally important. The Legislature must also consider the impact of the reduction on the long-term health of the state’s economy.

## WHAT IS THE STATE ROLE IN MAKING CATEGORICAL FUNDING DECISIONS?

The Governor's budget proposes to spend \$7.2 billion, or about 26 percent of K-12 Proposition 98 funds, for 51 existing categorical programs in 1997-98. In addition, the budget requests the Legislature to approve the expenditure of \$500 million in Proposition 98 funds (plus \$88 million in federal Goals 2000 funds) to expand 13 existing programs and create eight new programs.

In contrast, the 1997-98 budget does not propose any increases for revenue limits above the cost of a statutory COLA. While the budget reflects a \$304 million increase in local general purpose funding beginning in 1996-97, this increase results from a provision in the 1996 budget trailer legislation. No new increase in general purpose funding is proposed in 1997-98. This emphasis on state categorical programs raises a fundamental issue regarding the role of the state in directing the use of Proposition 98 funds.

### Categorical Programs Correct Negative Incentives

Categorical programs are designed to address situations where local school boards *under-invest* in specific areas. This can result from the existence of incentives that encourage local decision-makers to make a *lower level of expenditures than is desired*. Special education is a good example of a categorical program. The average cost of educating special education students in California is about twice the amount of a nondisabled student. This higher cost creates a dilemma for districts—providing the appropriate level of services to disabled students may mean reducing the level of service to all other students. To eliminate any potential financial incentive for schools to provide too few resources to disabled students, the state provides additional funding through the categorical Special Education program. The program is “categorical” in that districts may only spend these funds for special education services.

In other areas, unfortunately, it is harder to tell whether schools under-invest in certain types of expenditures or whether local behavior is the result of locally determined choices about how best to spend available funds. Take the example of computers. The 1997-98 budget allocates \$50 million in Proposition 98 funds to match local high school computer purchases.

What is the need for the state to create a special categorical program just for computers? The argument in favor of the proposal is that California schools have fewer computers than do schools in many other

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states—that schools in California do not spend enough on computers. In fact, California ranks low among the 50 states in the number of computers per student.

The argument against creating this categorical program is that there is no barrier for districts to use local funds for this purpose. Many schools have well-equipped computer laboratories that were often funded through the School Improvement program or federal Title 1 program. There are also school districts that have obtained voter-approved tax increases to purchase computers and train teachers in the use of computers. As a result, we do not think the relatively low level of computers in California's classrooms is evidence of a systematic incentive that works to minimize the number of computers. Instead, we think it more likely reflects the school boards' decisions over the use of the state's per-student funding level.

### **Categoricals Can Reduce the Effectiveness of Funding**

By expanding categorical program spending, the state substitutes its judgment of what K-12 funds should buy for the views of local school boards. By doing so, the state short-circuits the local process for determining how additional funds can best translate into improved achievement. We have the following concerns with this development:

- From an intergovernmental standpoint, state determination of how K-12 funds should be spent runs counter to our system of local control, in which school boards—those closest to the problems—are empowered to make resource allocation decisions. The state should endeavor to support, not weaken, this system of governance.
- Categorical programs can reduce the impact of educational spending by allocating funds for purposes that are not the highest priority local uses. This is, of course, why a system of local control was established in the first place—local decision makers can better understand the needs of students, parents, and teachers in the local area.

### **Criteria for Categorical Programs**

Based on these concerns, we think the Legislature should closely examine the rationale for new or expanded categorical program funding. We suggest the following guidelines for the creation of categorical programs:

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- **Student Needs.** Categorical funding is appropriate when funds are needed to ensure that students with special needs are adequately served.
- **Local Under-Investment.** In certain cases, the state may need to provide funding to correct documented problems of local under-investment in certain services or activities. Maintenance is one area where school districts are not providing sufficient support to protect the state’s investment in school buildings. Certain staff development programs may be another area.
- **Demonstration Programs.** Supporting demonstration programs (and evaluations) to determine the effectiveness of certain programs or services. These programs should be relatively short-term, rather than permanent, commitments of state funds.
- **Support for Reform.** School improvement requires time for planning and development. The state may want to encourage districts to examine whether “business as usual” best meets the needs of students and parents. As with demonstration programs, however, such funding should be provided on a short-term basis.

### The Problem of Collective Bargaining

Some school administrators believe that problems with local collective bargaining are the main reason to spend Proposition 98 funds in categorical programs. These observers believe that the existing local incentives have resulted in a collective bargaining process that tilts toward the teachers’ union—that increases in general purpose funding results in unjustified increases in teacher compensation.

At the current time we cannot advise the Legislature of whether the collective bargaining process is “broken.” Collective bargaining is a complex process. We have been unable to find any assessment of California law and practice that addresses the issue of whether the current process works to set a “fair” level of employee compensation to both teachers and districts.

From our discussions with district administrators and other school finance experts, it appears that increases in general purpose funding translate directly into increased employee compensation, at least in some districts. A few union contracts contain language identifying how new revenue limit funds must increase teacher pay. Most district contracts, however, contain a joint commitment to renegotiate compensation levels when revenue limit funding increases. These “reopener” clauses often result in a sharing of that increase with district staff.

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In our survey on class size reduction, we asked how districts would have used \$650 per student in *unrestricted* funds. One-third of districts that responded to the question indicated that much or most of the funds would have gone to employee salary increases due to collective bargaining. The other two-thirds of the districts indicated funds would have been used for school improvement activities, including class size reduction.

The fact one-third of K-12 districts would have provided employee raises is not necessarily an indication of problems with collective bargaining. It may be these raises would be entirely justified. Given the many different circumstances that districts currently face, the Legislature cannot know whether such increases would be justified in every district.

To summarize, the Legislature has two ways to distribute funds to districts: (1) through categorical programs or (2) through increased revenue limit funding. Both have potential drawbacks. Categorical funding may not meet the spending needs of districts and may result in local programs that are less effective than district-initiated programs. On the other hand, revenue limit increases will be negotiated with local unions and the Legislature cannot know whether resulting increases in employee compensation are warranted.

Despite this apparent dilemma, we think the answer is to reenforce the control of school boards over funding decisions. In the past, we have recommended structural changes to give local school districts more authority over aggregate funding decisions. Pending such changes, the Legislature should still insist that school boards make decisions regarding the best use of K-12 funds.

### The Legislature's K-12 Funding Options

***We recommend the Legislature develop its approach to funding K-12 education that reflects its long-term goals and the relative roles of the state and local school districts in the governance of public education.***

To reenforce the importance of school boards, the Legislature needs to (1) carefully review proposals for new spending on categorical programs and (2) strongly consider increasing district general purpose funding as part of its plan for K-12 Proposition 98 funding in 1997-98. In developing the K-12 budget for 1997-98, the Legislature should ensure that both new and existing programs reflect a balance between state and local decision-making authority as well as its long-term goals for K-12 education.




Figure 10 displays our recommended guidelines for K-12 education funding priorities. The first two guidelines focus on the existing K-12 funding program. Current program costs—including funding for growth in the student population, COLAs, state-mandates and other funding

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commitments—should take top priority for funding. These “base” programs, however, also should be assessed and altered as needed to make sure they are as effective as possible and further the state’s K-12 goals.

**Figure 10**

### LAO Guidelines for Establishing Long-Term K-12 Education Funding Priorities

-  **Fund the Continuing Costs of the Current Program.** The state should ensure that funding for growth, COLAs, and other financial commitments is provided.
-  **Review and Reform Current Programs Consistent With Long-Term Goals.** The Legislature should periodically review whether existing programs further the long-term goals of the state.
-  **Balance State and Local Funding Needs.** Once existing programs are adequately funded, the allocation of additional funds should reflect the shared state and local governance of the K-12 system.
  - **Increase and Equalize Local Revenue Limits.** The Legislature should dedicate about half of any additional funds for increasing and equalizing revenue limits.
  - **Support State Improvement Efforts.** The remaining funds should support state-directed uses based on a long-term plan of reform.

After meeting basic program costs, any additional Proposition 98 funds should be used to meet both state and local funding needs. As we discussed above, in California’s divided system of K-12 school governance, the Legislature, Governor and local school boards all play a role in identifying and funding school priorities. Under this system, it is our view that the state should be able to determine the priorities over about half of available new K-12 funds and the remainder should be the responsibility of school boards.

Thus, under our guidelines, about half of the available funds would be used to increase and equalize district revenue limits. With the remaining new Proposition 98 funds, the state should pursue programs for which there is a strong case for state intervention. Class size reduction is a central issue for the Legislature in 1997-98. Other reforms, such as the proposal jointly made by the LAO, Department of Education and DOF to

revamp the special education funding system, also merit the Legislature's consideration for funding in the budget year.

## LAO OUTLOOK SUGGESTS MORE PROPOSITION 98 FUNDS

Figure 11 details the Proposition 98 amounts available for 1996-97 through 1998-99 under the Governor's budget forecast of the Proposition 98 minimum funding guarantee and under the forecast developed by the Legislative Analyst's Office. (Our numbers include the impact of the tax cut in order to highlight the forecasting-related differences.)

<b>Figure 11</b>			
<b>LAO and Governor's Budget Proposition 98 Forecasts<sup>a</sup></b>			
<b>(In Millions)</b>			
<b>Forecast</b>	<b>1996-97</b>	<b>1997-98</b>	<b>1998-99</b>
Governor's budget	\$29,516	\$31,429	\$33,310 <sup>b</sup>
LAO (with tax cut)	29,564	31,592	33,595
<b>Difference with budget</b>	<b>\$48</b>	<b>\$163</b>	<b>\$285</b>

<sup>a</sup> Assumes funding at the minimum level required under Proposition 98.  
<sup>b</sup> LAO long-term extrapolation of economic and revenue projection underlying the 1997-98 Governor's Budget proposal.

For 1996-97, we estimate the revised Proposition 98 minimum guarantee at \$29.6 billion, or \$48 million higher than estimated by DOF. The Governor's tax proposal would not affect funding in 1996-97. In 1997-98 and 1998-99, our estimate of Proposition 98 funding is \$163 million and \$285 million higher, respectively. These increases result from our higher projection of General Fund revenues compared to the Governor's budget.

If the Legislature rejects the tax reduction proposal, an additional \$58 million would be available in 1997-98. Combined with our higher revenue forecast, a total of \$221 million in 1997-98 would be available to meet the Legislature's priorities.



## OPTIONS FOR 1997-98 K-12 FUNDS

***We recommend the Legislature build its 1997-98 K-12 budget using the long-term funding priorities discussed above.***

Figure 12 displays the Governor's proposal and the LAO recommendations for the level of Proposition 98 funds assumed in the Governor's Budget. Our alternative proposes to fund K-12 at \$184.5 million more than the Governor's Budget level. Of this amount, \$163.2 million is due to our higher Proposition 98 forecast. The remaining \$21.3 million represents Proposition 98 funds proposed in the budget for the community colleges that we recommend, instead, satisfy high priority K-12 activities (please see our discussion of this issue in the Higher Education chapter of this *Analysis*).

The amount in Figure 12 (see next page) represents the K-12 increases that are proposed *after* funding enrollment growth and COLAS for revenue limits and special education. Since we also make a number of recommendations later in this section to reduce funding for specific ongoing programs, we include these reductions in Figure 12.

The LAO-recommended plan has many similarities to the Governor's proposal. As Figure 12 displays, we recommend approval of all the budget's proposed COLA increases and those increases requested to keep previous state commitments. We also propose to spend \$74 million that is not included in the budget to provide statutorily required COLAs for other categorical programs.

In the area of new or expanded improvement programs, our alternative uses the available funds in a somewhat different manner. Most significantly, our proposal would provide only \$100 million in new class size reduction (CSR) funds, much less than the \$297 million proposed in the Governor's budget. In our CSR proposal, the \$100 million would add to the one-time money available for facilities in 1997-98 (please see our discussion of CSR below).

Our alternative plan includes a number of other significant departures from the budget's plan, including proposals to: (1) increase revenue limits by \$149.7 million, (2) earmark \$100 million to begin a ten-year plan to address the problem of inadequate ongoing district maintenance budgets, and (3) increase by \$28.3 million the proposed set-aside for special education funding reform. Below, we discuss in more detail two areas in which we recommend a different amount than proposed in the Governor's budget. Other differences are discussed in separate sections later in this chapter.

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**Figure 12****1997-98 K-12 Proposition 98 Increases  
LAO and Governor's Budget Proposals****(In Millions)**

	<b>Governor's Proposal</b>	<b>Legislative Analyst's Proposal</b>
<b>Fund the continuing costs of the current program</b>		
Base programs and adjustments	\$18,286.7	\$18,286.7
Categorical program COLAs	—	73.7
Child development COLA	13.4	13.4
Class-size COLA	31.1	31.1
<b>Pay program deficiencies and other commitments</b>		
Class-size adjustment	\$160.1	\$160.1
Child development—minimum wage	13.1	13.1
Child development—half-year costs	10.0	10.0
Volunteer mentor	10.0	10.0
Student assessment	4.4	4.4
Other child development	3.0	3.0
<b>Review current programs consistent with long-term goals</b>		
Child development—base adjustment	—	-\$43.9
Community day program	—	-22.6
<b>Increase revenue limits</b>	—	149.7
<b>Support state improvement efforts</b>		
Class-size reduction	\$296.8	\$100.0
Special education reform	76.7	105.0
Deferred maintenance	—	100.0
Beginning teacher support	10.0	10.0
K-12 fiscal data	0.5	0.5
<b>Reject other proposed augmentations</b>		
Early mental health	\$3.0	—
Education technology	1.0	—
<b>Reserve</b>	—	\$100.0
<b>Totals</b>	<b>\$18,919.8</b>	<b>\$19,104.3</b>
<b>General Fund sources:</b>		
<i>Governor's proposal</i>	<i>\$18,919.8</i>	<i>\$18,919.8</i>
<i>LAO additional revenue</i>	<i>—</i>	<i>163.2</i>
<i>Transfer from Community Colleges</i>	<i>—</i>	<i>21.3</i>

### Create a Proposition 98 Reserve

***We recommend the Legislature set aside \$100 million for a Proposition 98 reserve to protect against over-appropriating the minimum guarantee in the event General Fund revenues are lower than projected.***

In the years after Proposition 98 was passed by the voters, the Legislature created a reserve account to protect the state in the event the projection of General Fund revenues assumed in the budget was too optimistic. During the early 1990s, a reserve was not created and, as a result, the state overappropriated the minimum funding guarantee several times.

General Fund revenues can be hard to predict. Even in relatively good times, a brief slowdown in the economy can translate into relatively large Proposition 98 consequences. In that event, a reserve would give the Legislature some measure of protection from overappropriating the minimum guarantee without reducing amounts already provided to schools. If the reserve were not needed, the funds would be available as “settle-up” funds in the following year to meet high-priority expenditures, such as deferred maintenance.

Therefore, to create a measure of protection from an unanticipated reduction in General Fund revenues, we recommend the Legislature set aside \$100 million as a Proposition 98 reserve.

### Provide a COLA to Categorical Programs

***We recommend approval of \$73.7 million to provide a COLA to most categorical programs.***

The budget proposes a COLA for only two categorical programs—child development and CSR. Funding for the other 35 or so programs would continue at 1996-97 levels. Among the programs that would not receive a COLA under the budget proposal are adult education, Regional Occupational Centers and Programs, and the Economic Impact Aid Program.

These programs constitute an important part of the K-12 base program. If the budget denies a COLA to these programs, inflation will reduce the value of state funding and the programs will be forced to purchase fewer services. For the same reason the budget proposes a COLA for child development and CSR—increasing district costs for staff, utilities, and supplies due to inflation—a COLA is an appropriate way to maintain spending power.

Therefore, we recommend the Legislature appropriate \$73.7 million in available funds for a 2.53 percent COLA for other categorical programs.

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### **Deny Two Proposed Augmentations**

***We recommend the Legislature delete \$4 million proposed in the Governor's Budget for new or expanded categorical programs.***

As Figure 12 displays, we recommend approval of most increases proposed in the 1997-98 budget. A few of these proposals do not, in our view, meet the criteria discussed above for a state categorical program. Some simply lack the detail necessary for a complete evaluation of the proposals' costs and benefits. For these reasons, we recommend the Legislature deny the requests and redirect the funds to other high priority uses. We discuss the proposals in more detail below.

***Early Mental Health Program Expansion (\$3 Million).*** This program supports three-year startup grants for school-based mental health services for elementary students with moderate behavior problems. The budget currently contains \$12 million for the program, which is administered by the Department of Mental Health (DMH). Even without new funding, the program will continue to expand in 1997-98, as the budget provides funding for a new set of local programs each year. A recent program evaluation revealed that program services had little impact on student achievement, which raises the issue of whether Proposition 98 funds should support the program. We have concerns, however, about the quality of the evaluation (please see our discussion of the DMH budget in the Health and Human Services chapter of this *Analysis*). We therefore recommend the Legislature maintain the current program funding level.

***Technology Center in the San Diego County Office of Education (\$1 Million).*** The proposal would provide partial funding for equipment and other infrastructure needs for a regional technology center. This is an example of a proposal for which state funding is neither needed nor desirable. Other county offices have technology centers that are supported locally. From the state's standpoint, it makes more sense to have these centers funded by district contributions or by user charges. By insisting on local funding for these projects, the Legislature can ensure that what the county office chooses to do will be desired and used by schools. For that reason, we recommend the Legislature deny this request.

### **OPTIONS FOR PRIOR-YEAR FUNDS**

***We recommend relatively modest changes in the budget's plan for the use of one-time Proposition 98 funds.***

As we discussed above, the budget also proposes to spend a significant amount of Proposition 98 funds that are available in the current year. This includes "settle-up" monies from 1995-96 and 1996-97 as well as unspent

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Proposition 98 funds from previous budgets. Figure 13 displays the Governor's budget proposal and our recommendations for the use of these additional funds. Our recommendations total \$43.2 million more than the Governor's Budget. This is because our LAO forecast of General Fund revenues—and Proposition 98 minimum funding level—is somewhat higher than DOF's. We have also included the impact of our recommended reductions in current-year spending for two existing programs (community day schools and child development).

<b>Figure 13</b>		
<b>Prior-Year Proposition 98 Increases LAO and Governor's Budget Proposals</b>		
<b>(In Millions)</b>		
	<b>Governor's Proposal</b>	<b>Legislative Analyst's Proposal</b>
<b>Pay program deficiencies and other commitments</b>		
Revenue limit increases	\$304.2	\$304.2
Revised attendance	264.4	264.4
Standardized account code	9.0	9.0
Assessments	6.0	6.0
Oxnard HSD extended year	3.9	3.9
Other	1.0	1.0
<b>Review current programs consistent with long-term goals</b>		
Community Day Schools	—	-\$35.0
Child development		-43.9
<b>Support state improvement efforts</b>		
Facilities for class size reduction	\$151.0	\$200.0
Deferred maintenance	—	100.0
Child care facilities	15.0	15.0
Student information system	10.0	10.0
Alternative credential program	9.0	9.0
<b>Reject other proposed augmentations</b>		
High school technology	\$50.0	—
Angel Gate Academy	6.4	—
Single gender schools	5.0	—
Kern Telecommunications	2.0	—
<b>Reserve</b>	—	36.6
<b>Totals</b>	<b>\$836.9</b>	<b>\$880.1</b>

Generally, we recommend the Legislature use the same principles discussed above to determine the expenditure of these one-time funds. We recommend approval of the increases proposed to retire funding deficiencies and other program commitments. This includes \$304.2 million proposed for revenue limit increases (half for an additional COLA, half for equalization) as required by the Legislature's actions on the *1996-97 Budget Act*. We also recommend the Legislature approve the proposed increase in funding due to higher-than-estimated prior-year attendance.

We also support a number of the budget's proposed new programs. We recommend approval of the \$10.4 million for a student information system, which would establish the infrastructure for a statewide student data base. We also recommend approval of \$9 million for an expanded alternative credential program, which supports district and university programs that train prospective teachers.

### **Increase CSR Facility Funding**

***We recommend the Legislature appropriate \$200 million in one-time support for district facility costs of implementing the CSR program.***

The budget proposes \$151 million to provide districts additional funds for CSR-related facility needs. In 1996-97, the Legislature provided \$200 million in one-time funds to help defray this expense.

Facility costs continue to be a major issue in the implementation of the CSR program. As we discuss in our review of the CSR program below, districts estimate their additional CSR facility costs to fully implement three grades of smaller class sizes at \$600 million (assuming 18.8 students per classroom).

Because of the great need for additional facilities funds, we recommend the Legislature increase the amount for facilities to \$200 million. This \$200 million plus the additional \$100 million in ongoing funds that we recommend earmarking for CSR facilities in 1997-98 would bring the total to \$300 million. While this is a very large sum, even for K-12 education, it provides only about half of the amount districts will need to fully implement three grades of smaller classes.

### **Delete Proposed Augmentations**

***We recommend the Legislature deny four proposals for new or expanded programs for a savings of \$63.4 million.***

As Figure 13 displays, we recommend the Legislature deny four of the Governor's proposed uses of prior-year Proposition 98 funds. These

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requests do not meet the criteria discussed above for categorical programs. We discuss each proposal below.

**High School Technology Initiative (\$50 Million).** This request is the first-year of funding for a planned \$500 million high school technology proposal. The proposal requires districts to match state funding, bringing to \$1 billion the total amount of technology purchased under the proposal. The Governor's Budget also mentions future increases in district revenue limits to pay for the maintenance of the new technology. As we discussed above, we do not believe this proposal justifies state intervention. Without a clear rationale, the Legislature should let local school boards determine the best use of funds.

**Angel Gate Academy (\$6.4 Million).** These funds would support a five-week residential program for middle school students (grades six through eight) who are "at-risk" of becoming youthful offenders. The residential program is operated jointly with the California National Guard and has been supported with federal funds for the past three years. The proposal has a number of problems. First, the request would expand—without any clear rationale—the size of the program threefold, from 400 students to 1,440. Second, the program is very expensive (\$4,400 per student for a five-week program) and only benefits students from the Los Angeles Unified School District. The budget offers no reason why the state should become involved in a purely local issue of resource allocation. The district has a variety of resources that could be used to fund this program if it is a priority. We see no appropriate state role for such a program and, therefore, recommend the Legislature deny this request.

**Second-Year Funding for Single-Gender Schools (\$5 Million).** As part of the 1996-97 Budget Act, \$5 million in one-time funds were appropriated to provide start-up funding for schools that would serve only boys or girls. This was developed as another approach to addressing the needs of "at-risk" students. According to the State Department of Education (SDE), the start-up grants have not been issued. The DOF could not provide any additional information indicating that ongoing funding would be needed to operate these academies. For this reason, we recommend the Legislature not approve this request.

**Telecommunications Center in the Kern County Office of Education (\$2 Million).** Similar to the technology proposal for San Diego County discussed above, this proposal would provide state support for a regional telecommunications project. For the same reasons as we discussed above, we recommend the Legislature deny this proposal.

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### Create a Reserve of Prior-Year Funds

***We recommend the Legislature establish a reserve of \$36.6 million to ensure against overappropriating the Proposition 98 minimum in 1996-97.***

Just as we believe the Legislature should create a \$100 million reserve of Proposition 98 funds in 1997-98, we think a reserve for 1996-97 funds also is prudent. The need for the reserve will lessen as the year progresses because the Legislature will have a better idea of what final Proposition 98 funding levels will be. Even in May, however, some uncertainty will remain about the final level of funding. For that reason, we recommend the Legislature establish a reserve of \$36.6 million in 1996-97 funds to protect against overappropriating in the current fiscal year.

### POPULATION ESTIMATES DIFFER

***We recommend the Legislature adopt legislation to change the policy of allowing revisions to population estimates used in the Proposition 98 calculations. Further recommend the Legislature require this estimate to be established in the annual budget bill.***

In our companion document, *The 1997-98 Budget: Perspectives and Issues* (Part 2, California's Demographic Outlook), we note that our demographic projections are lower than those of the Department of Finance due to differing assumptions about migration. As stated in our K-12 *Overview Section*, state population is one of the five major factors involved in the calculation of each of the Proposition 98 "Tests." The population estimates used in the Proposition 98 calculation are provided by the Department of Finance.

State population plays a key role in the level of the Proposition 98 minimum guarantee. Tests 2 and 3 are based on changes in *per capita* personal income and General Fund revenues. As a result (assuming no other changes), as population increases the Proposition 98 guarantee decreases.

***Current Policy on Population Estimates Is Inconsistent.*** Education Code Section 41206 directs that within nine months following the end of any fiscal year, the Superintendent of Public Instruction and the Director of Finance shall recalculate, as necessary, and jointly certify all *actual* data pertaining to school districts for the prior fiscal year. For example, by the end of March 1997, the final Proposition 98 factors for 1995-96 should be certified by the DOF and the SDE.

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This is not a difficult task with regard to General Fund revenues, local property taxes, and K-12 ADA, where the state has actual data. The California per-capita personal income factor is also straightforward because it is set prior to the start of the fiscal year and never changed.

However, state population estimates used for per-capita General Fund revenues are problematic. When population estimates change, so does the per-capita General Fund guarantee. And, since no actual counts are available for population—except for the once-a-decade census count—Proposition 98 can change every time the DOF revises its estimates.

### How Should Population Be Adjusted?

Our population estimates are lower than the DOF estimates throughout the period 1995-96 to 1997-98. We estimate that, if the Legislature used our state population estimates throughout this period, the following additional amounts would be needed to satisfy the minimum guarantee: (1) \$99.4 million for 1995-96; (2) \$182.8 million for 1996-97; and (3) \$289.4 million for 1997-98.

As demonstrated in these amounts, allowing population estimates to change does introduce the possibility of large changes to the General Fund cost of Proposition 98. In the current case (a *reduction* in the population estimates), the threat is to the General Fund budget. If on the other hand, the revised estimate of population was higher than the previous estimate, the General Fund could benefit and K-14 education would be at-risk due to the lower minimum funding guarantee. Since K-14 districts would have already spent or encumbered most of the funds, however, adjusting school funding downward by any significant amount is not feasible. Thus, a floating population estimate primarily serves to increase Proposition 98 spending, thereby threatening the state General Fund.

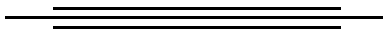
We recommend the Legislature revise state law to permanently set the population estimate used in the Proposition 98 calculation as part of the budget process. Once the estimate has been openly reviewed in the budget process and adopted in the budget bill (like the California per capita personal income factor), it no longer would be subject to change. This would reduce the General Fund threat caused by changing estimates of population and provide the Legislature the opportunity to review the estimate as part of the budget process.

With regard to the population adjustments for 1995-96 through 1997-98, we see two options:

- Adjust the guarantee for all three years, at a cost of \$572 million to the General Fund.
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- Adjust the guarantee for only the budget year, at a cost of \$289.4 million to the General Fund. This would set the 1997-98 minimum guarantee at a level consistent with our revised population estimate.

We recommend the latter option because it is more consistent with the long-range policy of not revising past population estimates. Since the DOF may revise its estimate of population this spring, we do not include these funds in our alternative spending plan. We will revisit this issue in the May revision.



## CLASS SIZE REDUCTION

The *1997-98 Governor's Budget* includes \$1.26 billion in ongoing operations funds for the Class Size Reduction (CSR) program. This represents an increase of \$488 million over the \$771 million level of funding for the program in the current year. This increase consists of (1) \$160 million to fully fund the CSR program base, (2) \$297 million to expand implementation to a fourth grade, and (3) \$31 million for a cost-of-living-adjustment (COLA). The Governor's budget also includes \$151 million in one-time monies to fund new facilities for CSR. The current-year budget provided \$200 million in one-time funds for facilities.

### IMPLEMENTATION OF CLASS SIZE REDUCTION

The Legislature and the Governor created the CSR program as part of the *1996-97 Budget Act*. The program is intended to increase educational achievement by reducing average class size from 28.6 to no more than 20 in up to three grades, from kindergarten through third. Figure 14 (see next page) summarizes the provisions of the CSR program.

Almost all school districts elected to participate in the program. Of the 895 school districts eligible for the CSR program, 95 percent, or 853 districts, elected to participate. Of the participating districts, about 85 percent began reducing class sizes at the beginning of the school year. Other participating districts must implement the program by February 1997 in order to receive funding in the current year. Figure 15 (see page 37) summarizes district participation and funding.

As Figure 15 shows, districts expect to claim \$630 million, or 82 percent, of the funding appropriated for CSR. Of districts implementing CSR, fewer than 2 percent have chosen Option 2 in grades one through three. In kindergarten, 20 percent of implementation has occurred under Option 2. The *1996-97 Budget Act* assumed districts would use Option 2 about 25 percent of the time. Thus, the use of Option 2 is substantially lower than anticipated.

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**Figure 14****Features of the Class Size Reduction Program**

- Almost \$1 Billion Appropriated in 1996-97.** The Legislature provided \$771 million in ongoing operational funds and \$200 million in one-time facilities funds.
- Districts May Implement CSR in Up to Three Grades.** On a school- by-school basis, implementation must begin with grade one, followed by grade two, and then either kindergarten or grade three. Districts may not implement CSR in a grade until all classes in the higher-priority grade(s) have been reduced to 20 or below.
- Districts Have Two Implementation Options.** Districts receive funding for reducing class size to no more than 20 under either of two options:
  - Under "Option 1," districts receive \$650 for each student in a class of no more than 20 for a *full* day.
  - Under "Option 2," districts receive \$325 for each student in a class of no more than 20 for a *half* day.
- Implementation Deadline.** In 1996-97, districts receive funding only for implementation that occurs by February 16, 1997.
- One-Time Grants Are Available.** Districts may apply for facilities grants of \$25,000 per new classroom.
- Governor's Budget Would Extend CSR to a Fourth Grade.** The Governor's proposal would add \$297 million in ongoing funds to expand CSR to a fourth grade. The proposal also would provide \$151 million in one-time funds for facilities.

Figure 15 also shows that 54 percent of the state's K-3 students will be in smaller classes this year. As shown in Figure 16, district implementation of CSR focused on grades one and two. Ninety-two percent of the state's grade one students and 74 percent of grade two students will be in small classes by the implementation deadline of February 1997. Implementation in kindergarten and grade three is significantly less common.

One-time funds for facilities have been insufficient to meet demand created by CSR. As Figure 15 shows, the entire \$200 million appropriation in the *1996-97 Budget Act* was distributed to schools. The State Department of Education (SDE) received 14,000 requests for facilities grants to implement the CSR program. Available one-time funds will cover 8,000 of these requests. Eligibility was based on the same space standards used in the State School Building Program.

**Figure 15**

**Participation in the Class Size Reduction Program 1996-97**

Districts participating	853 out of 895
Amount of ongoing funds claimed	\$630 million out of \$771 million
Amount of facilities funds claimed	\$200 million out of \$200 million
Percent of CSR districts implementing in first semester of 1996-97 school year <sup>a</sup>	85 percent
Percent of all K-3 students in a CSR class	54 percent

<sup>a</sup> Data from School Services of California.

**Figure 16**

**Percent of Students Who Will Be in Small Classes**

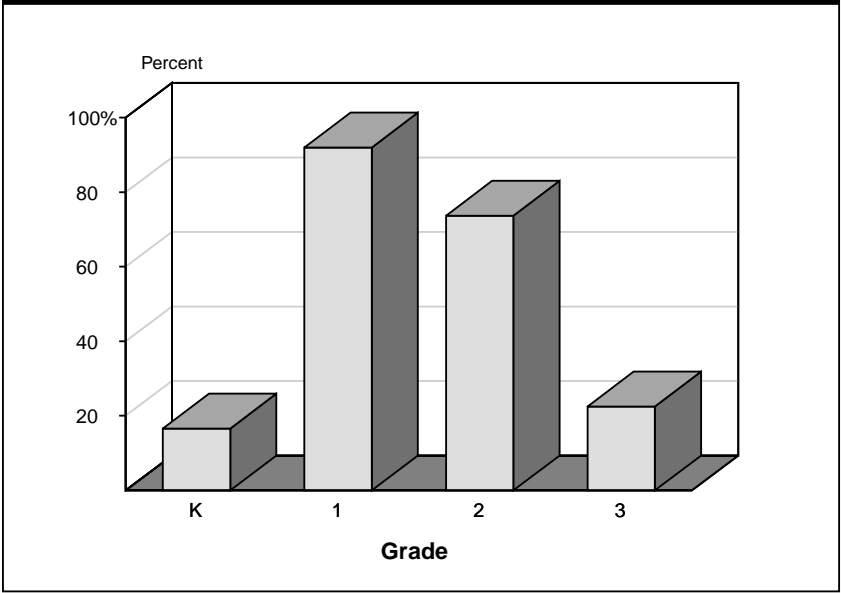
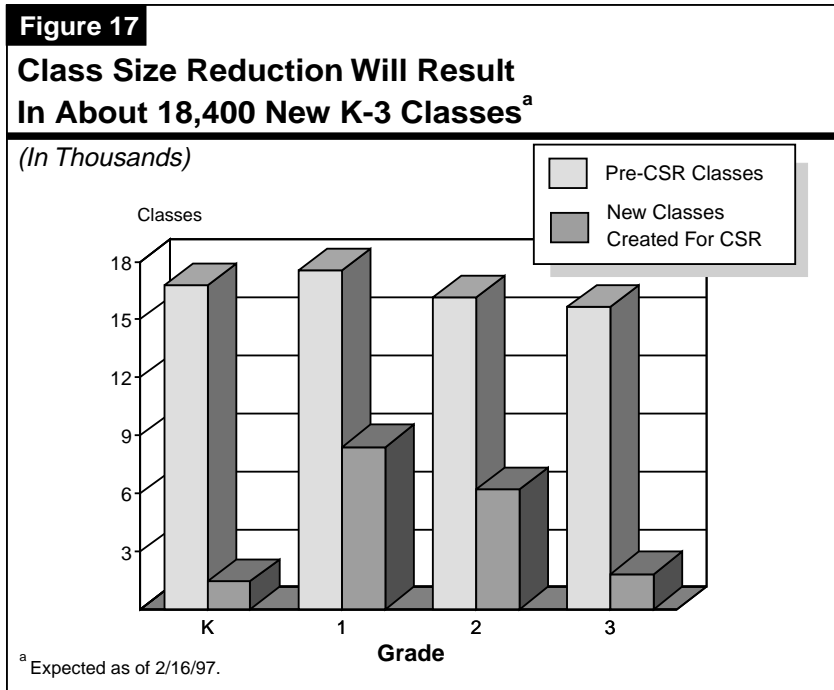


Figure 17 shows the existing number of K-3 classes in the state in 1995-96 and the number of new classes that will be created by CSR in 1996-97. Overall, CSR will add about 18,400 new K-3 classes in the state in 1996-97, an increase of 28 percent. We estimate that the state's overall K-3 class size will be lowered from 28.6 students in 1995-96 to about 23.5 students by the end of the 1996-97 school year.



### Why Did Some Districts Not Participate in CSR?

Forty-two districts did not participate in the CSR program in 1996-97. Most of these districts have very low enrollments. Overall, nonparticipating districts represent less than 1 percent of the state's enrollment in grades kindergarten through third. Figure 18 summarizes the enrollments of nonparticipating districts.

The SDE surveyed nonparticipating districts to find out why these districts did not participate. Modesto City Elementary, the only very large district that is not participating, estimated the program would result in a budget deficit in future years. Modesto does plan to implement CSR in two grades in 1997-98.

Of the other districts that did not participate, most of those with enrollments greater than 200 stated that they already have small classes (21 to

24 students) and did not feel that the disruption and cost of going down to 20 would be worth the potential benefits. The 28 districts with enrollments of less than 200 cited two main reasons for not participating: (1) the district had class sizes slightly above 20 but did not have enough children at each school to create another class or (2) the district had class sizes of 20 or under already and administrators did not realize that the district could nevertheless qualify for the program. About 40 percent of all the nonparticipating districts surveyed stated that they plan to participate next year.

**Figure 18**

**Size of Districts Not Participating  
In Class Size Reduction—1996-97**

District Enrollment	Number of Districts
More than 10,000	1
2,000 - 10,000	0
1,000 - 2,000	3
200 - 1,000	10
Less than 200	28
<b>Total</b>	<b>42</b>

## BUDGET PROPOSAL WOULD EXPAND CSR TO FOUR GRADES

The Governor's budget proposes expansion of the CSR program to four grades in 1997-98. There are four facets to the Governor's proposal:

- **Expand CSR to Four Grades.** The budget proposes \$297 million to fund a fourth grade of CSR. With these funds, the program would provide funding to implement CSR in all of grades kindergarten through third.
- **Increase CSR Base Funds to Account for Higher-Than-Planned Use of Option 1.** As discussed above, use of Option 1 was substantially higher than the 75 percent rate originally assumed. The budget would provide \$160 million to account for the greater costs of Option 1 over Option 2, as well as enrollment growth.
- **Provide a COLA to the Per-Pupil Amount.** The budget proposes \$31 million for a COLA that would raise CSR per-pupil funding from \$650 in the current year to \$666 in the budget year.

- **Provide One-Time Facilities Funds.** The budget requests \$151 million in one-time funds to be distributed as facilities grants for CSR.

**LAO AND SDE SURVEYED DISTRICTS  
FOR INFORMATION ON CSR IMPLEMENTATION**

In order to obtain more detailed data on the CSR program to inform the budget and policy process, the Legislative Analyst’s Office (LAO), in collaboration with SDE, sent surveys to 200 California school districts.

We surveyed the 50 largest districts and 50 districts chosen at random from each of three groups: (1) districts with enrollments between 5,000 and 20,000, (2) districts with enrollments between 1,000 and 5,000, and (3) districts with enrollments of less than 1,000. Figure 19 summarizes the number and enrollment of the state’s school districts in the most recent year for which data are available.

**Figure 19**

**Number and Enrollment in California K-12 School Districts by District Size 1995-96**

Enrollment Range	Number of Districts	Enrollment	Percent of Statewide Enrollment
Greater than 20,000	51	2,380,350	44%
5,000 - 20,000	209	2,091,294	39
1,000 - 5,000	303	781,445	14
Less than 1,000	436	156,798	3
<b>State Totals</b>	<b>999</b>	<b>5,409,887</b>	<b>100%</b>

Source: Data from the California Basic Education Data System (CBEDS).

We chose this sampling plan with the twin goals of covering a large proportion of the state’s total enrollment while at the same time gathering information about the issues faced by districts of different sizes. Of the 200 districts surveyed, about 150 responded, with similar response rates among all four district size groups. Responding districts represent about half of the state’s K-3 school enrollment.



The survey questions fell into four groups:

- **Costs for CSR.** We asked districts how much they are spending to compensate new CSR teachers as well as other teachers already in that district. We also asked districts how much their new CSR facilities cost.
- **Teacher Background and Experience.** We asked districts how many teachers they hired for CSR, their experience, what these new teachers were doing before they were hired, and the district's judgment of the new teachers' skill levels compared with new teachers the district had hired in the past.
- **Facilities.** We asked districts how they are providing new classrooms for CSR and if facilities were redirected from other uses for CSR classrooms.
- **Other Issues.** We asked districts (1) if they had noticed an increase in students transferring from private schools to public schools in their district; (2) how they would have spent the CSR funds they received if the funds were given to the district as unrestricted revenue, rather than solely for class size reduction; and (3) initial impressions regarding the effect of CSR on teacher and parent morale, and on student attendance.

**Data Quality.** The analysis presented below is based mainly on data reported to us and to SDE by school districts. We have followed up with many districts in order to ensure the accuracy of the data on which our conclusions are based. Nevertheless, as with all surveys, there may remain some divergence between the information districts provided and the actual situation in their schools.

In general, our survey sample appears to be representative of the state as a whole and also of each district size group. However, due to the large variability among the smallest districts, the results we obtained from our sample may be less representative of small districts as a whole.

## WHAT DOES CLASS SIZE REDUCTION COST?

***Districts are maintaining CSR classes at about 19:1 in order to be sure of remaining under the 20:1 cap. This increases per-pupil CSR costs by as much as 21 percent. As a result, CSR costs about \$770 per pupil on a statewide basis under these circumstances. If CSR classes could be kept at 20:1, costs would be about \$630 per pupil.***

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There are a number of factors that determine the ongoing cost to a district of class size reduction:

- **Initial Average Class Size.** Average class size prior to CSR varies a great deal among districts. Those with lower initial class sizes will need to spend less for CSR than those with higher class sizes. In 1995-96, before CSR was implemented, the statewide average class size in grades kindergarten through third was about 28.6 students, with 84 percent of districts falling between 26 and 32 pupils.
- **Final Average Class Size.** The law requires that a class average no more than 20 pupils during the course of a school year to qualify for CSR funds. In order to ensure they do not exceed this limit, many districts kept their class sizes below 20. As a result, the statewide average class size in CSR classes appears to be slightly under 19. This increases the cost of the program substantially.
- **Cost of Teachers Hired for CSR.** Districts that pay higher salaries will have higher CSR costs. The cost of teachers hired for CSR will depend both on the salary schedule of each district, and the experience level of the teachers hired. Including salary and benefits, the average annual cost of teachers hired for CSR ranged from about \$30,000 to \$50,000 on a district-by-district basis. Teacher costs will increase with time as these newly hired teachers move up the salary scale.
- **Other Ongoing Costs.** Districts generally report additional ongoing costs for CSR. These include costs for substitute teachers, utilities, custodial services, and clerical services. We were not able to collect uniform data on these costs for each district, but they appear to be in the range of \$3,000 to \$5,000 per classroom per year (that is, about 10 percent of teacher costs).

**Average Costs Are Higher Than Expected.** When CSR was created in the 1996-97 Budget Act, we estimated, including only teacher costs, that the *long-run* ongoing costs of reducing class size to 20 students per class would be about \$750 per pupil per year. We arrived at this estimate based on statewide average cost of \$50,000 per teacher per year, a statewide average class size in grades kindergarten through third of 28.6, and a final average class size of 20. We expected that *first-year* costs would be lower than long-run costs because new teachers would start out near the bottom of the salary scale, rather than at the statewide average. The survey data we received from districts now allows more accurate estimates of the costs of CSR.

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We developed these cost estimates for CSR using the following information and assumptions: (1) survey data on the average salary of the teachers each district hired for CSR; (2) survey data on the average salary of the rest of each district's teaching staff (that is, not including those hired for CSR); (3) overhead costs assumed to be equal to \$4,000 to account for other ongoing costs of CSR (such as substitute teachers, utilities, custodial services, etc.); (4) data from the California Basic Education Data System (CBEDS) that gives average class size for each school district before CSR was implemented; and (5) data from district CSR funding applications submitted to SDE from which we calculated the final average class size.

Figure 20 lists the estimated average per-pupil cost of CSR given the data and assumptions listed above. Figure 20 shows the following:

- **Districts of Greater Than 20,000 Enrollment.** The largest districts have the lowest costs (\$690 per student) for two reasons. First, their new teacher salaries are the lowest and second, the average class size in their CSR classes is the highest.
- **Districts From 1,000 to 20,000 Enrollment.** These districts have higher CSR costs (about \$800 per student) than the largest districts because of higher average new teacher salaries and a lower final class size for CSR classes.
- **Districts of Under 1,000 Enrollment.** Although these districts pay the lowest new-teacher salaries and have low initial class sizes, their costs (\$710 per student) are slightly higher than the largest districts because of the low number of pupils in their CSR classes.

<b>Figure 20</b>				
<b>Estimated Costs for Class Size Reduction</b>				
<b>1996-97</b>				
<b>Enrollment Range</b>	<b>Current CSR Cost Per Pupil</b>	<b>Average Teacher Cost</b>	<b>Average Initial Class Size</b>	<b>Average Final Class Size</b>
Greater than 20,000	\$690	\$37,300	28.7	19.3
5,000-20,000	810	39,000	29.0	18.8
1,000 - 5,000	800	40,000	28.1	18.6
Less than 1,000	710	35,700	25.9	17.6
<b>State Average</b>	<b>\$770</b>	<b>\$38,300</b>	<b>28.6</b>	<b>18.8</b>

This group of districts also had the widest range of costs, with 7 of 25 districts incurring no costs because their class sizes were already at 20 or below.

Costs for the state as a whole average \$770 per pupil, with an average CSR class size of 18.8. However, costs varied a great deal from district to district. For districts of over 1,000 students, almost all districts had costs between \$400 and \$1,000 per pupil.

**Long-Run Costs of CSR.** The estimates above are for current-year CSR costs. We can estimate the long-run per-pupil costs of CSR by using data on *average* teacher costs, rather than *new* teacher costs. Teachers hired for CSR are lower on the salary scale than the average teacher. However, in five to seven years, their salaries will be more like those of the average teacher. We estimate the long-run per-pupil CSR cost will be about \$1,020 (in current dollars) assuming average class sizes of 18.8.

**More Flexibility Would Reduce Costs.** The CSR program requires districts to reduce classes to no more than 20 students per teacher in order to receive funding. In practice, however, districts appear to be reducing classes to average sizes well below the required minimum. At least two factors may account for this. First, districts are fearful of losing CSR funding if they exceed the 20:1 cap. Districts do have to plan for enrollment changes during the school year, but the severe penalties for going over 20:1 may be pushing them into creating an extra safety margin, resulting in typical class sizes of 19, rather than 20. Second, some districts have less flexibility in dividing their children between classes and may be forced into low class sizes. A school with three classes of 28 students each, for instance, would have to make four classes of 17 students and one of 16 in order to participate in the program.

To the extent that districts maintain classes averaging less than 20 on an annual basis, costs rise dramatically. For example, the cost of the program increases by 21 percent if average class size is 18.8 rather than 20 statewide.

Figure 21 below shows current per-pupil costs for the program when districts maintain average class sizes of 18.8 students and 20 students. Note that at an average class size of 20, current per-pupil funding (\$650 per student) is more than enough to cover the costs of CSR for the average district (\$630 per student). In the long term, costs would rise to about \$840 per pupil, well below the \$1,020 necessary to fund CSR at average class sizes of 18.8. On a statewide basis, we estimate the full-year difference in costs for implementing CSR in three grades at 18.8:1 rather than 20:1 is about \$180 million in the budget year.

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**Figure 21****Estimated Current Average Per-Pupil Costs  
Of Class Size Reduction Under Two Scenarios<sup>a</sup>**

District Size	Cost at 18.8 to 1	Cost at 20 to 1	Difference
Greater than 20,000	\$690	\$620	\$70
5,000-20,000	800	660	150
1,000 - 5,000	800	630	170
Less than 1,000	710	490	220
<b>State Average</b>	<b>\$770</b>	<b>\$630</b>	<b>\$140</b>

<sup>a</sup> Estimates are for 1996-97 and are based on stated student/teacher ratios.

**TEACHER RECRUITMENT AND STAFF DEVELOPMENT**

*Teachers hired for CSR on average have less teaching experience, fewer qualifications, and a lower skill level than teachers hired in previous years. In addition, shortages of substitutes and lack of funds for staff development may be hindering districts' ability to provide staff development that could make up for deficits in training and experience.*

While CSR has the potential to increase student achievement by placing fewer students in each classroom, the success of the initiative hinges on placing competent teachers in those classrooms. The CSR program will result in the hiring of about 18,400 teachers this year. These are in addition to the approximately 16,000 elementary teachers that will be hired for normal replacement and growth needs. Thus, CSR has resulted in a 115 percent increase in demand for new elementary-grades teachers this year.

**Inadequate Supply of Credentialed Teachers**

Figure 22 lists the qualifications and experience level of teachers hired for CSR for the state overall and by district size. As Figure 22 shows, on a statewide basis, 24 percent of teachers hired for CSR do not have a teaching credential. Of the total, 21 percent have an emergency permit. Emergency permits are issued to people entering the teaching profession who have not completed some of the legal requirements for a teaching credential. Emergency permit holders may have no formal training or experience in teaching, although some may have experience as substitute

teachers. Holders of emergency permits must meet minimal annual training requirements in order to be eligible for renewal of their permit.

Three percent of teachers hired for CSR have a waiver. Persons issued a waiver need not have fulfilled any of the legal requirements for a teaching credential, and therefore may be less qualified than holders of emergency permits. As can also be seen in Figure 22, larger districts were much more likely to hire noncredentialed teachers than were smaller districts.

<b>Figure 22</b>					
<b>Experience Level of Teachers Hired for CSR—1996-97</b>					
Experience Level	Statewide	District Enrollment Range			
		Greater Than 20,000	5,000 to 20,000	1,000 to 5,000	Less Than 1,000
<b>Credential:</b>					
Greater than five years experience	14%	16%	10%	17%	23%
One to five years experience	23	22	22	27	35
Entry level	34	25	42	40	30
University intern	3	3	3	0	4
District intern	2	3	1	2	0
<b>Non-Credential:</b>					
Emergency	21	28	20	9	8
Waiver	3	3	3	5	0
<b>Totals</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>	<b>100%</b>

We estimate the increase in emergency permits and waivers due to CSR represents an increase of at least 60 percent in the use of these teaching authorizations in elementary schools. According to data from the Commission on Teacher Credentialing, in 1995-96, 6,000 elementary classroom teachers (out of about 140,000) were working under emergency permits. Based on the results of our survey, we estimate that teachers hired for CSR will add between 3,500 and 4,000 additional emergency permits statewide this year. The vast majority of newly hired teachers will be teaching in CSR classes. Thus, teachers with emergency permits will be more concentrated in the earliest grades.

**Big Districts Rate New Teachers Lower.** Districts had very different assessments of the quality of new CSR teachers. We asked school district administrators to make a subjective judgment of the skills of new CSR teachers compared to the skills of teachers hired in previous years. On average, the smaller districts felt that CSR teachers were slightly *more* skilled than in previous years while the larger districts felt that the teachers they hired were slightly *less* skilled than in previous years. Of particular concern are districts with enrollments over 20,000, of which 35 percent answered that CSR teachers possessed skills that were “somewhat lower” than teachers hired in previous years.

Thus, based on data for teacher qualifications and subjective judgments of teacher skills, the teachers hired for CSR are less prepared and less experienced, on average, than teachers hired in the past. This appears to be a problem mainly for larger districts, as smaller districts have generally been able to hire qualified teachers.

**Staff Development Concerns.** At the same time that some districts are hiring teachers with lower qualifications and experience than in the past, they are also experiencing difficulties in providing teachers with staff development programs that could improve their teaching skills. Figure 23 lists the types of problems districts say they experienced in implementing staff development for the CSR program.

**Figure 23**

**Problems Experienced by Districts  
In Implementing Staff Development—1996-97**

Problem Experienced	Statewide	Greater	5,000 to	1,000 to	Less
		Than 20,000	20,000	5,000	Than 1,000
Insufficient substitutes	69%	71%	73%	54%	44%
Insufficient funds	49	53	51	38	33
Not enough time	48	45	56	43	22

Once again, larger districts were more likely to experience difficulties than smaller ones. The most common problem, a lack of substitute teachers to provide release time for classroom teachers to receive staff development, is directly related to the demand for new teachers in implementing CSR. One in four teachers hired for CSR were former substitutes.

**Future Teacher Demand of CSR.** During the 1996-97 school year, CSR will require districts to hire about 18,400 teachers. As described earlier, class sizes in CSR classes average about 18.8. Substantially more teachers are necessary to implement CSR with classes smaller than 20. Figure 24 shows the number of teachers necessary to implement CSR depending on the average class size and the number of grades implemented.

<b>Figure 24</b>			
<b>Number of New Teachers Needed For Full Implementation of CSR</b>			
<b>Implementation Level<sup>a</sup></b>	<b>Statewide Average Class Size</b>		
	<b>18.8</b>	<b>20</b>	<b>Difference</b>
Three grades	7,800	3,200	4,600
Four grades	16,500	10,400	6,100

<sup>a</sup> Assumes full implementation.

Given current average CSR class sizes (18.8), schools will have to hire about 7,800 additional teachers to fully implement CSR in three grades statewide. Adding a fourth grade would require the hiring of an additional 8,700 teachers, for a total of 16,500 new teachers next year (these are in addition to the new CSR teachers hired this year). With an average class size of 20, however, only 3,200 teachers would be needed to implement the program in three grades, 10,400 teachers would be needed to continue in four grades, or a difference of 59 percent and 37 percent fewer new teachers, respectively.

## PROVIDING FACILITIES FOR CLASS SIZE REDUCTION

**Most new classrooms for CSR were created by installing portables. In addition, a significant number of facilities were converted from other uses, potentially curtailing other programs or services. New facilities to expand CSR next year to more classes and grades will be much more expensive on a per-classroom basis, suggesting that districts now have fewer options for creating CSR facilities than they did this year.**

Along with the challenge of finding qualified teachers, CSR created the need for about 18,400 new classrooms this year. As Figure 25 shows, districts took several different approaches to creating new classrooms for



CSR. Fifty-six percent of CSR classrooms were created by purchase or rental of portable buildings. Most of the other 44 percent of classrooms were created by reconfiguring existing space.

**Figure 25**

### How Districts Created Classrooms For CSR—1996-97

Means to Create New Classrooms	Percent of CSR Classrooms
Purchase or rent portables	56%
Use existing unoccupied space	8
Share classrooms	8
Convert classrooms from other uses	8 <sup>a</sup>
Reconfigure grade levels among schools	7
Divide classrooms	4
Other	9
<b>Total</b>	<b>100%</b>

<sup>a</sup> Includes only permanent conversions

An unintended side effect of CSR has been conversion of some spaces used for other purposes into classrooms. As shown in Figure 25 above, about 8 percent of classrooms for CSR were created by converting space from other uses. These facilities include libraries, computer and science labs, teacher lounges and prep rooms, gymnasiums and cafeterias, and child care facilities, among others. On a statewide basis, we estimate that about 3,400 facilities were converted on a temporary basis (that is, for less than one year) and an additional 1,400 facilities were converted on a permanent basis. Permanent conversions included about 200 to 300 each of computer labs, music rooms, and child care facilities. The full impact of these conversions is difficult to estimate because conversion of a facility does not mean that the service provided at the facility has been lost. For example, some districts combined their computer labs with their libraries and some child care programs were able to find other space in which to continue operating. Nevertheless, some programs and services have undoubtedly been curtailed due to CSR.

**Facilities Costs of CSR.** In addition to the ongoing costs of CSR, districts incurred significant one-time costs for providing new classrooms. Based on data in our survey, we estimate that total statewide expenditures for CSR facilities will be at least \$500 million in the current year or

about \$28,000 per new classroom, on average. This figure is relatively low, primarily because many CSR classrooms were created by reconfiguring existing space (it also may underestimate actual costs, as some districts appear to have underestimated the full cost of portable classrooms in their responses to our survey). The state provided \$200 million of these funds as one-time facilities grants in 1996-97.

Future facilities costs of CSR depend on whether districts can average 20 children per class. Given current average class sizes of about 19, we estimate facilities to complete implementation in three grades (starting from where the state will be at the end of the current year) will cost about \$600 million or about \$73,000 per new classroom, on average. These costs would drop to about \$250 million for average class sizes of 20. We estimate an additional \$500 million would be needed to implement CSR in four grades, as proposed by the Governor, assuming average facilities costs of \$73,000 per new classroom and average class sizes of 20.

***Districts May Have Few Options for Providing Additional CSR Facilities.*** We were not able to determine directly from the data in our survey whether districts have the space to add new classrooms or the land to build new schools. Both of these will be necessary to continue expansion of CSR to three grades, and even more so if a fourth grade is added. Nevertheless, the data suggest districts generally are hard-pressed to find enough space for new classes. In the current year, most new facilities were created with portables, which are expensive, or by converting other facilities, which is potentially damaging to other programs. As shown above, facilities to continue CSR implementation next year will be more than 2.5 times as expensive, on a per-classroom basis, as this year. This suggests that most districts now see new buildings as their *only* option for creating new CSR classrooms.

## OTHER RESULTS OF THE SURVEY

The survey provided information on other aspects of the CSR program besides costs, teachers, and facilities. These results include:

- ***Transfers From Private Schools.*** We asked districts how many children, if any, transferred from private schools to public schools as a result of CSR. We estimate that at least 0.5 percent of students in CSR classes transferred from private schools. This number may understate the actual rate, as many districts did not know whether any of their students had transferred from private schools. If more families choose to attend public school as a result of CSR, the increase in the Proposition 98 minimum guarantee could be substantial. For example, if CSR causes an 0.5 percent increase in K-3 en-
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- rollment, the Proposition 98 minimum guarantee would increase by about \$50 million.
- **Teacher Morale.** Districts generally reported that the morale of CSR teachers went up, while the morale of upper-grade teachers stayed the same or went down.
  - **Parent Morale.** Districts generally reported that parent morale went up.
  - **How Would Districts Have Spent the Money Without CSR?** We asked districts how they would have spent their CSR funds if they received the funds as general revenues with no strings attached. About one-third said they would have reduced class size to some extent, but not necessarily all the way to 20. Another third said they would have spent the funds in a range of other ways, such as technology, staff development, facilities improvements, increasing their reserve, etc. Finally, one-third said that the collective bargaining process would require them to spend substantial portions on salary increases for teachers.

## ISSUES AND RECOMMENDATIONS

Based on the data and analysis discussed above, we drew the following conclusions:

- **Staying Under the 20:1 Cap Pushes Up Costs Substantially.** Districts have set CSR class sizes at a statewide average of about 18.8 primarily to avoid losing CSR funding, which occurs when any individual CSR class exceeds an annual average class size of 20. If CSR classes average 18.8 students instead of 20, however, the cost of the program is *21 percent higher*.
  - **Insufficient Qualified Teachers Are Available to Staff CSR Classes.** Twenty-four percent of teachers hired for CSR are not credentialed and are working under an emergency permit or waiver. School districts rate teachers hired for CSR as being less skilled, on average, than teachers hired in previous years. At the same time districts are hiring less qualified teachers, most are also experiencing difficulties in implementing staff development for those teachers.
  - **New Facilities Will Be Expensive.** Most new classrooms for CSR were created by installing portables. In addition, a significant number of facilities were converted from other uses, potentially curtailing other programs or services. New facilities to expand
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CSR next year to more classes and grades will be much more expensive on a per-classroom basis, suggesting that districts now have even fewer options for creating CSR facilities than they did this year.

Based on our analysis of the survey data detailed above, we believe the Legislature should take a number of steps to modify the Governor's proposed CSR plan.

### Provide More Flexibility in Use of CSR Teachers

***We recommend the Legislature provide districts with increased flexibility in the CSR program. Ideally, the Legislature should allow districts to choose other ways to deploy new teachers, such as small-group tutoring, in addition to CSR.***

Last year, in our *Analysis of the 1996-97 Budget Bill* we recommended that the Legislature fund a more flexible program that would include reducing class sizes as well as other options. Under our proposal, districts would be required to hire the same number of teachers they would have hired to reduce class size to 20, but they would be allowed to deploy these teachers in a more flexible fashion. Our recommendation has two advantages, which we discuss below.

***Flexibility to Choose the Best Educational Strategies.*** There are a number of educational interventions with demonstrated effectiveness that require additional teaching staff. Under our proposal, schools could direct staff resources to a wider range of activities that have been shown to increase student achievement, including (1) one-to-one or small group tutoring to supplement classroom instruction, (2) implementation of a structured reform program that requires additional teaching staff, or (3) any other purpose that involves direct instruction of students.

***Mitigation of Problems Caused by Inflexibility in the Current CSR Program.*** The strict 20-student CSR cap creates a number of administrative and educational problems, including:

- ***Substantial Increases in Statewide Costs.*** The Legislature intended to reduce class sizes to 20 and provided funding on that basis. But districts appear to be putting about 18.8 pupils in their CSR classes, on average, largely in order to be sure of staying under the 20:1 cap. This will result in substantial increases—as much as 21 percent—in the cost of the program. Some districts may even be forced into class sizes of 16 or 17, which further increases district costs.
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- **Busing to Achieve Smaller Class Sizes.** Some larger districts have resorted to busing children between schools to remain under the 20:1 cap in each class. Busing students out of the neighborhood school is disliked by parents and students and creates additional costs for districts. The disruption to students has unknown educational consequences.
- **Questionable Education Practices.** Some very small districts have had to shuffle children between upper and lower grade combination classes in ways that may not be educationally sound, solely to stay under the 20:1 cap. Clearly, the Legislature did not intend CSR to create a worse educational environment for students.
- **No Space for Expansion.** Some schools' participation will be limited due to lack of space for new classrooms.

For these reasons, we continue to recommend that the Legislature provide broad flexibility to schools in determining the best use of additional teacher resources in meeting student needs.

#### Provide More Flexibility Within the CSR Program

***If the Legislature chooses not to adopt our recommendation for greater flexibility in how CSR teachers are deployed, we recommend that the Legislature enact greater flexibility in the 20:1 cap within the current CSR program. This will reduce costs and reduce the incidence of busing and inappropriate class assignment that have occurred due to inflexibility in the program***

If the Legislature wants to continue the existing program, increasing the flexibility over the way it is implemented would go a long way towards helping districts administer and finance CSR.

***Districtwide Averaging Would Solve Many Problems.*** Allowing districts to maintain average class sizes of 20 students over the whole district, with a maximum of up to 22 in any one class, would create substantial additional breathing room for districts. Such flexibility *would not increase average class sizes from the level originally intended by the Legislature* but would have a number of beneficial effects:

- **Reduction in Ongoing Costs.** If districts average 20 per class, per-pupil costs would be reduced significantly below their likely level this year.
  - **Reduction in New Teachers Hired.** Implementation in three grades would require 4,600 fewer new teachers, reducing the pressure to hire less qualified teachers that CSR has created.
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- **Reduction in Facilities Needs.** Correspondingly, fewer classrooms would be needed, reducing pressure on already limited space at schools participating in CSR.

This simple change would greatly help most districts implement CSR. Because of the special problems for small districts, however, they may need additional flexibility.

**Provide Flexibility for Schools That Do Not Have Room for Facilities.** In addition to flexibility on class size, the Legislature should provide flexibility for schools that have no way to add new classrooms. Schools in this position could be allowed to certify to SDE that no space exists and be given greater flexibility in determining how the additional teacher resources should be used.

Schools need additional flexibility to meet the challenge of reducing class sizes. We recommend the Legislature adopt relatively modest changes to increase local flexibility in the CSR program. This would reduce the cost of CSR and avoid many of the implementation problems schools currently confront.

### Delay Implementation of a Fourth Grade

**We recommend the Legislature delay expansion of CSR to four grades due to shortages of qualified teachers and potential lack of facilities. The Legislature should provide \$100 million on a one-time basis in the budget year for class-size facilities. By this action, the Legislature will reserve \$100 million in ongoing funds that can be spent on a fourth grade of CSR in subsequent years.**

As we discussed above, teachers hired for CSR this year are less qualified than new teachers hired in previous years. The current three-grade CSR program will result in thousands more teachers being hired next year as districts continue implementation in the three grades that are already funded. Adding a fourth grade would create additional downward pressure on teacher quality as schools scramble to staff classrooms.

In addition, there is also evidence that many districts have exhausted existing spaces for expanding class sizes. This means further expansion will require adding portables or even new construction. This will create major district costs.

For these reasons, we recommend the Legislature delay expansion of the CSR program for at least one year. This will give districts time to continue implementing the existing program without creating the new pressure of expanding to additional grades. We will continue monitoring

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CSR implementation in order to provide information in the future on the status of the program.

We do think that extending the program to *all* of K-3 is warranted. For that reason, we recommend the Legislature signal its intent to provide expansion funds in the future. This will give districts a better understanding of the state's long-term plans for CSR. For this reason, we recommend the Legislature earmark \$100 million in the 1997-98 Proposition 98 "base" for support of class size reduction in subsequent years. This \$100 million can then be appropriated in 1997-98 as a one-time augmentation to the class size facilities grant.

This approach has three benefits. First, it provides additional support for class size facilities in 1997-98—when these monies are needed. Second, it clearly states the Legislature's long-term intentions for class size reduction. Finally, it works into the base \$100 million, or about one-third, of the approximately \$300 million needed to expand CSR to a fourth grade. The remaining funds needed for a fourth grade could be added to the base in future years, in step with districts' ability to implement CSR in all four grades.

### **Maintain Per-Pupil Funding Level for CSR**

***We recommend that the Legislature maintain CSR per-pupil funding at the original level (adjusting it only for cost of living, as the budget proposes for 1997-98). We further recommend that the Legislature direct any discretionary Proposition 98 funds to district revenue limits, which could be used to cover unfunded CSR costs (if any) or for any other locally determined priority.***

Many districts have stated that CSR actually costs around \$750 to \$800 per pupil, and that, at a 1996-97 funding level of \$650 per pupil, CSR is "encroaching" on district general funds. In fact, many districts commented in our CSR survey that the state should set aside full per-pupil funding for the program. Some districts advocating higher per-student levels indicated that this would help the districts because the funds would not then be subject to collective bargaining. There are two main points to consider.

First, what does CSR cost? As discussed above, the cost of the program is around \$770 per pupil, on average, *this year*. The cost would go down to about the amount included in the budget *next year* if the Legislature provides districts additional flexibility so that they are able to average 20 pupils per class, rather than 18.8. Even at 20 students per class, about half of the districts would experience costs in excess of the budgeted amount. The factors driving these costs—including teacher salary levels and pre-

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CSR class sizes—result from past district choices regarding the use of funds. Conversely, about half the districts would experience savings. Increasing the CSR per-pupil amount would simply add to the “windfall” benefits experienced by these districts.

The second issue is whether new Proposition 98 funds should be used to increase per-student CSR funding or to increase district revenue limits. By adding available funds into revenue limits, districts could then prioritize these funds for CSR if they so desired or spend them in other ways. Either way, districts would receive the same amount of revenue. The only difference would be in how much flexibility they would have in spending the funds.

Districts generally say they prefer local control, and complain of state micro-management when limitations are placed on local financial discretion. As we discussed in our K-12 Priorities section, we think the Legislature should opt for local control over funds whenever possible. Local administrators and school board members have more information about specific local needs than do policymakers in Sacramento.

On the other hand, some districts would prefer to see more funds in the CSR program, rather than the revenue limit, because the funds would not be subject to collective bargaining or available to other constituencies that would advocate using the funds for other purposes.

In effect, many districts would like to have it both ways. If the Legislature places additional funds in the revenue limit, districts could continue to complain that CSR encroaches on their general fund even though they would actually have *greater* flexibility over expenditures. If the Legislature places more funds in the CSR program, the Legislature would be unnecessarily directing the use of these funds, district discretion would be reduced, and the state would short-circuit the local process of determining how new revenues would best serve student needs.

***Analyst’s Recommendation.*** We recommend the Legislature maintain the current CSR per-pupil funding level, adjusted annually only for the cost of living. For 1997-98, this is the same as proposed by the Governor’s budget, which provides \$666 per pupil. Based on our data, a per-student amount of \$666 for CSR adequately covers the statewide average costs of the program—if districts have the flexibility to keep class sizes at 20 students.

The budget contains at least a \$300 million increase in district revenue limits. In our K-12 Priorities section above, we recommend that \$149.7 million in additional funds be added to district revenue limits. Together, these discretionary funds would provide more than enough

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ongoing funding for the CSR program for virtually all districts. Districts with lower CSR costs could spend the funds for other purposes.

If new funds are added to districts' revenue limits rather than CSR, districts will continue to argue that CSR encroaches on their general funds. Despite that, the Legislature needs to send a signal to districts that they are responsible for prioritizing their revenues. Adding available funds to revenue limits instead of CSR would increase district responsibility for determining the local cost of CSR and prioritizing funds for that purpose.

Increasing per-pupil funds for CSR would free districts from having to prioritize these funds through the collective bargaining process. But, class size reduction *should* be part of collective bargaining because it represents a workload reduction for K-3 teachers. Just as teacher contracts often compensate teachers when class sizes exceed a certain level, contracts could recognize the workload reduction and improvement in working conditions when classes are small.

### **Provide Staff Development Funds**

***We recommend the Legislature broaden the allowable uses of the \$52 million in Goals 2000 funds proposed for staff development in reading to include the staff development needs of newly hired CSR teachers.***

The Governor's budget proposes \$52 million in federal Goals 2000 funds for reading skills development for elementary school teachers. The federal funds are available for a wide variety of state school improvement activities. All of the funds would be devoted to reading skills training, with \$46.4 million allocated to training teachers in grades four through eight, and \$5.6 million to augment training programs for teachers in grades kindergarten through three. In the current year, \$39.4 million in Goals 2000 and General Fund monies are dedicated for K-3 teacher training in reading.

The amount proposed for teachers in grades four through eight represents about \$600 per teacher. The total amount provided to K-3 teachers—including both the \$39.4 million in the current year plus the additional \$5.6 million proposed for 1997-98—amounts to about \$500 per K-3 teacher. The DOF could not justify either the purpose or the amount of funds set aside for the intermediate and middle school teacher training.

Our CSR survey indicates a pressing need for providing staff training to new CSR teachers. As noted above, teachers hired for CSR are less qualified and have fewer teaching skills than typical new teachers. In addition, districts have had difficulty finding sufficient funds to provide

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staff development. If CSR is going to result in improved achievement, a qualified teaching force is essential.

For these reasons, we recommend the Legislature approve the proposal to use the Goals 2000 funds for staff development. Because CSR has created an acute need for new-teacher staff development, we further recommend the Legislature broaden the allowable uses of the funds so that districts may also use the funds for staff development of teachers hired for CSR.



## REVENUE LIMITS

School district revenue limits provide general purpose support for schools. Revenue limits were established in Chapter 1406, Statutes of 1972 (SB 90, Dills) as part of the state's response to the *Serrano v. Priest* state Supreme Court decision of 1971. The revenue limit was calculated to be equal to the per student amount of general purpose state aid and local property taxes that a district received in 1972-73. The limits do not include state categorical funds (such as state aid for special education or class size reduction), lottery revenue, or any federal aid to local school districts. Currently, approximately 72 percent of school support is provided through the revenue limit mechanism.

In practice, there are at least five different revenue limits. Each of these is defined in Figure 26 (see next page). In this section, we review the state's system of revenue limits used to provide general purpose funding to K-12 districts, and make several recommendations that would speed up the equalization of amounts provided to districts.

### THREE-AGENCY REPORT ON REVENUE LIMIT PROCESS—UPDATE

***As directed by the Legislature, the Department of Education, the Department of Finance and the Legislative Analyst's Office are currently working on a joint report on the revenue limit apportionment process.***

Last year in our *Analysis of the 1996-97 Budget Bill*, we commented on a number of complexities with the state's revenue limit system. As Figure 26 illustrates, the revenue limit system is complex, making it difficult to understand and cumbersome for state and local agencies to use.

Based on this analysis, the Legislature adopted language in the *Supplemental Report of the 1996 Budget Act* directing the State Department of Education (SDE), the Department of Finance (DOF), and the Legislative Analyst's Office (LAO) to jointly review the revenue limit apportionment process and make recommendations to simplify the process. The stated

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**Figure 26**

**Revenue Limits—General Definitions**

**Statutory Base Revenue Limit**

The revenue limit defined in statute before any adjustments. Based on 1972-73 actual funding plus COLAs, and equalization and other adjustments that have been provided subsequently.

**Equalization Base Revenue Limit**

Equal to the statutory base revenue limit less additional funds for longer school day, longer school year, and minimum teacher salaries. Used for revenue limit equalization, this limit divides districts into six categories based on type (elementary, high school, and unified) and average daily attendance (small and large).

**Blended Revenue Limit**

Equal to the district's statutory base revenue limit times the ADA enrolled in 1982-83 and 105 percent of the statewide average statutory base revenue limit times any growth in ADA since 1982-83. Applicable only for about 161 districts that have revenue limits in excess of 105 percent of the state average.

**Deficited Base Revenue Limit**

Equal to about 90 percent of a district's statutory or blended revenue limit. The deficit factor reflects the experience of the early 1990s, when revenue limit entitlements were inflated by statutory COLAs each year, but were not fully funded in the annual budget acts. All school districts are affected by this adjustment.

**Adjusted Funded Base Revenue Limit**

Equal to the deficited base revenue limit less recaptured savings in the Public Employees' Retirement System (PERS) costs. With the exception of San Francisco Unified School District, which is not part of PERS, every school district has a unique PERS adjustment.

intent of the review is to (1) make the process more understandable and (2) reduce unnecessary workload at the state and local levels.

**LAO Proposals.** The three-agency report is not due to the Legislature until May 1, 1997. We have made a number of suggestions to the DOF and the SDE including:

- Discontinuing all revenue limits other than the “adjusted funded base revenue limit.” This revenue limit would become the new “statutory base revenue limit.”

- In the future, have the district pay any increase, or benefit from any decrease, in Public Employees' Retirement (PERS) costs.

Our discussions with the SDE and DOF are ongoing.

## USING THE COLA TO EQUALIZE

***We recommend that the Legislature adopt legislation to replace the current uniform revenue limit COLA with a new formula that equalizes revenue limits over time. We recommend making this change effective in 1998-99 rather than in the budget year to allow districts to adjust to the change. We further recommend increasing revenue limits by \$149.7 million above the Governor's proposed levels and using a new formula to distribute this additional amount.***

In each of the past three years the Legislature provided significant amounts of funding to partially equalize revenue limits. Below, we provide some background on the state's COLA and equalization policy. We then analyze problems with the current approach and recommend an alternative COLA and equalization methodology.

### Background

The Legislature has, since the first Supreme Court *Serrano* decision in 1971, periodically enacted legislation to equalize revenue limits among the state's school districts. Chapter 894, Statutes of 1977 (AB 65, Greene) established a school finance funding mechanism that provided school districts with different COLA amounts depending upon their per-pupil revenue limits. In general, a district with a revenue limit above the statewide average would receive a smaller COLA than a district with a revenue limit below the statewide average. Under this system, per-pupil funding levels would be drawn to the statewide average (squeezed) over time. Thus, funding disparities stemming from differences in district wealth gradually would be reduced.

Current revenue limit COLA and equalization policy is based on Chapter 498, Statutes of 1983 (SB 813, Hart). Senate Bill 813 eliminated the "squeeze" formula, and instead provides that all districts of the same type (elementary, high school, and unified) receive the same fixed dollar amount as a COLA. In 1995-96, for example, all elementary school districts received a COLA of \$82 per ADA, high school districts received \$100 per ADA, and unified districts received \$86 per ADA. This approach does nothing to reduce the dollar differentials among districts and only slightly reduces the *percentage* differentials.

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Since the enactment of SB 813, the Legislature has provided periodic “leveling up” funds for revenue limit equalization. That is, funds are provided periodically to increase the revenue limits of below-average districts to the state average. In calculating equalization adjustments, districts are divided into six categories by type (elementary, high school and unified) and ADA (small and large). The amount of equalization aid a district qualifies for depends on the amount necessary to bring its revenue limit to the average revenue limit in its category.

### Problems With the State’s Current Approach To COLA and Equalization

Our analysis finds two major problems with the state’s current approach: (1) the COLA does very little to help provide equalization, and (2) the equalization leveling up mechanism is costly and inefficient (in fact, by its design, it probably will never fully equalize revenue limits among the districts).

**Current COLA Does Little for Equalization.** The current uniform fixed-dollar COLA is described as a “percentage equalizing” COLA. Figure 27 illustrates the operation of this COLA over time using two hypothetical districts—A and B. Our illustration assumes District A’s revenue limit is at the state average.

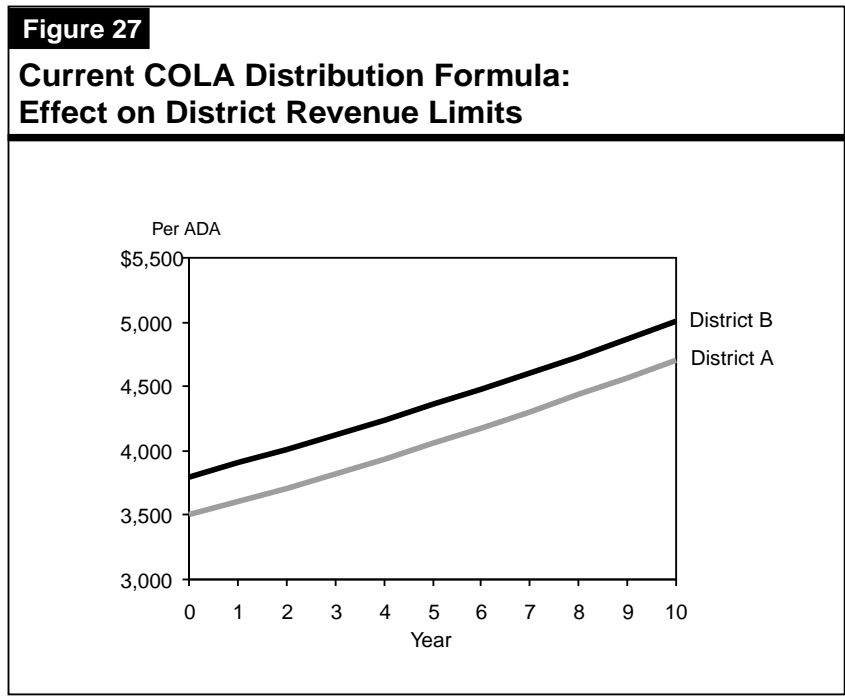


Figure 27 shows that the dollar difference between the two districts does not change over time. The dollar difference was \$300 in year one and remains at \$300 in year ten. Because the total revenue limit increases over time, the percentage difference between the two gets smaller over time. In year one, District B's \$300 advantage is 9 percent higher than District A's (\$3,800 compared to \$3,500). By year ten dollar the \$300 advantage is only 6 percent higher than District A's (\$5,004 compared to \$4,704). However, no progress has been made to reduce the dollar differences in revenue limits between these two districts.

**Equalization—Costly and Inefficient.** Current law uses a “leveling-up” approach to equalize revenue limits. “Leveling up” assumes that districts with high revenue limits are funded at an appropriate level (and low revenue limit districts are underfunded). While the goal is to bring districts up to the average in their category, in fact what happens is that the districts are being increased toward the highest revenue limit in their class. Each “round” of funding increases the “average,” necessitating a new round of equalization.

The dollar differences in revenue limits get smaller and smaller but never go to zero. To fully equalize all districts under the leveling-up approach, the Legislature would have to provide sufficient funds—estimated by the SDE to be \$11.1 billion—to bring each district to the *highest* revenue limit in its category.

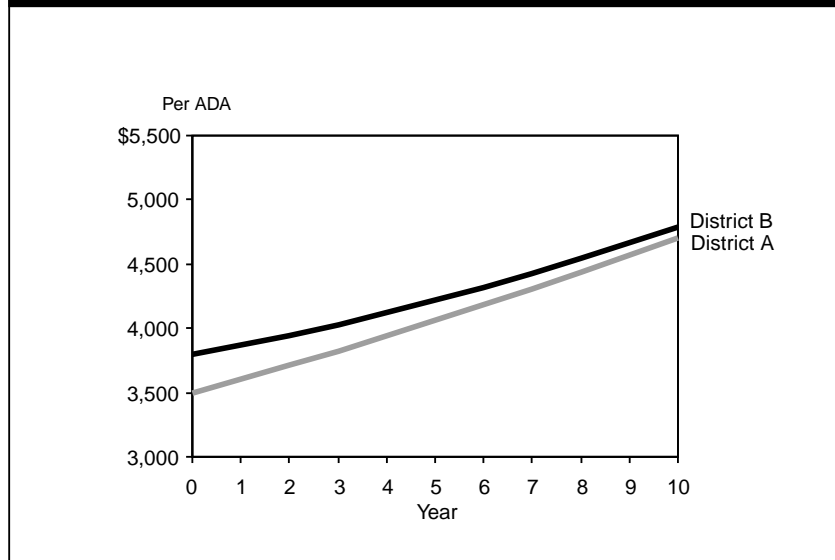
### More Efficient COLA Would Equalize Revenue Limits

Figure 28 (see next page) illustrates how an AB 65-type COLA would affect revenue limits over time. The figure shows that the dollar difference between the two districts gets smaller over time. This closure is the result of providing a sliding scale COLA to districts whose revenue limits are not at the state average. COLAs are granted in relationship to the distance the district's revenue limit is from the statewide average. The farther below the average, the greater the COLA and, conversely, the farther above the average the smaller the COLA.

This type of adjustment can guarantee a COLA to every school district. The important point, however, is that no matter what parameters are chosen, an AB-65-type COLA eventually does reach a point at which revenue limits are equal.

Accordingly, we recommend that the Legislature enact legislation to adopt an AB 65-type COLA for revenue limits. Because districts are already in the process of developing budget plans for 1997-98 based on current law, we recommend distributing the budget-year COLAs based on current law.

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**Figure 28****LAO Proposal for COLA Distribution:  
Effect on District Revenue Limits**

In our discussion of *K-12 Priorities*, we recommend increasing revenue limits \$149.7 million *above* the Governor's proposed levels. We recommend that this additional \$149.7 million be distributed using an AB 65-type formula. Starting in 1998-99, all revenue limit COLAs would be distributed by this new formula.

### PROVISION OF "BASIC AID" HINDERS EQUALIZATION EFFORTS

*We recommend that the Legislature enact legislation to phase out, over a three-year period, "basic aid" provided to high property-wealth school districts, because (1) providing basic aid is contrary to the state's policy of eliminating wealth-related disparities in education spending and (2) the provision of such aid is not necessary in order to comply with the requirements of the State Constitution.*

In 1976, we first recommended that the Legislature eliminate basic aid payments. Our recommendation built on the Los Angeles County Superior Court's 1974 *Serrano* decision holding that the state's then-existing school finance system was unconstitutional primarily because the amount of educational spending was largely determined by the assessed value of property within each district. The State Constitution's requirement that



the state provide at least \$120 per pupil—so-called “basic aid payments”—contributed somewhat to the wealth-related disparities.

**Background.** As we discussed above, general purpose aid is allocated to school districts through a “revenue limit” system. These funds are provided through a combination of local property taxes (together with other specified revenues) and state aid. For most school districts, the amount of local property taxes received in a year is not sufficient to fund revenue limits. Thus, the state provides these districts with sufficient funds to make up the difference between the revenue limit and the amount of property taxes received by the district.

For 56 school districts, however, the amount of local property taxes received *exceeds* the revenue limit guarantee. For these districts (referred to as “basic aid districts”), the state does not recapture any of the excess amount—estimated by the Department of Education to be \$70 million in 1995-96. On the contrary, the state adds to the excess by providing these districts with additional funding—estimated by the Department of Education to be \$11.2 million in 1995-96—in the form of state basic aid.

**Basic Aid Exacerbates Wealth-Related Disparities.** School districts whose income from local property taxes exceeds the revenue limit guarantee clearly receive large amounts of revenue from local sources. The provision of state basic aid on top of this *exacerbates* the wealth-related disparities in educational spending per pupil and is thus contrary to the Legislature’s efforts to equalize revenue limit funding.

**Basic Aid Not Constitutionally Required.** The provision of basic aid derives from a common assumption that Article IX, Section 6 of the California Constitution requires that each school district receive *general-purpose apportionment aid from the state* of at least \$120 per ADA. Legislative Counsel has opined, however, that the constitutional requirement can be satisfied by the provision of at least \$120 per pupil in state aid of *any type*, including aid provided under categorical programs that flow through the State School Fund. If a district did not receive the minimum from the combined sources, only *then* would the state be obligated to provide the difference.

**Phase-Out of Basic Aid.** We find no analytical basis to continue basic aid payments. In the past we recommended eliminating basic aid payments in the budget year. However, we realize that school districts are already developing their budgets for 1997-98. We also realize that eliminating basic aid over a longer period would allow districts more time to adjust their budgets. Accordingly, we recommend that the Legislature enact legislation effective in 1998-99 to phase out the \$120 basic aid payments at the rate of \$40 per ADA over the following three years.

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## CHARTER SCHOOL LIABILITY AND ACCOUNTABILITY NEED CLARIFICATION

***We recommend that the Legislature adopt budget bill language directing the State Department of Education to adopt a policy on fiscal accountability and liability of charter schools selected for its “Charter School Direct Funding Pilot Project” prior to starting the pilot.***

Chapter 781, Statutes of 1992 (SB 1448, Hart) provides opportunities for teachers, parents, pupils, and community members to establish and maintain “charter” schools that operate independently from the existing school district structure. Since the passage of the law, over 100 charters have been issued by school boards and county offices of education around the state.

Chapter 781 provides for direct funding of charter schools by the Superintendent of Public Instruction. Currently, the State Department of Education (SDE) identifies most fund sources for a charter school separately and passes the funds to the charter *through the sponsoring school district*. However, starting in July 1997, the SDE plans to begin a pilot project to provide funds *directly to the charter school* without passing the funds through the sponsoring school district. The SDE plans to include up to seven schools in this pilot project.

We are concerned that providing funds more directly to charter schools and bypassing the fiscal controls of the county and/or the sponsoring school districts could potentially put the sponsoring school districts, the county office of education, or the state, at financial risk in the event a charter school fails or creates a liability that exceeds the school’s capacity to pay. Among the questions we have on accountability and liability are:

- Is the charter school an entirely separate entity from the sponsoring school district?
- Who specifically is fiscally responsible and accountable for the actions of the charter school?
- Who specifically has oversight responsibility for fiscal solvency?
- Is the exposure to liability of the sponsoring school district and/or county office of education limited?

The SDE convened a working group on the pilot project last fall. One of the areas that this group is working on is the accountability and liability issues. The SDE’s broadly based working group is well equipped to address the many facets of these issues.

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However, we believe that the SDE should insure that these issues are clarified *prior to* implementing its pilot project. Accordingly, we recommend that the Legislature adopt budget bill language directing the SDE to provide the Director of Finance and the Legislature with a resolution of these issues prior to implementing the pilot. We recommend adoption of the following budget bill language:

The State Department of Education (SDE) shall not begin the charter school direct funding pilot project until the Director of Finance has approved the SDE's policy for fiscal accountability and liability of charter schools selected for the pilot. The Director of Finance shall notify the Legislature's policy and budget committee chairs and the Chairperson of the Joint Legislative Budget Committee, not less than 30 days prior to the effective date of this approval of the policy.

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## REFORMING CATEGORICAL PROGRAMS

***We recommend the Legislature simplify and consolidate 21 K-12 categorical programs into four categorical block grants in order to increase local flexibility and eliminate negative incentives created by the programs. We further recommend the Legislature make these same changes in statute so that school districts can begin long-term planning based on this new program structure.***

Just as *new* categorical programs should meet a rigorous test for approval, *existing* programs should be reviewed periodically to ensure the need for state intervention still exists and that the programs are designed to allow school districts to make the most effective use of the funds as possible. In this section, we review the system of K-12 categorical programs and suggest reforms to make these programs more flexible for districts and increase local accountability for results.

### PROBLEMS WITH THE CURRENT STRUCTURE

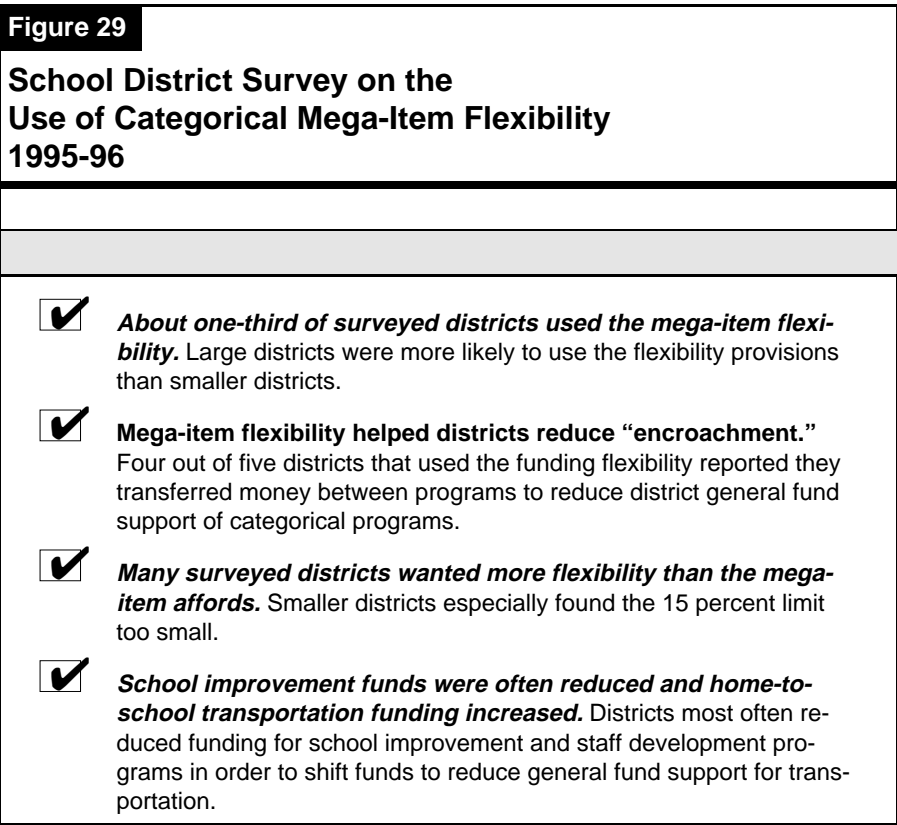
#### **Mega-Item Provides Inappropriate Flexibility**

Currently, most categorical funds are appropriated through the categorical “mega-item,” which provides \$2.5 billion in General Fund support for 37 individual programs in 1996-97. The budget proposes \$2.4 billion for these programs in 1997-98. The Legislature originally created the mega-item to minimize the Governor’s ability to make specific categorical program reductions through the use of line-item vetoes. In addition, the mega-item allows districts to move up to 15 percent of funds from one program to another as a way to help districts to reallocate funding in order to meet district categorical program needs.

In our *Analysis of the 1995-96 Budget Bill*, we discussed the results of a district survey we conducted on the value of the mega-item to school districts. The results of the survey are displayed in Figure 29. The overall results of the survey established that the mega-item provided the wrong type of local flexibility. Rather than permit districts to meet high-priority categorical program funding needs, districts used the flexibility to in-

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crease their overall financial flexibility *at the expense of* categorical programs. Based on these results, we concluded that the mega-item failed to further the Legislature’s policy goals in establishing the categorical programs.



**Problems With the Overall System**

We have also reviewed the functioning of the overall system of K-12 categorical programs. In our report *Reform of Categorical Education Programs* (April 1993), we reviewed problems in the design and operation of categorical programs. Figure 30 (see next page) displays our findings. In short, we concluded there is little evidence that categorical programs successfully meet their intended goals. Categorical programs also emphasize administrative and fiscal requirements rather than program goals. As a result, we concluded the existing system of categorical programs in K-12 education was not as effective as possible in meeting the needs of students or schools.

**Figure 30**

### Problems With California's System Of Categorical Education Programs

- No conclusive evidence on the success of categorical programs.** Most programs are never evaluated. Categorical programs that have been evaluated reveal a mixed record of success.
- State rules restrict needed local flexibility.** Complex and detailed program requirements in some programs reduce the flexibility needed by schools to maximize the impact of funds on improving student achievement.
- A fragmentation of local programs.** Without a local strategy for integrating categorical programs with the basic educational program, process requirements of the categorical programs shape local responses rather than the needs of students.
- Funding formulas create negative incentives.** Some categorical programs create financial incentives that encourage schools to act in ways that are not in the best interests of students.
- Blurred accountability for meeting student needs.** Creating separate programs for specific student needs creates confusion about who is responsible for improving student achievement.

## CONSOLIDATE AND SIMPLIFY CATEGORICAL PROGRAMS

To increase local flexibility and eliminate negative incentives created by the current system of categorical programs, we recommend the Legislature consolidate 21 existing programs into four categorical block grants. The remaining programs would continue to be budgeted either separately or in a smaller mega-item. The four largest programs remaining in the mega-item would be Home-to-School Transportation (477.9 million), Year-Round Schools (\$62.8 million), Child Nutrition (\$58.2 million), and Gifted and Talented Education (\$50.7 million). We also recommend the Legislature appropriate \$10 million in federal funds to begin a program of evaluating K-12 categorical programs. Figure 31 illustrates the components of our recommended changes, which are discussed in more detail below.

**Figure 31**

**LAO Recommended  
K-12 Categorical Block Grants**

- School Improvement Block Grant.** This block grant would consolidate \$675 million in funding currently provided through nine programs. Funding would be provided to school sites and would be available to meet a range of school improvement needs.
- Staff Development Block Grant.** The funding from two existing programs would comprise this \$91 million block grant, which would support staff development needs at each site, with a priority for new teacher support services.
- Compensatory Education Block Grant—Part A.** Four programs would be consolidated to provide \$941 million for school district compensatory programs. Included in this block grant is funding currently provided through the Economic Impact Aid program and the Court-Ordered and Voluntary Desegregation programs.
- Compensatory Education Block Grant—Part B.** Six programs currently supporting alternative education settings would be consolidated into a \$158 million block grant. Funds could only be used to support programs lasting at least five hours each day.
- K-12 Evaluation.** This program would supply \$10 million each year to support rigorous evaluation of K-12 programs, replacing the defunct “sunset” process that previously provided the Legislature with information on the effectiveness of education programs.

Before describing the individual block grants in more detail, we first discuss three issues affecting all the categoricals: standards, program rules, and per student funding allocations.

**Block Grants Based on State Standards.** We recommend creating a categorical accountability system that uses three common educational indicators to measure the success of local programs. Most importantly, the accountability system should measure whether students are making adequate academic progress. While we would prefer a uniform state standard, there are no existing state standards of academic achievement. The Commission on Academic Content and Performance standards is

currently working to develop such standards. Until these standards are in place, our recommended accountability system would use existing local standards of adequate student progress.

The accountability system also would include two measures of student attendance. Student attendance rates, routinely collected by all schools, would measure the success of schools in working with parents to ensure students attend school. Student dropout rates, also currently collected by districts, indicate a school's effort in keeping all students involved in learning.

Using these three indicators, schools and districts would be required to assess their success in meeting the standards for each program's targeted group of students. For instance, the school improvement and staff development block grants—which would target school-wide concerns—would require schools to assess how well *all* students at the school were meeting these three goals. The school improvement plan would focus on improving the school's program for those students who did not meet the standards. Similarly, the compensatory education block grant—which would target the needs of low-performing and limited English students—would require districts to measure how well these students are progressing towards meeting the standards.

***Old Program Rules Would Not Apply.*** Our proposed block grants would contain a minimum of state rules or directives. Schools would be required to spend block grant funds for the purpose specified — no funds could be transferred by districts to other categorical programs or purposes. Except in limited instances, the state would not define the appropriate uses of the funds or program models eligible for funding.

***Per-Student Funding Allocations.*** Block grant funds would be distributed on a per-student basis in our proposal. Current funding allocations by district would not be affected, however. To equalize district funding levels, we recommend using cost-of-living adjustments to provide a larger COLA to lower-funded districts. This would even-out per-student funding levels over time.

### **A School Improvement Block Grant**

***We recommend the Legislature consolidate nine separate categorical programs into one school improvement block grant that would provide \$676 million in funding to school sites.***

Figure 32 displays nine programs that provide funding to (1) meet specific school site needs or (2) support improved curriculum and instruction. We recommend the Legislature consolidate these programs into a single grant. This would place about \$676 million in General Fund

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support for school improvement activities at the school level—about \$315 million more than is currently made available under the School Improvement Program (SIP). The block grant would have the following features:

- **School Plans.** School plans would be developed by a site council, as in the existing SIP. These plans, however, would require a three-year program of improvement compared to the current one-year plan requirement. Plans would focus on improvements affecting all students at the school.
- **Textbook Set-Aside.** Funding currently provided through the Instructional Materials program would be reserved for instructional materials needed at the site. Current restrictions on the use of these funds, however, would be eliminated.

**Figure 32**

**Programs Under the Proposed School Improvement Block Grant**

(In Millions)

Program	1997-98 Proposed Budget
School Improvement program	\$ 360.4
Instructional materials	157.1
Categorical block grant	67.8
Educational technology	35.6
Class size reduction (high school)	32.3
Tenth grade counseling	13.3
Demonstration programs in intensive instruction	5.4
Agricultural vocational equipment	3.6
School-based management	0.9
<b>Totals</b>	<b>\$676.4</b>

**Staff Development Block Grant**

*We recommend the Legislature create a Staff Development Block Grant by consolidating two existing categorical programs in order to provide \$91 million in flexible funds at school sites to meet staff training needs.*

Currently, the Mentor Teacher Program and the School Development Plans and Resources Program (also known as the SB 1882 Staff Develop-

ment Program) provide resources to schools and districts for staff development and new teacher assistance. We think these funds would be more effectively used if the site level determined the highest priority uses of staff development funds. By consolidating these two programs, the Legislature would make \$91 million available to schools each year, or about \$7,500 for a typical elementary school.

Planning for staff development would be part of the three-year school site plan required under the school improvement block grant and would support training and mentor teachers needed to improve teacher skills and, ultimately, student achievement.

**Priority for New-Teacher Assistance.** We recommend the block grant establish a priority for staff development assistance for beginning teachers. Evaluations of the Beginning Teacher Support and Assessment program showed that program services substantially increased teacher retention and teaching skills. Therefore, we suggest the Legislature establish a priority for new teacher assistance services similar to those found in BTSA.

### Compensatory Education Block Grants

***We recommend the Legislature merge all existing categorical programs for disadvantaged and high-risk youth into a single block grant with two parts: Part A would provide up to \$941 million in compensatory funding that currently flows through four programs. Part B would provide \$150 million in funding for alternative programs for those at-risk students who benefit from a different educational setting.***

There are ten existing programs for students who need additional services to be successful in school. These students include low-performing students, limited-English-proficient students, and students who may be more successful in an alternative education setting. There are two groups of programs. One group provides funding for supplemental services that are usually provided as part of, or in addition to, the regular classroom program. The second group provides support for alternative education settings some students require. Given these two groups, our proposed block grant also would have two parts.

### Compensatory Education Block Grant—Part A

The Legislature currently funds four programs that provide supplemental services to assist low-performing and limited-English-proficient students. Figure 33 describes these four programs. In total, the 1997-98 budget proposes \$941 million for these programs. Of these programs, two—the Economic Impact Aid (EIA) program and the Miller-Unruh

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program—support local programs focused solely on improving student achievement.

**Figure 33**

**Programs Under the Proposed Compensatory Education Block Grant—Part A**

(In Millions)

Program	Description	Proposed 1997-98 Budget
Court-ordered desegregation	Reimburses 13 districts for court-ordered activities to integrate students and provide supplemental services to groups historically disadvantaged by segregation.	\$448.4
Voluntary desegregation	Reimburses 52 districts for carrying out voluntary plans to integrate students and provide supplemental services to students.	97.1 <sup>a</sup>
Economic impact aid	Provides formula grants to districts for compensatory education and supplemental services for limited-English-proficient pupils.	366.3
Miller-Unruh Reading Program	Provides grants to districts to improve reading for economically disadvantaged students in early grades.	29.1
<b>Totals</b>		<b>\$940.9</b>

<sup>a</sup> The Governor's budget proposes to change the way the Voluntary Desegregation Program is budgeted in 1997-98. Program funding levels would not change.

The court-ordered and voluntary desegregation programs have two goals—assisting low-performing students and encouraging racial integration of schools. As a result, district desegregation programs spend up to 25 percent of state funding for busing and the remainder on compensatory activities such as smaller class sizes, magnet programs and other supplemental services.

The compensatory services funded through the EIA and Miller-Unruh programs have the same general goals as the compensatory activities funded through the desegregation programs—increasing student achievement. The existing system of programs has created a number of problems, however, including overlapping program missions, a lack of outcome measures that indicate student progress, rigid state funding

rules for reimbursement, and a negative incentive for schools to end court-ordered programs due to fears of a loss of state funding.

**Governor Proposes to Eliminate Voluntary Desegregation.** The Governor's budget proposes to eliminate the voluntary desegregation program by merging it into two existing compensatory education categorical programs: court-ordered desegregation and Economic Impact Aid. Specifically, the budget proposes shifting the \$97.1 million in voluntary desegregation funds as follows:

- **\$49.3 Million Would Be Shifted to the EIA Program.** This is the amount that currently goes to 44 districts that receive voluntary desegregation funds but are not under any court desegregation order. Under the Governor's proposal, this money would continue to go to these 44 districts, but as part of their EIA grant.
- **\$47.8 Million Would Be Shifted to the Court-Ordered Desegregation Program.** This is the amount that currently goes to eight districts that receive voluntary *and* court-ordered desegregation funds. These districts use the voluntary money as part of their court-mandated program. Under the Governor's proposal, total desegregation funding levels for these districts would not change.

We see two issues with this proposal. First, the 44 districts with voluntary desegregation programs would experience significant near-term funding reductions. This is because the EIA allocation formula automatically reduces district allocations by up to 15 percent a year whenever a district's actual funding exceeds its formula-based allocation. As a result, by adding voluntary desegregation funding to a district's EIA allocation in 1997-98, districts would begin experiencing reductions in EIA funding in 1998-99.

Second, as discussed above, many desegregation programs involve busing students to achieve a better racial balance. State law, however, requires districts to spend EIA funds to serve limited-English or low-performing students. Thus, busing costs may not qualify as an appropriate expenditure under EIA. In addition, we question whether the Legislature should open the door to allow districts to spend EIA funds for transportation. This is because EIA is designed to provide supplemental education services, not administrative services such as transportation.

**Create a New Compensatory Block Grant.** We do agree with the basic idea of program consolidation behind the Governor's proposal. However, we believe that the Legislature should go further with this idea, and combine *all* categorical programs into a block grant that would provide extra help to disadvantaged pupils. With the exception of desegregation-related busing, all four programs have similar goals. Combining them

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would allow districts more flexibility to use the money as part of an overall strategy to improve the educational outcomes of disadvantaged students.

We think a block grant would have several benefits:

- First, our proposal would eliminate the current restrictions on eligible program activities. This flexibility would allow districts to use the funds more effectively to meet student needs and to better coordinate state programs with the federal Title 1 program.
- Second, our proposal would eliminate the current uncertainty created by the claiming procedures required under the desegregation programs. We also would eliminate the local match under the Miller-Unruh program and the requirement that funds support district reading specialists.
- Third, our proposal would lessen and eventually eliminate inequalities in funding levels for compensatory education (by using the COLA to equalize).

For these reasons, we recommend the Legislature combine the four existing programs into a Compensatory Education Block Grant—Part A. Our block grant would contain the following features:

- **Per-Student Funding Formulas.** Our block grant would distribute funds based on the number of students with a pre-existing economic or language disadvantage.
- **Hold District Funding Levels Constant.** Overall funding for the block grant would be equal to the amounts currently provided through the four programs. Individual district allocations would stay at current levels, but future COLA increases would be used to equalize funding levels among districts over time.
- **Move Transportation Funds.** Funding currently spent by districts for desegregation busing would be transferred to the Home-to-School Transportation categorical.
- **Outcome Data.** Districts would be required to determine whether students that generate the block grant money (LEP students and low-income students) meet standards on attendance, dropout and student achievement.

**Add Budget Bill Language.** The elimination of separate desegregation funding programs could raise legal questions about the state's obligation to fund court-ordered desegregation costs. To make clear that the state is continuing to provide funding for local desegregation programs, we

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recommend the addition of budget bill language declaring that the block grant contains such funding and that, if additional funds are needed, resources should be redirected by districts from funds provided by the state in the block grant or in the Home-to-School Transportation program. The language would read as follows:

The Legislature declares that funds previously provided under the Court-Ordered Desegregation and Voluntary Desegregation Programs are included in this item and Item 6110-111-0001 and shall continue to be spent for that purpose as necessary. If additional funds are needed for district desegregation efforts, districts may redirect other funds received through this item to support additional compensatory costs or through item 6110-111-0001 to pay for additional busing costs.

### **Compensatory Program Block Grant — Part B**

***We recommend merging six programs currently providing \$150 million for alternative K-12 programs for disruptive and other at-risk students into a block grant that would provide districts greater flexibility in meeting student needs.***

In addition to the compensatory programs discussed above, the Legislature currently funds six state categorical programs that are designed to provide support for schools that serve as alternatives to regular district-run high schools. These programs are summarized in Figure 34. These programs are different than the general compensatory programs recommended for Part A of the compensatory block grant in that they are designed for a more specific profile of student—the student who most likely is low-performing but also has additional risk factors, including a history of poor attendance or behavioral problems, and who would benefit from a different educational setting.

The existence of these multiple programs creates a number of significant problems for schools. First, most of the programs mandate a specific model of service delivery, which restricts the ability of schools to provide services in a way that best meets student needs. Second, schools have no direct control over the County Community Schools Program. This separation creates a barrier to the kind of coordination that is needed to ensure that a student (1) continues to attend school and (2) has an appropriate educational program.

In addition, since schools cannot access these funds, services provided to students through the county program are “free” to districts. This creates a financial incentive for districts to use the county programs rather than create district programs that may better meet student needs. Finally, there is no system of outcome measures that promotes accountability for program results in this area.

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<b>Figure 34</b>		
<b>Programs Under the Proposed Compensatory Education Block Grant—Part B</b>		
<b>(In Millions)</b>		
<b>Program</b>	<b>Purpose</b>	<b>1997-98 Proposed Funding</b>
Community Day Schools	District alternative schools for pupils that are expelled from regular programs or are in need of a separate program.	\$52.6
County Community Schools	County office of education alternative schools for students that are expelled, on probation, or referred for other reasons by districts.	44.6
Continuation High Schools	District alternative high schools for students in grades 10-12 who have poor performance, poor attendance, or behavioral problems.	21.4
Dropout Prevention	Funding to certain districts for specific models of alternative programs serving those at-risk of dropping out.	17.3
Partnership Academies	Funding to districts for combined academic/vocational programs for students at-risk of dropping out.	8.0
Opportunity Programs	District alternative programs for students in grades 7-9 who have truancy or discipline problems.	6.5
<b>Totals</b>		<b>\$150.4</b>

**An Alternative Program Block Grant.** Because of these problems with the current system, we recommend the Legislature create a Compensatory Program Block Grant—Part B that would provide funding to districts for alternative education settings as follows:

- **No Restrictions Over Program Model.** Districts could choose the program models that best meet student needs.
- **At-Risk Students.** Students eligible for funding under the block grant would be low-performing students that are at risk of dropping out or entering the juvenile justice system.
- **Funding Based on District Attendance.** District funding would consist of a per-pupil amount based on a fixed percentage of a district's ADA. (This is similar to the community day school fund-

ing formula under Chapter 974, Statutes of 1995 [AB 922, Friedman].) Funds may only be spent on programs that require students to attend school for at least five hours a day, including vocational instruction. Funds currently going to county community programs would be transferred to school districts over a three-year period.

- **Hold Districts Harmless.** District allocations would continue at existing levels. Future COLA amounts would be used to equalize funding levels between districts over time.
- **Outcome Data.** Districts would be required to determine whether students who attend alternative programs meet standards for the three accountability measures.

### A Program of Evaluation

***We recommend the Legislature appropriate \$10 million in federal Goals 2000 funds for an ongoing program of evaluation of state categorical programs and other critical areas of K-12 education.***

As we discussed above, there is very little good information on the effectiveness of education services. We believe that well-conceived evaluations are essential to further improvements in school performance. Good data on the effectiveness of educational programs would be very valuable to both state and local decision makers.

The Legislature, in making policy and budget decisions, needs good information on the impact of state programs on student achievement. Until recently, the state “sunset” process required SDE to issue periodic program evaluations of the major state categorical programs. These reports rarely provided an assessment of the impact of services on student achievement, however. The sunset process has been discontinued due to funding reductions that occurred during the early 1990s.

Local educators have a need for good data on how different program models meet the needs of different types of students. For educators, evaluations can answer the question of what is the most effective way to address student needs. Assessing the effect of different program models can give educators better insight into how best to serve their students.

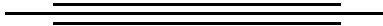
This is clearly an appropriate state role. Schools are unlikely to support these types of evaluations, for two reasons. First, most districts cannot afford the cost of these evaluations. Second, the benefits of evaluations are available to all schools, not just those who pay the costs. As a result, the state can generate important data on program effectiveness at a relatively low cost to districts.

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Good evaluations are costly and take a number of years to bear fruit. The payoff to students—in terms of more effective programs—and decision-makers is great, however. In 1992, the National Academy of Science concluded: “[W]ithout high-quality and credible evaluations, school districts will never be able to choose wisely among available innovations . . . . The committee is convinced that widespread school reform will require partnerships between researchers and practitioners”.

For these reasons, we recommend the Legislature appropriate \$10 million in federal Goals 2000 funds to begin an ongoing program of evaluations. The program would support high quality evaluations and would be guided by a representative group of legislators, the SDE and other state agency staff, local school representatives and academic experts.



## ADDRESSING THE K-12 SCHOOL MAINTENANCE PROBLEM

*The current system of funding K-12 ongoing maintenance and deferred maintenance creates counterproductive fiscal incentives that encourage K-12 districts to defer maintenance. California school districts report maintenance deferrals totaling \$2.6 billion. We recommend specific steps the Legislature should take to eliminate the existing maintenance backlog and provide for ongoing maintenance to avoid future deferrals.*

### BACKGROUND

One of the most common complaints about the state's education system—from parents and school employees alike—is the physical disrepair of school facilities. Stories abound regarding unpainted buildings, leaky roofs, broken heaters, and failing plumbing. These situations are representative of serious maintenance problems in California schools—both in inadequate ongoing funding and in huge deferred maintenance backlogs. There is a growing body of educational research that suggests there is a positive relationship between student achievement and the condition of the facility in which they are schooled.

In this section, we estimate the magnitude of these maintenance problems, describe existing state funding for deferred maintenance, and analyze problems with the state's current approach. We then offer our recommendation for a long-term plan to adequately fund routine facility maintenance and to eliminate current backlogs. First we define the key maintenance terms used in this section.

**Maintenance Definitions.** Many terms are used to describe maintenance needs. A State Department of Education (SDE) publication issued in 1986 defines the terms we use in this report. For our purposes the following two definitions are most useful:

- **Annual Ongoing Maintenance.** Annual ongoing maintenance is defined as maintenance requirements that should be performed
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each year to keep buildings and infrastructure in the proper state of repair. Examples of annual ongoing maintenance include such things as replacing mechanical/electrical equipment, painting exteriors, and replacing roofs, but do *not* include janitorial and groundskeeping activities. Funds to sustain an appropriate level of ongoing maintenance should be included in the annual school district operating budget.

- **Deferred Maintenance.** Deferred maintenance results from not fully meeting the ongoing maintenance need. If ongoing maintenance is not sustained at the appropriate level the result is a backlog of projects. The backlog is referred to as deferred maintenance.

If repairs to key building and infrastructure components are constantly deferred, facilities can eventually require more expensive investments, such as emergency repairs (when systems break down), capital improvements (such as major rehabilitation), or replacement. Generally, deferral of maintenance projects reduces the useful life of facilities and thus increases future capital outlay needs. As a result, while deferring annual maintenance needs can save districts money in the short run, it results in substantial additional costs in the long run.

### Reported Deferred Maintenance Backlogs Are Huge

Inadequate ongoing maintenance has long been a problem for K-12 school districts resulting in huge backlogs of deferred maintenance. In 1979 the SDE estimated that the deferred backlog among K-12 school districts was approximately \$900 million, or \$1.7 billion in *today's* dollars. By 1995-96 the backlog totaled \$2.6 billion, which even after adjusting for inflation, is a 53 percent increase over 1979. The reliability of this \$2.6 billion estimate is questionable. For example, the report includes *no* data from 137 districts, including such large districts as San Jose and San Francisco. In addition, our discussions with districts indicate that there is little consistency in the way districts report the deferred maintenance figure. For several reasons, the actual amount may be seriously over- or under-estimated. There is no alternative source, however, against which to compare the school district reports.

## STATE'S CURRENT APPROACH TO MAINTENANCE AND DEFERRALS

The state has provided funding for deferred maintenance in different ways:

**Deferred Maintenance Program.** The state created a School Deferred Maintenance program with the passage of Chapter 282, Statutes of 1979

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(AB 8, Greene). The AB 8 program focused on working down the deferred maintenance backlog by providing state funds for deferred maintenance that districts had to match with local funds. The initial state match was dollar-for-dollar, with a maximum match of 0.5 percent of the school district's general fund budget. Assembly Bill 8 funded this program from construction loan payments received from school districts in excess of the amount required for debt service payments under the State School Building Aid Program. This basic approach to the problem has not changed since 1979. The budget includes \$35.5 million for the deferred maintenance program in 1997-98.

**One-Time Block Grants.** The state has also provided additional funds for deferred maintenance on an ad hoc basis. For example, last year the Legislature provided \$50 million specifically for deferred maintenance projects from Proposition 98 "settle-up" funds. In addition, the Legislature from time-to-time has provided one-time block grant funds to school districts that also could be used for deferred maintenance (or any other one-time purpose). Last year the Legislature provided \$387 million in such grants directly to school sites and an additional \$200 million to school districts.

**Modernization Program.** The state is also funding deferred maintenance to some extent with debt financing through the Lease-Purchase Modernization Program. Oftentimes, deferred maintenance projects are completed as part of an overall school modernization project. Since 1986, the state has provided almost \$2 billion in general obligation bond funds to upgrade schools that are at least 30 years old. For modernization projects, districts are eligible to receive funds up to 25 percent of the replacement value of a school building and have considerable flexibility in spending these monies to upgrade schools—including addressing deferred maintenance needs such as replacing electrical and mechanical systems. The most recent bond measure (Proposition 203) also allows up to \$40 million of bond proceeds to be used for roof replacement projects.

## PROBLEMS WITH THE STATE'S CURRENT APPROACH

The state's current approach treats the symptom—maintenance deferrals—rather than the cause of the problem: the underfunding of ongoing maintenance. Most importantly, the state's current approach treats deferred maintenance as an ongoing "program." The existence of deferred maintenance, however, really represents a maintenance program *failure*. A deferred maintenance project is one that should have been addressed in a prior year under a properly functioning ongoing maintenance program.

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The primary reason for the failure of K-12 school districts' ongoing maintenance programs is simple—ongoing maintenance has been underfunded. Both the state and the local school districts have contributed to the underfunding. At the local level, many California school districts have given maintenance programs a low priority in the annual budget process. At the state level, the current School Deferred Maintenance Program and state funding for school modernization may actually create a fiscal incentive to defer projects rather than deal with them in a more timely manner. Below, we discuss these problems in detail.

**Local School District Funding: Maintenance Has Been a Low Priority.** School facilities represent a multibillion dollar taxpayer investment entrusted to the management of local governing boards and school managers. Local boards and managers, however, face demands and needs on several fronts for funds. The growing backlog of maintenance deferrals is one clear indication that ongoing maintenance has been given a lower priority in the local district budgeting process.

Two different reports identify the approximate level of ongoing maintenance support that provides sufficient funds to avoid maintenance deferrals. In a 1986 report, the SDE states that ongoing maintenance budgets set at approximately 2.9 percent of the current replacement cost of the buildings should be adequate to avoid deferrals. A report issued by the Building Research Board in 1990 entitled *Committing to the Cost of Ownership* recommends a budget allocation in the range of 2 percent to 4 percent of the current replacement value of those facilities.

Based on these reports and discussions with other experts, we recommend that local school districts budget ongoing maintenance at 3 percent of current replacement value. The SDE does not collect school expenditure data on building maintenance. As a result, we were unable to determine the current level of maintenance spending by districts. Anecdotal information suggests districts spend less than 2 percent of current replacement value on ongoing and deferred maintenance.

**State Fiscal Incentive to Defer Makes Bad Situation Worse.** The state's current method of funding deferred maintenance actually provides an incentive for school districts to defer projects. This is because the state has addressed the maintenance problem by adding state funds for deferred maintenance or providing modernization bonds rather than developing incentives for school districts to increase ongoing maintenance to avoid deferrals. Districts must set financial priorities in the face of many competing needs. If the state supplies funding for deferred maintenance—but none for ongoing maintenance—it is clearly in the district's short-term interest to delay certain maintenance projects and have the state contrib-

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ute to the cost of the project later as part of the state's deferred maintenance program or a modernization project.

The current arrangement is making a bad situation worse. While deferred maintenance was a problem in 1979, the size of the backlog increased by more than 50 percent by 1995-96. This has resulted in steadily deteriorating school buildings—a source of concern to parents and teachers. To the state, the backlog of maintenance projects signals a growing demand for future modernization funds for projects that are unnecessarily expensive because of inadequate ongoing maintenance.

## NEW STATE-LOCAL APPROACH NEEDED

*We recommend that the Legislature adopt a ten-year plan to (1) create an incentive to local school districts to allocate sufficient funds within their operating budgets to support an adequate level of annual ongoing maintenance and (2) provide sufficient funds from state and local district resources to eliminate deferred maintenance backlogs. To accomplish this plan, we recommend a state commitment of \$2 billion in new funds over a ten-year period funded by (1) an annual baseline budget increase of \$100 million and (2) an additional \$1 billion over the next ten years from Proposition 98 settle-up funds.*

The state and the local school districts need to refocus their approach to addressing the maintenance needs of K-12 school districts. We recommend a two-part approach to eliminate the backlog of projects and to fund ongoing maintenance at an adequate level.

- **Address the Backlog.** The first part would consist of \$2 billion in new state funds (over ten years) to help school districts reduce or eliminate their current deferred maintenance backlog.
- **Ensure Adequate Ongoing Maintenance.** The second part is a local commitment to increase ongoing maintenance over three years to a level that ensures that districts are no longer deferring needed maintenance. Districts would be eligible for the \$2 billion in deferred maintenance funds only if this commitment to adequate maintenance is made.

Figure 35 summarizes the components of our proposal. Below we discuss the elements of the plan in more detail.

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**Figure 35****LAO Ten-Year Maintenance Plan****State's Commitment*****\$2 billion in new funds over ten-year period for deferred maintenance:***

- ***Provide \$100 Million Annually in Base Budget.*** Starting in 1997-98, and annually thereafter for ten years, the K-12 budget will include \$100 million in support for deferred maintenance.
- ***Provide \$1 Billion Over Ten-Year Period From Proposition 98 Settle-Up Funds.*** Provide an additional \$1 billion over the next ten years from Proposition 98 settle-up funds.
- ***Distribution of Funds on an Average Daily Attendance (ADA) Basis.*** The entire \$2 billion commitment will be distributed on a per- ADA basis.
- ***State Program Limited to Ten Years.*** No state funds would be available for deferred maintenance after the end of the ten-year period.
- ***Districts Reaching Goal Prior to End of Program.*** If a district eliminates all of its deferred maintenance backlog prior to the end of the program and provides the state's required ongoing maintenance level, it will continue to be eligible to receive state funds.
- ***Current Program Funds Continue But Under New Program.*** Funding from the state's current deferred maintenance program will be allocated on a per ADA basis through the new program. No local match would be required.

**Districts' Commitment**

- ***Increase Ongoing Maintenance Budget.*** Local school districts must increase funding for ongoing maintenance budget by 1999-2000 to at least 3 percent of the current replacement cost of their facilities.
- ***Certification by Local School District Governing Board.*** Each local school district governing board must certify, on an annual basis, that the district is spending the required ongoing maintenance amount as set forth in this plan. The level of districts' maintenance spending would be subject to audit verification.
- ***Current Backlog.*** Districts assume responsibility for funding any deferred backlog beyond the state's commitment of \$2 billion.

**State's Commitment**

***\$2 Billion in New Funds.*** The state would provide \$2 billion in *new* funds over a ten-year period for deferred maintenance from the following sources:

- **Provide \$100 Million Annually in Base Budget.** Starting in 1997-98, and annually thereafter for ten years, the K-12 budget will include \$100 million support for deferred maintenance.
- **Provide \$1 Billion Over Ten-Year Period From Prior-Year Proposition 98 Funds.** Starting in 1997-98, the state will allocate \$100 million from prior-year funds for deferred maintenance. If this \$100 million is not available in one-time funds, the state will increase funding in future years to satisfy the commitment of providing \$1 billion over the ten-year period.

In our K-12 Priorities section (please see above), we include in our alternative budget plan funding needed to carry out the first year of this deferred maintenance plan.

**Distribution of Funds on an Average Daily Attendance (ADA) Basis.** We recommend the distribution of funds on an ADA basis rather than in relationship to current deferred backlogs. School districts have made varying efforts to manage their maintenance workloads. Distributing new monies in relationship to the current backlog would reward districts that may not have been fiscally diligent. We believe a distribution based on ADA is neutral with regard to past efforts of districts.

**State Program Limited to Ten Years.** The magnitude of the backlog problem necessitates an extended period for recovery. However, we recommend that the program be limited to a specific time period to avoid any appearance of accepting deferred maintenance as an ongoing program. In addition, the time limit sends a clear message to schools that any remaining deferred maintenance is their responsibility.

**Districts Reaching Goal Prior to End of Program.** Our rationale for continuing funds to districts that have eliminated their backlogs is the same as that for basing the distribution of funding on an ADA basis. We should not penalize districts that have made the financial effort in the past to adequately maintain their facilities.

**Current Program Funds Merged Into New Program.** Funding from the state's current deferred maintenance program will be allocated on a per ADA basis through the new program and no local matching funds will be required. These monies are *in addition* to the \$2 billion in new state funds. For 1997-98, the Governor's budget includes approximately \$35.5 million that will be available from excess loan repayments made in the current year. The excess bond repayments are declining each year as more districts retire their loans under the State School Building Aid Program. It is our understanding that these payments will phase out within the next ten years.

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## District Commitment

Participation in the ten-year plan requires a local school district to increase funding for ongoing maintenance over a three-year period to 3 percent of the current replacement cost of its facilities. Local school districts also assume responsibility to fund any deferred maintenance that is above the \$2 billion state commitment. The following are the specific requirements we would recommend:

**Phase-In Increase in Ongoing Maintenance.** We recommend the following phase-in to an appropriate sustainable level of ongoing maintenance:

- Starting in 1997-98, local school districts would be required to maintain 1996-97 maintenance spending levels. In addition, districts would have to increase operating budgets for maintenance by the amount of local funds that districts would have spent under the existing State Deferred Maintenance Program (assuming full state funding of the program—about \$150 million statewide). Since many districts currently budget some or all of these funds for deferred maintenance each year, we think this is a reasonable first step to take in 1997-98.
- Starting in 1998-99, districts would be required to increase maintenance budgets to at least 2.5 percent of the current replacement cost of their facilities.
- Starting in 1999-2000, districts would be required to increase maintenance budgets to 3 percent of the replacement value.
- If the 3 percent requirement is not sufficient to sustain an appropriate level of ongoing maintenance (no new deferrals), the district assumes responsibility to provide whatever additional amount is required to reach the point of sustainable ongoing maintenance.

**Certification by Local Governing Boards.** We recommend that local district governing boards certify, on an annual basis, that the district is providing the required ongoing maintenance amount as set forth in this plan. By 1999-2000, the local board must certify that the district is spending at the required 3 percent level. This certification requirement should increase public awareness and discussion of the adequacy of ongoing maintenance levels.

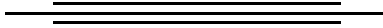
**Current Backlog.** Since the \$2 billion state program will probably not fully eliminate the current backlog, local school districts must assume responsibility for funding any deferred backlog beyond the state's commitment. Some districts may thus have to spend local district funds to fully eliminate their current deferred backlog. In creating this new pro-

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gram, however, it is our goal that local school districts would address their most critical deferrals with the new state funds. Sources for additional funding include the district's operating budget and/or local bond issues.

## CONCLUSION

A long-run strategy to address maintenance failures within local school districts is essential to protect the taxpayers' multibillion dollar investment in school facilities. We believe our proposal provides a combined state-local approach that resolves the maintenance and deferrals issue in an effective and efficient manner. Unless the state and the local school districts act now to (1) increase school districts' ongoing maintenance spending to adequate levels and (2) hold school district governing boards accountable for addressing maintenance needs, maintenance will continue to be deferred. If deferrals are allowed to continue, the state and local school districts will face future additional costs of renovating and replacing prematurely worn out facilities.



## CHILD DEVELOPMENT

The 1997-98 Governor's Budget proposes \$556 million from the General Fund for child development programs. This represents an increase of \$39 million from the current-year level of funding for the program. The change is a result of (1) a \$10 million increase to provide full-year funding for an expansion of child care programs started in 1996-97, (2) a \$13.1 million increase to meet higher costs in child care programs due to increases in the minimum wage, (3) \$13.4 million for a cost-of-living adjustment, and (4) a \$3 million increase to replace one-time federal carryover funds with ongoing General Fund monies.

The budget also proposes \$353 million in federal child care funds, an increase of \$225.7 million from 1996-97. This large increase stems from two major changes in the federal program. First, \$125.5 million in welfare-related child care funds from the Title IV-A program that used to appear in the budget of the Department of Social Services (DSS) now appear in the State Department of Education (SDE) budget. Of this amount, \$75.3 million will be transferred to the DSS. Second, federal funds for child care will increase in 1997-98 by \$100.2 million (\$20 million of this increase are new federal funds received in 1996-97 but budgeted on a one-time basis in the budget year).

An additional \$33.7 million in federal funds also are available in the current year but are not shown in the Governor's budget document. The Governor's budget also provides \$1.5 million in new federal funds for state operations in 1997-98.

In response to these federal changes, the budget combines state and federal funds into one budget item and requires the department to develop new rules that will merge the contracting and management systems for federal and state-funded child care programs. Currently, SDE administers the state and federal funds under separate contracts.

The budget also proposes 22 new positions in the department for child development programs. Currently, about 89 SDE positions are devoted to child care programs. As a result, the budget proposal represents a 25 percent increase from existing levels of staff. Of the proposed new

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positions, 13 would be funded with federal funds and nine from the General Fund.

## THE SUBSIDIZED CHILD CARE SYSTEM

The SDE-subsidized child care system consists of about a dozen programs serving low-income families at little or no cost, which fall into four categories: (1) State Pre-School, which provides half-day educational programs with a school-readiness focus; (2) center-based programs, which provide a full-day program similar to State Pre-School in state-contracted child care centers; (3) Alternative Payment programs, which provide voucher-based child care; and (4) resource and referral programs, which provide information and referral services to all child care consumers.

The DSS provides child care through (1) several voucher-based programs and (2) the AFDC Income Disregard Program. These programs provide child care to welfare recipients and those transitioning off of welfare who continue to need subsidized child care. In addition, the federal Head Start program, which provides \$395 million in preschool services in California, is funded and managed directly by the federal government without state involvement.

### Welfare Reform Adds New Federal Funds And New Rules

Before the enactment of welfare reform, California received federal child care funds in two funding streams. First, the SDE received about \$110 million in federal child care funds in the Child Care and Development Block Grant (CCDBG). Of these funds, 75 percent supported voucher-based child care, and 25 percent could be spent for a variety of purposes, including state administration, center-based care, and quality improvement activities. Second, DSS received child care funds through the federal child care entitlement to welfare recipients (Title IV-A).

Welfare reform has changed this funding system in the following ways.

**Three Funding Streams.** There are now *three* different streams of federal funds: (1) the former CCDBG funds are now known as “discretionary” funds, (2) the former Title IV-A funds are now known as “mandatory” funds, and (3) there is now a new source of funds known as “matching” funds. Together, these funds are now known as the Child Care and Development Fund (CCDF), which is capped at a certain amount each year.

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**More Restrictive Expenditure Time Limits.** The CCDBG and Title IV-A child care rules provided states significant flexibility over when federal funds had to be spent. Under the new system, each of the three funding streams has different spending time limits and all are *more restrictive* than the previous system. The more restrictive expenditure time limits will require increased vigilance by the department to ensure that the state does not lose federal funds by missing expenditure deadlines.

**Increased Funding for Quality Improvement Activities.** Four percent of CCDF funds must be spent on quality improvement, which includes training for parents in selecting appropriate child care and training for providers in delivering higher quality child care. The state currently spends about \$9 million on these activities. An additional \$12 million must be spent in the budget year to meet CCDF expenditure requirements.

**Expanded Reporting Requirements.** Before welfare reform, the department was required to file summary reports on child care costs and number of children served with federal funds. The new law expands the kinds of data that must be collected. Instead of summary reports, the state must collect data on a child-by-child basis. Although no regulations have been issued, the federal Department of Health and Human Services has stated its intent to require data collection for only a sample of children served, rather than for all children served. This will substantially reduce the effort necessary for information collection when compared with what SDE envisioned when welfare reform was first enacted.

## PROBLEMS WITH THE CURRENT SYSTEM

For the last several years, SDE—along with other legislative and administrative staff—have been discussing ways to improve the state's child care system. California's subsidized child care programs have been beset by a number of ongoing problems. Major issues include the following:

**The Subsidized Child Care Delivery System Is Unnecessarily Complex.** California has about 18 different child care programs. These programs can have different funding sources, eligibility criteria, points of entry, and separate waiting lists. The uncoordinated manner in which the programs have been designed and administered impedes families' access into the system.

**Child Care Providers Cannot Easily Absorb Large Funding Increases.** The subsidized child care market has difficulty expanding to absorb increases in funds. For example, in 1991 the state began receiving federal funds from the CCDBG. During the first two years of the grant, the SDE

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accumulated \$85 million in CCDBG funds that it was unable to spend. Based on legislative action, the SDE developed a plan to spend down these “carryover funds” over a three-year period. Three years have passed since that plan was originally implemented and over \$40 million in federal carryover still remains to be spent. Spending new federal funds in a timely manner will become even more critical as a result of the new funding rules under welfare reform.

**Administration of Child Care Contracts Is Complex and Expensive.** The complexity of SDE’s child care program rules creates problems for both state administrators and child care providers. This complexity permeates every aspect of the child care system. For example, different programs have different eligibility rules and different rate structures. Providers that operate under more than one program also have to negotiate separate contracts for each program. Providers must follow complex rules regarding allowable expenditures and attendance accounting, and collect detailed administrative information on these factors. This information is audited and then reviewed by state administrators. Most of the 89 child care-related positions in SDE are devoted to assisting contractors and implementing the cumbersome rules and requirements.

**Programs Lack Basic Data.** While contractors must file a great deal of paperwork to show they have met detailed administrative requirements, all of this effort provides little useful data for making policy decisions. For example, the state does not collect even the most basic data on key program variables, including number of children served, statewide need for services, and quality or outcomes of child care programs. Thus, the level of state funding for child care programs has never been tied to any hard data on what the state is receiving for its child care expenditures.

While these problems remain, SDE made progress this year in providing information for the budget process. In our past three budget analyses, we discussed SDE’s ongoing difficulties in managing and accounting for expenditures. This year, SDE staff have been very responsive and generally have been able to provide accurate and timely budget information.

### **Department Has Not Acted to Simplify Contracting And Reporting**

To resolve some of the problems detailed above, the *Supplemental Report of the 1995-96 Budget Act* required the SDE to consult with the Legislative Analyst’s Office (LAO) and the Department of Finance (DOF) and develop recommendations for simplifying the contracting system for child development programs. The department released its report and recommendations in February 1996.

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In response to this report, the Legislature included a requirement in an education trailer bill to the *1996-97 Budget Act* directing the department to design and implement a streamlined contracting system to test on a small number of child care providers. The plan for this pilot project was due in January 1997. Implementation of the plan was to have occurred in July 1997, subject to approval by the DOF and the Legislature.

The department decided to delay for one year the development of the required plan and has formally notified the LAO and the DOF of this decision. In its letter to the two agencies, the SDE stated, “postponing implementation of a prototype contracting system for one year will allow details of federal welfare reform to be fully understood. In addition, the one-year delay would provide all state agencies the opportunity to better prepare for California’s version of the Temporary Assistance for Needy Families program [welfare reform].”

**Most Streamlining Issues Are Independent of Welfare Reform.** The department contends that restructuring of child care administration should wait until after welfare reform is implemented. But the problems that plague the system are independent of welfare reform:

- **Most Child Care Dollars Are General Fund Dollars.** The state spends about \$500 million on center-based programs, almost all out of the General Fund. These programs’ complex rules, high administrative overhead, and lack of useful data for policy formulation *are almost solely the state’s own doing.*
- **Welfare Reform Changes the Rules, but Underlying Problems Remain the Same.** We already have a system supported by both state and federal funding, with different rules for different programs. On an administrative level, welfare reform simply creates a new set of rules. These changes will create short-term challenges for state administrators as they come up to speed on the new rules, but are unlikely to have major program impacts.

In short, the program structure and administrative requirements of the system are largely under state control—and federal welfare reform will not require major changes in the system. Changing federal rules, however, provides an excellent opportunity to rethink many aspects of the existing system—a system that is in serious need of restructuring. Such a restructuring can make the state system less complex, less expensive, and easier for families to access. In the long-run, these changes also can help the state ensure that a sufficient supply of affordable child care is available to low-income families in the state.

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## BUDGET COULD EXACERBATE PROBLEMS

The Governor's budget attempts to address several of the issues posed by the current state system and the changing federal program. However, we believe the budget proposal could exacerbate the problems that plague the existing system.

***Combining Funds Could Pose Problems in the Short-Run.*** The budget proposes to combine all state and federal funds for child care. This would require many child care programs to meet *both* state and federal rules at the same time. This would have the effect of making program administration more complex.

In the long-run, the budget proposal to combine state and federal rules makes sense. Merging state and federal funds as part of a single streamlined child care system would be a significant improvement for families, child care providers, and SDE. The department, however, is not prepared for such a thorough overhaul of the program at the current time.

***Child Care Providers Cannot Absorb Huge Increases in Funding.*** The budget assumes the state-subsidized child care system can supply an extra \$71 million in child care services in the budget year. This flies in the face of past experience with federal child care funds, as discussed above.

***Data Collection Should Be Driven by Need for Policy-Relevant Data.*** The budget provides funds and positions for data collection geared to meet expected federal reporting requirements. Even if the state satisfied federal requirements, however, the data may not address the basic information the Legislature needs to make informed decisions about SDE's program.

***Welfare Reform Should Not Drive Staff Increases.*** The budget assumes the department will need a major, permanent increase in staff to adequately meet both existing workload requirements and new workload requirements generated by welfare reform. While some short-term staff may be needed, most of the department's staffing problems result from existing program requirements.

## LAO RECOMMENDATIONS FOR A SIMPLIFIED APPROACH

The budget proposal could make a complex program even more complicated. There is, however, a way to budget new federal funds that works to simplify the system. Below, we make a series of recommendations to begin reform of the state's child care delivery system. The following principles guide our recommendations:

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- ***Simplify Child Care Administration and Contracting.*** Instead of combining all state and federal funds, we think the Legislature should, to the extent possible, *separate* programs so that they are funded by one source—either federal or state funds—rather than by both. In the short run, this reduces administrative complexity in the system by allowing individual programs to operate on one set of rules. The Legislature also should take steps to require the department specifically to develop and implement plans for further simplifying the cumbersome child care administration and contracting system. This will serve the state's long-run goals for child care far more effectively than simply providing new staff for a system that is not working.
- ***Limit Funding Increases to What Providers Can Reasonably Absorb.*** As discussed above, child care providers have not been able to quickly absorb huge increases in funding. Rather than create a large carryover problem or risk losing federal funds, we recommend the Legislature limit funding increases to what the program can reasonably spend in 1997-98. Funding can be augmented in the future as the supply of child care increases.
- ***Data Collection Should Serve Policy Improvement, Not Administrative Requirements.*** The state needs data to formulate future state child care policies. The Legislature should provide funds to enable the department to develop a data collection and reporting system. Of course, the state needs to comply with federal reporting requirements, but policy improvement should be the main goal of data collection.

Below we detail specific recommendations to implement these principles.

### **SDE Should Consolidate Funding for Most Programs**

***We recommend the Legislature fund (1) the School-Age Parenting and Infant Development (SAPID) and Migrant Child Care programs solely out of the General Fund and (2) the Extended Day Care (Latchkey) programs and alternative payment programs solely out of federal funds. These changes will reduce complexity in the contracting system by funding each of these programs from a single source.***

The Legislature should make the following budget changes in both the current and budget years (these are accounting changes only, and will not affect funding for these programs):

- ***Migrant Program.*** Replace \$2.3 million in federal funds with General Fund monies.
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- **SAPID Program.** Replace \$991,000 in federal funds with General Fund monies.
- **Latchkey Program.** Replace \$18.4 million in General Fund monies with federal funds.
- **AP Program.** Fund the AP program entirely with federal funds (\$48 million). This requires using \$19.2 million of General Fund savings from this switch to maintain funding for the “general” child care program.

These four programs would then be funded from a single funding source, easing program administration. As a result of these actions, only one program—general child care—would still be funded from both federal and state funds. Consistent with this action, we also recommend the Legislature separately schedule federal and General Fund child care monies to provide greater control over expenditures.

### Trim Child Care Program Expansion

***We recommend the Legislature replace \$43.9 million in General Fund child care programs in 1996-97 and 1997-98 with new, ongoing federal Child Care and Development Fund monies. This action will increase the level of child care expenditures by an amount that programs can reasonably absorb (\$26.2 million).***

The budget proposes \$100.2 million in local assistance from new federal child care funds in 1997-98. In addition, \$33.7 million in current-year federal funds are available for expenditure but not shown in the Governor’s budget document. Whenever child care funds increase, the SDE must find (1) *existing* center-based providers who can increase the number of available slots at their facilities or create new facilities, (2) *new* center-based providers, and/or (3) alternative payment contractors who can expand their programs.

***Child Care Programs Have Not Been Able to Quickly Absorb Large Increases in Funds.*** As discussed above, the child care market needs a few years to absorb large increases in funding. The Legislature has several options regarding these large increases in federal funds. First, all the funds *could* be budgeted to expand SDE child care programs. The likely outcome, however, would be substantial General Fund or federal fund carryover. We think this is the least desirable course of action because the department would be unable to use most of the additional funds. Second, the Legislature could send available federal funds to DSS for use in support of welfare reform. The need for additional funding in 1997-98 is uncertain, however, and depends on the design of the state’s new welfare program and the speed at which counties can implement the program.

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Third, the Legislature could replace General Fund support for state child care programs with federal funds. This would free up Proposition 98 funds for other legislative K-12 priorities.

**Analyst's Recommendation.** We recommend the Legislature choose a combination of these options. Specifically, we recommend (1) a \$26.2 million increase for the Alternative Payment and Latchkey programs, and (2) a \$43.9 million reduction in General Fund support for SDE programs in both the current and budget years. This reduction in General Fund support would not affect the level of services provided, which would be supported with federal funds instead (see previous recommendation). We think this would provide SDE with an amount that can reasonably be absorbed in 1997-98 and create the greatest fiscal flexibility for the Legislature in addressing the K-12 budget priorities.

The federal fund base will increase over the next four years by a total of \$82 million over the budget-year level. Thus, the Legislature will have new sources of funds to meet increasing demand for child care in the future. If the Legislature's actions on welfare reform indicate a greater budget-year need for child care funds, any portion of the federal funds used to free-up Proposition 98 funds could, instead, be transferred to DSS.

### Create Capacity For Data Collection

**We recommend the Legislature reject the Governor's proposal to spend \$22 million in federal Child Care and Development Fund (CCDF) matching funds on a one-time basis for development of a new data collection and reporting system to meet federal reporting requirements. Instead, we recommend the Legislature provide \$4.2 million for the department to develop a data collection system that meets (1) the state's need for policy-relevant data and (2) federal reporting requirements.**

The Governor's budget provides \$22 million to support the data collection and analysis costs of meeting potential new federal reporting requirements. Of these funds, \$2 million is for consulting services to develop a Feasibility Study Report (FSR) for a data collection and analysis system, and \$20 million is reserved for implementation of the FSR once it is approved. All \$22 million would come from the current-year increase in federal funds. The budget also includes three positions in the department for data analysis staff.

**\$22 Million Is Excessive.** This large sum was reserved because, at the time the budget was put together, it appeared that the federal government might require the state to collect data on every child receiving subsidized care. Without knowing what might be involved in such a

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massive data collection effort, the DOF reserved these funds as a contingency. The federal government has now stated its intention to require data collection for only a sample of children (likely to be a few hundred) on a monthly basis. This modest requirement may not require the development of *any* new data collection system, as the DSS was required to collect data on small samples of children as part of the former Title IV-A child care programs.

***State Needs Data to Drive Effective Policy.*** As we discussed above, the state has little systematic data on key aspects of the state-subsidized child care system. Up to this point, the state has continued to increase funds for child care programs with little or no information on what the state is getting for its money. Welfare reform creates an opportunity for the Legislature to create a data system that would allow the Legislature to make informed decisions about SDE's programs.

For these reasons, we recommend the Legislature reject the \$22 million proposed in the budget for a data system. Instead, we recommend the Legislature provide \$4 million for development and implementation of a data collection system and \$229,000 for three two-year, limited-term positions devoted to data collection and analysis. All expenditures would be from federal CCDF funds. We recommend that the Legislature adopt the following budget bill language relating to these funds:

Of the amount provided in this item, \$4,000,000 is for developing and implementing a feasibility study report (FSR) for a child care data collection system. The department shall consult with the Legislative Analyst's Office and the Department of Finance in determining data collection needs and developing the data collection system. Of the amount provided in this item, \$229,000 is for three positions for data collection and analysis. These positions may only supplement and not supplant three existing positions devoted to data analysis. These positions and associated funding are provided on a two-year, limited-term basis. Continuation of the positions is contingent on implementation of a data collection system that meets the state's policy-related child care data needs.

### **Provide New Positions to Reform State Administration, Not Expand Current System**

***We recommend the Legislature (1) delete 19 positions and \$2.1 million (\$781,000 from the General Fund and \$1.31 million in federal funds) from the Governor's budget. Instead, the Legislature should provide \$970,000 in federal funds for seven two-year, limited-term positions.***

The Governor's budget proposes a total of 22 new positions in the department for child care programs. This represents a 25 percent increase in the 89 positions in the department already devoted to child care. We

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addressed three of the new positions above. The Governor's proposal targets the remaining 19 new positions in the following fashion.

- **Child Development Division (CDD)—Eleven Positions.** Of these positions, six would be devoted to existing contractor monitoring and assistance functions, and five are proposed to meet expected new workload due to welfare reform.
- **Education Finance Division (EFD)—Five Positions.** Of these positions, two would be devoted to existing child care apportionment workloads, and three would be devoted to expected workload increases due to welfare reform.
- **Auditing and Accounting—Three Positions.** Of these positions, one would be devoted to closing out the existing workload of annual audits of child care contractors, one would be devoted to expected new audit workloads due to welfare reform, and one would be devoted to expected new accounting and budgeting workloads due to welfare reform.

**Proposal Overstates Need for Staff.** As detailed above, the state administration system is already overly complex and cumbersome. Yet the budget proposal for the new federal funds justifies increasing the department's child development staff based on expected *increases* in the complexity of the child care system. Rather than require the department to fix the cumbersome state administration system, the budget funds its expansion.

Our review indicates that the proposed new positions are more than can be justified by either existing workload increases or the new workload created by the new federal funds.

- **Review of Contractor Business Plans Unjustified.** The budget requests two staff in the EFD largely on the basis of reviewing business plans from child care contractors. There is currently no requirement for child care contractors to provide business plans to the state. We do not believe such a requirement is appropriate, as it would *increase* both state and local administrative costs and add little in improved accountability.
  - **Staffing Overstates Federal Workload Increase.** The budget proposal justifies many new positions on the basis of the large increase in federal funds (\$195 million) and associated workload increases. In fact, federal fund expenditures by SDE will increase by only about \$78 million in the budget year. The remaining funds will simply be passed through to DSS or spent by SDE on existing child care programs.
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- **Quality Improvement Funds Will Not Increase Workload to Degree Claimed.** The budget cites the large increase in federal quality improvement expenditures (\$12 million) as justification for providing new staff to manage improvement contracts. But the actual increase in quality expenditures will be only about \$6 million in federal funds. This is because federal rules require the state to match this \$6 million in federal funds with General Fund expenditures. The budget proposes that *existing* state programs will provide this match, resulting in a net increase of only \$6 million in quality expenditures.

**Provide Modest Staff Increases.** From our review, we conclude that many of the new positions requested by the department are not needed. Furthermore, our recommendations to redirect most new federal funds to existing activities will further reduce the need for new staff. But the most important reason for limiting the number of new positions is that the department needs to develop and implement plans that will *simplify* the cumbersome contracting system and reduce the long-term administrative overhead of the program, both at the state and the local level. Therefore, we recommend the Legislature provide seven two-year, limited-term positions for the following purposes:

- **Short-Term Workload Relief.** We recommend three positions in the Child Development Division (CDD), one position in the Education Finance Division (EFD), and one position in the Office of External Audits, at a cost of \$432,000 in federal funds.
- **Reform Child Care Administration.** We recommend one position in CDD and one position in EFD at a cost of \$197,000, for reform of the system. We further recommend the adoption of following budget bill language:

Two positions and \$197,000 are provided for the purpose of developing and implementing recommendations to reform the child care administration and contracting system to reduce costs and increase accountability. These positions shall have the responsibility to (1) identify current administrative requirements of child care programs that create local and state costs without contributing significantly to accountability for quantity and quality of service delivered by child care providers; (2) identify new administrative procedures that will decrease costs of administration and increase accountability for quantity and quality of service in child care programs; and (3) develop an implementation plan for reforming administration of child care programs to (a) reduce both state and local administrative costs, and (b) reduce the complexity of rules that providers must understand and adhere to. These positions shall not include regular program administration duties normally carried out by the Child Development Division and the Education Finance Division.

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### **Budget Excludes Legislature from Key Decisions and Oversight**

***We recommend the Legislature amend several provisions in the budget bill to include appropriate legislative oversight of key changes that will be made to the state-subsidized child care system over the next year.***

In the course of the Legislature's deliberations on the budget, important issues often cannot be resolved without further information and analysis. Sometimes, resolution of an issue is not feasible until well into the budget year. In these instances, the Legislature often will adopt language requiring later legislative input into the decision process.

The *1997-98 Budget Bill* contains two instances where the budget requires budget-year resolution of and action on important decisions affecting state child care programs, yet excludes the Legislature from any oversight role:

- ***Approval of a Plan for Development and Implementation of a New Data Collection and Retrieval System (Provision 10).*** The budget bill requires only that the DOF transfer the funds after approval of a feasibility study report.
- ***Overall Reform of the State-Subsidized Child Care System (Provision 14).*** The budget bill excludes the Legislature from the development of a reform plan, and allows administrative approval and implementation of the plan without legislative review.

Normally, the Legislature should have the details of these proposals as it considers the budget. Given the complexity of the tasks, however, we think giving the department more time to complete these tasks is reasonable. Legislative oversight of these decisions, however, also is necessary. Therefore, we recommend the Legislature amend the budget bill to add notification of the Legislature 30 days before final approval of these decisions. We further recommend the Legislature add the LAO and the appropriate fiscal and policy committee representatives to the list of agencies who will provide input into the plan for reforming the child care system.

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## SPECIAL EDUCATION

***In November 1995, the State Department of Education, the Department of Finance, and the Legislative Analyst's Office released a joint report proposing a new funding model for special education and related program reforms. The Governor's budget includes a set-aside of \$76.7 million for these reforms. We recommend the Legislature enact funding-reform legislation in 1997-98.***

The Governor's budget includes \$2 billion in General Fund support for special education in 1997-98. This is \$175.7 million, or 9.4 percent, above the revised current-year amount. The budget reflects the following General Fund increases:

- \$74.5 million to pay for growth in the number of special education students. In general, growth for most special education programs is based on the percentage change in K-12 average daily attendance (ADA), which is projected to increase by 2.3 percent in 1997-98.
- \$76.4 million for a cost-of-living adjustment (COLA) for special education programs, an increase of 2.5 percent. This is the same increase as proposed for K-12 revenue limits.
- \$76.7 million for a set-aside for reform legislation. We discuss this proposal in detail below.

Offsetting these proposed increases is a net reduction of \$51.9 million. This net reduction results from an "entitlement increase" of \$60.7 million offset by revenue increases of \$112.6 million. (We discuss the entitlement issue below.) The largest revenue change is an increase in federal funds for special education of \$77 million.

In summary, the Governor's budget proposal for special education provides statutory growth and COLA plus an additional \$76.7 million for funding reform. The amount set aside for funding reform is about equal to the 1997-98 increase in federal funding.

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## **Background, Enrollment, and Overall Funding**

Federal law defines the disabilities that qualify a child for special education and mandates school responsibilities and parental rights. Federal law sets out three basic principles that apply to children with disabilities: (1) all children with disabilities must be provided a free, appropriate public education; (2) each child's education must be determined on an individualized basis and designed to meet his or her unique needs in the least restrictive environment; and (3) the rights of children and their families must be ensured and protected through procedural safeguards.

Consistent with these federal requirements, California's Master Plan for Special Education (MPSE) requires schools to assess each child's unique educational needs and consider a range of service delivery options for each eligible child. The MPSE, implemented statewide in 1980 with the enactment of Chapter 797, Statutes of 1980 (SB 1870, Rodda), established an area-wide approach to the delivery of special education services. The current areas are called Special Education Local Plan Areas (SELPA's).

The intent of the SELPA structure is to deliver special education services in an efficient and cost-effective manner. Differing population densities around the state have resulted in SELPA's that consist of either multiple counties, single counties, a group of school districts within a county, or single school districts. In 1995-96, there were 116 SELPA's. Of these, three were multicounty SELPA's; 33 were countywide SELPA's; 48 were multidistrict SELPA's; and 32 were single district SELPA's.

In 1995-96, approximately 594,000 pupils ages 22 and under, were enrolled in special education programs throughout the state. This is approximately 11 percent of the estimated total K-12 school enrollment for that year. The increase in special education enrollment between 1994-95 and 1995-96 was 3.8 percent. By comparison, the increase in K-12 enrollment was 2.4 percent.

The proposed 1997-98 General Fund appropriation of \$2 billion does not reflect the total amount that would be spent on special education programs in the budget year. First, the Governor's budget proposal also includes \$48.4 million for the state's special School for the Blind at Fremont and Schools for the Deaf at Fremont and Riverside. Second, in addition to state special education funds, federal funds and district revenue limit funds are also spent on special education programs by local districts. In 1994-95, districts and counties reported spending \$3.4 billion on special education programs from all fund sources (excluding transportation costs). Based on a 1992-93 study, we estimate the state share of this

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amount to be approximately 70 percent, the federal share 5 percent, and the local share 25 percent.

### **Need for Funding Reform Well Documented, Timing Right for Reform**

In November 1995, the State Department of Education, the Department of Finance, and the Legislative Analyst's Office released a joint report proposing a new funding model for special education and related program reforms. The joint report documented the major problems with the state's current special education funding formula: (1) unjustified funding variations among local education agencies (LEAs), (2) unnecessary complexity, (3) constraints on local innovation and local response to changing requirements, and (4) inappropriate fiscal incentives. The report made specific recommendations for reform.

**Update on Outcome of Three-Agency Report.** During the 1996-97 legislative session SB 1678 (Greene) was introduced. This legislation incorporated many of the recommendations made in the three-agency report. The bill, however, was not heard by any committee. A major issue of concern was the report's assumption that the population of disabled children is evenly distributed among school districts. Key to this assumption was the lack of research evidence showing a link between poverty and the incidence of special education pupils. The report relied on a literature review made by the U.S. Office of Education.

In October 1996, a year after the three-agency report came out, the U.S. Department of Education advised that there may in fact be such a link. As a result, the Legislature should consider these findings if a link can be demonstrated.

**1997-98 Is a Good Year for Reform.** We remain convinced that reform of the Special Education funding model is sorely needed. Several factors point to the 1997-98 legislative session as a desirable year to enact major reforms in special education finance:

- **Special Education Statutes Sunset on June 30, 1998.** The sunset process is designed to allow the Legislature to periodically review the design and operation of K-12 programs. With the sunset date on the horizon, the Legislature will have to take action within the next 18 months to extend the program. We recommend that the Legislature view the extension of the program as an opportunity to incorporate reforms of the type recommended in the three-agency report.

- **Significant Funding Is Available for Reform in 1997-98.** The Governor's budget proposes \$76.7 million for reform. These funds are available as a result of an increase in federal funds to the state for special education. The primary cost of reform is in equalizing per-student funding levels, which various sources estimate will cost up to \$200 million over the long-term.
- **Riverside Mandate Case Coming to a Close.** The Commission on State Mandates (COSM) is now hearing a claim submitted by the Riverside County Superintendent of Schools to determine whether new special education costs were imposed upon school districts by federal mandate (PL 94-142) or by state choice (the MPSE) in the implementation of the federal mandate. The test claim includes 19 specific areas. A final decision by the COSM should be made early in 1997. The Legislature should review the outcome of this mandate claim as part of its discussions on reform legislation.

The three-agency report continues to generate considerable discussion on funding reforms among special and general education groups, administrators, and parents. These discussions are entering their third year. The combination of all of these factors point to the 1997-98 legislative session as a good opportunity for the Legislature to consider and enact major funding reform legislation.

### Funding for Reform Should Be Carried in Separate Legislation

***We recommend that the Legislature provide funding for special education reform in the reform legislation itself rather than in the budget bill. Accordingly, we recommend that the Legislature delete the set-aside item for special education reform from the budget bill. We further recommend that the set-aside amount for special education reform legislation be increased from \$76.7 million to \$105 million. (Delete Item 6110-162-0001).***

The Governor's budget proposes \$76.7 million for special education reform in an item in the budget bill (Item 6110-162-0001). However, budget bill language specifies that if reform legislation is not enacted by October 15, 1997 the set-aside will be used for additional growth funding for special education.

We think the budget bill item should be deleted for several reasons. First, the item's language creates a disincentive for some districts to support reform simply because they would get more funding through growth. Second, we believe that any alternative use of the set-aside amount should be decided by legislative action rather than inaction. The decision to fund additional growth should be made on its own merits rather than on lack of consensus on reform. Finally, the budget proposal

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already includes full statutory growth funding of \$74.5 million. We do not think additional growth dollars are needed. Accordingly, we recommend that Item 6110-162-0001 be deleted.

In our K-12 Priorities section (please see above), we recommend that the Legislature increase the set-aside amount from \$76.7 million to \$105 million. If no reform legislation is enacted in 1997-98, this amount would be available for appropriation in the 1998-99 year for any purpose the Legislature chooses. We recommend that if no reform is enacted in 1997-98, the set-aside amount be reserved for special education reform in 1998-99.

#### Technical Issue—Is Entitlement Amount Correct?

***The Governor's budget proposal includes \$60.7 million for entitlement adjustments. Based on our preliminary discussions with the Departments of Finance (DOF) and Education (SDE), we find that this adjustment is not in accord with our understanding of legislative intent. We are continuing our discussions with DOF and SDE to get a clearer understanding of the adjustment, and will report further on this issue during budget hearings.***

The education trailer bill to the 1996-97 Budget Act contains a cap on special education spending equal to the amount contained in the budget. This cap limits overall state spending for special education services. In developing the 1997-98 budget proposal, the starting point is adjustments to the 1996-97 "base." Once that is done, increases for growth and COLA are applied. There are two appropriate types of base adjustments:

- First, funding for growth may need to be adjusted based on a revised estimate of overall growth in K-12 students for the base year. As noted above, the legislative appropriation for special education growth funding is based on the percentage change in K-12 ADA. If ADA is revised, revising special education growth funding to reflect this change would be consistent with the Legislature's action on the special education budget.
- Second, several sources of revenue are used to offset the need for state General Fund support, including federal funds and local property taxes. If actual revenue is different than the budget estimate for 1996-97, an adjustment would likewise be regarded as within the Legislature's intent.

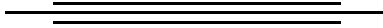
The proposed \$60.7 million entitlement adjustment, however, is not based on these ADA and revenue adjustments. Our preliminary review finds that it is based on a number of different factors, including changes in the way LEAs claim their special education reimbursement from the

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state. The changes do not affect the 1996-97 General Fund appropriation.

However, it appears the budget includes these changes in the base budget for 1997-98 as an “entitlement” adjustment. If this is the case, we do not believe it is consistent with the Legislature’s actions on the special education budget. By making this adjustment, the DOF is recognizing cost increases that were never authorized by the Legislature. If these adjustments permit districts to manipulate the claiming system to obtain higher funding, then including them in the base would be defeating the purpose of the funding cap. Thus, the budget proposal may be too high by \$60.7 million.

As mentioned earlier, one of the major problems with the current funding mechanism is its unnecessary complexity. This prior-year entitlement adjustment is a good example of the system’s complexity. We will report further to the budget subcommittees on this issue during budget hearings.



## OTHER ISSUES

### School Safety Initiatives Over-Budgeted

***We recommend the Legislature reduce by \$35 million in 1996-97 and \$22.6 million in 1997-98 General Fund support for community day school programs to reflect realistic population projections for the program.***

The Governor's budget proposes \$52.6 million for the community day school program, which was established by the Legislature in 1995—Chapter 974, Statutes of 1995 (AB 922, Friedman). This funding level, which is the same as for 1996-97, is sufficient to serve approximately 25,000 ADA.

The community day program was established as a district alternative to county community programs for students who (1) would benefit from an alternative educational setting and (2) were expelled from school or were referred by the county probation department. Districts also have discretion to direct other high-risk pupils to these community day programs.

Under the community day school program, schools are eligible for additional funding for each student placed in an alternative program. Specifically, districts receive \$750 per student if the student attends school for five hours each day and \$1500 per student for those attending a six-hour daily program. District claims are capped at a maximum of 0.5 percent of total district ADA.

### Community Day Schools Still Over-Budgeted

In our *Analysis of the 1996-97 Budget Bill*, we found that the community day program was over-budgeted for two main reasons. First, delays in start-up would prevent those districts that wanted to set up programs from reaching their maximum ADA cap in the first year of the program's existence, 1996-97. Second, not all districts would want to start community day schools in the first year or two of the program.

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District implementation of the program appears to validate these concerns. For example:

- **Less than 10 Percent of Districts Expect to Start a Program in 1996-97.** Based on letters of intent submitted to the State Department of Education (SDE), only 80 districts (about 8 percent) indicated they planned to set up community day schools in 1996-97. The maximum these districts could serve under their community day school cap is 7,000 ADA. This would result in program costs of \$10.5 million—far below the \$52.6 million included in the *1996-97 Budget Act*.
- **Most Districts Don't Plan to Reach Program Caps in the First Few Years.** Program spending could be much lower than \$10.5 million in the current year, because many districts that plan to implement the program do not plan to fully implement the program in 1996-97.
- **District Plans for 1997-98 Suggest That the Budget Proposal Is Too High.** Only eight districts have advised SDE that they plan to set up community day schools in 1997-98. We also surveyed five large districts that did not begin a program in 1996-97 and found that only two planned to begin day schools in the budget year. Similar to the schools that implemented in 1996-97, districts that were planning to begin schools in 1997-98 did not expect to reach the district caps during the first year of operation.

**Reduce Community School Funding.** District implementation of the community day school program has gone slowly. Budget-year district plans also suggest continued slow implementation. As a result, it seems apparent that the \$52.6 million included in the *1996-97 Budget Act* and 1997-98 proposed budget greatly overstate the program's need for resources. Funds not needed in this program could be redirected to support legislative priorities in other areas.

Therefore, we recommend the Legislature appropriate \$30 million for the program in the budget year, for a savings of \$22.6 million. We further recommend the Legislature reduce expected program expenditures in the current year by \$35 million, leaving \$17.6 million to satisfy district claims in 1996-97. In making these recommendations, we have tried to ensure funding is more than sufficient to meet program claims. Districts will submit preliminary 1996-97 claims this spring. We will update the fiscal committees of any changes in our estimates based on this data.

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### Program Should Charge for Computers

***We recommend the Legislature reduce funding for the California Donated Computer program by \$2.9 million and add budget bill language requiring the program to charge schools for refurbished computers.***

The budget proposes \$10 million in Goals 2000 funds to continue the State Department of Education's California Donated Computer (CDC) program. This program is operating in the current year with \$10 million in Proposition 98 funds that were provided as part of the settlement of the *CTA v. Gould* lawsuit. The funds proposed in the budget would allow the program to continue in 1997-98.

The program refurbishes used computers donated by the private sector and redistributes them to schools around the state. Under the current program, schools are eligible for computers by matching the CDC computer with a similar computer donated by a parent or community member. The program typically spends between \$200 and \$400 to refurbish the computers.

The program seems to be working as planned except for one factor. Schools that cannot obtain a locally donated computer have no access to the CDC computers, even if the school is willing to pay the full cost of refurbishing the equipment. The CDC computers generally are relatively recent vintage and, at \$400 per computer, represent a good value to schools.

Requiring that the program charge for the costs of refurbishing would have a couple of advantages. First, it would allow schools that cannot obtain locally donated computers to participate in the program. Second, it would ensure that schools have weighed the costs of additional computers and the impact of such a purchase on student achievement.

We also see the value of encouraging schools to engage parents and local businesses in helping support local computer needs. Because of these competing interests, we recommend the Legislature require all schools to pay a portion of the refurbishing costs of CDC computers. For schools that were able to obtain locally donated computers, the charge would be half the cost of the refurbishing. For schools without a local match, the charge would be the total costs of refurbishing.

This change would reduce the state funding needs of the program. Consequently, we recommend a \$2.9 million reduction in the CDC program. We also recommend adoption of the following budget bill language that would require the program to charge schools for all or part of the cost of refurbishing.

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The California Donated Computer program shall require schools receiving computers through the program to pay for all or part of the cost of refurbishing the computers. Schools that obtain matching donated computers from local sources shall pay half of the refurbishing cost. Schools that cannot obtain local matching computers shall pay the full cost of refurbishing.

### **Deny New Categorical Programs**

***We recommend the Legislature deny two new categorical programs for a savings of \$7.1 million in federal Goals 2000 funds.***

As we discussed in our K-12 Priorities section, the Legislature should closely examine the rationale for categorical programs and should only approve programs that can be justified based on certain criteria. In our review of the proposed use of federal Goals 2000 funds, we identified two programs that did not meet our criteria. We discuss these proposals below.

***Student Academic Partnership Program (\$5 Million).*** This program would pay college students to tutor elementary school students. This type of program already exists in many areas—either on a paid or unpaid basis. Some students receive college credit for tutoring. We see no need for the state to intervene. Funding for tutoring should be determined by local school boards after an assessment of existing tutoring resources and the impact of tutoring on student achievement. For this reason, we recommend the Legislature deny this request.

***Family/School Partnerships Program (\$2.1 Million).*** This proposal, similar to a request made in the *1996-97 Governor's Budget*, would support a regional system of technical assistance to encourage parental involvement in schools. While the proposal is much improved from last year, it still does not address why technical assistance will solve the problem of parental involvement. As we stated in our *Analysis of the 1996-97 Budget Bill*, there are multiple state and federal requirements for schools to involve parents and many existing sources of technical assistance available to schools that want to increase parental involvement. The proposal does not answer the question of how further state intervention will fix the problem of inadequate parental involvement. For that reason, we recommend the Legislature reject this proposal.

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# FINDINGS AND RECOMMENDATIONS

## *K-12 Education*

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### **K-12 Priorities**

1. **The Legislature's K-12 Funding Options.** Recommend the Legislature develop an approach to funding K-12 education that reflects its long-term goals and the relative roles of the state and local school districts in the governance of public education. E-22

### **Options for 1997-98 K-12 Funds**

2. **Create a Proposition 98 Reserve.** Recommend setting aside \$100 million in a Proposition 98 reserve to protect against over-appropriating the minimum funding guarantee. E-27
3. **Provide a COLA to Most Categorical Programs.** Recommend approval of \$73.7 million to provide a COLA to most categorical programs. E-27
4. **Deny Two Categorical Program Requests.** Recommend deleting \$5 million in proposed new categorical programs because the proposals are not adequately justified. E-28

### **Options for Prior-Year Funds**

5. **Facility Funding.** Recommend increasing funds for facilities needed to implement class size reduction by \$150 million in 1997-98. E-30
6. **Deny Unjustified Augmentations.** Recommend deletion of \$63.4 million proposed for new or expanded K-12 categorical programs because the proposals are not adequately justified. E-30
7. **Proposition 98 Population Adjustment.** Recommend enactment of legislation to permanently set the estimate of population used in the Proposition 98 calculation as part of the budget process. E-32

### Class Size Reduction—Findings

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| 8.  | <b>Inflexibility in 20:1 Cap Increases Costs.</b> Districts are maintaining class sizes of less than 20 on average , which increases costs for the program by 21 percent statewide. Per-pupil funding in budget proposal would cover average costs if class sizes average 20:1.                                  | E-41 |
| 9.  | <b>CSR Teachers Are Less Qualified.</b> Teachers hired for CSR have less teaching experience and fewer qualifications, on average, than teachers hired in previous years. Twenty-four percent do not have a credential.  | E-45 |
| 10. | <b>CSR Results in Conversion of Other Facilities.</b> About 1,400 facilities statewide, such as computer labs or libraries, were converted from other uses for CSR, potentially curtailing other programs and services. New buildings may be the only option for most districts wishing to expand CSR next year. | E-48 |

### Class Size Reduction — Recommendations

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| 11. | <b>Allow Greater Flexibility in Use of Teachers.</b> Recommend allowing school districts to use new teachers more flexibly than for just smaller class sizes.   | E-52 |
| 12. | <b>Provide Greater Program Flexibility.</b> If significantly greater flexibility over the use of teachers is not adopted, then we recommend increasing flexibility in the way districts calculate the CSR cap. This would significantly reduce costs.                               | E-53 |
| 13. | <b>Delay Implementation of A Fourth Grade.</b> Recommend delaying implementation of a fourth grade due to shortages of qualified teachers and potential lack of facilities. The Legislature should reserve \$100 million for partial funding of a fourth grade in subsequent years. | E-54 |
| 14. | <b>Maintain Per-Pupil Funding Level Plus a COLA.</b> Recommend not providing increases in per pupil funding for CSR. Instead, provide new funds in revenue limits that districts can use for CSR, if needed, or for any other priority.   | E-55 |
| 15. | <b>Provide Staff Development Funds for CSR Teachers.</b> Recommend expanding allowable uses of \$52 million in Goals 2000 federal funds to include staff development of newly hired CSR teachers.   | E-57 |

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### Revenue Limits

- 16. **Using the COLA to Equalize.** Recommend enactment of legislation to replace the current uniform revenue limit COLA with a new formula that equalizes revenue limits over time. Further recommend increasing revenue limits \$149.7 million above the Governor's proposed levels. E-61
- 17. **Phase Out Basic Aid.** Recommend enactment of legislation to phase out basic aid over a three-year period. E-64
- 18. **Charter School Fiscal Liability and Accountability.** Recommend the State Department of Education (SDE) clarify the fiscal liability and accountability of charter schools before apportioning funds directly to individual charter schools. E-66

### Reforming Categorical Programs

- 19. **A School Improvement Block Grant.** Recommend consolidation of nine programs into one school improvement block grant that would provide \$676 million in funding to school sites. E-72
- 20. **Staff Development Block Grant.** Recommend creating a \$91 million block grant to consolidate two existing programs. E-73
- 21. **Compensatory Education Block Grants.** Recommend merging ten existing programs into two block grants to provide support for compensatory and alternative programs. E-74
- 22. **A Program of Evaluation.** Recommend appropriating \$10 million in Goals 2000 funds to begin an ongoing program to evaluate state categorical programs and other critical areas of K-12 education. E-80

### Deferred Maintenance

- 23. **New State-Local Approach Needed.** Recommend a \$2 billion, ten-year plan to increase district maintenance spending and eliminate deferred maintenance backlogs statewide. E-82

### Child Care

- 24. **Consolidate Funding for Most Programs.** Recommend separately scheduling federal and General Fund monies and funding each child care program from only one funding source, either state or federal. E-97
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	Analysis Page
25. <b>Trim Child Care Program Expansion.</b> Recommend replacing \$43.9 million in General Fund monies for child care programs with new federal funds because SDE child care programs can not absorb these new funds in a single year.	E-98
26. <b>Create Capacity for Data Collection.</b> Recommend providing \$4 million and three two-year positions for SDE to develop and implement a child care data collection system.	E-99
27. <b>Trim Staffing Expansion.</b> Recommend denying 19 new positions related to administering existing and expanded child care programs. Instead, recommend providing seven limited-term positions for (1) short-term workload relief and (2) restructuring child care administration.	E-100
28. <b>Budget Excludes Legislature from Oversight of Child Care Programs.</b> Recommend amending several provisions in the budget bill to include appropriate legislative oversight of changes in child care policy.	E-103

### Special Education

29. <b>Set-aside for Special Education Reform.</b> Recommend that funding for reform should be contained in legislation rather than the budget bill. Further recommend increasing the set-aside from \$76.7 million to \$105 million.	E-107
30. <b>Is Entitlement Amount Correct?</b> Governor's budget includes \$60.7 million for "entitlement adjustments." This adjustment may not be in accord with legislative intent. We will report further on this issue during budget hearings.	E-108

### Other Issues

31. <b>School Safety Initiatives Still Over-Budgeted.</b> Recommend reducing funding for community day schools by \$22.6 million in 1997-98 and \$35 million in 1996-97 to reflect realistic population projections for the program.	E-110
32. <b>Programs Should Charge for Computers.</b> Recommend reducing funding for the California Donated Computer Program by \$2.9 million and adding budget bill language requiring the program to charge schools for refurbished computers.	E-112
33. <b>Deny Two Categorical Program Requests.</b> Recommend rejecting two programs funded with \$7.1 million in federal Goals 2000 funds because the programs are not adequately justified.	E-113