Senate Budget and Fiscal Review—Mark Leno, Chair

SUBCOMMITTEE NO. 1 Agenda

Senator Carol Liu, Chair
Senator Ted Gaines
Senator Roderick Wright

Monday, April 9, 2012
Noon
Room 112, State Capitol

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Background. The CCC are publicly supported local educational agencies that provide educational, vocational, and transfer programs to approximately 1.2 million full-time equivalent students. The CCC system is the largest system of higher education in the world, with 72 districts, 112 campuses, and 71 educational centers. In addition to providing education, training, and services, the CCC contributes to continuous workforce improvement. The CCC also provides remedial instruction for adults across the state.

Figure 1: CCC Resident FTES Enrollment, Core Funding, and Fees

	2007-08 Actual	2008-09 Actual	2009-10 Actual	2010-11 Actual	2011-12 Estimated	2012-13 Proposed	Amount Change from 2007-08	% Change from 2007-08
Enrollment	1,182,627	1,260,498	1,258,718	1,230,649	1,181,792	1,158,156	-24,471	-2%
Core Funds								
GF	$4,272.2	$3,975.7	$3,735.3	$3,994.0	$3,276.7	$3,740.2	-$532.	-12%
Fees	281.4	302.7	353.6	316.9	353.9	359.2	77.7	28%
LPT	1,970.8	2,028.8	1,992.6	1959.3	2,107.3	2,101.1	130.3	7%
ARRA			35.0	4.0	0.0		0.0	NA
Lottery	168.7	148.7	163.0	172.8	178.6	178.6	9.9	6%
Total	$6,693.1	$6,455.9	$6,279.6	$6,447.0	$5,916.4	$6,379.0	-314.0	-5%
Fees[1]	$600.00	$600.00	$780.00	$780.00	$1,080.00	$1,380.00	$780.00	130%

[1]Fee totals for a full-time student taking 30 units in an academic year.
Source: Legislative Analyst's Office

THE GOVERNOR'S LONG-TERM PLAN FOR THE CCC

Similar to its plan for UC and CSU, which was discussed at the Subcommittee's March 15 hearing, the Administration's long-term plan for the CCC is rooted in the belief that higher education should be affordable and that student success can be improved. The Administration proposes stable and increasing state funding and fiscal incentives to allow the CCC to better manage its resources. The significant components are:

1. *Affordability*. The plan will curtail tuition fee increases and lessen the pressure for students to take out loans.
2. *Student Success*. The plan will make annual GF augmentations contingent upon the CCC achieving the Administration's priorities or performance targets, including successful basic skills course completion.
3. *Stable Funding Source*. The state will increase its GF contribution annually by a minimum of four percent per year, from 2013-14 through 2015-16, contingent upon the passage of the Governor's tax initiative in November 2012.
4. *Flexibility*. The plan will provide additional flexibility to CCC districts in how they spend their funds, to direct resources based on what is needed locally to achieve student success, by: (a) consolidating categorical programs and providing increased flexibility on the expenditure of those funds; (b) reforming mandates; and (c) repealing the current statutory funding model for apportionments.

Should the Governor's tax initiative be rejected by the voters, the CCC budget would be reduced mid-year as part of an overall $4.8 billion K-14 Proposition 98 reduction, as follows: (1) $218.3 million in apportionment funding would again be deferred (returning the total inter-year deferral to $961 million) and (2) there would be a $292 million programmatic reduction.

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Item 1: 2011-12 Budget Issues

Governor's Budget Proposal. The January budget requests a reduction of $146.9 million in 2011-12 GF apportionment funding to reflect an identical increase in offsetting local property taxes available to CCC districts resulting from the California Supreme Court decision to eliminate redevelopment agencies (RDA). The Administration has requested early action, by March 2012, to ensure the savings can be achieved.

Additional Current Year Emerging Issue. The CCC currently reports an unanticipated current year deficit of $149 million, due to lower than anticipated enrollment fee revenue collections ($107 million) and local property tax receipts ($41 million). This translates to a deficit of 2.75 percent less funding per student.

The CCC indicate that the contributing factors to the fee revenue shortfall are the economy and increased eligibility for Board of Governor's (BOG) Fee Waivers (the BOG Fee Waiver program is discussed further as Agenda Item 6).

Background. Apportionment funding, which CCC districts use for general purposes, comes from three main sources: (1) enrollment fee revenues; (2) local property taxes; and (3) the GF, with local property taxes and the GF accounting for CCC's funding under Proposition 98. The enacted budget assumes a specified amount of fees and property taxes that will be collected and retained by CCC that year. The assumption about fee revenue is based on estimates of the number of students who will pay fees and the number of students who, because of their financial need, will receive a BOG Fee Waiver. Based on these estimates, the enacted budget provides the necessary GF support to meet the system's apportionment amount.

When systemwide fee revenues or local property tax receipts fall short, the total amount of apportionment funding available to CCC districts that year similarly falls short. Unlike K-12, there is no automatic mechanism to backfill a CCC shortfall. Therefore, the CCC system must contend with lower total funding that year unless the Legislature and Governor decide to provide a GF backfill. Regardless of whether a backfill is provided, the following year's budget assumption of fee or local property tax revenues is adjusted to reflect the underestimate so that the shortfall does not carry forward.

Staff Comment. The initial CCC concerns with the January budget RDA-related property tax proposal centered on: (1) the estimate of the increased property tax revenues and (2) the likelihood that those revenues would materialize in the current year. Since the release of the January budget, staff has gained a better understanding of the Administration's estimates on the RDA-related local property tax revenues. It is a reasonable expectation that there will be increased property tax revenues in the current year (and ongoing) from the elimination of RDAs. There is still uncertainty, however, which explains the CCC concern with this proposal, especially in light of the fact that there is not an automatic GF backfill if these RDA-related property tax revenues fail to materialize in the current year.

With regard to the current year emerging issue, it appears that the current year fee revenue estimate, which was based on an assumption of a 52 percent waiver rate, was too conservative. The current year fee waiver rate is now estimated at 63 percent of credit courses. The Administration does not propose a GF backfill. Staff generally agrees with the Administration that it is premature to act on the current year emerging issue, given that a revenue update will be provided at the time of the May Revision. Further, in past years local property tax revenues have self-corrected and, in some years, self-corrected enough to make-up some or all of a fee revenue shortfall. Absent a backfill, the Chancellor's Office has indicated that any resulting deficit, once revenue numbers are updated as part of the May Revision, would be spread across all districts statewide. To balance budgets, districts would have to reduce costs, such as cancelling summer school or spending from reserves.

Given these two issues, and their interactions, the CCC have a legitimate concern. Should the Legislature: (1) adopt the January budget RDA-related local property tax proposal and (2) not provide a backfill of the emerging current year issue, and then should these revenues not materialize in part or full, the CCC could be looking at up to a $296 million shortfall in the current fiscal year.

Finally, staff notes that absent any action on the part of the Legislature on the January budget proposal, CCC districts will begin receiving RDA revenues through the traditional AB 8 property tax shares. These revenues will be additional for the districts. By allowing CCCs to keep these RDA-related revenues, the emerging current year issue shortfall would be addressed in some amount. However, not adopting the January budget proposal creates a $146.9 million "hole" in the overall budget architecture.

LAO Recommendation. The LAO agrees with the need to adjust the CCC 2012-13 budget with accurate assumptions about fee revenues. The significant increase in the number of fee waivers over the past few years, however, raises questions about the BOG Fee Waiver program. *Note, please see Agenda Item 6 for further LAO recommendations on the BOG Fee Waiver program.*

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. Does the Administration or the Chancellor's Office have more updated current year enrollment fee revenue and local property tax projections?
2. Is the RDA-related increased local property tax estimate still $146.9 million?
3. Recent past history indicates that the current year shortfalls attributable to local property tax self-correct. What is the likelihood of that occurring this year?

Staff Recommendation. Staff recommends that this issue be held open, pending the May Revision.

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Item 2: LAO Overview of Major CCC Proposition 98 Budget Changes

Description (Informational Item). The LAO will provide a brief overview of the major changes proposed for CCC Proposition 98 spending in the current and budget years.

Figure 2: Governor's CCC Proposition 98 Budget Proposal (Dollars in Millions)

2011-12 (Enacted)	**$5,414.6**
Trigger cuts	-102.0
Technical adjustments	$11.8
2011-12 (Revised)	**$5,324.4**
Restore one-time actions	$129.0
Pay down prior-year deferrals	218.3
Adjust for revised fee-revenue estimate	97.4
Create CCC mandates block grant	12.5
Adjustment for Financial Aid Administration	14.3
Technical adjustments	-12.2
2012-13 Proposal	**$5,783.6**
Change from 2011-12 Revised Budget	
Amount	$459.2
Percent	8.6%

Source: Legislative Analyst's Office

Figure 2 above summarizes the changes proposed for CCC Proposition 98 spending in the current and budget years, including the $102 million reduction in the 2011-12 funding level as a result of the January 2012 trigger cuts. The January budget proposal for 2012-13 (which assumes voter approval of the Governor's tax initiative in November 2012) would increase Proposition 98 funding for CCC to $5.8 billion, which is $459 million (8.6 percent) over the revised current year level. This net augmentation includes:

- ✓ A technical adjustment of $129 million, which restores base funding to CCC following a prior-year deferral.
- ✓ An increase of $218 million to pay down existing CCC deferrals.
- ✓ A base increase of $97 million to account for lower-than-expected fee revenues in the current year.
- ✓ An increase of $12.5 million to create a proposed CCC mandate block grant.
- ✓ A workload adjustment of $14.3 million for CCC financial aid programs.

Under the January budget proposal, 2012-13 apportionment funding would total $5.3 billion, which reflects an increase of $432 million, or 9 percent, from the revised current-year level. The Governor's budget would increase total funding for categorical programs by $14.3 million. As proposed by the Governor, the CCC would receive 11 percent of total Proposition 98 funding in 2012-13.

Finally, the January budget proposal maintains the current fee increase, effective summer 2012, whereby fees will increase from the current $36 per unit to $46 per unit. The January budget proposes no additional changes to the fee level in 2012-13.

Staff Recommendation. None; this is an informational item.

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Item 3a: Flexibility Proposals – State Mandates

Governor's Budget Proposal. To provide school and CCC districts with new flexibility, the January budget proposes to: (1) eliminate a number of existing K-14 mandates and (2) provide $200 million for a new optional block grant to fund the remaining mandated activities. Of the total block grant funding provided, $22 million is for CCC districts, providing participating districts with an estimated $20 per student. The January budget proposal allows districts to choose either to participate in the block grant or to submit mandate claims through the reimbursement process (districts would be prohibited from doing both.)

Figure 3: Governor's CCC Mandate Proposal

Mandates Suspended in 2012-13; Intent to Eliminate in 2013-14	
Active	**Suspended**
Absentee Ballots	Grand Jury Proceedings
Agency Fee Arrangements	Health Benefits for Survivors of Peace Officers and Firefighters
Mandate Reimbursement Process	Integrated Waste Management
Threats Against Police Officers	Law Enforcement Jurisdiction Agreements
Health Fees/Services	Sexual Assault Response Procedures
Reporting Improper Governmental Activities	Student Records
Mandates in Block Grant	
California State Teachers Retirement System Services Credit	Prevailing Wage
Collective Bargaining	Sex Offenders: Disclosure Requirements
Open Meetings/Brown Act	Enrollment Fee Collection and Waivers
Cal Grant Grade Point Average	Tuition Fee Waivers

Source: Legislative Analyst's Office

With regard to the Health Fees/Services mandate, which only applies to CCC districts that provided health services in fiscal year 1986-87 and required them to maintain that level in 1987-88 and ongoing, the January budget proposes budget trailer bill language to eliminate the mandate and instead allow students the choice (via a vote) on whether they want to have health centers and to what extent.

Background. In 1979 voters passed Proposition 4, which added a requirement to the California Constitution that local governments be reimbursed for new programs or higher levels of service the state imposes on them. Currently, the state has about 50 K-14 education mandates, with each mandate requiring school districts and/or community colleges to perform as many as a dozen specific activities. The 2011-12 budget included $90 million for these claims. The state went seven consecutive years (2003-04 through 2009-10) making only negligible mandate payments. As a result, a backlog of unpaid K-14 claims has developed that now totals an estimated $3.6 billion. The state has a constitutional obligation to pay off this backlog. Moreover, in December 2008, a superior court found the state's practice of deferring education mandate payments unconstitutional and ordered the state to fully fund mandated programs "in the future." While constitutional separation of powers means the court cannot force the Legislature to make appropriations for past mandate costs, its decision increases pressure on the state to pay its mandate obligations.

Staff Comment. Mandate reform is not a new concept, as concerns with the costs of mandates have prompted prior legislative action. Most recently, these actions included suspending about a dozen local education mandates. In addition, the 2010 Budget Act included statutory changes to reduce the costs of several K-12 mandates, requested that the Commission on State Mandates reconsider the collective bargaining mandate, and required the LAO to convene a working group to consider the future of K-14 mandates. However, the depth and breadth of the January budget proposal goes well beyond these prior efforts.

The full Senate Budget and Fiscal Review Committee held a February 16 hearing focused on the K-12 aspects of this proposal. This Subcommittee is currently scheduled to again consider the K-12 proposals at its April 26 hearing.

Staff notes that mandate reform has been of greater controversy on the K-12 level. In fact, the LAO work group on education mandates achieved notable agreement and developed a generally comprehensive CCC mandate reform package. Further, what state mandates are eliminated, suspended, funded through the block grant, or maintained is a policy choice; the Administration has presented its policy choices in this proposal.

LAO Recommendation. The Administration's proposal addresses several mandate problems, but also raises some concerns. Most notably, the proposal still allows districts to file claims. This means that the problems with the current claims system could continue and costs could increase if some districts receive more funding by filing claims than they otherwise would through the grant. The proposal also does not address certain out-year issues. For example, it is unclear how block grant funding might change in the future, and whether new mandates would be included in the block grant. The LAO recommends that the Legislature adopt the proposed block grant approach, but modify the proposal so that districts cannot file mandate reimbursement claims. In addition, the LAO recommends that the Legislature establish a working group to: (1) review the list of K-14 mandates proposed for elimination and (2) address remaining implementation details.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. Is the Administration proposing any further modifications to its K-14 mandate proposal?
2. This proposal captures all existing mandates; however, there are a number of potential mandates in the pipeline. How does the Administration propose to address new mandates?
3. Is this proposal contingent on ballot outcomes, or is it proposed regardless of the outcome of the fall election?

Staff Recommendation. Staff recommends that this issue be held open, pending the May Revision.

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Item 3b: Flexibility Proposals – Categorical Programs

Governor's Budget Proposal. To provide CCC districts with new flexibility, the January budget consolidates nearly all categorical programs and permits CCC districts to use the "flexed" categorical funds for any general operating cost. The "flex" item would total $378.4 million, which is the sum of 2011-12 funding level for the included programs plus a proposed $14 million workload adjustment in 2012-13.

The categorical programs excluded from the "flex" item are: (1) Foster Care Education Program ($5.3 million) and (2) Telecommunications and Technology Services ($15.3 million). The Disabled Students Programs and Services categorical is partially excluded; i.e., $12.6 million of the $69 million in total funding is excluded from the "flex" item.

Background. The state provides two primary types of funding to the CCC system: (1) apportionments, which are intended to fund CCC basic operating costs (such as employee compensation, utilities, and supplies); and (2) categorical programs, which collectively support a wide range of supplemental activities that the state views as critical statewide priorities, including for child care, support services for underprepared students, and financial aid advising, among others. In 2011-12, the CCC received about $5.4 billion in apportionment funding and $397 million in categorical funding.

The 2009 Budget Act reduced ongoing Proposition 98 GF support for categorical programs by $263 million (about 37 percent). To help districts better accommodate the reduction, the 2009 Budget Act combined over half of CCC categorical programs into a "flex" item. Through 2014-15, districts are permitted to use funds from categorical programs in the flex item for any categorical purpose. By contrast, funding for categorical programs that are excluded from the flex item must continue to be spent on specific associated statutory and regulatory requirements.

Figure 4: CCC Categorical Flexibility

Programs Currently Included in the "Flex Item" ($113 million)	
Academic Senate	Part-Time Faculty Compensation
Apprenticeship	Part-Time Faculty Health Insurance
Campus child care support	Part-Time Faculty Office Hours
Economic and Workforce Development	Physical Plant and Instructional Support
Equal Employment Opportunity	Transfer Education and Articulation
Matriculation	
Programs That Would Be Added to the "Flex Item" ($298 million)	
Basic skills initiative	Financial Aid Administration
CalWORKs student services	Foster Care Education Program[1]
Career Technical Education Pathways	Fund for Student Success
Extended Opportunity Programs & Services	Nursing Grants

[1]The January budget proposes to partially protect funding for this categorical program.
Source: Legislative Analyst's Office

Staff Comment. The current categorical flex item is in place through 2014-15. This spring the Legislature will receive a report from the CCC Chancellor's Office detailing the degree to which CCC districts have utilized the flex item in the current year. The 2010-11 report indicated that 32 districts exercised the flexibility and a total of $1.1 million was shifted. The Part-Time Faculty Compensation categorical program represented about 87 percent of the funds shifted; Apprenticeship was the second most shifted funds, with a total of $70,000 shifted (seven percent of the funds moved). The two categorical programs receiving the bulk of the transferred dollars were Matriculation and Disabled Students Programs and Services.

The Governor's proposal goes quite a bit farther than the current "flex" item, in that it would flex 90 percent of all of the categorical funds and authorize their expenditure for any purpose. This approach would completely negate current assurances that these dollars will be spent on identified state priorities. Districts could continue to spend the flexed funds on categorical programs, but they would not be required to do so.

Categorical programs do have drawbacks. For instance, the program parameters and requirements are quite prescriptive and do not necessarily allow CCC districts to meet their student and local resource needs. Categoricals are also costly to administer. However, given that the state is only in the third fiscal year of providing categorical flexibility, the Subcommittee may wish to consider the degree to which the current flex item is working as intended before proceeding full throttle to cut all strings to the funding and on a permanent basis as proposed by the Administration.

LAO Recommendation. CCC districts would benefit from more categorical flexibility. However, the Governor's approach could result in local decisions that undermine the Legislature's original intent for these funds. The LAO has identified two alternatives for the Legislature to consider, both of which would enhance local flexibility while still ensuring that categorical funds are spent on support services for students and faculty. The first option is a more limited version of the Governor's flex item, by including statutory language that limits spending to existing categorical program purposes. The second option is to consolidate 15 categorical programs into two block grants, one centered on student success and one on faculty support. This option would exclude six programs, including the three the Governor proposes to protect, because they serve various unrelated and specialized purposes.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. When can the Legislature expect the next report on the current flex item? Is there any advance information available as to district usage levels?
2. What explains the low rate of usage of the current flex item in the 2010-11 year? Is this a function of programs already up and running, or contracts being signed, all of which would limit a district's ability to participate? Or is it because districts do not want this type of flexibility?
3. Is the January budget proposal contingent on ballot outcomes, or is it proposed regardless of the outcome of the fall election?
4. Please explain the approach to exclude only $12.6 million of the $69 million provided in 2011-12 for the Disabled Students Programs and Services.

Staff Recommendation. Staff recommends that this issue be held open, pending the May Revision.

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Item 3c: Flexibility Proposals – Apportionment Funding Methodology and Enrollment

Governor's Budget Proposal. To provide CCC districts with new flexibility, the January budget proposes significant changes to how funding is allocated to CCC districts, by repealing the current statutory funding model for apportionments which is based primarily on student enrollment. In its place, the budget specifies that CCC GF monies in 2012-13 will be allocated to districts on the same proportionate share that districts received in 2011-12. However, the CCC Chancellor's Office may deviate from this new methodology if it develops an alternative that is approved by the Board of Governors and Department of Finance.

Background. For years the amount of general purpose or "apportionment" funding the state provided for each credit FTE student varied considerably by CCC district. This was due to tax base differences that predate Proposition 13 (1978), coupled with complex district allocation formulas. In 2004-05, the Legislature began providing funding toward the goal of "equalizing" district funding within three years. The 2006 Budget Act included the final installment of monies to fully achieve the goal that at least 90 percent of statewide CCC enrollments receive the same level of funding per credit FTE student.

Along with providing funds to equalize districts, Chapter 631 (Statutes of 2006; SB 361) changed the method for allocating apportionment funds to districts to ensure that district funding remained equalized in subsequent years. Chapter 631 replaced the program-based funding system, under which districts did not receive equal funding rates on a per-FTE student basis (instead allocations were influenced by such items as headcount enrollment and total square footage of district facilities). Under Chapter 631, virtually all CCC districts are provided with apportionment funding at the same amount per credit FTE student.

Currently, the annual budget drives statutory formulas and calculations which result in enrollment targets for each of the state's 72 CCC districts. The amount of apportionment funding received by each district depends on the number of students it enrolls, up to (but generally not beyond) that enrollment target. Although not specifically included in the annual budget act, an overall enrollment target for the entire CCC system is calculated by the Department of Finance.

Staff Comment. Chapter 631 was the result of roughly four years of work and was in response to a critical mass of CCC districts expressing discord with the program-based funding model. The January budget eliminates the Chapter 631 FTES model. In its place, funding will go out on a proportionate basis to what districts received in 2011-12 or under a yet-to-be identified alternative methodology.

Given that it took roughly four years to develop and adopt the current FTES model, it is not clear to staff that it is feasible that a new methodology would, or could, be ready by the start of the 2012-13 fiscal year. Effectively this means that 2012-13 funding will go out on a proportionate basis to what districts received in 2011-12. This approach steps backward to the old model of un-equalized funding; i.e., the funding will be allocated in 2012-13 without regard to, for instance, district-level enrollment changes.

The Administration has stated that it would theoretically be an option for the Chancellor's Office to conclude that retention of the current FTES model is the best approach. However, given that the Administration effectively rejected that model in the January budget, it is not clear to staff that this is actually a feasible option.

This is not to say that the current FTES model is without flaws – it creates an incentive to enroll in, as opposed to complete classes, and for students to take any class as opposed to the classes needed to progress to a degree or a certificate. The reality is that there are positives and negatives with any allocation methodology, and it is naive to think that such a significant change can happen quickly and outside the policy arena. Further, the budget provides the Administration with veto power on any alternative methodology and does not provide a role for the Legislature should the Chancellor's Office develop such a methodology.

Finally, the Administration indicates this proposal is similar to its approach with UC's and CSU's budget, in that the intent is to provide CCC districts with maximum flexibility. While the CCC is a higher education system, the CCC has a K-12 governance structure with 72 local districts, each with its own elected board members. In addition, there are separate statutory requirements dictating expenditure levels on faculty salaries and the percentage of full-time versus part-time faculty that restrict budgetary flexibility. It is not readily clear how the UC and CSU model can apply to the CCC reality without major structural and statutory changes that are not part of the January budget proposal.

LAO Recommendation. The LAO recommends that the Legislature reject the proposed trailer bill language to decouple CCC funding from enrollment.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. Will the Administration be proposing additional budget flexibility measures for the CCC system?
2. SB 361 was developed over a four year period. It is unclear there is sufficient time for a new model to be developed in time for implementation in the 2012-13 year. On the K-12 side, the Administration is proposing a similar type of reform, yet the new formula is phased-in over a period of several years. Why the rush to a new allocation formula on the CCC side?

Staff Recommendation. Staff recommends that this issue be held open, pending the May Revision.

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Item 4: 2012-13 Budgetary Triggers

Governor's Budget Proposal. The January budget relies on revenue from a tax package to be placed before voters in November 2012. In the event voters reject that plan, the January budget proposes a number of automatic reductions ("trigger cuts") to GF appropriations, primarily in the areas of Proposition 98 and the universities, which would take effect January 1, 2013.

The midyear trigger cuts would reduce the CCC's Proposition 98 funding level by about $249 million to $5.5 billion. Of that reduction, $218 million would be achieved by abandoning the proposal to buy down CCC's deferral "credit card." This would have no programmatic impact on CCC. The remaining reduction would come in the form of $30 million in yet-to-be determined programmatic cuts (either to apportionments, categorical programs, or a combination of the two). Under this proposal, the 2012-13 Proposition 98 funding level for CCC would technically be $5.5 billion. On a *programmatic basis*, however, community colleges would be cut more deeply. This is because the Governor's proposed trigger actions also include shifting responsibility for the funding of CCC's general obligation bond debt service obligations to Proposition 98. Currently, CCC's annual general obligation bond debt service payments are covered by non-Proposition 98 General Fund monies. Shifting $262 million of payment obligations into Proposition 98 would have the effect of displacing a like amount of CCC programmatic funds. Taken together, CCC's midyear programmatic cuts would total $292 million.

Prior Budgetary Triggers. The 2011 Budget Act included $102 million in reductions for the CCC to be triggered if estimates of state revenues as of December 2011 were below the forecasted amount. This trigger was pulled effective January 1, 2012.

Staff Comment. Should the voters reject the Governor's tax initiative, the "trigger" reductions for the CCC would total $292 million. All of these reductions would come at the end of the fall semester, making the reductions so disruptive that the CCC likely would feel compelled to adopt budgets assuming the reductions will happen. However, taking this approach in 2012-13 will be even more challenging for the CCC. After years of reduced state funding, it is appropriate to question what budgetary levers actually remain for districts in planning for further reductions.

LAO Recommendation. Given that a significant portion of the Governor's revenue assumptions is subject to voter approval in November, it makes sense to include a contingency plan in the event voters reject the tax proposal. However, the Legislature has choices as to how the contingency plans are structured. For example, the Governor places almost all the trigger cuts in K-14 education and higher education. The Legislature could instead allocate the cuts differently among the state's education and non-education programs. For example, the cuts could be targeted to programs most able to respond to a mid-year reduction, or they could be spread across more programs to reduce their impact on any one program. In the alternative, the Legislature could instead take the opposite approach: build a budget that does not rely on the Governor's tax package, with contingency augmentations if the tax package is approved.

Given the potential for mid-year trigger cuts and the high likelihood that districts are building budgets assuming the lower funding level, the Legislature should give districts some tools to help mitigate the effect on education programs. The LAO recommends that these tools be part of the initial budget package and effective beginning July 1. For the CCC, the Legislature should consider: (1) removing additional categorical and mandate requirements (beyond current-law requirements); (2) suspending the requirements on the number of full-time faculty that districts must employ; (3) modifying the 50 percent law (which requires districts to spend at least 50 percent of their general operating budget on compensation for in-classroom faculty) to include expenditures on counselors and librarians or suspending the law for one year; and (4) allowing for a special post-election layoff window.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following question:

1. Does CCC budget planning for 2012-13 take into account the possibility of trigger cuts? If so, how? If not, how would districts accommodate mid-year trigger cuts in December 2012?

Staff Recommendation. Staff recommends that this issue be held open, pending the May Revision.

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Item 5: Accountability and Annual Increases – A New "Funding Agreement"

Governor's Budget Proposal. A central component of the Governor's long-term plan for higher education is a new funding agreement in years 2013-14, 2014-15, and 2015-16, committing to a minimum four percent annual base budget increase for the CCC, contingent upon the passage of the Governor's tax initiative in November 2012 and in exchange for the CCC meeting certain Administration-identified performance targets.

Staff Comment. As was discussed at the Subcommittee's March 15 hearing, "funding agreements," or "compacts" as they have been previously called, are not a new idea or approach with UC and CSU. However, in the case of the CCC, a funding agreement is a new idea, as agreements between prior administrations and the segments <u>did not</u> include the CCC.

At this juncture, more questions than answers are available about this funding agreement. At the March 15 hearing, the Administration testified that the frameworks are a "work in progress" and that the Administration's intent was for the agreements to be an "intrinsic part of the spring budget process."

LAO Comment. CCC funding is subject to Proposition 98. As a result, GF support for the CCC is intertwined with local property tax revenues received by the districts, since Proposition 98 counts the combination of these two fund sources together. This means that an increase in local property taxes would result in a reduction in the amount of GF needed for a given level of Proposition 98 support. For this reason, simply increasing CCC's GF support by four percent does not ensure any particular level of Proposition 98 resources for CCC, since property tax revenues do not necessarily move in tandem with GF revenues.

The Administration has clarified that it intends for CCC's four percent base increases to be applied to its entire Proposition 98 base (including both GF and local property taxes). However, this raises a new set of concerns. For example, if property taxes were to increase by less than four percent from one year to the next, fulfilling the Governor's promise of a four percent increase in CCC's Proposition 98 funding could cost well more than a four percent increase in CCC's GF appropriation. This is because the GF would have to make up for the inability of property taxes to cover their share of the overall four percent augmentation. Another difficulty arises because CCC and K-12 schools together share total Proposition 98 funding. If the overall Proposition 98 minimum guarantee were not to increase by at least four percent in a given year, meeting the Governor's proposed increase for CCC would require either shifting some of K-12's share to CCC, or appropriating above the minimum guarantee (which would increase overall state costs).

LAO Recommendation. The Legislature has shown a strong interest in accountability over the past decade. While prior attempts to adopt a framework have failed, the Legislature is currently considering SB 721 (Lowenthal). This bill would establish higher education goals and create a working group of representatives of the Legislature, Administration, segments, and others to develop specific accountability metrics. Other current and recent legislative efforts have focused on similar objectives.

The Governor's proposal provides a good opportunity to move forward with the Legislature's accountability efforts. However, the LAO recommends that accountability metrics be used to help the Legislature in identifying policy and budget priorities, rather than as a mechanism for triggering the preset four percent augmentations for the segments. Further, because accountability remains a difficult and elusive goal, it would be unrealistic to expect to complete such an effort as part of this year's budget process. Therefore, the LAO recommends that these efforts be directed through policy committees and the regular legislative process.

Finally, promising out-year base augmentations to the segments would complicate budgeting in other areas and reduce the Legislature's discretion in allocating resources. For these reasons, the LAO recommends that the Legislature reject the Governor's approach of promising base increases to the CCC. Instead, the LAO recommends that the Legislature continue its current practice of making higher education funding decisions as part of each year's budget deliberations.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. Does the Administration have a further update as to the timing of the agreement with the CCC? Is the intent still that the CCC agreement, as well as with UC, CSU, and Hastings, will be an “intrinsic part of the spring budget process?”
2. The LAO has raised several key considerations regarding including the CCC in a funding agreement, due to the fact that CCC funding is subject to Proposition 98. What further response can the Administration provide to address these concerns?
3. The proposed funding agreement would remove key budget tools that the Legislature uses to guide the CCC, while plugging in automatic spending increases disconnected from actual costs and the state’s fiscal condition. How does the Administration respond to this concern?

Staff Recommendation. Staff recommends that this issue be held open, pending the May Revision.

6870 CALIFORNIA COMMUNITY COLLEGES

Item 6: Board of Governor's Fee Waiver Program

Description (Informational Item). The LAO will present to the Subcommittee an informational item regarding the Board of Governor's (BOG) Fee Waiver program.

Background. Generally speaking, the BOG Fee Waiver program waives enrollment fees for CCC students who demonstrate financial need. The cost of the program, which is covered by Proposition 98 GF monies, has grown rapidly in recent years, and waiver costs are projected to total $855 million in the budget year. In recent years, about one-third of students (head count) have received BOG waivers. The Administration projects fee waivers in 2012-13 will represent 70 percent of units taken by students.

Figure 5: CCC BOG Fee Waiver Program Costs

Fiscal Year	Fees Paid	Fees Waived
2003-04	$248,510,000	$168,138,000
2004-05	341,519,000	266,001,000
2005-06	351,125,000	273,789,000
2006-07	325,047,000	244,559,000
2007-08	297,258,000	225,188,000
2008-09	309,000,000	253,996,000
2009-10	360,790,000	369,260,000
2010-11 (Estimated)	323,352,000	410,633,000
2011-12 (Estimated)	361,075,000	614,680,000
2012-13 (Projected)	366,484,000	855,241,000

Under current law and regulation, there are three ways for students to be eligible for a fee waiver: (1) Part A, if students or their parents receive cash assistance from other need-based programs (such as CalWORKs); (2) Part B, if a student's or his/her family adjusted gross income is at or below 150 percent of the federal poverty level; and (3) Part C, if students have any financial need (cost of attendance exceeds their federally determined family contribution by $1 or more). Students can apply for a fee waiver by completing: (1) the Free Application for Federal Student Aid (FAFSA) or (2) for Part A and B waivers, the BOG Fee Waiver application. Verification policies differ by which type of fee waiver is sought. For instance, under Part A, appropriate documentation includes copies of a student's benefits check. Under Part B, Chancellor's Office guidelines give districts flexibility to determine what "documentation" means; acceptable methods include verifying tax records or "self-certification," whereby students are taken at their word about their or their family's income level. All students signing the BOG Fee Waiver application form do so under penalty of perjury.

In fall 2012, an administrative change will take effect for Part C waivers. The minimum standard will be tied to the amount of fees charged to a full-time student taking 24 units in an academic year, which translates to a minimum need threshold of $1,104 (instead of $1). This change is consistent with how the Cal Grant program is structured, which also requires that a student's demonstrated need be at least as much as the maximum amount of the award. The CCC Chancellor's Office estimates that this new policy will affect about 20,000 students, or 1.7 percent of current recipients, resulting in savings in the BOG Fee Waiver program of approximately $12 million in 2012-13.

Other than the financial eligibility requirements discussed above, and unlike other federal and state financial aid programs, the BOG Fee Waiver program imposes few other criteria on students to receive or retain a waiver. For instance, students may receive a waiver regardless of their reason for attending a CCC. Students may also earn failing or otherwise substandard marks for two or more academic years before they are dismissed from the CCC and lose their fee waiver. There is also no limit to the number of years students may receive a fee waiver, nor is there any limit on the number of credit units a student can accumulate.

Chapter 409, Statutes of 2010 (SB 1143; Liu), required the CCC BOG to establish a task force to examine best practices for promoting student completion and adopt a plan for improving student success rates within the CCC. The Student Success Task Force completed its work early this year; the BOG subsequently adopted the Task Force's recommendations. Of the recommendations, one concerns the BOG Fee Waiver program – that satisfactory academic progress toward a declared goal be required of students renewing their BOG Fee Waiver, and that academic and progress standards be established, including a maximum unit cap, as defined by the BOG. As statutory authority is needed to add these conditions to the BOG Fee Waiver program, the Chancellor's Office is pursuing SB 1456 (Lowenthal).

Staff Comment. The BOG fee waiver program continues to be a critical tool for access to the CCC system. The program was designed to make sure that students with financial need did not face a barrier to enrollment. However, a program structure adopted in 1984 when fees were first instituted at $5 per unit can perhaps not be justified under modern conditions without some modifications. The recent administrative changes the Chancellor's Office made are a step in the right direction, as they begin to make the program structure similar to that of other state and federal financial aid programs. The changes proposed by the Student Success Task Force, and contained in SB 1456, are intended in the same construct and merit further consideration.

LAO Recommendation. The LAO recommends that the Legislature enact the statutory changes necessary to add satisfactory academic progress requirements to the BOG Fee Waiver program. The LAO also recommends that the Chancellor's Office count dependent students' income to assess need (current policy only requires campuses to consider only parents' income). Finally, the LAO recommends that the Legislature require students to apply for a waiver using the FAFSA to ensure that they are considered for the full spectrum of federal and state aid.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. The LAO has recommended that the Chancellor's Office count dependent students' income to assess need? Is the Chancellor's Office pursuing this recommendation? If not, why not?
2. How many students will be impacted by the proposed academic and progress standards, including a maximum unit cap? What characteristics describe these students?
3. What is the genesis of the administrative changes to the Part C fee waivers?

Staff Recommendation. None, this is an informational item.

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Item 7: Prioritization of Course Enrollment

Description (Informational Item). The LAO will present to the Subcommittee an informational item regarding prioritization of course enrollment at the CCC.

Background. Current law provides that the primary mission of the CCC is to offer academic and vocational education at the lower division level for both recent high school graduates and those returning to school. Another primary mission is to advance the state's economic growth and global competitiveness through education, training, and services that contribute to continuous workforce improvement. In addition, current law provides that essential and important functions of the CCC include: basic skills instruction, providing English as a second language, adult noncredit instruction, and providing support services that help students to succeed at the postsecondary level. Finally, the CCC is also authorized to provide community service courses and programs, so long as their provision is compatible with an institution's ability to meet its obligations in its primary missions.

In recent years, CCC enrollment has been constrained by two major factors: (1) reductions in course-section offerings as a result of state budget cuts, and (2) strong demand for CCC services, including by adults seeking retraining and other skills at a time of weak state and national economic growth. The CCC system reports that many students, particularly first-time students, have not been able to enroll in the classes they need to progress toward their educational goals. Thus, in effect, CCC enrollments are currently being "rationed." This access problem became even more serious in the current year, given the magnitude of the enacted reductions. The situation in 2012–13 is similar, to the extent that budget reductions dependent on the outcome of the November ballot further reduce available funding to support enrollment slots.

In recent budget acts, the Legislature has declared its intent that the CCC implement workload reductions (a decrease in funded FTES) in courses and programs outside of those needed for students to achieve their basic skills, workforce training, or transfer goals, consistent with the primary missions of the CCC.

Staff Comment. The recent budget reductions have had a real and detrimental impact on the ability of the CCC to maintain its "open access" mission under the state's Master Plan. The budget act and related trailer bills have provided direction and guidance to CCC districts as to the prioritization and focus of these reductions in state support. Nevertheless, questions have been raised as to whether these statements are sufficient. For instance, it is unclear if districts have restricted the enrollment of students in classes for purposes of personal enrichment under the state funded program, in order to prioritize offerings and support to students in programs or courses for transfer, basic skills, or career technical education.

Certainly, there is an intersection between budget and policy that warrants careful deliberation of these issues. The Subcommittee may wish to consider if further guidance via the budget bill or a budget trailer bill is necessary to better ensure that the priority for expenditure of limited state funds is on courses and programs needed for students to achieve their basic skills, workforce training, or transfer goals. These considerations are critically important given the uncertainty in the January budget related to the potential of mid-year trigger cuts.

LAO Recommendation. Given limited resources, it is more important than ever for the state to target funds that best meet the state's highest priorities for CCC services. To accomplish this, the Legislature should: (1) adopt statewide registration priorities that reflect the Master Plan's primary objectives, (2) place a limit on the number of taxpayer-subsidized credit units that students may earn, and (3) restrict the number of times that a student may repeat physical education and other classes at taxpayers' expense.

Subcommittee Questions. Based on the above comments, the Subcommittee may wish to ask the following questions:

1. The Student Success Task Force recommended the adoption of systemwide enrollment priorities and other strategies for ensuring access for students with a certificate, degree, or career enhancement goal. What is the status of the implementation of these recommendations? In their implementation, how can/will compliance with these priorities by districts be monitored and enforced?
2. What enrollment management strategies for expanding and targeting access on transfer, basic skills, or career technical education have been adopted locally? What proportion of districts have implemented these types of strategies?
3. What proportion of districts have eliminated the use of state funding to offer courses or support students in programs or courses outside of transfer, basic skills, or career technical education?
4. How many districts have adopted policies that restrict the enrollment of students in classes for purposes of personal enrichment under the state funded program?
5. How many districts have implemented policies to ensure that enrollment is prioritized for continuing students who are making satisfactory progress toward their educational goals?
6. What do we know about the types of students who are not being served at campuses, even with the articulation of the Legislature's priorities for these funds?

Staff Recommendation. None, this is an informational item.