Senate Budget and Fiscal Review—Holly J. Mitchell, Chair

SUBCOMMITTEE NO. 1 Agenda

Senator Richard D. Roth, Chair
Senator Connie M. Leyva
Senator Mike Morrell

Thursday, March 14, 2019
9:30 a.m. or upon adjournment of session
State Capitol - Room 3191

Consultant: Elisa Wynne

AGENDA

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6100 DEPARTMENT OF EDUCATION

Issue 1: Proposition 98

Panel I:

- Aaron Heredia, Department of Finance
- Ken Kapphahn, Legislative Analyst's Office

Background:

California provides academic instruction and support services to over six million public school students in kindergarten through twelfth grades (K-12) and 2.4 million students in community colleges. There are 58 county offices of education, approximately 1,000 local K-12 school districts, more than 10,000 K-12 schools, and more than 1,200 charter schools throughout the state. Of the K-12 students, approximately 3.9 million are low-income, English learners, or foster youth students or some combination of those categories. Approximately 1.3 million of the K-12 students served in public schools are English learners. There are also 72 community college districts, 114 community college campuses, and 70 educational centers. Proposition 98, which was passed by voters as an amendment to the state Constitution in 1988, and revised in 1990 by Proposition 111, was designed to guarantee a minimum level of funding for public schools and community colleges.

The proposed 2019-20 budget includes funding at the Proposition 98 minimum guarantee level of $80.7 billion. The Governor's budget also proposes to provide total Proposition 98 funding for 2017-18 of $75.5 billion, a decrease of $120 million over the 2018 final budget act level, but $44 million above the revised 2017-18 Guarantee level. For 2018-19, the Governor estimates a decrease in the total Guarantee of $526 million (for a total of $77.9 billion), but provides $475 million in settle-up funding to offset the need for expenditure reductions. These adjustments are the result of revised average-daily attendance (ADA) numbers for each of the years and the certification of prior year guarantee levels. Additional Proposition 98 funds in 2019-20 are proposed to be used primarily to provide a cost-of-living-adjustment (COLA) for the Local Control Funding Formula (LCFF) and to provide funding for special education-related services. These proposals are more fully described later in this section.

Proposition 98 Funding. State funding for K-14 education—primarily K-12 local educational agencies and community colleges—is governed largely by Proposition 98. The measure, as modified by Proposition 111, establishes minimum funding requirements (referred to as the "minimum guarantee") for K-14 education. General Fund resources, consisting largely of personal income taxes, sales and use taxes, and corporation taxes, are combined with the schools' share of local property tax revenues to fund the Proposition 98 minimum guarantee. These funds typically represent about 80 percent of statewide funds that K-12 schools receive. Non-Proposition 98 education funds largely consist of revenues from local parcel taxes, other local taxes and fees, federal funds and proceeds from the state lottery. In recent years, there have been two statewide initiatives that increased General Fund revenues and therefore, the Proposition 98 minimum guarantee. Proposition 30, passed by the voters in 2012, raised sales and income taxes, but was designed to phase out over seven years. Anticipating the expiration of the Proposition 30 taxes, Proposition 55 was passed by voters in 2016, extending the

income tax portion of Proposition 30 for another 12 years.

The table below summarizes overall Proposition 98 funding for K-12 schools and community colleges since 2007-08, or just prior to the beginning of the recent recession. 2011-12 marks the low point for the guarantee, with steady increases since then. The economic recession impacted both General Fund resources and property taxes. The amount of property taxes has also been impacted by a large policy change in the past few years—the elimination of redevelopment agencies (RDAs) and the shift of property taxes formerly captured by the RDAs back to school districts. The guarantee was adjusted to account for these additional property taxes, so although Local Educational Agencies (LEAs) received significantly increased property taxes starting in 2012-13, they received a roughly corresponding reduction in General Fund.

Proposition 98 Funding
Sources and Distributions
(Dollars in Millions)

	Pre-Recession **2007-08**	Low Point **2011-12**	Revised **2017-18**	Revised **2018-19**	Proposed **2019-20**
Sources					
General Fund	42,015	33,136	52,887	54,028	55,295
Property taxes	14,563	14,132	22,610	23,839	25,384
Total	**56,577**	**47,268**	**75,498**	**77,867**	**80,680**
Distribution					
K-12	50,344	41,901	66,683	68,605	71,155
CCC	6,112	5,285	8,720	9,174	9,438
Other	121	83	95	88	87

Source: Legislative Analyst's Office and Department of Finance

Calculating the Minimum Guarantee. The Proposition 98 minimum guarantee is determined by comparing the results of three "tests," or formulas, which are based on specific economic and fiscal data. The factors considered in these tests include growth in personal income of state residents, growth in General Fund revenues, changes in student ADA, and a calculated share of the General Fund. When Proposition 98 was first enacted by the voters in 1988, there were two "tests", or formulas, to determine the required funding level. Test 1 calculates a percentage of General Fund revenues based on the pre-Proposition 98 level of General Fund that was provided to education, plus local property taxes. The test 2 calculation is the prior year funding level adjusted for growth in student ADA and per capita personal income. K-14 education was initially guaranteed funding at the higher of these two tests. In 1990, Proposition 111 added a third test, Test 3, which takes the prior year funding level and adjusts it for growth in student ADA and per capita General Fund revenues. The Proposition 98 formula was adjusted to compare Test 2 and Test 3, the lower of which is applicable. This applicable test is then compared to Test 1; and the higher of the tests determines the Proposition 98 minimum guarantee. Generally, Test 2 is operative during years when the General Fund is growing quickly and Test 3 is operative when General Fund revenues fall or grow slowly.

Proposition 98 Tests
Calculating the Level of Education Funding
(Including the 2019-20 Governor's Budget Estimate)

Test	Calculated Level	Operative Year	Times Used
Test 1	Based on a calculated percent of General Fund revenues (currently around 38 percent).	If it would provide more funding than Test 2 or 3 (whichever is applicable).	6
Test 2	Based on prior year funding, adjusted for changes in per capita personal income and attendance.	If growth in personal income is ≤ growth in General Fund revenues plus 0.5 percent.	13
Test 3	Based on prior year funding, adjusted for changes in General Fund revenues plus 0.5 percent and attendance.	If statewide personal income growth > growth in General Fund revenues plus 0.5 percent.	11

The Governor's proposal assumes that in 2017-18 and 2019-20 the Proposition 98 minimum guarantee is calculated under Test 1 and that in 2018-19, the minimum guarantee is calculated under Test 3.

Generally, the Proposition 98 minimum guarantee calculation was designed in order to provide growth in education funding equivalent to growth in the overall economy, as reflected by changes in personal income (incorporated in Test 2). In a Test 3 year, the Proposition 98 minimum guarantee does not grow as fast as in a Test 2 year, in recognition that the state's General Fund is not reflecting the same strong growth as personal income and the state may not have the resources to fund at a Test 2 level; however, a maintenance factor is created, as discussed in more detail later.

The Test 1 percentage is historically-based, but is adjusted, or "rebenched," to account for large policy changes that impact local property taxes for education or changes to the mix of programs funded within Proposition 98. In the past few years, rebenching was done to account for property tax changes, such as the dissolution of the RDAs, and program changes, such as removing childcare from the Proposition 98 minimum guarantee and adding mental health services. In the budget year, the Test 1 calculation is adjusted to reflect RDA changes and for a new state preschool policy change. In 2019-20, the Governor's Budget adjusts the portion of the state preschool program that is provided by non-profit agencies for COLA and growth for a total program cost of $297 million. The budget then proposes to move this program outside of the guarantee and rebench the guarantee level by a like amount. The portion of the state preschool program that is provided through local educational agencies remains within the Proposition 98 guarantee. The 2019-20 Proposition 98 guarantee is likely to remain a Test 1 even with some changes in factors at the May Revision. Revenues are growing steadily but slowly, ADA is declining, and also property tax growth is high, all contributing to a Test 1 for 2019-20 and for the out-years.

Suspension of Minimum Guarantee. Proposition 98 includes a provision that allows the Legislature and Governor to suspend the minimum funding requirements and instead provide an alternative level of funding. Such a suspension requires a two-thirds vote of the Legislature and the concurrence of the Governor. To date, the Legislature and Governor have suspended the Proposition 98 minimum guarantee twice; in 2004-05 and 2010-11. While the suspension of Proposition 98 can create General Fund savings during the year in which it is invoked, it also creates obligations in the out-years, as explained below.

Maintenance Factor. When the state suspends the Proposition 98 minimum guarantee or when Test 3 is operative (that is, when the Proposition 98 minimum guarantee grows more slowly due to declining or low General Fund growth), the state creates an out-year obligation referred to as the "maintenance factor." When growth in per capita General Fund revenues is higher than growth in per capita personal income (as determined by a specific formula also set forth in the state Constitution), the state is required to make maintenance factor payments, which accelerate growth in K-14 funding, until the determined maintenance factor obligation is fully restored. Outstanding maintenance factor balances are adjusted each year by growth in student ADA and per capita personal income.

The maintenance factor payment is added on to the minimum guarantee calculation using either Test 1 or Test 2.

- In a Test 2 year, the rule of thumb is that roughly 55 percent of additional revenues would be devoted to Proposition 98 to pay off the maintenance factor.

- In a Test 1 year, the amount of additional revenues going to Proposition 98 could approach 100 percent or more. This can occur because the required payment would be a combination of the 55 percent (or more) of new revenues, plus the established percentage of the General Fund—roughly 38 percent—that is used to determine the minimum guarantee.

Prior to 2012-13, the payment of maintenance factor was made only on top of Test 2; however, in 2012-13, the Proposition 98 guarantee was in an unusual situation as the state recovered from the recession. It was a Test 1 year and per capita General Fund revenues were growing significantly faster than per capita personal income. Based on a strict reading of the Constitution, the payment of maintenance factor is not linked to a specific test, but instead is required whenever growth in per capita General Fund revenues is higher than growth in per capita personal income. As a result, the state funded a maintenance factor payment on top of Test 1 and this interpretation can result in the potential for up to 100 percent or more of new revenues going to Proposition 98 in a Test 1 year with high per capita General Fund growth. This was the case in 2014-15, when the maintenance factor payment was more than $5.6 billion. However, in the past few years, the state has significantly increased funding for K-14 education due in part to payments made towards reducing the maintenance factor balance. As a result, the maintenance factor obligation is essentially paid off and the possibility of the Proposition 98 calculation absorbing an unusually large portion of state revenue gains is unlikely within the next few years.

For 2017-18 the Governor's proposal reflects a $1.2 billion maintenance factor payment, fully paying off the obligation in that year. The estimated Test 3 calculation in 2018-19 creates a maintenance factor obligation of $143 million. Adjusted for growth in ADA and per-capita personal income, this obligation grows to $150 million in 2019-20. No maintenance factor payment is required in 2019-20 as General Fund revenues are not growing significantly year over year, and low maintenance factor obligation balances mean maintenance factor creation and pay-off requirements will have only a minor impact on the Proposition 98 guarantee in the current multi-year window.

Average Daily Attendance. One of the factors used to calculate the Proposition 98 minimum guarantee level is growth in ADA. In a Test 2 or Test 3 year, the guarantee is adjusted for changes in ADA. However, there is a hold harmless provision for reductions in ADA. Under that provision, negative growth is only reflected if the preceding two years also show declines. Under current projections, which reflect birth rates and migration, K-12 ADA is expected to decline slightly in

coming years and the hold harmless will no longer apply for the guarantee calculation, contributing to a dampening effect on Proposition 98 guarantee growth in future years.

Settle-Up. Every year, the Legislature and Governor estimate the Proposition 98 minimum guarantee before the final economic, fiscal, and attendance factors for the budget year are known. If the estimate included in the budget for a given year is ultimately lower than the final calculation of the minimum guarantee, Proposition 98 requires the state to make a "settle-up" payment, or series of payments, in order to meet the final guarantee for that year. The Governor's budget proposes General Fund settle-up payments of $475.3 million in 2018-19 and $211.3 million in 2019-20, fully paying off settle-up obligations from 2016-17 and prior years. In the recent past, the state was not required to make settle-up payments on schedule; however, Proposition 2, passed in 2014, requires the state to spend a minimum amount each year to buy down eligible state debt. In past years, Proposition 98 settle-up payments have counted towards the state's Proposition 2 requirement. By contrast, the Governor is not counting the settle-up payments proposed in the Governor's budget towards Proposition 2.

Proposition 98 Certification. The 2018 budget package included a new process for certifying the Proposition 98 guarantee. Under current statute, certification of the guarantee is a process by which the Department of Finance (DOF), in consultation with the Department of Education (CDE) and the Chancellor's Office of the Community Colleges, verifies the factors for the calculation of the Proposition 98 guarantee and the appropriations and expenditures that count towards the guarantee level. Certifying the guarantee results in a finalized guarantee level for the year, as well as finalizing any settle-up owed as a result of changes in the guarantee level. Prior to this new process, the guarantee was last certified for 2008-09. The new process for certifying the Proposition 98 guarantee for a given year is detailed below:

- Each year, as part of the May Revision process, DOF shall calculate the state's Proposition 98 guarantee level for the prior fiscal year based on the most recently available underlying data and publish the proposed certification calculation and underlying data.

- The Superintendent of Public Instruction, the Chancellor of the Community Colleges and other stakeholders are provided the opportunity to comment on the proposed certification of the Proposition 98 guarantee. DOF is required to provide written responses to the comments on their website and to provide this information in a report to the Legislature.

- The Legislature is provided with the opportunity to review the comments and responses and to provide additional feedback to DOF prior to the final certification of the prior-year Proposition 98 guarantee. The final certification is followed by a 90-day period during which a legal challenge may be filed. DOF is required to publish the final certification of the Proposition 98 Guarantee and the underlying data in a separate schedule of the Governor's budget no later than January 10th of the following year.

- If the Director of Finance determines that, pursuant to the certification process, the state has provided appropriations in excess of the Proposition 98 guarantee for the prior fiscal year, it is required that the excess, not to exceed one percent of the value of the Proposition 98 guarantee in the certified year, be credited to a newly created Proposition 98 Cost Allocation Schedule. Any amounts in the Proposition 98 Cost Allocation Schedule may be credited to satisfy an outstanding obligation for K-14 education under the Proposition 98 guarantee in any prior year.

- To the extent an outstanding obligation remains for K-14 education under the Proposition 98 guarantee in any prior year, after any adjustments for amounts in the Proposition 98 Cost Allocation Schedule are made, the amounts necessary to satisfy the obligations to K-14 education entities are continuously appropriated. They are allocated by the State Controller pursuant to a schedule determined by DOF.

- The Legislature may adopt an alternative plan for repayment of any outstanding obligations determined as a result of the certification process through the annual budget process or other statute.

- For the 2009-10 through 2016-17 fiscal years, a truncated version of this process was established to certify the Proposition 98 guarantee. Related to this process, the 2015-16 Proposition 98 guarantee was rebenched to account for additional child care wraparound services related to the State Preschool program that were funded within the Proposition 98 guarantee beginning in 2015-16. According to the Legislative Analyst's Office (LAO), this rebenching increased the Proposition 98 guarantee levels by a total of approximately $350 million over the 2016-17, 2017-18, and 2018-19 period.

- In August 2018, DOF released the proposed certification for the 2009-10 through 2016-17 fiscal years. The total settle-up obligation associated with those five years was calculated at $687 million, an increase of $347 million compared to previous estimates, and is proposed to be paid off in the 2018-19 and 2019-20 years.

Proposition 98 Rainy Day Fund and District Reserve Caps. Proposition 2 also requires a deposit in a Proposition 98 Rainy Day Fund under certain circumstances. These required conditions are that maintenance factor accumulated prior to 2014-15 is paid off, Test 1 is in effect, the Proposition 98 guarantee is not suspended, and no maintenance factor is created. Related statute required that in the year following a deposit into this fund, a cap on local school district reserves would be implemented. However, SB 751 (Hill), Chapter 674, Statutes of 2017, amended the requirements to trigger the cap to specify that the trigger is when the Proposition 98 Rainy Day Fund is funded at three percent of the K-12 share of the Proposition 98 guarantee. SB 751 also loosens the requirements on local school districts in implementing the reserve cap. Under the Governor's estimates, small deposits to the Proposition 98 Rainy Day Fund may be required within the multi-year projection period.

Governor's Proposal

As discussed above, the Governor's budget includes some adjustments to prior year guarantee levels. In 2017-18, the budget proposes to provide total Proposition 98 funding (K-14) for 2017-18 of $75.5 billion, a decrease of $120 million over the 2018 final budget act level, but $44 million above the revised 2017-18 guarantee level. For 2018-19, the Governor estimates a decrease in the total guarantee of $526 million (for a total of $77.9 billion), but provides $475 million in settle-up funding to offset the need for expenditure reductions. These adjustments are primarily the result of revised ADA numbers for each of the years and the certification of prior year guarantee levels.

Certification Process Changes. The process adopted in the 2018-19 budget act to certify the Proposition 98 guarantee and use a separate account to help smooth increases and decreases in the guarantee level was intended to create stability for LEAs. The Governor's budget proposes to instead eliminate the separate account and no longer adjust the guarantee level down if the prior year

calculation changes after the fiscal year is over. The Governor proposes to still make adjustments to increase the guarantee after the fiscal year is over if the calculation results in an increase in a prior year.

Funding Level. The budget includes a proposed Proposition 98 funding level of $71.2 billion for K-12 programs (including preschool provided by LEAs). This includes a year-to-year increase of $2.5 billion in Proposition 98 funding for K-12 education, as compared to the revised Proposition 98 K-12 funding level for 2018-19. Under the Governor's proposal, ongoing K-12 Proposition 98 per pupil expenditures increase from $11,574 provided in 2018-19 (revised) to $12,018 in 2019-20, an increase of 3.8 percent. The Governor's major K-12 spending proposals are identified below.

K-12 Programs. The bulk of funding for school districts and county offices of education for general operations is provided through the LCFF and the majority of K-12 Proposition 98 growth funding is used to provide a COLA of 3.46 percent, approximately $2 billion, for the 2019-20 fiscal year. The proposed budget also includes $576 million in Proposition 98 General Fund ($390 million ongoing) for special education-related services for LEAs and a variety of other smaller proposals. Proposition 98 proposals will be discussed in more detail in future subcommittee hearings.

LAO Analysis and Recommendations

For the 2019-20 budget, the sensitivity of the minimum guarantee calculation to changes in underlying factors is described in the LAO's recent publication, *Overview of the Governor's Proposition 98 Budget Package*. In 2018-19, the LAO notes that for a dollar increase or decrease in revenues, the guarantee would increase or decrease by approximately 55 cents. However, if revenues increase over $250 million, there will be no impact on the guarantee for the additional revenue, as the calculation would become a Test 2 at that point and not rely on revenue growth. For 2019-20, an increase or decrease of one dollar in revenue would increase or decrease the guarantee by approximately 40 cents. The LAO notes that a Test 1 is likely to remain operative in 2019-20, and therefore changes in 2018-19 will not roll forward to impact the 2019-20 guarantee.

The LAO notes that the Legislature may wish to prepare for a lower amount of Proposition 98 funding within the guarantee for the final budget negotiations. The LAO projections include some caution around economic events that could lead to less overall General Fund revenues being available, reducing the guarantee level. The LAO also identifies several proposals, workload and others, that are not accounted for in the Governor's budget under Proposition 98, including: 1) a property tax backfill for San Francisco, 2) adjustments for Community College shortfalls, 3) funding for county offices of education, and 4) funding for Oakland and Inglewood school districts based on the 2018-19 budget act agreement. The combination of changes in the guarantee level and adjustments to workload expenditures within the guarantee may reduce the amount of available discretionary funding at the May Revision. The LAO suggests that the Legislature consider identifying proposals that could be reduced or rejected, and consider utilizing more ongoing dollars within the guarantee for one-time priorities to help build a cushion against a future reductions.

In regards to the Governor's proposal on changing the certification process, the LAO notes that the suggested changes would make future budget balancing more difficult and instead recommends retaining the agreement put into place during the 2018-19 budget.

Staff Comments

Calculation of the Guarantee Level. The minimum guarantee level is calculated based on the best available factors at the time. However, between the January budget proposal and the May Revision of the budget, the minimum guarantee calculation can change significantly, usually due to changes in state revenues. The Legislature will want to consider potential changes in preparing a Proposition 98 expenditure package. The LAO notes that their estimate of the Proposition 98 minimum guarantee is very similar to the Governor's, however both the LAO and the Governor note that there is some economic risk that may impact revenues and the guarantee level going into the May Revision. In particular, since the LAO's November forecast and the release of the Governor's budget, there has been significant stock market volatility at the end of 2018 and beginning of 2019 that has not been factored in to either set of estimates.

One-Time or Ongoing Funding. In the past six years, enacted budgets have included substantial one-time expenditures within Proposition 98, from $413 million to $1.2 billion. While these funds have been dedicated to various one-time education priorities, they have also provided a cushion against having to make difficult cuts should the minimum guarantee decrease in future years. The Governor's proposed 2019-20 budget includes almost no one-time funding (only $3 million in the 2019-20 guarantee). In addition, about $77 million in ongoing program costs are being funded with one-time funds. As a result, the budget proposal essentially assumes the 2020-21 Proposition 98 guarantee grows enough to accommodate these program costs, as well as growth in other programs. If the guarantee should drop in a recession, without any built-in one-time cushion, cuts would need to be made to ongoing programs. The Legislature may wish to consider out year projections for the minimum guarantee and how they prefer to balance ongoing needs with prudent budgeting.

Rebenching of the Guarantee. The Governor's budget includes a proposal to move the non-LEA portion of the state preschool program outside of the guarantee and to fund it with General Fund. This action reduces the guarantee by a like amount, resulting in a budget neutral shift from the state's perspective. The Legislature may wish to consider the out-year consequences of such a shift. If a program is growing and if it is within the Proposition 98 guarantee, the risk is that the program grows faster than percentage growth in the guarantee, crowding out the availability of funding for other programs. Given that the Governor has proposed to increase the state preschool program for non-LEAs by $125 million each year for the next three years, this would have taken up substantial "room" within the guarantee if the proposal had not shifted it to the General Fund. However, in the event of a recession, programs within the guarantee generally have some degree of protection from reductions. While the guarantee may drop in a recession, in the past more of the reductions are borne on the General Fund side.

Certification of the Guarantee. Finally, the Legislature will want to consider the Governor's proposal to change the Proposition 98 guarantee level certification process agreed to as part of the 2018-19 budget act. Under current law, with the use of a Proposition 98 true-up account, the increases and decreases in the guarantee would be smoothed out, protecting LEAs from painful adjustments. The Governor's Budget not only eliminates the true-up account, but prevents the Proposition 98 guarantee from being adjusted downward after the end of the fiscal year. However, if the guarantee increases after the end of the fiscal year, that amount would still be owed to K-14 education under the Governor's proposal. The Governor's budget proposal is beneficial for LEAs, but comes at the expense of the General Fund. Under current law, the funds due to the guarantee in the event of an increase are balanced with the funds (essentially due to the General Fund) in the event of a decrease. Under the proposal, additional funding for Proposition 98 must be allocated from the General Fund in the event of an increase; however, the General Fund gets no relief when the guarantee is realized to have been

over-estimated. The Legislature will want to consider whether to maintain the status quo or to retain discretion over when to over-appropriate the guarantee in prior years, based on the availability of General Fund resources.

Subcommittee Questions

- LAO/DOF: What are the multi-year projections for growth in the Proposition 98 minimum guarantee? Under potential recession scenarios, how does the guarantee level change?

- DOF: Under the new certification proposal, the state would be required to pay settle-up for prior years that are under appropriated, but not reduce the guarantee or score excess appropriations towards future years. Why are the two scenarios treated differently under the Governor's proposal?

Staff Recommendation

No action, the Proposition 98 guarantee calculation will be updated at the May Revision.

Issue 2: Local Control Funding Formula

Panel I:

- Aaron Heredia, Department of Finance
- Ryan Anderson, Legislative Analyst's Office

Background:

K-12 School Finance Reform. Commencing in the 2013-14 fiscal year, the state significantly reformed the system for allocating funding to LEAs - school districts, charter schools, and county offices of education (COEs). The LCFF replaced the state's prior system of distributing funds to LEAs through revenue limit apportionments (based on per student average daily attendance) and approximately 50 state categorical education programs.

Under the previous system, revenue limits provided LEAs with discretionary (unrestricted) funding for general education purposes, and categorical program (restricted) funding was provided for specialized purposes, with each program having a unique allocation methodology, spending restrictions, and reporting requirements. Revenue limits made up about two-thirds of state funding for schools, while categorical program funding made up the remaining one-third portion. That system became increasingly cumbersome to LEAs as they tried to meet student needs through various fund sources that were layered with individual requirements.

Local Control Funding Formula. The LCFF combines the prior funding from revenue limits and more than 30 categorical programs that were eliminated, and uses new methods to allocate these resources, additional amounts of new Proposition 98 funding since 2013-14, and future allocations to LEAs. The LCFF allows LEAs much greater flexibility in how they spend the funds. There is a single funding formula for school districts and charter schools, and a separate funding formula for COEs that has some similarities to the district formula, but also some key differences.

School Districts and Charter Schools Formula. The LCFF is designed to provide districts and charter schools with the bulk of their resources in unrestricted funding to support the basic educational program for all students. It also includes additional funding based on the enrollment of low-income students, English learners, and foster youth for increasing or improving services to these high-needs students. Low-income students, English learners, and foster youth students are referred to as "unduplicated" students in reference to the LCFF because, for the purpose of providing supplemental and concentration grant funding, these students are counted once, regardless of if they fit into more than one of the three identified high-need categories. Major components of the formula are briefly described below.

- **Base Grants** are calculated on a per-student basis (measured by student ADA) according to grade span (K-3, 4-6, 7-8, and 9-12) with adjustments that increase the base rates for grades K-3 (10.4 percent of base rate) and grades 9-12 (2.6 percent of base rate). The adjustment for grades K-3 is associated with a requirement to reduce class sizes in those grades to no more than 24 students by 2020-21, unless other agreements are collectively bargained at the local level. The adjustment for grades 9-12 recognizes the additional cost of providing career technical education in high schools.

- **Supplemental Grants** provide an additional 20 percent in base grant funding for the percentage of enrollment that is made up of unduplicated students.

- **Concentration Grants** provide an additional 50 percent above base grant funding for the percentage of unduplicated students that exceed 55 percent of total enrollment.

- **Categorical Program** add-ons for Targeted Instructional Improvement Block Grant and Home-to-School Transportation provide districts the same amount of funding they received for these two programs in 2012-13. The transportation funds must be used for transportation purposes. Charter schools are not eligible for these add-ons.

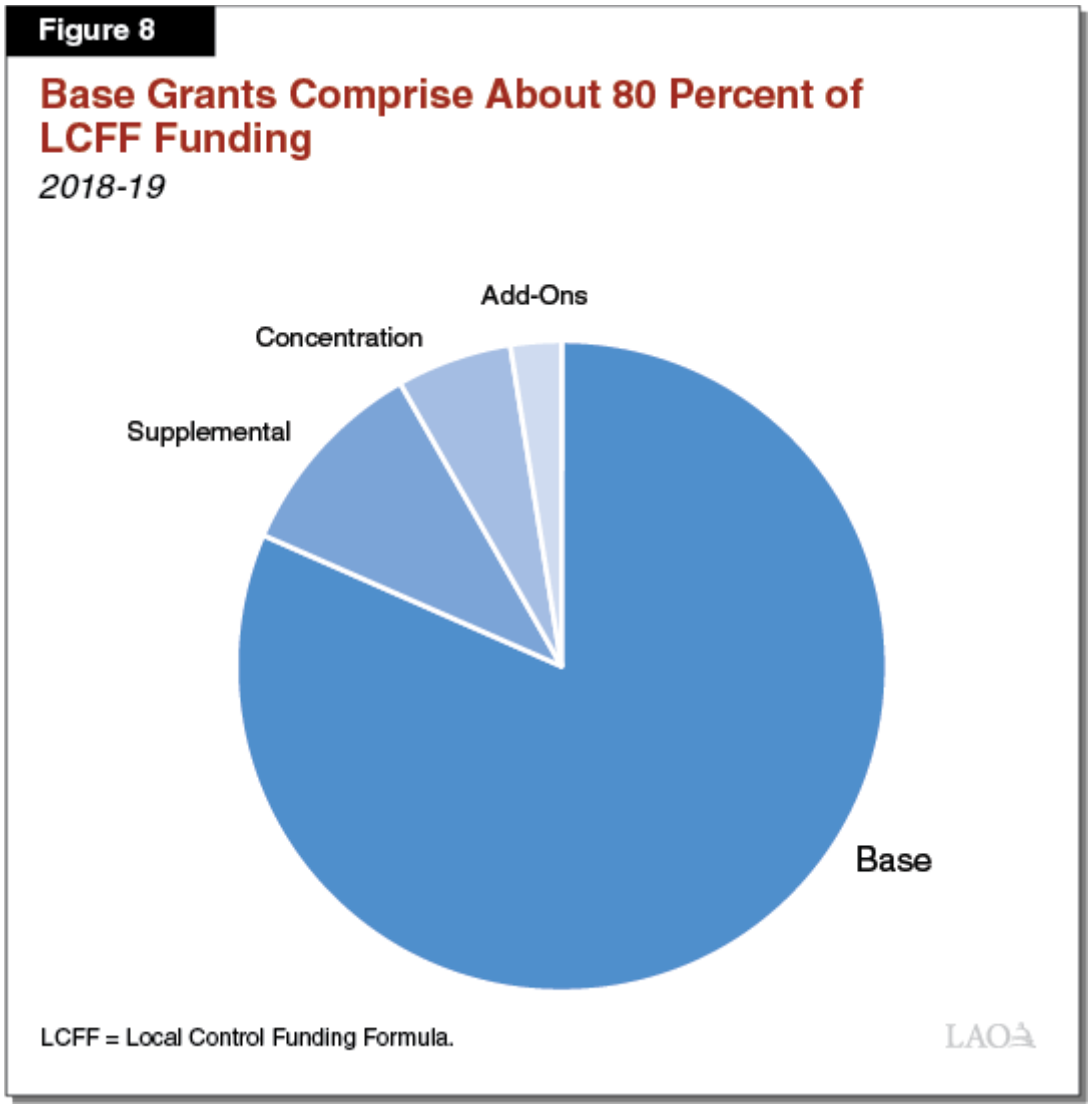
- **LCFF Economic Recovery Target** add-on ensures that districts receive, by 2020-21, at least the amount of funding they would have received under the old finance system to restore funding to their 2007-08 level adjusted for inflation. Districts are not eligible for this add-on if their LCFF funding exceeds the 90th percentile of per-pupil funding rates estimated under the old system.

- **Hold Harmless Provision** ensures that no school district or charter school will receive less funding under the LCFF than its 2012-13 funding level under the old system.

Budget Appropriations. The LCFF established new "target" LCFF funding amounts for each LEA, and these amounts are adjusted annually for COLA and pupil counts. When the formula was initially introduced, funding all school districts and charter schools at their target levels was expected to take eight years and cost an additional $18 billion, with completion by 2020-21. However, Proposition 98 growth exceeded expectations and LCFF was fully funded in the 2018-19 fiscal year for school districts and charter schools. COEs reached their target funding levels in 2014-15, which adjusts each year for COLAs and ADA growth. The 2018-19 budget also provided an additional amount above the required COLA to provide a $670 million increase to LCFF grants. With full-funding of the formula, LEAs and stakeholders can see how much funding is received through base, supplemental, and concentration grants on the CDE website and reported through each LEA's local control and accountability plan (LCAP).

Restrictions on Supplemental Funding. Statute requires LEAs to increase or improve services for unduplicated students in proportion to the supplemental funding LEAs receive for the enrollment of these students. The law also allows this funding to be used for school-wide and district-wide purposes. The State Board of Education (SBE) adopted regulations governing LEAs expenditures of this supplemental funding that require an LEA to increase or improve services for unduplicated students, compared to the services provided for all students, in proportion to the supplemental funding LEAs receive for the enrollment of these students. LEAs determine the proportion by which an LEA must increase or improve services by dividing the amount of the LCFF funding attributed to the supplemental and concentration grant by the remainder of the LEA's LCFF funding. Whereas, this percentage (known as the minimum proportionality percentage (MPP)), relied on an LEA's estimates during the transition period, under a fully funded system is based on the actual allocation to each LEA as determined by the CDE. The regulations allow an LEA to meet this requirement to increase or improve services in a qualitative or quantitative manner and detail these expenditures in their LCAP.

The following chart shows that the majority of funds that LEAs receive under LCFF are for the base grant, with other grants and add-ons making up a much smaller share of overall LCFF funding.



Source: Legislative Analyst's Office

County Offices of Education Formula. The COE formula is very similar to the school district formula, in terms of providing base grants, plus supplemental and concentration grants for the students that COEs serve directly, typically in an alternative school setting. However, COEs also receive an operational grant that is calculated based on the number of districts within the COE and the number of students county-wide. This operational grant reflects the additional responsibilities COEs have for support and oversight of the districts and students in their county.

Similar to the LCFF formula for school districts and charter schools, COEs were also guaranteed that they would not get less funding than was received in 2012-13. In addition, COEs were held harmless for the amount of state aid (essentially the value of the categorical funding) received in 2012-13. Unlike school districts, for COEs this minimum state aid amount floats above their target, meaning that as local property tax revenue grows in a county over time and funds their LCFF allocation, the minimum state aid allotment for that COE becomes a new bonus in base funding on top of the their LCFF level.

Governor's Proposal:

K-12 Local Control Funding Formula – The bulk of funding for school districts and COEs for general operations is provided through the LCFF and is distributed based on the numbers of students served and certain student characteristics. The state fully funded the LCFF in 2018-19 and provided an additional COLA. The proposed budget provides a COLA of 3.46 percent, approximately $2 billion, for the 2019-20 fiscal year, bringing total LCFF funding to $63 billion.

The Administration also proposes to cap the continuous appropriation of COLA for LCFF, existing in current law, during future years if the COLA for LCFF and other K-14 programs would exceed growth in the minimum guarantee.

LAO Analysis and Recommendations

The LAO reviewed the Governor's LCFF related proposals in their recent publication, *The 2019-20 Budget: Proposition 98 Education Analysis*. The LAO notes that the COLA included in the Governor's budget is similar to the 3.26 percent COLA they estimated in their November revenue forecast and while the COLA factors will be updated in April, they do not anticipate significant changes.

In regards to the proposed COLA cap, the LAO notes that the Governor's proposal may create an additional formula that leads to further complication in the way the state budgets for education each year. The LAO reviewed prior year budgets and notes that since 1990-91, in about one-third of the state's budgets the COLA for K-12 was not fully funded. While the Governor's proposal would adjust the LCFF COLA in years where the state could not support the full COLA, the LAO recommends that instead of this automatic adjustment, the state go back to making the decision about funding COLA in the budget each year. This approach would allow the Governor and Legislature to consider all needs within the K-12 budget and make a decision related to COLA each year based on their priorities.

Finally, the LAO notes that in regards to the COE LCFF formula, growth in property taxes is widening inequities between the counties. A subset of counties with higher local property taxes and growth benefit from the minimum state aid provision of the formula, while others do not. The LAO also notes that the cost of the minimum state aid provision continues to grow. DOF projected this cost to be flat at $113 million in 2019-20, while the LAO notes that the actual figure will likely be closer to $134 million and funding this provision results in less ongoing Proposition 98 funding for other K-12 education priorities. As a result, the LAO recommends the Legislature adopt a hold harmless for minimum state aid at the 2018-19 value, and repeal the minimum state aid provision of the COE formula going forward.

Subcommittee Questions:

1) DOF: When will trailer bill language on the proposed LCFF COLA cap become available?

2) DOF/LAO: What COLAs are DOF/LAO predicting in the out years? Would they outpace anticipated growth in the minimum guarantee level?

3) Does DOF agree with the LAO's estimate of additional COE funding that may be needed at the May Revision due to the growth in the minimum state aid portion of the formula?

Staff Recommendation:

Hold Open.

Issue 3: Statewide Accountability System Update

Panel:

- Sara Cortez, Legislative Analyst's Office
- Keric Ashley, Deputy Superintendent, Department of Education
- David Sapp, State Board of Education
- Tom Armelino, Executive Director, California Collaborative for Educational Excellence
- Dan Hanower, Department of Finance

Background:

State Accountability

Local Control and Accountability Plans (LCAP). To ensure accountability for LCFF funds, the state requires that all LEAs annually adopt and update a LCAP. The LCAP must include locally-determined goals, actions, services, and expenditures of LCFF funds for each school year in support of the state educational priorities that are specified in statute, as well as any additional local priorities. In adopting the LCAP, LEAs must consult with parents, students, teachers, and other school employees.

The eight state priorities that must be addressed in the LCAP, for all students and significant student subgroups in a school district and at each school, are:

- *Williams* settlement issues (adequacy of credentialed teachers, instructional materials, and school facilities).
- Implementation of academic content standards.
- Parental involvement.
- Pupil achievement (measured in part by statewide assessments, Academic Performance Index, and progress of English-language learners toward English proficiency).
- Pupil engagement (measured by attendance, graduation, and dropout data).
- School climate (measured in part by suspension and expulsion rates).
- The extent to which students have access to a broad course of study.
- Pupil outcomes for non-state-assessed courses of study.

COEs must address the following two priorities, in addition:

- Coordination of services for foster youth.
- Coordination of education for expelled students.

School district LCAPs are subject to review and approval by COEs, while COE LCAPs are subject to review and approval by the State Superintendent of Public Instruction (SPI). Statute also established a process for districts to receive technical assistance related to their LCAPs. The SPI is authorized to intervene in a district that is failing to improve outcomes for students after receiving technical assistance.

In addition, under changes made as part of the 2017 Budget Act, COEs are also required to provide a summary of the plan for supporting schools and school districts within their county, including a description of goals for LCAP review, and provision of technical assistance and support. COEs must measure progress towards meeting these goals by identifying and assessing metrics, as well as specifying the actions and expenditures to meet these goals. Finally, COEs must identify how they are collaborating with the California Collaborative for Educational Excellence, the CDE, and other COEs.

Finally, the 2018-19 budget agreement specified updates to the LCAP including: 1) a summary table of planned expenditures for all actions for each goal included in the LCAP, broken out by fund source; 2) a summary of the actions and planned expenditures to increase or improve services for English learners, low-income and foster youth students; 3) specified that LEAs can prioritize their goals, actions and related expenditures within the eight state priorities; and 4) required the LCAP and Annual Update template adopted by SBE to use language that is understandable and accessible to parents and required school districts and county offices of education to post prominently on the homepage of their website their approved LCAP. These changes will be reflected in the next LCAP template cycle.

Evaluation Rubrics. Pursuant to LCFF statute, the SBE developed an online tool and interface for an evaluation rubric, called the California School Dashboard, which was launched at the end of 2017 and redesigned at the end of 2018. This tool includes the following components, some of which are still in progress:

1) State and local performance indicators that reflect performance on the LCFF priorities:

- State level indicators are available through the CDE data system, CALPADS, are comparable statewide, and include the following:
    - Academic indicator based on student test scores on English Language Arts (ELA) and Math for grades 3–8, including a measure of individual student growth, when feasible, and results on the Next Generation Science Standards assessment, when available.
    - College/career indicator, which combines Grade 11 test scores on ELA and Math and other measures of college and career readiness.
    - English learner indicator that measures progress of English learners toward English language proficiency and incorporates data on reclassification rates.
    - High school graduation rates.
    - Chronic absence rates, when available.
    - Suspension rates by grade span.
- Local indicators rely on local data and are not reported at the state level. These include:
    - Appropriately assigned teachers, access to curriculum-aligned instructional materials, and safe, clean and functional school facilities.
    - Implementation of state academic standards.
    - Parent engagement.

- School climate – local climate surveys.
- Coordination of services for expelled students (COEs).
- Coordination of services for foster youth (COEs).

2) Performance standards for each indicator allowing LEAs and schools to identify both progress and needed improvements. For each state indicator, the SBE has determined a measurement based on a LEAs current performance and improvement over time (over a three-year period if available). This combined measure then falls into a color-coded range, with each LEA, school, and student group measured annually. This method allows for an easily accessible display as part of the dashboard for district and school administrators, teachers, students, parents, and other stakeholders. Currently the SBE has approved performance standards for the state indicators and for local indicators, the SBE has approved some self-reflection tools and a method for LEAs to self-assess as "met", "not met", or "not met for more than two years." The SBE and CDE have several working groups in special subject areas that will continue to inform and help refine the indicators over the next few years.

The dashboard uses a color-coded indicator to show how an LEA scores on a particular indicator. For example, blue means that the LEA is in the highest performance category, while red means that an LEA is in the lowest performance category. Additional functionality allows for the user to look at school and student group data and understand if an LEA is improving in any indicator area.

The LCAP template was updated in 2017 to include a description of those indicators for which the LEA scored orange or red and the actions and services an LEA is undertaking in these areas.

Technical Assistance and Support of LEAs. Along with the release of the Dashboard, beginning in December 2017, the SBE identified LEAs in need of assistance based on LEA scores on the dashboard indicators and created a tiered structure, based on statute, to provide this assistance. The tiers of support are described below in more detail.

Overview of Statewide System of Support

Level of Support	Description of Supports Available
Support for All LEAs and Schools (Level 1)	Various state and local agencies provide an array of resources, tools, and voluntary assistance that **all** LEAs may use to improve student performance at the LEA and school level and narrow disparities among student groups across the LCFF priorities, including recognition for success and the ability to share promising practices.
Differentiated Assistance (Level 2)	County superintendents, the CDE, charter authorizers, and the California Collaborative for Educational Excellence (CCEE) provide **differentiated assistance** for LEAs and schools, in the form of individually designed assistance, to address identified performance issues, including significant disparities in performance among student groups.
Intensive Intervention (Level 3)	The State Superintendent of Public Instruction or, for charter schools, the charter authorizer may require more **intensive interventions** for LEAs or schools with persistent performance issues over a specified time period.

Source: State Board of Education: January 18, 2018 Agenda, Item 3

In the first cohort identified for differentiated assistance in December of 2017, a total of 228 districts were identified with approximately two-thirds of the identified LEAs identified based on the performance of their students with disabilities student group in one or more priority areas. In December of 2018, the second cohort of LEAs was identified; totaling 374 LEAs are eligible to receive differentiated assistance in 2018, based solely on state indicators. Of the 374 LEAs, 239 obtained differentiated assistance eligibility status for the first time in 2018, 135 maintained their eligibility status from 2017, and 93 eligible for differentiated assistance in 2017 are no longer eligible for assistance in 2018. In January 2019, 12 additional LEAs were identified for differentiated assistance based on local indicator data. The three student groups in greatest need of support (based solely on state indicator data) are:

- Students with disabilities: 243 LEAs are eligible for differentiated assistance
- Homeless students: 145 LEAs are eligible for differentiated assistance
- Foster youth: 106 LEAs are eligible for differentiated assistance

As part of the 2018-19 budget agreement, a structure for providing support for LEAs identified for differentiated assistance or intervention was refined in statute, specifying the process for COEs to support school districts in need of technical assistance and the ability of a school district to seek assistance from the COE and other providers. Similar adjustments were made to the process for the SPI to assist struggling COEs.

Statute also established a formula for providing funding for COEs to support school districts. Under this formula, COEs would receive base funding plus additional funding determined by the number of school districts identified as in need of differentiated assistance on the dashboard, and a total of $53.8 million in ongoing funding was provided to COEs for this purpose in 2018-19.

Additional Support Structures. In 2018-19, statute also established various lead agencies to provide support and spur capacity building across the state as well as to provide a resource for specific issue areas. These lead agencies are described below:

- **Geographic Lead Agencies.** The 2018-19 budget provided $4 million in ongoing Proposition 98 funding to establish between six and 10 COEs as geographic lead agencies in their region. The responsibilities of the lead COEs include building the capacity of other COEs in the region, coordinating and collaborating technical assistance across the region, providing technical assistance to a school district if a COE is unable to, and identifying existing resources and developing new resources upon request of the CCEE or the SPI. As of March, 2019, seven geographic lead agencies have been established.

- **Special Education Local Plan Areas (SELPAs) Lead Agencies.** The 2018-19 budget also included $10 million in ongoing Proposition 98 funding to establish between six and 10 (SELPAs) to serve as special education resource leads to work with COEs to improve outcomes for students with disabilities.

- **Expert Lead Agencies.** The 2018-19 budget also included funding from a variety of sources for lead agencies with different expertise.

California Collaborative for Educational Excellence. The CCEE was created as part of the new LCFF accountability framework, with its goal to advise and assist school districts charter schools, and COEs to achieve identified outcomes in their LCAPs under the LCFF. Statue allows the CCEE to accept requests or referrals for technical assistance after consulting with the SPI. The CCEE may contract with individuals, LEAs, or organizations with expertise in the LCAP state priority areas and experience in improving the quality of teaching, improving school and district leadership, and addressing the needs of student populations (such as unduplicated students or students with exceptional needs.) Since its inception, the CCEE has been provided one-time funding, totaling over $30 million for its initial operations and one-time work to inform future operations. Although the initial infusion of funding was provided in the 2013-14 year, the CCEE has taken a few years to fully staff up and develop as an agency. Since 2018-19, the CCEE has been provided with approximately $11 million in ongoing funding.

The CCEE has conducted statewide training for LEAs and education stakeholders on the LCAP and the school dashboard, with a focus on improving student outcomes and closing the achievement gap. Statewide trainings and webinars focusing on different components of the accountability system are continuing, as well as training for individual LEAs by request, or groups of stakeholders. In addition, the CCEE has facilitated the development of Professional Learning Networks (PLNs) made up of COEs, statewide organizations, and non-profits led by facilitators to support collaborative efforts to build capacity. The CCEE is currently reviewing results and deliverables from the PLNs.

The CCEE was also charged with conducting a pilot program designed to assist the CCEE in developing and designing their work in providing technical assistance and intervention to LEAs. The CCEE has undertaken pilot projects in 11 LEAs that reflect urban, suburban, and rural areas with different needs for technical assistance, including a COE and a charter school. LEAs volunteered for the pilot program and the CCEE selected LEAs to participate based on whether the LEA had: 1) persistent academic/achievement challenges as evidenced by achievement gaps between student

demographic groups, test scores, or other metrics; 2) a leadership team, including the Board of Trustees overseeing the LEA, that fully commits to participating in pilot process; and 3) the support of their COE. The CCEE is currently wrapping up the pilot program.

The work of the CCEE moving forward will be focused to a greater extent on capacity building through the regional leads and providing support for LEAs in differentiated assistance or intervention, as needed.

Federal Accountability.

In December 2015, Congress passed the Every Student Succeeds Act (ESSA), which reauthorized the Elementary and Secondary Education Act of 1965 and required every state to develop a plan for using supplemental federal funding that states receive under ESSA for low-income students and English learners. The SBE was responsible for developing California's state plan as a condition of receiving approximately $2.5 billion in annual federal funding under ESSA. The state plan, which the U.S. CDE approved in July 2018, aligned California's approach to meet federal requirements to the greatest extent possible with state law. ESSA requires states to identify schools for different types of support, including:

1. At least the lowest performing five percent of Title I schools (comprehensive support)

2. High schools with graduation rates below 67 percent (comprehensive support)

3. Schools with "consistently underperforming" student groups (targeted support)

4. Schools identified under number three where a student group on its own is performing at or below the level of schools identified under number one additional targeted support

The table below shows the number of schools identified as eligible for federal support.

Identification Status	Number of Non-Charter Schools	Number of Charter Schools	Total
CSI (Based on Graduation Rate Only; Title I and non-Title I Schools)	206	94	300
CSI (Based on State Indicator Results; Title I Schools Only)	447	34	481
ATSI (Title I and non-Title I Schools)	818	41	859
General Assistance (Title I and non-Title I Schools)	7,230	1,040	8,270
Total	8,701	1,209	9,910

Governor's Accountability-Related Proposals:

County Office of Education Technical Assistance – The proposed budget includes $20.2 million in Proposition 98 General Fund for COEs to support school districts that are in need of improvement under the state's accountability system to be distributed pursuant to a statutory formula enacted in the 2018-19 budget. These funds would support 374 school districts identified in 2018-19 through the state's accountability measures to need targeted technical assistance.

Online Accountability Systems Alignment. The Administration proposes to provide $350,000 in one-time Proposition 98 funding to support the alignment and integration of online platforms supporting the California School Dashboard, LCAP, and School Accountability Report Card. This project would allow for the streamlining of information, such that the public may access the data through one point of entry and eliminate duplicative information. This funding would go to the San Joaquin COE which currently supports each of these online platforms.

Key Agency Coordination. The Administration proposes trailer bill language that would require the CCEE, and the CDE, in consultation with the SBE, to establish a formal process for coordinate the work of the Departments and agencies (including geographic, expert, and special education resource lead agencies) in supporting LEAs.

Charter School LCAP transparency. The Administration proposes trailer bill language to specify that charter schools must comply with LCAP requirements, including holding a public hearing and specifies that charter schools must address state priorities 2-8 in their LCAP. The language would also require charter school LCAPs or links to the plans to be posted on the school district, COE, and CDE websites. Finally, the language would require charter schools to provide translation services if 15 percent or more of their students speak a primary language other than English, consistent with school district requirements.

Federal Accountability Funding. The Administration includes $130.1 million in federal funding for schools identified for comprehensive support and improvement under ESSA.

Subcommittee Questions:

1) The budget has provided one-time support for various online projects supported by the San Joaquin COE. Does the Administration have an estimate on the amount of ongoing resources that will be needed to maintain these projects?

2) What initial activities have been undertaken by the regional leads and what does the CCEE anticipate their role will be in the upcoming year?

3) What feedback has been received on the differentiated assistance provided to LEAs to date?

Staff Recommendation:

Hold Open.