
EDUCATION

Preserving Education

Recognizing that the education of the state's students is the most important underpinning of the economy and the long run hope for increased prosperity, the May Revision maintains education as the Administration's highest priority by providing full funding of the Proposition 98 guarantee; funding growth for apportionments at 1.34 percent in 2003-04; increasing funding for the California Community Colleges by \$305 million and making limited reductions in higher education programs. K-12 Proposition 98 per pupil spending is increased by \$231 over the 2002-03 fiscal year as estimated in the May Revision and hits a new high of \$6,869 in 2003-04. The May Revision provides \$708 million more for Proposition 98, above the \$803 million needed to fund child care within the guarantee.

Responding to Priorities

The Administration has listened to the voices of the education community and the Legislature, and has engaged in a dialogue about priorities and ways to manage with a level of education funding lower than that which all parties, including the Administration, wish were possible. In the current fiscal situation, funding at the Proposition 98 guarantee is a significant accomplishment, requiring sacrifices throughout the rest of the budget.

The January Governor's Budget reflected an approach to reductions that spread the impact over as many programs as possible to minimize the impact on each, while preserving as much funding as possible for classroom instruction. The May Revision continues the priority of preserving flexible funding for classroom instruction by lowering the cut to revenue limit funding from \$612 million to \$350 million, now only a 1.2 percent reduction compared to 2.15 percent proposed in January. To help pay for this, the May Revision reduces or eliminates lower priority categorical programs, with the hope that some of the more effective programs can gradually be restored as future funding permits.

The Administration understands that the block grant for categorical aid proposed in January, while providing significant flexibility for local priority setting, was not considered the best approach for providing the remaining funding. The May Revision does not propose a specific alternative. The Administration is ready to work with all parties to craft a mechanism for school funding that helps schools to adapt to the funding changes in the 2003-04 Budget. The Administration is open to block grant type funding or other mechanisms to provide increased local choice while protecting the neediest students and preserving the State's accountability programs and high student achievement goals. The Administration proposes that districts be allowed to use reserves more flexibly, while encouraging fiscal responsibility.



Priority Programs Fully Funded

- ◆ Class Size Reduction
- ◆ Special Education
- ◆ Accountability
- ◆ Child Nutrition
- ◆ School Safety

Class Size Reduction funding is fully restored with a \$180 million increase. Special Education is fully funded with an increase of \$28 million in Proposition 98 General Fund, and an increase of \$69 million in federal funding is proposed to fund mental health services. Programs to assist underperforming schools as part of the school accountability system are fully funded to meet the needs of current participants, with an increase of over \$60 million from the Governor's Budget level. Nutrition programs are fully funded. School safety programs are funded at the 2002-03 level.

Proposition 98 Guarantee

2002-03	-\$60.3 million
2003-04	\$1,502.9 million

Combining the years 2002-03 and 2003-04, Proposition 98 funding is \$1.5 billion higher than the mid-year revision level established by Chapters 4 and 10, Statutes of 2003, First Extraordinary Session (SB 18X and SB 28X), a 1.8 percent change from the Governor's Budget level.

In the Governor's Budget, the minimum funding level for the budget year was established by Test 3, which adjusts the prior guarantee level for growth in attendance and the change in per capita General Fund revenues. A 0.34 percent increase in average daily attendance (ADA), an increase in General Fund revenues, and increases in the prior year base for the Proposition 98 calculation, results in an increase of \$1.511 billion to the guarantee.

The May Revision proposes to fully fund the guarantee under Test 2. The General Fund share of the guarantee increases by \$1.503 billion. An \$879 million adjustment is made to the guarantee to reflect the restoration of the child care program to Proposition 98. The local revenue share of the guarantee increases \$7.9 million after adjusting for a revision to the excess tax proposal.



Funding the Guarantee

In order to fund the General Fund share of the guarantee, \$1.82 billion in undisbursed 2002-03 General Fund appropriations have been deferred until 2003-04 through current year special legislation, Chapters 4 and 10, Statutes of 2003, First Extraordinary Session (SB 18X and SB 28X). These appropriations will be counted toward the 2003-04 guarantee. The Administration proposes to defer \$1.16 billion in appropriations to 2004-05 but does not propose making this practice permanent.

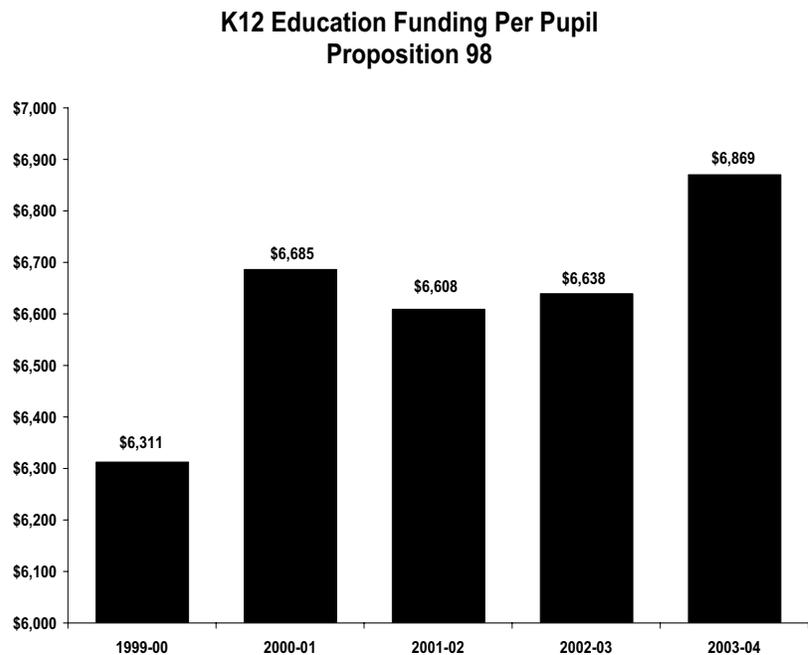
The reductions in Proposition 98 appropriations from the 2002 Budget Act level totaling \$2.53 billion still leave the total appropriations at \$122.3 million above the Test 2 guarantee level in the current year.

Funding per pupil under Proposition 98 continues to increase. Appropriations for 2002-03 will provide a funding level of \$6,638 per pupil. Per pupil funding of \$6,869 in 2003-04 represents an increase of 3.5 percent over the current year. Funding per pupil grows more than \$200 for 2003-04 from the Governor's Budget.

FIGURE EDU-1

Proposition 98 January vs. May Revision (Dollars in thousands)			
2002-03	Mid-Year Revision	May Revision	Change
General Fund	\$29,397,125	\$29,336,823	-\$60,302
Local Revenue	14,513,835	14,612,403	\$98,568
Total Guarantee	\$43,910,960	\$43,949,226	\$38,266
2003-04	January Proposal	May Revision	Change
General Fund	\$28,225,485	\$29,728,383	1,502,898
Local Revenue	15,867,659	15,875,526	7,867
Total Guarantee	\$44,093,144	\$45,603,909	\$1,510,765
Total Two-Year Funding	\$88,004,104	\$89,553,135	\$1,549,031

FIGURE EDU-2



K-12 Education

2002-03	–\$29.8 million
2003-04	\$1,672.2 million

The May Revision increases funds for K-12 education by \$1,642.4 million over two years in General Fund resources compared to totals enacted in mid-year legislation. Proposition 98 General Fund increased by \$1,174.6 million, contributions to the State Teachers' Retirement System (STRS) increased \$450.9 million because the proposal to defer or bond 2003-04 payments has been rescinded, and bond debt service increased \$70.4 million. Total General Fund allocations of \$29.1 billion for K-12 education now represent 41.2 percent of the General Fund budget.

Total K-12 Funding

Funds available to K-12 education from all sources are increasing from \$54.5 billion in 2002-03 to \$55.5 billion in 2003-04, a 1.8 percent increase. General Fund declined \$536.7 million, while local property taxes grew by \$1.1 billion and federal funds grew by \$450.2 million. Major General Fund changes include:

- ◆ A reduction of \$465.7 million for STRS payments
- ◆ An increase of \$803.9 million to Proposition 98 General Fund
- ◆ A decrease of \$93.4 million for Scholarshare funding
- ◆ A decline of \$779.6 million in the use of Proposition 98 Reversion Account General Fund

Attendance Changes

Current Year

The May Revision includes estimated K-12 ADA growth of 1.75 percent, up from 1.48 percent in the Governor's Budget. General Fund costs for school district and county office of education revenue limits decrease by \$29.9 million, resulting primarily from significant increases in local property taxes that are partially offset by increased estimates of ADA, and other miscellaneous adjustments.

Budget Year

In the budget year, the revised ADA growth is up slightly, from 1.00 percent to 1.34 percent (about 36,000 ADA higher than the January estimate). The total number of ADA is estimated to be 5,911,519 in 2002-03 and 5,990,495 in 2003-04.



Growth Adjustments

The May Revision provides over \$272 million in new funds to provide an increase in the estimated Proposition 98 ADA growth rate from 1.00 percent to 1.34 percent in budget year. Major adjustments include increases of \$183.4 million for K-12 school district apportionments, \$12.8 million for special education, and a decrease of \$0.5 million for county office of education apportionments. Other major adjustments include significant costs to pay for reductions in Public Employees' Retirement System (PERS) offset funding of \$51.7 million and an increase in unemployment insurance costs of \$25.2 million. The PERS and unemployment insurance adjustments reflect estimated rate increases to 10.42 percent and 0.30 percent, respectively, of projected salaries.

Revenue Limits

Revenue limit funding constitutes the basic funding source for classroom instruction. The May Revision provides a net increase of nearly \$262.4 million to revenue limits, after restoring current year across-the-board reductions totaling \$612.4 million and then reducing revenue limits by approximately 1.2 percent, or \$350.0 million.

Basic Aid District Excess Taxes

The May Revision modifies the Governor's Budget proposal to offset the General Fund with \$126.2 million in basic aid excess taxes by reducing the offset to \$20 million. Further, the proposal is modified to offset only State categorical funding that would otherwise be provided to excess tax districts. The revised proposal would limit the impact on basic aid districts—together with the previously proposed elimination of the \$120 per pupil basic aid payment—to a reduction of approximately 4.5 percent, consistent with the overall level of reduction to non-basic-aid districts.

Class Size Reduction

The May Revision proposes to increase funding for the K-3 Class Size Reduction Program by \$179.7 million to rescind the across-the-board reductions proposed for the program. This increase fully restores the program's base funding level for 2003-04.

Accountability

The May Revision provides an additional \$65.3 million for accountability programs to fund schools participating in Immediate Intervention/Underperforming Schools Program (II/USP) (\$44.4 million) and the High Priority Schools Grant Program



(HPSGP) (\$20.9 million) at \$200 per pupil and \$400 per pupil, respectively, less a 20 percent deferral. The augmentation to HPSGP allows an additional 86 schools to participate in HPSGP so that these schools in the first decile of the Academic Performance Index with an application for participation that has been approved by the Department of Education (SDE) would be funded at \$400 per pupil, less a 20 percent deferral, beginning in 2002-03. The May Revision contains a balance of \$4 million for HPSGP that will be available to expand the HPSGP subject to the enactment of legislation for this purpose.

The increase in funding is comprised of the restoration of the across-the-board cuts to these programs (\$41.8 million) and payment of the 20 percent deferral of 2002-03 funding contained in SB 18X (\$81.6 million). These increases are offset by continuing the 20 percent deferral established by SB 18X (-\$66.0 million). Additionally, the May Revision proposes to reduce Proposition 98 funding for these programs by \$23 million, which is offset by an increase of \$30.8 million from the Proposition 98 Reversion Account for II/USP; this last action also removes the last of the II/USP shortfall in the 2003-04 Governor's Budget.

Statewide Assessments

The May Revision continues the Administration's efforts to reduce testing time and streamline the State's system of assessments. Funding for the Golden State Examinations (GSEs) are eliminated and the English Language Arts and Mathematics GSEs are integrated into the Standardized Testing and Reporting (STAR) Program to be used in a pilot program by the California State University for the purposes of placement and remediation. This action provides not only a savings of approximately \$11.7 million from the 2002 Budget Act level, it also eliminates 11 examinations and links standards and assessments between the secondary level and higher education that has not previously existed. Further, the May Revision includes an unallocated reduction of \$13 million in the Testing Programs. The Administration notes the Legislature's concerns regarding testing volume and time and will work with the Legislature to determine how the \$13 million reduction will be allocated.

Special Education

The May Revision provides a net General Fund increase of \$27.8 million and also includes an additional \$35.6 million in federal funding over amounts proposed in the Governor's Budget. These increases allow for full funding of growth and maintain the year over year State aid funding commitment. In addition to growth funding, \$138,000 in additional federal funds is allocated to schools as a permanent increase to the base funding level for the Special Education program. Further, the May Revision provides \$4.9 million in funding from the Proposition 98 Reversion Account to fund prior year costs resulting from growth-related increases.



Individuals with Disabilities Education Act-Required Mental Health Services

The May Revision provides \$69 million in federal funds to provide mental health services for children with exceptional needs, as required by the Federal Individuals with Disabilities Education Act. These funds will offset reimbursable mandate activities for services provided to children with exceptional needs as part of the pupil's individualized education plan (IEP). The Administration plans to work with the Legislature and interested parties to develop trailer bill language and Budget Bill language to ensure these services are provided.

Equalization

The May Revision proposes to eliminate \$250 million previously proposed for 2003-04, including \$203 million appropriated by Chapter 1167, Statutes of 2002, and \$47 million in additional funding proposed in the Governor's Budget.

PERS Offset Mitigation

The May Revision proposes \$35 million to mitigate the PERS offset to revenue limits. This represents a restoration of a proposed reduction in the Governor's Budget.

Fiscal Crisis and Management Assistance Team Restoration

The May Revision proposes \$912,000 to ensure that core school district budget management and fiscal services provided by the County Office Fiscal Crisis and Management Assistance Team (FCMAT) will be provided during these difficult fiscal times.

Categorical Funding Adjustments

In the Governor's Budget, \$854 million in categorical program reductions were proposed on an across the board basis. Of these, \$835 million are proposed to be restored in the May Revision, while \$19 million are retained because they reflect natural savings. To replace these reductions and increase funding for apportionments, specific program reductions are proposed. These reductions reflect the Administration's discussions with the education community and members of the Legislature. The table below lists the most significant reductions.



Categorical Program	Reduction (in millions)
Equalization	\$250
Deferred Maintenance	129
Summer School	85
Defer Mandates	125
Teaching as a Priority	89
Instructional Materials	76
Elementary Intensive Reading	31
Peer Assistance and Review	25
Miller-Unruh Reading	29
School Improvement	42
Supplemental Grants	80

Child Care

Defer Realignment Proposal—Child care, originally a part of the \$8.2 billion realignment proposal, is proposed to be reinstated in the 2003-04 Budget. Realignment remains a crucial component of structural reform. However, to provide more time for legislative consideration, the majority of the Administration's January realignment proposal is being deferred to the remainder of this legislative session for implementation in 2004-05.

The Administration believes child care realignment continues to be a viable way to resolve a number of policy and fiscal concerns that have plagued the State's subsidized programs. By giving counties both responsibility to administer child care services in conjunction with other social services for the same families and a financial stake in child care expenditures, it was expected that the proposal would create more equitable access and improve coordination of services for the neediest families, enhance accountability, decrease fraud, and facilitate integration of local priorities and funding sources. Moreover, the Administration had proposed a revenue stream that would have provided a growing revenue source including over \$1 billion from new revenues. Unfortunately, the State's fiscal problem has not improved so cost reductions are necessary as the program is restored to state operations.

The Administration continues to be concerned with growth in CalWORKs Stage 3. While the May Revision restores the child care programs in their current form, the Administration will work with stakeholders, implementing agencies, and the Legislature to address these problems.

Reforms, Cost Reductions, and One-Time Fund Shifts—In order to restore child care to State administration and meet competing priority needs in Proposition 98 education programs, the Administration has carefully reviewed restructuring options included in the 2002-03 Governor's Budget comprehensive restructuring proposal. Based on that effort and combined with the availability of one-time Temporary



Assistance for Needy Families (TANF), the Administration proposes a series of reasonable reforms that are aimed at preserving existing programs, preserving access for current subsidized populations and striking a balance with other K-14 funding needs for 2003-04.

Overall, the Administration proposes a total funding level of \$1.867 billion for the restored programs. However, this funding level continues reliance on one-time funding solutions which will create additional problems in the future, absent realignment. Specific solutions produce a total of \$384 million in Proposition 98 General Fund cost savings as follows:

Reforms—\$216 Million Cost Reduction

- ◆ \$4 million caseload savings by limiting child care services to children 12 years of age and under. No other state offers subsidies to 13 year old children.
- ◆ \$12 million savings by eliminating child care services to “grandfathered” families who earn above the current income limits for subsidized care. No other state offers subsidies for incomes at the level California currently provides.
- ◆ \$123 million savings by implementing Regional Market Rate (RMR) regulations, consistent with legislative intent expressed in the 2002 Budget Act that: (1) lowers providers’ rate limits if those providers do not participate in the market by serving only non-subsidized families; (2) prohibits payment of an hourly rate for full-time care; and (3) limits the evening/weekend premium rate to licensed providers.
- ◆ \$44 million savings by reducing the RMR ceiling for licensed providers to the 80th percentile of the regional market. No other state offers reimbursement to this level.
- ◆ \$33 million savings by implementing a modified family fee schedule. Families would begin contributing a share of child care costs when family income reaches 40 percent of the current income level index used for determining eligibility. Fees would increase on a sliding scale with family income, but would be capped at 10 percent of the family’s income at the highest income level, consistent with federal guidelines. Families still on cash aid would pay no fees.

Other Cost Reductions, Savings, and Fund Shifts—\$168 Million Savings:

- ◆ \$39 million caseload savings, including (a) \$35 million reduction in Stage 3 caseload costs from the January estimate; and (b) \$4 million State Preschool participation savings.



- ◆ \$13 million reduction to non-direct care services including: (a) teacher retention bonuses, which is offset by recent implementation of a \$24 million Proposition 10 Commission initiative; and (b) \$3 million reduction to Resource and Referral programs (\$17 million remains for the most essential supportive services).
- ◆ \$15 million Proposition 98 General Fund reduction by utilizing one-time federal funds and unliquidated CalWORKs carryover funds that are available.
- ◆ \$101 million in one-time TANF funds to offset Proposition 98 General Fund.

Caseload Changes and Adjustments for Stage 2 and 3

Stage 2—Based on April revised estimates, the average monthly caseload for Stage 2 has increased from the Governor's Budget estimate of 101,800 to 102,500 children due to adjustments in the calculations of the number of families affected by the federal five-year CalWORKs time limit. The \$48.3 million of additional cost for the caseload is funded through TANF transfers to the Child Development Block Grant.

Current Year Stage 3—As mentioned previously, Stage 3 caseload decreased for a savings of \$35 million, reflecting a caseload drop from 70,400 to 64,200. Additionally, savings of \$12 million in Proposition 98 for the revised current year estimate are proposed for reversion to the Proposition 98 Reversion Account.

After School Safety and Education Programs

The May Revision proposes to rescind the across-the-board reductions proposed for the After School Safety and Education Program in the amount of \$14.3 million. This action fully restores the program's base funding level of \$121.6 million and will help increase opportunities for school age children, including 13 year olds who may be displaced due to the child care reform proposal.

Principal Training Program

The May Revision reduces funding for this Administration initiative that provides 15,000 principals and vice-principals with training in instructional standards and effective school management techniques by \$22.5 million. This reduction will delay completion of this program into 2004-05. The Administration remains committed to this program and has reached an agreement with the Gates Foundation to continue providing 25 percent (\$1,000) of the \$4,000 per participant cost through 2004-05.



Longitudinal Pupil Database

The May Revision continues \$12 million in federal funding for the assignment of student identifiers and for the development of the database, which is necessary to comply with the data reporting requirements of the federal No Child Left Behind Act. In addition, the May Revision contains an additional \$9.7 million in federal Title VI funds that could also be used for the development of the database, if necessary. The SDE is scheduled to complete a feasibility study report for the development of the database in 2003-04.

California State Library

2002-03	—
2003-04	–\$0.6 million

Due to current fiscal constraints, the May Revision proposes the following budget adjustments:

- ◆ \$12,145,000 General Fund increase to rescind the prior proposal to shift funding for Transaction Based Reimbursements to local fees. The State Library advises that this program is a high priority, relative to other local assistance programs. This proposal will ensure that cost-effective resource-sharing infrastructure remains intact and that California continues to receive federal funds for one-time projects and system enhancements.
- ◆ \$2,000,000 General Fund increase to offset a lower, more achievable level of user fees (\$1,000,000) for supporting State Library services.
- ◆ \$14,766,000 reduction for the Public Library Foundation to offset the restoration of Transaction Based Reimbursements and contribute to the overall budget solution. Remaining foundation resources would be provided for the libraries most in need on a fiscal basis.

