

# SUBCOMMITTEE NO. 1 on Education



**Subcommittee No. 1**  
**Chair, Carol Liu**  
**Member, Robert Huff**  
**Member, Roderick Wright**

**Monday, February 7, 2011**  
**2:30 p.m. or**  
**Upon Adjournment of Session**  
**Room 4203, State Capitol**  
**(Note Room Change)**

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Public Comment

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**ISSUE 1. Governor’s Proposal to Eliminate OSE & Increase Funds for the State Board of Education**

**DESCRIPTION:** The Governor proposes to eliminate the Office of the Secretary of Education (OSE) and shift some of the savings to the State Board of Education. More specifically, the Governor proposes to decrease funding for OSE by **\$1.9 million** in 2011-12 and shift **\$274,000** to the State Board of Education in 2011-12 to continue some OSE activities. This proposal provides net General Fund savings of **\$1.6 million** in 2011-12, as well as **\$400,000** in 2010-11, since the Governor proposes immediate elimination of OSE.

**BACKGROUND:**

**Office of the Secretary of Education (OSE).** The Secretary of Education is a member of the Governor’s Cabinet, responsible for advising the Governor and making recommendations on state education policy and legislation. While the Office of the Secretary of Education (OSE) is not established in statute, it has operated for a number of years in an advisory role to the Governor

The Office of the Secretary is funded annually through two separate budget items. Half of the OSE’s budget appropriation is contained in its main support item (0558-001-0001); the other half of its appropriation is provided through the Governor’s Office of Planning and Research (0650-011-0001).

**GOVERNOR’S BUDGET PROPOSAL -- OSE:** The Governor’s budget includes a decrease of **\$400,000** General Fund in 2010-11 and **\$1.9 million** General Fund in 2011-12 to reflect the elimination of OSE. The Governor proposes to shift a portion of state operations for OSE to the State Board of Education in 2011-12 in order to streamline government operations.

**Office of the Secretary for Education**

<b>Summary of Expenditures</b> <i>(Dollars in thousands)</i>	<b>Positions</b>			<b>Expenditures</b>		
	2009-10	2010-11	2011-12	2009-10	2010-11	2011-12
	15.0	16.2	--	\$1,803	\$1,485	\$--
<b>Funding</b>						
General Fund				\$1,676-	\$1,361	\$--
Reimbursements				127	124	--
<b>Total</b>				\$1,803	\$1,485	\$--

**GOVERNOR’S BUDGET PROPOSAL FOR STATE BOARD OF EDUCATION:** The Governor proposes to increase funding for the State Board of Education (SBE) by **\$274,000** in 2011-12 to continue some activities previously provided by the OSE. These funds are being shifted from General Fund savings resulting from the elimination of the OSE.

<b>State Board of Education</b>						
<b>Summary of Expenditures</b> <i>(Dollars in thousands)</i>	<b>Positions</b>			<b>Expenditures</b>		
	2009-10	2010-11	2011-12	2009-10	2010-11	2011-12
	8.1	9.0	9.0	\$1,195	\$1,904	\$2,217
<b>Funding</b>						
General Fund				\$xxx	\$xxx	\$xxxx
Reimbursements				\$xxx	\$xxx	\$xxx
<b>Total</b>				\$1,195	\$1,9048	\$2,217

The SBE currently has nine authorized positions. According to SBE staff, seven of these nine positions are filled, leaving two vacancies – one full-time Chief Counsel position and one part-time Office Technician position. (The Chief Counsel position is an exempt position appointed by the Governor, which has made this position difficult to fill per SBE staff.)

As a part of the \$274,000 funding shift, the Governor also proposes to shift three permanent, full-time positions authorized within the California Department of Education budget to the State Board of Education budget. This increases total SBE authorized staff from nine to twelve positions.

The SBE plans to use the three shifted positions to cover some of the responsibilities previously handled by OSE and to staff the State Board President. For example, OSE was responsible for preparing bill analyses and recommendations to the Governor. In addition, SBE staff are working with the Administration to ensure adequate board staff to fulfill some of its basic functions such as providing public agendas and materials and posting minutes of all meetings in a timely fashion. SBE staff and the Administration are working together to determine the workload requirements of the new leadership for the SBE. For example, the SBE is in the process of identifying top priority issues and deciding how many meetings it will hold in the 2011-12 fiscal year.

**STAFF COMMENTS:**

- **Senate Has Supported Elimination of OSE in Recent Years.** Senate has taken budget action in recent years to phase out OSE as a means of achieving General Fund savings without eliminating education programs and achieving greater government efficiencies by reducing duplicative services.
- **Governor’s Proposal Creates Permanent General Fund Savings.** The Governor’s proposal to eliminate OSE and shift limited funds to the State Board results in net, ongoing General Fund savings of **\$1.6 million** beginning in 2011-12.

- **Governor’s Action Has Resulted in Additional One-Time Savings in Current Year.** Since the Governor has already acted to phase out the OSE, additional one-time savings of **\$400,000** are likely in 2010-11.
- **Governor’s New Appointees Create New SBE Leadership.** The State Board includes 11 members, including one student member. The Governor appointed seven new members to the State Board in January 2011. One of those new appointees was elected President of the State Board in January.
- **Governor’s Proposals Does Not Increase Authorized Positions and Does Not Require New General Funds, But More Justification Needed to Justify Positions.** SBE staff is currently finalizing their position request. As a part of this effort, SBE staff is currently preparing a workload analysis to determine precisely what workload functions SBE will assume from OSE and what types of positions will be needed.

**STAFF RECOMMENDATION:** In progress – awaiting final information from Administration and SBE staff.

#### **SUGGESTED QUESTIONS:**

1. Staff understands the State Board is currently developing more specific information to describe workload for the three shifted positions per the Governor’s proposal. When will that information be available?

## **ISSUE 2. Governor’s Budget Proposal – Special Education Mental Health Related Services (AB 3632 Services)**

### **DESCRIPTION:**

The Governor continues to declare that the state AB 3632 mandate on counties is suspended in 2010-11, consistent with the veto by the previous Administration last Fall. This action returns the federal mandate for mental health related services to K-12 schools. The Governor continues \$69 million in federal special education funds for AB 3632 services, but does not provide any additional funding to the schools to cover full provision of these services in 2010-11.

In 2011-12, the Governor proposes to realign AB 3632 services to counties using and paying for these services with \$99 million in Proposition 63 funds, \$72 million in realignment funds for residential services, and \$69 million in federal special education funds.

In 2012-13 and beyond, the Governor proposes to fund AB 3632 services with \$176 million in realignment funds -- reflecting \$104 million for mental health related services and \$72 million for residential services -- and \$69 million in federal special education funds.

### **Background**

The federal Individuals with Disabilities Education Act (IDEA) requires schools to provide “special education and related services” to students with disabilities. Related services are defined to cover “transportation, and such developmental, corrective, and other supportive services as may be required to assist a child with a disability to benefit from special education.” Mental health services clearly fall into the category of a related service. For example, federal law explicitly states that related services include, but are not limited to – social work, counseling, and psychological services.

Until 1984, California schools provided mental health services to special education pupils who needed the services to benefit from their Individualized Education Plans (IEP). The Legislature saw a need to assure coordination of services among publicly funded agencies. In 1984 the Legislature passed AB 3632 (W. Brown), Chapter 1747, Statutes of 1984, and assigned county mental health departments the responsibility for providing students these services [except students placed out of state].

In 1996, the Legislature expanded county responsibilities to include services to students placed in out-of-state schools [AB 2726 (Woods), Chapter 654, Statutes of 1995]. This program is generally known as -- the AB 3632 Program.

Approximately **20,000** students with disabilities receive mental health services under the AB 3632 program.

While AB 3632 was written in response to federal IDEA requirements, state law is more specific than federal law in articulating all allowable mental health services. The statute defines mental

health related services to include therapy and counseling, day treatment, medication management, and for children with the most severe problems, 24-hour therapeutic residential programs with on-site schools.

AB 3632 tasks mental health professionals, in consultation with educators, with deciding what services should be included in the student’s IEP. Once a service is included in the IEP, it is deemed an educationally necessary service.

**AB 3632 Funding.** The LAO has prepared the chart that summarizes AB 3632 funding in recent years.

Year	Department of Mental Health Categorical	Department of Social Services (Residential Care)	Federal Special Education	Mandate Claims	Total
1998-99	\$12	\$23	—	\$50	\$85
1999-00	12	24	—	68	104
2000-01	12	25	—	78	115
2001-02	12	31	—	119	162
2002-03	—	38	—	146	184
2003-04	—	39	—	57	96
2004-05	—	37	\$69	68	174
2005-06	—	38	69	72	179
2006-07	52	43	69	61	225
2007-08	52	48	69	83	252
2008-09	104	51	69	36 <sup>a</sup>	260
2009-10	—	59	69	Not Available	128

<sup>a</sup> Additional mandate claims being submitted for 2008-09 year.

Counties currently receive federal special education funds and General Fund resources from the California Department of Education (CDE), Departments of Mental Health (DMH) and Social Services (DSS). (Counties also receive funding from Medi-Cal for eligible students; however, these funds are not reflected LAO chart above.)

In addition, the state currently makes payments for mandate claims submitted by counties to cover costs in excess of other state and federal appropriations. The Constitution requires the state to pay mandate bills or suspend or repeal the mandate.

**2010-11 Budget Veto.** Governor Schwarzenegger proposed suspension of the AB 3632 mandate in his January 2010 budget. The Legislative Analyst’s Office noted that suspending AB 3632 would be temporary, confusing, and disruptive. The LAO found that the Governor’s proposal did not address the significant transitional issues associated with the change, and that eliminating AB 3632 funding could violate federal special education spending maintenance-of-effort (MOE) requirements, thereby jeopardizing receipt of federal funds. While several alternatives were considered throughout the budget process, ultimately the Legislature rejected the Governor’s proposal to suspend the mandate.

On October 8, 2010, Governor Schwarzenegger vetoed approximately **\$133 million** in funding for the AB 3632 mandate. In vetoing the funds, the Governor claimed to have suspended the mandate on county mental health departments for 2010-11. Legal action is pending as to whether the Governor has the ability to veto funding in order to suspend an underlying state law.

**Related Litigation.** Three lawsuits have been filed in response to the veto of the AB 3632 services. These lawsuits have been filed in both state and federal courts. They involve questions of constitutional law and executive power, unfunded state mandates, California's compliance with federal law, and ensuring that mental health services are provided to eligible special education students who require them.

- **Lawsuit on Behalf of State and Local Education Agencies.** On November 9, 2010, the California School Boards Association (CSBA), LAUSD, and Manhattan Beach Unified School District petitioned the California Court of Appeal for a writ to issue against the Governor, and various state agencies and officials, declaring the Governor's veto of the appropriation for AB 3632, and his proposed suspension of the mandate to be void. **(Note: The California Legislature filed a letter in support of the petition.)** The petition asks the Court of Appeal to set aside the Governor's actions as a violation of Article XIII B, section 6(b) and Article III, section 3 of the California Constitution, and to order the transfer of approximately \$133 million from California's reserve account in order to restore the Legislature's funding appropriation for AB 3632. **The Status:** Oral arguments are set to be heard on Tuesday, February 8 in the 2<sup>nd</sup> District Court of Appeals in Los Angeles.
- **Lawsuit on Behalf of Students with Disabilities.** On October 21, 2010, four special education students receiving AB 3632 services in Los Angeles County filed suit in federal District Court against the Governor and various state and local entities, seeking declaratory and injunctive relief under IDEA. On November 1, 2010, the court signed a stipulated Temporary Restraining Order (TRO) maintaining the status for students in Los Angeles County. On November 5, 2010, the California Department of Education (CDE) released \$76 million dollars statewide, with the Los Angeles County Office of Education (LACOE) being allocated \$13 million. Pursuant to the TRO, the Los Angeles County Department of Mental Health (LACDMH) agreed to continue to comply with AB 3632 to serve eligible students within Los Angeles County until January 14, 2011, unless the funds allocated by the CDE run out before that date. **Status:** In December the court declined to grant the preliminary injunction and "stay put" relief requested by plaintiffs and instead continued the hearing on their request to a future date pending further briefing.
- **Lawsuit on Behalf of Counties.** On November 5, 2010, twenty-three (23) counties in California filed suit in Sacramento Superior Court against the state and various state officials seeking a judicial declaration that AB 3632 is an unfunded, unenforceable state mandate under Government Code section 17612. Additional counties joined the lawsuit. This lawsuit seeks the court's declaration of an unfunded mandate to absolve mental health agencies of the responsibility of providing educationally-related mental health services under AB 3632. **Status:** The counties are still waiting for a decision on their case. The counties' motion for judgment was heard on January 7, 2011. The judge took the case under submission and will

render a decision within 90 days—noting he intends to issue a ruling before the CSBA lawsuit is heard on February 8, 2011.

### **Related Legislation:**

- **AB 39 (Beall).** Requires the Department of Mental Health to allocate **\$57 million** from the Mental Health Services Fund (Proposition 63) to county mental health departments for purposes of providing special education services. The bill also requires the Superintendent of Public Instruction and county mental health directors to jointly convene a technical working group to develop a transitional program to transfer responsibilities associated with special education services from county mental health departments to the State Department of Education. **Status:** The bill is pending referral to committee.

### **Governor's 2011-12 AB 3632 Proposal**

The Governor's budget does not propose any changes to funding for the AB 3632 program for 2010-11 and maintains that the mandate is suspended for 2010-11. This action returns the federal mandate for mental health related services to K-12 schools. The Governor continues \$69 million in federal special education funds for AB 3632 services, but does not provide any additional funding to the schools to cover full provision of these services in 2010-11. Per the Administration, K-12 schools will have to absorb the additional costs of providing services within their existing budgets.

Beginning in 2011-12, the Governor's budget proposes to realign AB 3632 services with county mental health agencies. While the Governor originally proposed to continue the state AB 3632 mandate, that is no longer the case. The Governor proposes to fund realigned AB 3632 services -- and services for two other programs (the Early and Periodic Screening, Diagnosis, and Treatment (EPSDT) Program and Mental Health Managed Care) -- with a combination of state and federal funds, as follows:

- In 2011-12, the Governor proposes to realign AB 3632 services to counties using and paying for these services with \$99 million in Proposition 63 funds, \$72 million in realignment funds for residential services, and \$69 million in federal special education funds.
- In 2012-13 and beyond, the Governor proposes to fund AB 3632 services with \$176 million in realignment funds -- reflecting \$104 million for mental health related services and \$72 million for residential services -- and \$69 million in federal special education funds.

### **LAO COMMENTS:**

- **3632 Services Appropriate for Realignment, but Better Aligned to Schools not Counties.** The LAO believes that AB 3632 services are merit realignment -- per the Governor's proposal. However, the LAO believes that AB 3632 services should be realigned to schools, not counties as proposed by the Governor.

More specifically, the LAO suggests schools should have programmatic and financial responsibility for this program in providing mental health services to special education pupils. They contend that while schools could contract with county mental health departments, the primary fiscal and program responsibilities should reside with schools.

- **Mandated Program Inefficient.** According to the LAO, the existing approach to delivery of AB 3632 services, by which the state reimburses counties for the provision of mental health services after-the-fact in response to claims, does not provide strong cost-control mechanisms or guarantee that state funds are well spent.
- **Need to Connect Services and Funding.** The LAO also notes that the current structure can result in inappropriate separation between county mental health and K-12 schools, whereby program services may lack sufficient input from educators or connection to students' educational outcomes.
- **More Accountability Needed.** The LAO also sites concerns that the existing structure lacks accountability to measure how well counties achieve the program's goals. Neither DMH nor CDE maintain quality data on services or outcomes for student receiving AB 3632 services.
- **2010-11 Budget Discussions Provided Some Movement.** During the 2010-11 Budget Conference Committee, the LAO presented an alternative to the current system that would allow for a one-year transition and then repeal the AB 3632 mandate. As a part of this repeal, the LAO would reaffirm that federal IDEA requires schools to provide mental health services contained in a student's IEP, but that federal law does not require anything additional.

The LAO proposal was not adopted by the Legislature. But the Conference Committee left the door open on the issue by appropriating \$500,000 in one-time federal IDEA funds to CDE to contract with an external entity to evaluate the state's approach to providing mental-health related services for pupils with disabilities. However, given the ambiguity over the status of the program, CDE has held off on moving forward with the study until they receive further direction from the Legislature.

#### **LAO RECOMMENDATIONS:**

The LAO recommends that the Legislature reject the Governor's proposal to fund the mandate with Proposition 63 funds in 2011-12 and realign funding to counties beginning in 2012-13. Instead, the LAO recommends that Legislature repeal the state AB 3632 mandate and realign responsibility and funding to schools, consistent with federal law.

#### **SUGGESTED QUESTIONS:**

1. How has the Administration's AB 3632 realignment proposal changed from the Administration's earlier version on January 10? What issues are behind the changes?

2. The Governor continues to “suspend” the AB 3632 mandate on counties in 2010-11. This proposal places most of the AB 3632 mandate back on schools. Does the Governor provide additional funding to schools to cover these services?
3. How are schools providing mental-health related services in the current year given the lack of funding for 2010-11?
4. How do other states deliver mental health related services – per the IDEA mandate – in other states? How does this practice differ in California?
5. What other related services are typically provided for students with disabilities? Do LEAs contract for other specialized “related services” for student with disabilities?
6. Do some LEAs in California provide mental health related services?
7. What benefits has the LAO identified in returning responsibility for mental health related services – as required by the federal IDEA – back to the K-12 education?
8. What are some of the transitional issues the state would need to consider in realigning the provision of mental-health related services either under the Governor’s proposal or the LAO’s proposal?
9. How does the Department of Mental Health monitor services and outcomes students with disabilities receiving mental health related services through the counties? How does the Department of Education monitor services and outcomes for these students?
10. The federal lawsuit in Los Angeles requested that CDE send a memorandum to all Local Educational Agencies (LEAs) reminding them of their responsibilities to ensure uninterrupted mental health services and assessments to special education students in compliance with IDEA, federal regulations, and AB 3632. CDE has complied with this order. How did CDE frame its responsibilities in this letter?

### **ISSUE 3. Governor’s Budget Proposal - Special Disability Adjustment**

**DESCRIPTION:** The Governor’s Budget reflects a reduction of **\$74 million** in Proposition 98 funds to reflect the repeal of the Special Disability Adjustment calculation in 2011-12, pursuant to Chapter 403, Statutes of 2010, which makes the adjustment inoperative on July 1, 2011.

**BACKGROUND:** The Special Disability Adjustment (SDA) or “incidence multiplier as it is commonly called, is a calculation that is included as a part of the AB 602 funding formula in order to account for students with high cost, low incidence disabilities.”

When AB 602 funding reforms were enacted in the late 1990s, the funding model changed from a model based upon the number of special education students to a model based upon the general school population. At that time, there was concern that the new model would not recognize the high costs for some special education students. To address that issue, AB 602 required a study to recommend a low incidence, high cost disability adjustment.

The resulting study, published by the American Institutes of Research (AIR) in 1998, recommended the creation of the incidence factor that was added to the AB 602 funding formula. That same study recommended that the formula be updated every five years.

As a result, the Legislature funded another study, published by AIR in 2003. The recommendations of this study would have made substantial changes to definitions, costs, and allocations for the incidence adjustments in place among SELPAs pursuant to the 1998 formula, which caused concerns about the new formula. In addition, there were concerns about the reliability of the data used in the updated study. As a result, the new SDA formula recommended by the 2003 AIR study was never implemented.

While the 1997 formula was clearly out-of-date, as reflected by the 2004 AIR study recommendations, there was no confidence in moving forward with the new recommendations. Instead of suspending the formula moving forward, the 1997 formula has continued since then.

According to the California Department of Education (CDE), the SDA is estimated to provide **\$70.0 million** in state Proposition 98 funds to approximately 32 of the state’s 122 Special Education Local Planning Areas (SELPAs) in 2010-11. The remaining 90 SELPAs statewide - including several large urban SELPAS (San Francisco Unified, Long Beach Unified, Stockton City Unified) receive no funding from the SDA.

In 2009-10, the state provided a total of **\$69.8 million** to these 32 SELPAs. Of this amount, Los Angeles Unified SELPA received \$22 million, San Diego City SELPA Unified received \$9 million, and Garden Grove Unified SELPA received \$6 million. Most of the remaining SELPAs—that received SDA funding had allocations of less than \$2 million.

## **2009-10 and 2010-11 Budgets Actions for SDA.**

In order to keep the original SDA formula going, it is extended annually in the budget trailer bill. In 2009-10, the budget package did not include language to continue the formula. This circumstance gave the Legislature a chance to reconsider continuation of the formula in both 2009-10 and 2010-11. As a result, the Conference Committee took action to phase out the existing SDA formula. Specifically, the Conference Committee took action to continue the existing SDA in 2009-10 and 2010-11, but to repeal the existing formula in 2011-12. This action was implemented in Chapter 403; Statutes of 2010.

The Conference Committee also approved \$300,000 in one-time federal IDEA funds for CDE to conduct a study to address questions surrounding the need for any adjustment factor in the future. The 2010-11 Budget Act (Item 6110-161-0890, Provision 38) requires CDE to contract for a study to include the following:

- 1) Summary of the extent to which incidences of severe disabilities are evenly or unevenly distributed across the state.
- 2) Determination of whether any observed differences in incidences have a significant effect on the relative costs to special education local plan areas (SELPAs) for providing special education services.
- 3) Suggested methods for adjusting the state's funding formula that do not create inappropriate fiscal incentives for identifying students as needing special education or for placing students in particular programs.

Before entering into the contract, CDE is required to work with the Department of Finance and the Legislative Analyst's Office (LAO) regarding the specific scope and design, and anticipated cost, of the study. The study is due to the Legislature by **April 1, 2011**.

CDE is continuing to work with DOF and the LAO - with input from Legislative staff - to define the scope of the study.

## **GOVERNOR'S BUDGET PROPOSALS:**

The Governor's Budget reflects a reduction of **\$74 million** in Proposition 98 funds to reflect the repeal of the SDA calculation in 2011-12, pursuant to Chapter 403; Statutes of 2010.

The Governor's Budget also proposes an increase of \$7.3 million in Proposition 98 funding in 2011-12 to reflect student attendance growth. This issue was discussed in an earlier hearing.

With this adjustment, the Governor proposes a total of \$4.1 billion for special education programs in 2011-12. This includes \$2.9 billion in state Proposition 98 funds and \$1.2 billion in federal funds authorized under the Individuals with Disabilities Education Act (IDEA).

## CDE COMMENTS:

- **Federal Maintenance of Effort Concerns.** CDE has expressed concerns that the \$74 million reduction in state Proposition 98 funds to eliminate the SDA may violate federal maintenance of effort (MOE) because it will reduce funding in 2011-12 below the 2010-11 level.
- **Revised 2011-12 SDA Estimates.** The Governor proposes a **\$74 million** reduction in 2011-12 to reflect repeal of the SDA. According to CDE, the SDA is estimated to total **\$70 million** in 2011-12. So per CDE, the Governor’s proposal overstates the amount of savings by \$4 million.

**Federal Maintenance of Effort (MOE).** Under federal IDEA, California is required to fulfill MOE requirements. These requirements generally prevent states from reducing current year state funding below spending levels for the previous year. Failure to meet these MOE requirements could result in a loss of federal funds in the amount of the MOE violation.

The IDEA allows states to apply for a waiver of MOE provisions. The U.S. Department of Education (USDE) grants such waivers when a state demonstrates that it is experiencing “exceptional or uncontrollable circumstances such as an unforeseen decline in the financial resources of the State.” Three states – Kansas, Iowa, and West Virginia – have been granted MOE waivers by USDE under these circumstances for the 2009-10 fiscal year.

The decision to grant a waiver is made on a case-by-case basis. When considering a waiver, USDE makes sure that any reduction in the level of state support for special education and related services is not greater than the percentage reduction in revenues experienced by the state, and that the state is treating special education equitably when compared to other programs within the state.

## STAFF COMMENTS:

- **Special Education Protected from Categorical Cuts to Date.** Special Education programs are among a handful of education categorical programs that have been protected from across-the-board reductions in recent years. As a result of state budget shortfalls, state categorical programs have been cut by approximately 20 percent for a five year period – 2008-09 through 2012-13.
- **State Benefitted from Substantial Influx of One-Time Federal Funds.** California received **\$1.2 billion** in ARRA one-time funds – essentially double the annual state grant amount. These funds were appropriated to the state in 2008-09 and 2009-10 and remain available through September 2011.
- **Annual Federal Funds Adjustments Helpful.** The Governor Budget reflects an estimated increase of **\$24 million** in federal IDEA grants to California grants in 2011-12. Federal

funds have increased to California in nine out of the last ten years. Increases have ranged from \$15 million to \$154 million annually.

**STAFF RECOMMENDATIONS:** Staff recommends that the Subcommittee support the Governor's proposed adjustments in 2011-12 when it takes action on the Proposition 98 package. Further analysis is needed to determine whether there is a federal MOE issue. If this is the case, other Proposition 98 savings would have to be redirected to the special education budget or the state could explore options for a federal MOE waiver.

**SUGGESTED QUESTIONS:**

1. What are CDE's specific MOE concerns with the Governor's proposal?
2. Does DOF have MOE concerns?
3. Does CDE believe that our state could qualify for a federal MOE waiver, if needed?
4. Does DOF agree with CDE's **\$70 million** estimate of the SDA reduction, rather than **\$74 million** per the Governor's proposal?

## **ISSUE 4. Governor’s Budget Proposal – Categorical Flexibility;**

### **LAO Report on School District Finance & Flexibility**

**DESCRIPTION:** The Governor proposes to extend current K-12 program and funding flexibility options for local educational agencies (LEAs) for an additional two years. This action extends most flexibility options, which became effective in 2008-09, through 2014-15.

#### **GOVERNOR’S BUDGET PROPOSAL:**

**Categorical and Program Flexibility Options.** In an effort to ease local impacts of state budget cuts, the February and July 2009 budget packages included a number of significant flexibility options intended to loosen program funding restrictions and to give school districts more control over spending decisions. Most of these flexibility options were authorized for a **five year period** -- from **2008-09 through 2012-13**. Some options had shorter timeframes. The Governor proposes to extend most of these program and funding flexibility options for local educational agencies (LEAs) by two additional years -- **through 2014-15** -- or **seven years** total, as follows:

- **Categorical Program Flexibility.** Allows LEAs to use funding from about 40 K-12 categorical programs for any education purpose through 2014-15 (seven years), instead of 2012-13, as currently authorized. Since 2008-09, funding for these categorical programs have been combined into a budget “flexibility item” and were also subject to across-the-board funding reductions. Under categorical flexibility, a district’s allocation for each program is based on its share of total program funding either in 2007-08 or 2008-09 -- with the earlier year being used for certain participation-driven programs.
- **Instructional Time Requirements.** Authorizes school districts to reduce the number of instructional days by five -- from 180 to 175 days per year -- through 2014-15 without losing longer-year incentive grants.
- **Instructional Material Purchases.** Allows LEAs to use standards-aligned instructional materials adopted prior to July 1, 2008, instead of purchasing new materials, through 2014-15.
- **K-3 Class Size Reduction (CSR).** Continues the existing reduction in penalties for not meeting the K-3 CSR requirements through 2013-14, which is one year less than the flexibility provided for most other flexibility programs. Existing penalty reductions are currently authorized through 2011-12.
- **Sale of Surplus Property.** Allows school districts to direct the proceeds from the sale of surplus property for general fund purposes through January 1, 2014, instead of 2012 per current law. Only proceeds from the sale of non-state funded property are eligible for this additional flexibility, which commenced in 2009-10.

- **Routine Maintenance Contributions.** Suspends the remaining routine maintenance reserve requirement of one percent for school districts that meet the facility requirements of the Williams settlement 2014-15. Allows remaining LEAs to reduce contributions for routine maintenance of school facilities from three percent to one percent of General Funds through 2014-15.
- **Deferred Maintenance Program Matching Requirements.** Suspends previously required General Fund set-asides for LEAs receiving Deferred Maintenance funds for school facilities through 2014-15.

**Fiscal Oversight Relief.** The Governor also proposes to continue one provision that reduces fiscal oversight for LEAs:

- **School District Budget Reserves.** Continues the authorization for districts to reduce their minimum budget reserves for economic uncertainty to one-third of previously required levels through 2011-12, instead of 2009-10 as currently required. Requires LEAs to make annual progress in restoring reserves in 2012-13, instead of 2010-11, and restores previously required reserve levels in 2013-14, instead of 2011-12.

**Flexibility Options and Fiscal Relief Not Covered by Governor's Proposal.** The Governor does not propose changes to several other flexibility options that became effective in 2008-09 as a result of the 2009 budget packages.

- **Access to Prior-Year Funding Balances.** Allows LEAs to access prior-year fund balances in 2008-09 and 2009-10 only for the following programs: Targeted Instructional Improvement Grants; Instructional Materials; California High School Exit Exam; Adult Education; ROC/P Facilities; and Deferred Maintenance. [Economic Impact Aid; Special Education; Quality Education and Investment Act (QEIA); Home-to-School Transportation; English Language Learner Acquisition and Development Pilot Program; Child Development; and Child Nutrition were protected.]
- **Federal Funds Losses.** Allows LEAS to avoid a negative or qualified fiscal certification due to a substantial loss of federal American Recovery and Reinvestment Act (ARRA) State Fiscal Stabilization Funds (SFSF) in 2011-12 and 2012-13. To ensure consistent statewide implementation, the Superintendent of Public Instruction is required to convene the Standards and Criteria Commission to modify the budget and fiscal review criteria to incorporate these changes.
- **High School Exit Exam.** Suspends the California High School Exit Exam (CAHSEE) as a requirement for student graduation for eligible students with disabilities, beginning in 2009-10, until the State Board of Education acts upon a recommendation for an alternative means of measurement for eligible students.

**Programs Excluded from Categorical Flexibility Option.** The Governor continues to exempt about 20 categorical programs from categorical flexibility. These programs include: Special Education, Economic Impact Aid, K-3 Class Size Reduction, After School Education and Safety, Home-to-School Transportation, Quality Education Investment Act, Child Nutrition, Student Assessments, Charter School Facility Grants, Year-Round School Grants, Partnership Academies, Apprenticeship Programs, Foster Youth, Adults in Correctional Facilities, County Office Oversight, K-12 High Speed Network, and Agricultural Education.

**LAO COMMENTS:** To help the Legislature in crafting its 2011-12 education budget, the LAO surveyed school districts to gather information regarding how they were affected by recent federal and state actions. Most importantly, the LAO survey responses indicated that many districts:

- (1) have reserved some federal Ed Jobs for 2011-12;
- (2) would find an additional deferral in 2011-12 more difficult to accommodate;
- (3) have benefited notably from existing flexibility provisions and desire additional flexibility; and
- (4) already have increased class sizes notably, instituted furlough days, laid off some teachers, and shortened the school year.

Given these survey findings, the LAO identifies several ways the Legislature could provide school districts with more flexibility in the short term. Even with the extra flexibility, however, many underlying problems would remain with California's system of K-12 finance. Thus, the LAO provides the Legislature with a relatively simple approach for making more lasting improvements to California's K-12 finance system.

**LAO RECOMMENDATIONS:** The LAO makes various recommendations for providing school districts with more flexibility in the short term, improving the state's K-12 finance system in the long term, and then aligning state operations with the streamlined K-12 finance system.

The LAO's recommendations are based on its survey findings as well as its ongoing assessment of the state's K-12 programs and statutory requirements. The LAO figure below summarizes these recommendations, which the LAO will discuss in more detail at the Subcommittee hearings.

- **Increase Flexibility in Short Term**
  - ✓ Remove strings tied to K-3 Class Size Reduction and Home-to-School Transportation
  - ✓ Remove strings from After School Education and Safety program by repealing Proposition 49
  - ✓ Link flex funding to students
  - ✓ Eliminate certain mandated education activities
  - ✓ Ease restrictions on contracting out for non-instructional services
  - ✓ Ease restrictions regarding pay rates and priority for substitute teaching positions
- **Improve K-12 Finance System Moving Forward**
  - ✓ Consolidate virtually all K-12 funding into revenue limits and a few block grants moving forward

- **Align State Operations With New Finance System**
  - ✓ Minimize California Department of Education's (CDE) focus on compliance monitoring
  - ✓ Refocus CDE mission on data, accountability, and dissemination of best practices

**STAFF COMMENTS:**

- **Per LAO Survey, Districts Relying Heavily on Flexibility Options.** The LAO's survey responses largely confirm that districts are relying heavily on one-time federal funds and deferrals to support more programmatic spending. However, districts also are relying heavily on categorical flexibility provisions—dismantling or significantly downsizing certain categorical programs to redirect support to core classroom instruction. Most respondents also are taking advantage of other flexibility options, such as shortening the school year, to balance their budgets. Survey responses indicate these flexibility provisions are helping districts protect certain local priorities in the midst of shrinking budgets. Per LAO, nonetheless, districts still have had to make notable programmatic reductions for example, increasing class sizes, instituting employee furloughs, and laying off staff.
- **Governor's Categorical Flexibility Proposal Locks Most Programs into 2008-09 Proportions for Seven Years.** Since 2008-09, funding for about 40 categorical programs has been combined into a budget “flexibility item” that applies to across-the-board funding reductions. Under categorical flexibility, a district's allocation for each program is based on its share of total program funding – at the reduced level – either in 2007-08 or 2008-09, with the earlier year being used for certain participation-driven programs. Under the categorical flexibility program, no growth funding is been provided for growing districts, and districts with negative growth are held harmless from any loss of funding associated with lower student attendance.
- **LAO Continues to Recommend Mandate Reforms.** In addition to removing strings attached to certain categorical programs, the LAO also continues to recommend the state eliminate certain mandated education activities. (Per the LAO, categorical programs and education mandates are very similar functionally, with the primary difference being that the state typically funds categorical programs up front whereas it funds mandates only on a reimbursement basis.) Although the state removed some requirements associated with certain K-12 mandated activities in 2010-11, the LAO recommends that additional requirements be removed in 2011-12. Specifically, in its 2009 report, *Education Mandates: Overhauling a Broken System*, the LAO highlighted 26 mandates that the state could eliminate (that have not already been eliminated), including Notification of Truancy, The Stull Act, and Intra-District Transfers. Given all other competing priorities, the LAO thinks these types of activities are lower priority and requiring districts to undertake them, particularly in this environment and potentially at the expense of other higher priority student services, makes little sense and places unneeded pressure on limited districts resources. Furthermore, the LAO continues to recommend that the state consider options for simplifying the process of funding whatever mandates it continues to require. For example,

for several of the active mandates, the state could create a block grant that would provide a standard rate to every district. In addition to simplifying the mandate finances system for districts and the state, a block grant approach would help reduce the notable inequities in the amounts districts now receive for performing the same mandated services.

**STAFF RECOMMENDATIONS:** Staff makes the following recommendations as the Subcommittee considers its decisions on the Proposition 98 package.

- **Support Extension of Program and Funding Flexibility Options Proposed by Governor in Short Term.** The Governor’s proposal to extend most of the current flexibility options for two years provides extended flexibility for LEAs as they make budget plans in the short term. The Governor’s proposal provides an important and timely signal to LEAs.
- **Support Additional Short Term Actions per LAO.** The LAO has suggested a few additional flexibility options that the LAO believes would give districts more tools to address immediate budget shortfalls, they also represent policy changes that would benefit districts in any fiscal climate. Moreover, taking these actions now will set the foundation for comprehensive improvements to the state’s education finance structure moving forward..
- ✓ **Add K-3 CSR and Home-to-School Transportation Programs to Flexibility Program.** Per LAO, K-3 CSR and HTS transportation are strong candidates to be placed in the flex program based upon their recent survey of school districts. More than 60 percent of school districts support additional flexibility for these two programs. The Senate took this action last year which was also supported by the LAO’s district survey findings at that time.

For K-3 CSR, the LAO believes the current funding structure is only tenuously linked to the underlying policy objectives. That is, most districts are no longer meeting the program’s central policy objective -- to reduce K-3 classes to 20 or fewer students.

For HTS transportation, the LAO notes that the existing funding structure is widely recognized as antiquated and unfair -- resulting in district funding allocations that are very poor reflections of district’s current underlying needs. The existing HTS formula also contains a “use it or lose it” provision that discourages districts from implementing more cost-effective practices, as decreasing costs in one year means losing funding.

- ✓ **Adopt LAO Recommendation to Link Flex Funding to Students in the Short Term.** Regardless of which specific programs are included in the flex item in 2011-12, the LAO recommends that the Legislature modify the methodology used to allocate flex-item funding to school districts. Specifically, the LAO recommends the Legislature develop a per-pupil rate for each district by dividing the amount it received for all flexed programs in 2010-11 by its total ADA. Linking this funding to students would help create a rational basis for making future funding adjustments per the LAO. If the Legislature chose to streamline its education finance system, the LAO believes transition

to such a system also would be less disruptive if most existing state funding already were linked to students and adjusted annually according to changes in the student population.

- **Begin Work with Administration to Develop Options for School Finance Reform in the Long Term per LAO Recommendations.** While the Governor attempted partly to address this issue by extending the flexibility provisions two years, the LAO believes the state needs a more definitive exit strategy. That is, the LAO thinks this is an opportune time for the state to rethink its overall K-12 finance system and craft a better system. Rather than extend current categorical flexibility for two more years, the LAO recommends that the Legislature improve the state's K-12 finance system on a lasting basis. Regarding a new finance structure, the LAO recommends the Legislature consolidate virtually all K-12 funding into revenue limits and a few block grants. Unlike the current flex item, a few block grants would provide flexibility while also allowing more opportunity for the state to ensure that at-risk and/or high-cost students continue to receive the services they need.

#### **SUGGESTED QUESTIONS:**

1. Can the LAO clarify its recommendations for categorical reform in the short term and long term? What kind of process does the LAO envision?
2. In the short term, does the LAO have any concerns about the Governor's proposal to allow LEAs to retain lower reserves for economic uncertainty for an additional two years?
3. As a part of its survey, did the LAO determine if the public hearing and expenditure reporting provisions of the categorical flexibility statute were being implemented?

## **ISSUE 5. Federal Striving Readers Program (Information Only)**

**DESCRIPTION:** The California Department of Education will provide an update on the development of a State Literacy Plan so that our state may soon compete for discretionary funds from a new federal grant program – the Striving Readers Comprehensive Literacy Program. If successful, CDE estimates California could receive up to \$50 million for this new program in 2010-11 or 2011-12.

### **BACKGROUND:**

The Striving Readers Comprehensive Literacy (SRCL) program is authorized as part of the Federal Fiscal Year (FFY) 2010 Consolidated Appropriations Act, which provides **\$250 million** for the program. The SRCL program provides state **discretionary grants** for the purpose of creating a comprehensive literacy program to advance literacy skills, including pre-literacy skills, reading, and writing, for students from birth through grade 12, including limited-English-proficient students and students with disabilities.

Of the \$250 million provided in FFY 2010, **\$10 million** is reserved for **formula grants** to assist states in creating or maintaining a State Literacy Team with expertise in literacy development and education for children from birth through grade 12 and to assist States in developing a comprehensive literacy plan.

### **Formula Grants for Comprehensive Literacy Plan.**

SRCL formula grants provide funds to states for development of comprehensive literacy plans that must address the needs of children from birth through grade twelve. The plans must also improve alignment and transition between grades. In addition, plans should include key components of an effective state literacy system, including clear standards; a system of assessments to inform instruction; guidance on the selection and use of curriculum and interventions; teacher preparation and professional development aligned with standards; and a system of data collection, evaluation, and program accountability.

The California Department of Education (CDE) California has received **\$841,000** in 2010-11 in SRCL formula grant funding to support a State Literacy Team and to develop a comprehensive literacy plan for children from birth through grade 12.

These funds were authorized in January 2011 through a Department of Finance (DOF) Section 28.00 Budget Act Letter. According to the Budget Letter request, the team will be comprised primarily of literacy development and education experts for children from birth through grade 12, the majority of whom will be local representatives. The literacy plan will be reviewed by the State Board of Education (SBE) prior to the submittal of the plan to the US Department of Education (USDE) no later than March 16, 2011.

In its concurrence with the DOF Section Letter request, the Joint Legislative Budget Committee (JLBC) requested that CDE provide the State Literacy Plan to the JLBC and legislative policy

committees when the plan is submitted to the SBE for review or by March 1, 2011, whichever is earlier.

The CDE reported last week that USDE has extended California's deadline for submitting the State Literacy Plan from March 16, 2011 to April 1, 2011. (The original deadline was February 1, 2011.)

### **Discretionary Grants.**

Discretionary grants will be awarded competitively to State Educational Agencies (SEAs) that must sub-grant at least 95 percent of the funds to Local Educational Agencies (LEAs) and early childhood providers.

Entities eligible for SRCL Discretionary subgrants are LEAs or other nonprofit providers of early childhood education that partner with a public or private nonprofit organization or agency with a demonstrated record of effectiveness in improving the early literacy development of children from birth through kindergarten entry and in providing professional development in early literacy.

States must give priority to LEAs and other entities serving greater numbers or percentages of disadvantaged children.

Funds will be used by LEAs and other entities for services and activities that have characteristics of effective literacy instruction through professional development, screening and assessment, targeted interventions for students reading below grade level and other research based methods of improving classroom instruction and practice for all students.

Of the SRCL discretionary grants, subgranted funds to LEAs and other eligible entities:

- 15 percent of funds shall be used to serve children from birth through age 5;
- 40 percent of funds shall be used to serve children in kindergarten through grade 5; and
- 40 percent of funds shall be used to serve students in middle and high school including an equitable distribution of funds between middle and high schools.

The USDE will consider each state's comprehensive literacy plan as part of the SRCL discretionary grant program application. The USDE expects that applications for the discretionary grant program will be available in early 2011 and will be due back in spring 2011.

Per USDE, total discretionary grant awards for the FFY 2010 appropriation will range from **\$10 million to \$50 million per state**, with average grants estimated at \$30 million per state. CDE estimates that California will be eligible for the maximum grant level of **\$50 million**. The continuation of discretionary grant awards will be dependent on future federal appropriations.

### **STAFF COMMENTS:**

- **Lessons Learned from Reading First.** The Striving Readers program is the President's new federal reading initiative. The Reading First program was another federal reading program

initiated during the Bush Administration. The state’s Reading First plan was developed and submitted to the U.S. Department of Education without input from the Legislature. As a result the Legislature had several concerns with the program and – against the recommendation of CDE in some cases – took a number of budget actions over the years to correct these problems.

- **Maximize Participation of Eligible Districts and/or Schools Statewide.** Approximately half of the eligible school districts never participated in the program. Some of the reasons for limited participation included, funding restrictions for services covered, grant extensions – beyond the original timeframe – for the original grantees, which limited access to new districts;
  - **Ensure Access for English Learners.** When Reading First was first implemented, the State Board of Education determined that bilingual education programs were not eligible for Reading First grants because of the higher hourly English Language Arts requirements for programs. The Legislature took action by allowing “waivered classrooms” to participate in the program.
  - **Ensure Access for Students with Disabilities.** The Reading First program limited participation to core curriculum teachers and excluded special education teachers, despite the specific mention of special education teachers in the federal law. A Special Education Pilot Program was added by the Legislature in 2007-08.
  - **Allow Funds to Be Used More Flexibly To Improve Reading, Most Notably for Direct Services.** Reading First focused upon teacher training, and did not allow funds to be used for direct instruction for students. Some districts that chose not to participate cited onerous program requirements and an overly restrictive, top-down program design as reasons for not applying.
  - **Ensure Transparency About Program Participation and Outcomes.** The Legislature had trouble accessing basic information about Reading First, such as the number and type of teachers participating and student outcomes. This was due in part to the decentralized governance structure that involved implementation centers and six regional lead agencies.
- **Collaboration Needed.** To avoid the problems of the past, it will be important for the State Board and CDE to work together and to engage with the Legislature on the development of the comprehensive reading plan and the subsequent proposal for a Striving Reader’s discretionary grant proposal. This new federal program could make substantial, new funding available for a statewide literacy program to address struggling readers – birth to grade 12 – in our state.

#### **SUGGESTED QUESTIONS:**

1. Has the State Board officially selected the State Literacy Team for the Striving Readers Program? If so, how were members of the State Literacy Team selected?

2. Will the State Literacy Team work from a preliminary plan or framework and if so can the Administration or CDE share the components of that framework?
3. Will the plan allow direct reading instruction? If so, how will the plan identify struggling readers for purposes of services?
4. How will the plan maximize allocation of funding to LEAs? Will funds reach all eligible LEAs? The Reading First program diverted funds to Regional Assistance Centers. Will this approach be utilized again?
5. How will the State Literacy Plan ensure access for English learner students?
6. How will the State Literacy Plan ensure access for students with disabilities?
7. Does CDE have an update on the timeframe for the competitive implementation grant? When will the application be available and when will it be due back?
8. If California is successful in securing competitive implementation grant funds, when will those funds arrive? In what state fiscal year?
9. What is the outlook at the federal level for continued SRLB appropriations?