California State Senate

COMMITTEE
ON
BUDGET AND FISCAL REVIEW

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Governor's 2013-14 Budget – Multi-Year Plan for UC, CSU, and CCC

I. Department of Finance

- Nick Schweizer, Program Budget Manager, Education Systems Unit

II. Legislative Analyst's Office

- Mac Taylor, Legislative Analyst

III. Segment Representatives (Panel)

- Patrick Lenz, Vice President of Budget and Capital Resources, University of California

- Robert Turnage, Assistant Vice Chancellor for Budget, California State University

- Dan Troy, Vice Chancellor, California Community College Chancellor's Office

IV. Public Testimony

ATTACHMENTS:

Legislative Analyst: Analysis of the Higher Education Budget (2013-14 Budget)

SBFR Summary and Analysis: Higher Education – Multi-Year Plan

Governor’s Budget Summary: Higher Education

The 2013-14 Budget:

Analysis of the Higher Education Budget

MAC TAYLOR • LEGISLATIVE ANALYST • FEBRUARY 12, 2013

LAO

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EXECUTIVE SUMMARY

Overview

California's public higher education system consists of the University of California (UC), California State University (CSU), California Community Colleges (CCC), Hastings College of the Law (Hastings), and the California Student Aid Commission (CSAC). The Governor's budget provides $11.9 billion in General Fund support for higher education in 2013-14. This is $1.4 billion (13 percent) more than the revised current-year level. After making adjustments for enrollment and accounting changes that otherwise would distort year-to-year comparisons, programmatic per-student funding increases 4 percent at UC, 7 percent at CSU, and 10 percent at CCC.

Higher Education System in Review

Governor Has Major Concerns About Higher Education in California. Most notably, the Governor is concerned about a higher education cost structure that "continually increases without necessarily adding productivity or value." He contends that neither the state's taxpayers nor students can continue to sustain the current system. The Governor also notes that current funding approaches—historically based solely on enrollment—reinforce the high-cost delivery model and do not focus attention on student success and efficiency. Additionally, he asserts that many students cannot get into the high-demand courses they need to meet graduation requirements, resulting in their taking unnecessary units to remain enrolled and longer to graduate. The Governor further calls attention to low graduation and transfer rates.

Data Generally Support Governor's Claims. The traditional higher education delivery model—based on a faculty member with an advanced degree teaching a relatively small number of students in a physical setting—is high cost relative to other potential higher education and industry models. These high labor and facility costs are even greater at institutions that focus heavily on research. Costs in California are particularly high given a greater share of its public university students attend institutions with very high research activity. Moreover, average spending per student at UC is more than 20 percent higher than other universities with very high research activity. Data also suggest excess unit-taking is an issue at CCC and CSU. For example, in 2011-12, CCC provided instruction to nearly 95,000 students who already had earned 90 or more degree-applicable units—one academic year beyond that typically required for an associate degree or transfer. Graduation rates also are low at CCC and CSU, with only 23 percent of full-time CCC students graduating or transferring within three years and fewer than half of CSU students graduating within six years.

Multifaceted, Multiyear Budget Plan. In response to these issues, the Governor proposes a multiyear budget plan. The main component of the plan is annual unallocated base General Fund increases for the universities, with similar increases in Proposition 98 funding expected for the community colleges. The Governor loosely links these base increases with an expectation the segments improve their performance but does not link them to enrollment expectations. The Governor's plan also provides the universities with more autonomy in funding debt service, changes how the state funds retirement costs at CSU, changes how the state funds CCC, earmarks funding for several technology-related initiatives, freezes tuition levels, caps the number of state-subsidized college units, and modifies two CCC financial aid policies.

Governor's Overall Approach Unlikely to Improve System

Justification for More Funding and Less Legislative Involvement Unclear. Although we believe the Governor's budget plan has drawn attention to some notable problems, we have serious concerns with several of his specific budget proposals. Most notably, by providing the segments with large unallocated increases only vaguely connected to undefined performance expectations, the Governor cedes substantial state responsibilities to the segments and takes key higher education decisions out of the Legislature's control. We recommend the Legislature reject the Governor's proposals relating to unallocated base increases, combining the universities' capital and support budgets, allowing the universities to restructure their debt, and eliminating enrollment targets. Instead, we recommend the Legislature allocate any new funding first to meet the state's highest existing priorities, including debt service, employee pension costs, and paying down community college deferrals. If more funding is provided than needed to meet these existing funding obligations, we recommend the Legislature link the additional funding with explicit enrollment and performance expectations.

Extended Tuition Freeze Likely Would Have Negative Long-and Near-Term Consequences. We also have serious concerns with the Governor's extended tuition freeze proposal, as it very likely would result in steep tuition increases during the next economic downturn and reduced accountability in the near term. Moreover, tuition levels and students' share of cost currently are low. After accounting for state and institutional financial aid, the average share of cost paid by California students is about 30 percent at UC and CSU and 6 percent at CCC.

Some Good Ideas but Associated Proposals Need Reworking

Some Problems Likely Addressed by Redistributing Rather Than Increasing Funding. In some cases, we think the Governor's basic ideas are worthwhile but likely could be implemented within existing resources. For example, increasing the availability of required courses while reducing the amount of excess course-taking could be done within existing resources. Likewise, the segments could leverage an existing repository of online courses developed by faculty and enable students to more easily access those courses largely, if not entirely, within existing resources.

Higher Education Funding Models Up for Redesign. We also think revisiting the ways the state allocates funding to the segments is worthwhile, but we again have concerns with the Governor's specific proposals. The Governor's approach for the universities appears to fund neither student access nor success whereas his approach for the community colleges focuses only on one poor measure of student success. We envision a better funding model that balances the state's dual goals of access and success. Under a redesigned system, instead of basing funding entirely on enrollment or on vague performance expectations, the Legislature would establish clear expectations in areas such as program completions, degrees earned, research activity, and cost reductions.

INTRODUCTION

In this report, we (1) provide a high-level overview of the Governor's 2013-14 higher education budget, (2) examine the Governor's concerns about California's public higher education system, (3) discuss the various components of the Governor's multiyear budget plan for higher education, and (4) provide an assessment of and alternatives to the Governor's plan. We discuss various other issues relating to the community colleges, including adult education restructuring, Proposition 39 energy efficiency projects, and payment deferrals in a companion report, *The 2013-14 Budget: Proposition 98 Education Analysis.*

OVERVIEW

Governor Proposes $1.4 Billion in Additional General Fund Support for Higher Education. California's publicly funded higher education system consists of the UC, CSU, CCC, Hastings, and CSAC. As shown in Figure 1, the Governor's budget provides $11.9 billion in General Fund support for higher education in 2013-14. This is $1.4 billion (13 percent) more than the revised current-year level. As shown in Figure 2 (see next page), the bulk of the new funding is for adult education restructuring, base increases at the universities, and a general purpose increase for the community colleges. A portion of the total ongoing General Fund increase is linked with provisions in the 2012-13 budget package that provided $125 million each to UC and CSU if they did not raise student tuition levels.

Total Core Funding for Higher Education Would Increase $1.2 Billion. Figure 3 (see page 7) offers a broader perspective on higher education funding in that it shows both General Fund support and support from other core funding sources, including student tuition revenue, federal funds, and local property taxes (for the community colleges). In 2013-14, higher education would receive $18.4 billion in total core funding—reflecting a year-to-year increase of 7 percent.

Figure 1
Higher Education General Fund Support[a]

(Dollars in Millions)

	2011-12 Actual	2012-13 Revised	2013-14 Proposed	Change From 2012-13 Amount	Change From 2012-13 Percent
University of California	$2,504	$2,567	$2,846	$279	11%
California State University	2,228	2,492	2,809	317	13
California Community Colleges	3,612	3,802	4,503	701	18
Hastings College of the Law	8	9	10	—	3
California Student Aid Commission	1,533	1,624	1,722	98	6
Grand Totals	**$9,885**	**$10,494**	**$11,890**	**$1,396**	**13%**

[a] For UC, CSU, and Hastings College of the Law, amounts include general obligation bond debt service in each year. For CCC, amounts include general obligation bond debt service and funding for the CCC Chancellor's Office. For the California Student Aid Commission, amounts include federal Temporary Assistance for Needy Families and the Student Loan Operating Fund support that directly offsets General Fund costs.

Figure 2
Governor's Major Higher Education Budget Changes[a]

Change From Revised 2012-13 Budget to Proposed 2013-14 Budget (In Millions)

Provide funding for CCC adult education	$300
Provide 5 percent base increases for UC, CSU, and Hastings College of the Law	251
Fund 2012-13 tuition buyout at UC and CSU	250
Provide general purpose funds to CCC	197
Fund increased Cal Grant costs	100
Allocate funds to CCC for energy efficiency projects	50
Fund new CCC online project	17
Create new CCC apprenticeship program	16
Other adjustments	216
Total Changes	**$1,396**

[a] Excludes transfer of $401 million in general obligation bond debt service funding to UC, CSU, and Hastings College of the Law since this has no immediate programmatic effect on the universities and does not increase overall state spending.

Programmatic Funding Per Student Would Increase at All Higher Education Segments. Figure 4 (see page 8) shows another perspective on higher education funding—one that adjusts for enrollment levels and any accounting changes (such as payment deferrals) that otherwise would distort year-to-year programmatic comparisons. This figure focuses on the amount of funding generally available to support operational costs. As shown in Figure 4, increases in programmatic per-student funding range from 4 percent at UC to 10 percent at CCC.

Package Includes Funding Increases for State's Financial Aid Programs. The Governor's budget includes Cal Grant funding increases of $60 million in the current year and an additional $100 million in 2013-14. The increased costs result from growth in student participation in the program and shifts in the types of awards for which students qualify (with more students qualifying for grants that cover both tuition and a portion of living costs). Figure 5 (see page 8) shows the number of Cal Grant recipients and total award amounts by segment.

HIGHER EDUCATION SYSTEM IN REVIEW

Governor Has Major Concerns About System

The *2013-14 Governor's Budget Summary* raises several concerns about higher education in California. Specifically, the Governor makes the following claims:

- ***High-Cost Delivery Model Is Not Sustainable.*** The Governor describes a higher education cost structure that "continually increases without necessarily adding productivity or value." He contends that neither the state's taxpayers nor students and their families can continue to sustain higher education institutions under the current model.
- ***Universities' Budget Plans Assume Continued Growth in Costs.*** The Governor points out that the UC Regents' and CSU Trustees' budget plans are predicated on the current high-cost model. They assume continued growth in funding at levels far exceeding projected growth in state revenues and personal income. The Governor deems such plans unrealistic and instead urges the segments to reduce instructional costs, decrease time to degree, and increase graduation rates.

Figure 3
Higher Education Core Funding

(Dollars in Millions)

	2011-12 Actual	2012-13 Revised	2013-14 Proposed	Change From 2012-13 Amount	Change From 2012-13 Percent
University of California					
Net tuition[a]	$2,558	$2,480	$2,523	$43	2%
General Fund[b]	2,504	2,567	2,846	279	11
Other UC core funds	388	441	385	-55	-13
Lottery	30	37	37	—	—
Subtotals	($5,479)	($5,525)	($5,792)	($267)	(5%)
California State University					
General Fund[b,c]	$2,228	$2,492	$2,809	$317	13%
Net tuition[a]	1,982	1,919	1,919	—	—
Lottery	42	56	56	—	—
Subtotals	($4,252)	($4,467)	($4,784)	($317)	(7%)
California Community Colleges					
General Fund	$3,612	$3,802	$4,503	$701	18%
Local property tax	1,974	2,256	2,171	-85	-4
Fees	354	387	387	—	—
Lottery	197	186	186	—	—
Subtotals	($6,137)	($6,631)	($7,247)	($616)	(9%)
Hastings College of the Law					
Net tuition[a]	$35	$37	$36	-$1	-1%
General Fund[b]	8	9	10	—	3
Lottery[d]	—	—	—	—	—
Subtotals	($44)	($46)	($46)	(—)	(-1%)
California Student Aid Commission					
General Fund	$1,471	$736	$720	-$16	-2%
Student Loan Operating Fund	62	85	60	-25	-29
TANF funds	—	804	943	139	17
Subtotals	($1,533)	($1,624)	($1,722)	($98)	(6%)
Totals[e]	**$16,465**	**$17,213**	**$18,413**	**$1,200**	**7%**
General Fund	$9,823	$9,606	$10,887	$1,281	13%
Net tuition/fees[e]	3,950	3,742	3,687	-55	-1
Local property tax	1,974	2,256	2,171	-85	-4
Other	450	1,329	1,388	59	4
Lottery	269	279	279	—	—

[a] Reflects tuition after discounts provided through institutional financial aid programs.
[b] Includes general obligation bond debt service for UC, CSU, and Hastings College of the Law.
[c] Beginning in 2012-13, health benefit costs for CSU retired annuitants are included in CSU General Fund.
[d] Hastings College of the Law receives about $200,000 in lottery funds.
[e] Does not include UC and CSU tuition paid from the General Fund for Cal Grant awards.
TANF = Temporary Assistance for Needy Families.

Figure 4
Programmatic Funding Per Student[a]

	2011-12 Actual	2012-13 Revised	2013-14 Proposed	Change From 2012-13	
				Amount	Percent
Hastings College of the Law	$32,483	$39,219	$41,048	$1,829	5%
University of California	24,411	24,909	25,940	1,031	4
California State University	11,667	12,729	13,656	927	7
California Community Colleges	5,349	5,447	5,969[b]	522	10

[a] Excludes lottery, general obligation bond debt service, and California State Teachers' Retirement System costs. Includes other General Fund, net tuition and fees, other university core funds, federal Education Jobs Act funds, and local property taxes.

[b] For 2013-14, the Governor's budget provides CCC with additional programmatic funding without assuming any increase in the system's funded enrollment level. To the extent that CCC's enrollment target is adjusted commensurate with any base increase, programmatic per-student funding will be lower.

- ***Enrollment-Based Funding Does Not Promote Innovation and Improvement.*** The Governor notes that current funding approaches—historically based on enrollment—reinforce the high-cost delivery model and do not focus attention on important outcomes such as student success and efficiency.

- ***Unavailability of Required Courses Increases Total Costs for State and Students.*** The Governor asserts that the high-demand courses many students need to meet graduation requirements often are unavailable. As a result, the Governor argues many students take unnecessary units to remain enrolled and take longer to graduate. These factors increase costs for both the state and students.

- ***Student Outcomes Generally Are Poor.*** Calling attention to low graduation and transfer rates, the Governor argues that poor student outcomes lead to

Figure 5
Cal Grant Recipients and Funding by Segment

(Dollars in Millions)

	2011-12 Actual	2012-13 Revised	2013-14 Proposed	Change From 2012-13	
				Amount	Percent
Number of Recipients					
California State University	77,485	88,645	97,426	8,781	10%
California Community Colleges	76,062	80,786	87,926	7,140	9
University of California	57,394	60,687	64,885	4,198	7
Private nonprofit institutions	23,798	25,483	26,840	1,357	5
Private for-profit institutions	15,220	13,278	11,542	-1,736	-13
Totals	**249,959**	**268,879**	**288,619**	**19,740**	**7%**
Funding					
University of California	$691	$733	$782	$48	7%
California State University	394	454	509	55	12
Private nonprofit institutions	219	226	238	12	5
Private for-profit institutions	104	90	66	-24	-27
California Community Colleges	88	91	99	9	10
Totals	**$1,496**	**$1,594**	**$1,694**	**$100**	**6%**

even greater inefficiencies in the higher education system.

- ***Rapid Tuition Increases Have Been a Hardship for Some Families.*** The Governor also notes that recent tuition increases have been difficult for some families that do not qualify for financial aid. At the same time, he acknowledges that despite these tuition increases California has some of the lowest fees in the country. He also points out that the state's financial aid programs are among the nation's most generous. As a result of low tuition and high aid levels, the Governor concludes that public postsecondary education remains relatively affordable for California families.

Data Generally Support Governor's Claims

Available data support many of the claims the Governor makes about higher education. For a few of his claims, however, the data are less compelling.

Traditional Delivery Model Is High Cost. The traditional higher education delivery model has a few basic attributes that result in high costs relative to other potential higher education models as well as other industry models. Most importantly, the model is based on a faculty member with an advanced degree teaching a relatively small number of students in a physical setting. These high labor and facility costs are even greater at institutions that focus heavily on research. This is because faculty at these institutions tend to have a lower teaching load compared to institutions that focus less on research. Universities with a very high research focus also have relatively expensive facilities given the additional need for laboratories and state-of-the-art technology. Another factor that contributes to high costs is the very common practice of measuring educational attainment by the amount of time a student spends in school (usually the equivalent of at least four years for a bachelor's degree and at least two years for an associate degree). This focus on time in school rather than more refined measures of learning perpetuates the traditional higher education cost structure.

University Costs in California Are Particularly High. Not only is the traditional higher education delivery model high cost, but data suggest that costs are particularly high in California. One reason is that a greater share of California's public university students attend institutions with very high research activity (which tend to be more expensive than other universities). While one-third of university students attend such institutions nationally, 40 percent of California's university students do. In addition, average spending per student at these UC universities is more than 20 percent higher than at their national counterparts. Several factors could result in higher costs, including lower faculty workload expectations, a more science-oriented mix of academic programs, and high compensation.

Universities' Budget Plans Predicated on State Maintaining High-Cost Delivery Model. In developing their own budget plans, the segments have included various components related to the high-cost delivery model, including proposed increases in compensation, employee benefit costs, and infrastructure needs. In addition, the universities' plans propose to reverse some recent budget reductions, for example by reducing student-faculty ratios. Overall, UC's and CSU's own budget plans reflect core spending increases of 8 percent and 11 percent, respectively, from the current year. Because both plans assume the state General Fund rather than tuition will cover the entirety of these spending increases, projected increases in state funding are higher—12 percent and 18 percent, respectively. As the Governor points out, these increases are very high relative to the projected 4.5 percent increase in state revenues.

Many Students Accrue More Course Units Than Required for Graduation. Higher education costs also are driven up by excess unit-taking. Standard course requirements for graduation generally total 60 semester units (or 90 quarter units) for an associate degree and 120 semester units (or 180 quarter units) for a bachelor's degree. Students who accrue units in excess of these requirements generally take longer to graduate, increase state and student costs, and crowd out other students. Excess unit-taking is most prevalent at CCC and CSU. In 2011-12, CCC provided instruction to more than 350,000 students who already had earned 60 or more degree-applicable semester units. Of these students, nearly 95,000 had earned more than 90 units. At CSU, about 90,000 students already had accrued 120 semester units *before* starting the current academic year. Of these students, about 13,000 had accrued at least 150 units and 2,000 had accrued at least 180 units.

Causes of Excess Unit-Taking Are Varied. Several factors contribute to excess unit-taking. Some of these involve choices students make, either intentionally or because they lack adequate information. Others are related to campus decisions. Unfortunately, due to data limitations, it is not possible to determine the share of excess unit-taking caused by each of these factors.

- ***Some Students Choose to Take Extra Courses.*** Some students choose to take courses that are not required for their majors because of interest in the subject or to make themselves more marketable to employers or graduate schools. Others change majors a number of times, repeat courses several times to improve their grades, or remain in school for other reasons after meeting degree requirements.

- ***Unavailability of Courses Also Has a Role.*** Students who cannot get into their required courses (due to oversubscribed courses or student scheduling constraints) sometimes substitute other, nonrequired courses to remain eligible for student financial aid, insurance, and other student benefits. As they enroll in substitute courses, these students crowd out others who may need the courses to meet degree requirements.

- ***Institutional Policies Limit Applicability of Some Units.*** Course articulation decisions made at the campus or department level also may result in a student accruing excess units. For example, transfer students may find that some of their community college courses are not accepted toward degree requirements by the receiving university.

Graduation Rates in California Tell Mixed Story. Student outcomes vary among California's public higher education segments. (Outcomes also vary significantly among institutions within each segment.) This variation is due in part to the pools of students from which the three segments draw. Currently, the top one-eighth of all graduating high school students are eligible for admission to UC, the top one-third are eligible for admission to CSU, and all persons 18 years or older are eligible to attend CCC. As Figure 6 shows, more than 80 percent of UC students graduate within six years, compared with 47 percent of CSU students. Only 23 percent of CCC students graduate or transfer within three years. These official graduation rates, reported by the U.S. Department of Education, reflect the share of first-time, full-time freshmen who graduate within 150 percent of the normal time needed to complete all program requirements. The graduation rate does not reflect student success broadly at CCC because only a small fraction of CCC students enter as full-time freshmen and some students may not be seeking degrees. Even considering these caveats, graduation rates at CCC are disconcertingly low. Figure 6 also shows that low graduation rates are a national problem, not only a California problem. In fact, graduation rates at UC and CSU are better than the rates for comparable institutions nationally, but the CCC rate is lower than the average of two-year public institutions in all other states.

Spending Per Degree Also High. One way of measuring the productivity of the state's investment is to consider average annual spending per degree. This measure is affected by both spending and the number of degrees conferred per student. Spending per degree cannot be compared readily across the segments because they (1) offer a different mix of undergraduate and graduate degrees and certificates and (2) do not track undergraduate and graduate instructional spending separately. California's public segments, however, can be compared with similar institutions nationally. Despite relatively high graduation rates, UC's average spending per degree ($166,000) is well above that of other universities with very high research activity ($140,000). (This measure is more difficult to interpret for CSU and CCC, as students transfering to CSU and CCC students not seeking degrees both complicate spending-per-degree comparisons.)

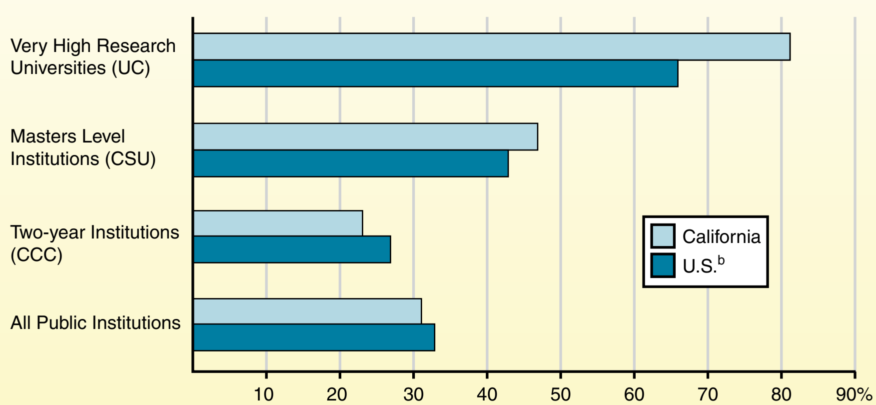
Tuition and Fee Levels in California Are Relatively Low. In addition to focusing on higher education costs and student outcomes, the Governor makes certain claims about tuition and fees in California. Although tuition and fee rates have nearly doubled since 2007-08 at UC and CSU—and more than doubled at CCC—these rates remain comparatively low. The per-unit fee ($46) at the CCC is lowest among the 50 states, undergraduate tuition at CSU ($5,472) is lowest among its 15 public university peers, and undergraduate tuition at UC ($12,192) is slightly above the average of its four comparison public research universities.

California's Financial Aid Programs Keep College Education Affordable for Financially Needy Students. About half of the students currently enrolled in public colleges and universities receive need-based financial aid specifically to cover full tuition and fee costs. These financial aid awards increase dollar-for-dollar as tuition and fees increase. As a result, spending for both Cal Grants and institutional financial aid has

Figure 6

California Graduation Rates Mixed Compared to Rest of Nation

2011 Graduation Rates for Undergraduates at Public Institutions[a]



[a] Reflects the percent of first-time, full-time, degree/certificate-seeking undergraduates who graduate within 150 percent of the normal time to completion, typically three years for an associate degree and six years for a bachelor's degree. For CCC, includes percent of students that transfer to other institutions within three years. Figure excludes UC San Francisco, UC Merced, San Diego State University, and California Maritime Academy due to classification issues.

[b] Reflects average for public institutions in all other states.

doubled since 2007-08 while the amount actually paid by families has increased far less.

With Low Fees and High Aid, Net Price Has Not Increased Much for Lower Income and Many Middle-Income Families. Figure 7 shows the increase in average net price for families at various income levels from 2008-09 to 2010-11. (Average net price is the total cost of attendance—including tuition, room and board, and other expenses—after subtracting government and institutional grants and scholarships. It is only reported for families receiving federal student aid, including student loans.) While tuition and fees increased between 30 percent and 45 percent during this period, average net price increased 4 percent or less for most families at the universities and 6 percent at the community colleges. For UC students with family income above $110,000 and CSU students with family income above $75,000, net price increased more significantly. Though they are less likely to qualify for need-based aid, these families may receive other types of federal assistance to help cover education costs, including tax credits, tax deductions, and student loans. Nonetheless, families with these higher income levels typically are more likely to bear the costs of tuition increases.

Student Debt Also Relatively Low. Another result of low fees and high aid is that average student loan borrowing is relatively low for California students. Recent data show that in 2010-11, about half of graduates from California's public universities had student loan debt, and the average debt for these students was $16,840. (This is lower than the amount cited in the Governor's budget, which includes graduates of nonpublic institutions.) By comparison, the average debt for public university graduates nationally—57 percent of whom had student loans—was more than $23,000.

Figure 7

Average Net Price of College

Total Cost of Attendance Less Financial Aid for Full-Time Resident Undergraduates[a]

Family Income Level	Percent of Students	2008-09	2009-10	2010-11	Two-Year Change Amount	Two-Year Change Percent
University of California						
$0 - 30,000	37%	$8,200	$8,267	$8,545	$345	4%
$30,001 - 48,000	19	9,811	9,858	9,765	-46	—
$48,001 - 75,000	18	14,403	13,939	13,526	-877	-6
$75,001 - 110,000	12	20,981	21,045	21,606	625	3
Over $110,000	14	23,477	25,032	26,591	3,114	13
California State University						
$0 - 30,000	40	5,626	5,387	5,489	-137	-2
$30,001 - 48,000	20	7,795	7,856	7,916	121	2
$48,001 - 75,000	17	11,245	11,377	11,654	409	4
$75,001 - 110,000	11	13,954	15,468	16,036	2,082	15
Over $110,000	12	14,628	16,338	17,166	2,538	17
California Community Colleges						
$0-30,000	100[b]	5,721	5,983	6,058	337	6

[a] Total cost of attendance is the sum of published tuition, required fees, books, supplies, room and board, and other expenses. Average net price is generated by subtracting the average amount of federal, state, local, and institutional grant aid from the total cost of attendance. The figure excludes students who did not apply for or receive federal student loans, grants, or work study.

[b] The proportion of CCC students with family income above $30,000 that complete the federal financial aid application is very small.

GOVERNOR'S MULTIYEAR BUDGET PLAN

As part of his overall approach to addressing these issues, the Governor proposes a multiyear higher education budget plan. The plan includes annual unallocated base increases for each segment. The Governor links these base increases with an expectation the segments improve their performance in certain areas. The Governor's plan also makes changes in the funding of debt service at the universities and retirement costs at CSU. The plan includes no enrollment targets for the universities but does include a proposal to change how funding is allocated to the community colleges. The Governor's plan also earmarks funding for several technology-related initiatives. In addition, his plan includes proposals to freeze tuition levels, cap the number of state-subsidized units, and change two CCC financial aid policies. Below, we describe each of these proposals. In the next section, we evaluate them and, in many cases, offer alternatives.

Proposes Annual Unallocated Base Increases. The main funding component of the Governor's multiyear higher education budget plan is annual unallocated base General Fund increases for each of the higher education segments over the next four years (2013-14 through 2016-17). For 2013-14, the Governor provides 5 percent base increases of $125 million each for UC and CSU and nearly $200 million for CCC. (The 5 percent base increases for the universities are identical because he bases them both on UC's budget.) University funding would increase by an additional 5 percent in 2014-15 and 4 percent in each of the following two fiscal years. The Governor also expects CCC funding to grow "significantly" over the next several years.

Desires Better Student Outcomes. The Governor links his proposed base increases with the segments' success in achieving certain objectives, including improving graduation rates at all segments, increasing the CCC transfer rate, and improving credit and basic skills course completion. To help achieve these objectives, the Governor expects the segments to implement certain strategies, including increasing the availability of courses, using technology to deliver quality education to greater numbers of students in high-demand courses, improving course management and planning, using faculty more effectively, and increasing use of summer sessions.

Combines Funding for Capital and Support Budgets . . . The Governor also proposes to shift a total of about $400 million in general obligation bond debt service for UC, CSU, and Hastings to the segments' support budgets. Each segment would receive the amount associated with 2013-14 general obligation debt service payments for its capital projects: $201 million for UC, $198 million for CSU, and $1 million for Hastings. Since these funds already were being accounted for in a separate appropriation, the shift does not increase state costs. The Governor also proposes to remove current restrictions specifying how much of the universities' support budgets are to be used to repay state lease-revenue debt. To ensure that state debt for all projects continues to be repaid, however, the State Controller would automatically transfer the appropriate amounts out of the universities' budgets each year.

. . . And Removes Legislative Prerogative in Capital Projects Moving Forward. Under the proposal, Department of Finance (DOF) would continue to review and approve capital projects for the universities, but the Legislature would no longer be involved in making these decisions. Projects using state funds would be limited to academic facilities needed for safety, enrollment growth or modernization purposes, as well as infrastructure projects that support academic programs. Though the administration indicates the universities potentially still could request state bond funding for their projects, the Governor also proposes to allow them to pledge General Fund monies to issue their own debt for capital projects.

Allows Universities to Restructure State Bond Debt. The Governor further proposes to allow UC and CSU to restructure existing state lease-revenue debt related to their projects. For example, the state currently has about $2.5 billion in outstanding lease-revenue debt for projects built at UC. In 2013-14, the state will spend about $221 million to service this debt. Under the Governor's proposal, UC would be granted the authority to repay the state's bondholders the $2.5 billion owed to them by issuing its own bonds on its own terms.

Limits Future Budget Adjustments for CSU Retirement Costs. Under state law, CSU is required to participate in the California Public Employees' Retirement System (CalPERS). The university system's annual contribution to CalPERS is determined by multiplying its payroll costs by its employer contribution rate. In 2012-13, for example, CSU had an estimated $2.2 billion in payroll subject to CalPERS, an employer contribution rate of 21 percent (for most of its payroll), and a resulting CalPERS contribution of $463 million. Each year, the state adjusts CSU's budget (as it does for other state departments) to account for changes in retirement costs due to changes in payroll and employer rates. Starting in 2013-14, the Governor proposes that future adjustments to CSU's budget for retirement costs be based permanently on 2012-13 payroll costs. According to the administration, this would require CSU to consider full compensation costs for any decision to increase its payroll.

Does Not Include Enrollment Targets for Universities. Figure 8 shows enrollment levels for each of the segments, as reflected in the Governor's budget, though the administration indicates the information is only for display purposes. Unlike historical budget practice, the administration indicates that it will not set enrollment targets for UC and CSU as part of the multiyear plan. The Governor also does not link any of the annual base augmentations to specified enrollment growth. The administration indicates the universities would have full discretion in determining how many students to serve, including how many additional students, if any, to serve. The Governor proposes to continue to fund community college districts based on enrollment (though he proposes to change the way enrollment is calculated, as discussed below). Despite keeping current-year CCC base funding linked with enrollment, the Governor does not require the community colleges to serve additional students in the budget year with his proposed base augmentation.

Bases CCC Funding on Course Completions Rather Than Enrollment. The Governor also proposes to change the basis on which community college districts are funded for credit instruction. Currently, the amount of funding a district receives depends largely on the number of students enrolled at "census"—a point defined in CCC regulations as one-fifth into a given academic term (typically the third or fourth week of the semester). If a student drops a course after this date, the college still earns full payment for that student. Beginning in 2013-14, the Governor proposes to add a second CCC census date at the end of each term. Over a five-year period, there would be a gradual shift in the relative weight of these census dates for purposes of calculating district enrollment. By 2017-18, community colleges would be funded exclusively on the number of students still enrolled in their courses at the end of each term. According

Figure 8

Higher Education Enrollment

Resident Full-Time Equivalent Students[a]

	2011-12 Actual	2012-13 Estimated	2013-14 Projected	Change From 2012-13 Amount	Change From 2012-13 Percent
University of California					
Undergraduate	175,505	173,690	175,040	1,350	1%
Graduate[b]	38,258	39,013	39,013	—	—
Subtotals	(213,763)	(212,703)	(214,053)	(1,350)	(1%)
California State University					
Undergraduate	302,817	294,331	294,331	—	—
Teacher Credential	5,969	5,808	5,808	—	—
Graduate[c]	32,494	31,577	31,577	—	—
Subtotals	(341,280)	(331,716)	(331,716)	(—)	(—)
California Community Colleges[d]	1,098,014	1,108,116	1,108,116	—	—
Hastings College of the Law	1,297	1,135	1,083	-52	-5%
Totals	**1,654,354**	**1,653,670**	**1,654,968**	**1,298**	—

[a] One full-time equivalent student represents 30 credit units for an undergraduate at UC and CSU, 24 credit units for an undergraduate at CCC, and 24 credits units for graduate and law students.

[b] Includes general campus and health science students pursuing graduate academic and professional degrees.

[c] Includes students in doctoral, masters, and postbaccalaureate programs other than teacher credential.

[d] For each year, reflects funded enrollment levels for CCC.

to DOF, any reduction in a district's enrollment (apportionment) monies resulting from this policy change would be automatically redirected to that district's Student Success and Support categorical program, which funds assessment and counseling services. Districts that do not show improvement in course completions after a certain period of time (as defined by the Board of Governors [BOG]) would have this redirected funding swept and reallocated to other colleges. According to the Governor, the purpose of his proposal is to "more appropriately apportion funding by focusing on completion" as well as to provide community colleges with incentives to ensure appropriate student placement and good course management.

Earmarks Funding for Several Online Education and Technology Initiatives. The Governor earmarks $10 million each for UC and CSU to expand the availability of courses through the use of technology. Budget bill language specifies that the funding is for high-demand courses that fill quickly and are required for many different degrees. Under the Governor's plan, UC and CSU would have discretion in allocating funds within their systems but would be required to prioritize development of new courses that can serve greater numbers of students while providing equal or better learning experiences. The Governor also proposes a new $16.9 million CCC categorical program, a portion of which would be used for a similar online initiative to increase the availability of high-demand courses. The CCC Chancellor's Office would be required to submit an associated allocation plan to the DOF for approval. The Governor proposes that CCC use some of the remaining increase to purchase a common learning management software system and the rest to expand opportunities for students to earn course credit by examination.

Proposes No Tuition and Fee Increases Over Extended Period. Figure 9 (see next page) shows tuition and fee levels at each of the segments. The

Governor expects the universities to maintain current tuition and fee levels for the next four years. As a result, tuition and fee levels would remain flat for a six-year period (2011-12 through 2016-17). For the community colleges, the Governor also proposes no fee increase in 2013-14 but DOF indicates the administration is silent as to potential fee increases in the future.

Places Cap on State-Supported Units. The Governor proposes placing a limit on the number of units the state would subsidize per student. Under the proposal, students taking units in excess of the cap generally would be required to pay the full cost of instruction. For 2013-14 and 2014-15, the Governor proposes a cap of 150 percent of the standard units needed to complete most degrees at UC and CSU. (The 150 percent cap equates to 270 quarter-units at UC and 180 semester-units at CSU.) Thereafter, the Governor proposes a cap of 125 percent of the standard required units at UC and CSU—about one extra year of coursework. For the community colleges, the Governor proposes a cap of 90 semester-units beginning in 2013-14. This cap also equates to about one extra year of coursework beyond that required for transfer or an associate degree. For CCC students who transfer to UC or CSU as juniors, the proposed cap is 150 percent in the first two years and 125 percent beginning in 2015-16 of the *additional* units needed to meet the requirements for a bachelor's degree. According to the Governor, the unit cap is intended to create an incentive for students to shorten their time to degree, reduce costs for students and the state, and increase access to more courses for other students.

Proposes Two Changes to CCC Financial Aid Policies. Currently, many CCC students have a choice to apply for a BOG fee waiver using either the Free Application for Federal Student Aid (FAFSA) or a separate BOG fee waiver form.

Figure 9
Annual Tuition and Fees

Mandatory Charges for Full-Time Resident Students

	2011-12 Actual	2012-13 Actual	2013-14 Proposed
University of California			
Systemwide tuition and fees			
Undergraduate	$12,192	$12,192	$12,192
Graduate—academic	12,192	12,192	12,192
Graduate—professional[a]	16,192 - 47,340	16,192 - 50,740	16,192 - 50,740
Average campus fee[b]	989	1,008	1,058
Hastings College of the Law	38,355	44,186	44,186
California State University			
Systemwide tuition and fees			
Undergraduate	5,472	5,472	5,472
Teacher credential	6,348	6,348	6,348
Graduate—masters[c]	6,738	6,738	6,738
Graduate—doctoral[d]	10,500	11,118 - 16,148	11,118 - 16,148
Average campus fee	1,047	1,140	1,140
California Community Colleges	1,080	1,380	1,380

[a] Reflects range for students in business, law, medicine, nursing, and other professional programs.
[b] Reflects average for undergraduates. Campus fees for graduate and professional students are somewhat lower.
[c] Graduate fees also apply to postbaccalaureate programs other than teacher credential programs.
[d] Includes professional doctorates in education, nursing, and physical therapy.

Beginning in 2013-14, the Governor proposes to require CCC students to use only the FAFSA. The purpose of the proposal is to ensure that all financially needy students gain access to the full spectrum of allowable federal and state aid—rather than being able only to access a CCC fee waiver. Requiring students to complete the FAFSA also would result in better information about students' financial means, as the current process for many CCC financial aid applicants relies on self-certified information. The Governor's second proposal is to require campuses to take both student and parent income into account when determining certain students' eligibility for a BOG fee waiver.

LAO ASSESSMENT AND ALTERNATIVES

In this part of the report, we analyze the Governor's specific higher education proposals. We group his proposals into three main sections. The first section focuses on several proposals relating to the Governor's base funding increases for the three segments. The second section assesses the Governor's three technology initiatives. The third section focuses on the Governor's proposals relating to tuition, caps on state-subsidized units, and financial aid.

Governor's Overall Approach Unlikely to Improve System

By providing the segments with large unallocated increases not tied to specific requirements, the Governor cedes substantial state responsibilities to the segments and takes key higher education decisions out of the Legislature's control. For example, the Governor defers to the segments the issue of how many students California's public higher education system will serve. We believe this type of decision should be made through the annual state budget process. Given our concerns with the Governor's overall budget approach for higher education, we recommend rejecting several of his proposals. Specifically, as discussed in more detail below, we recommend the Legislature reject the Governor's proposals to: (1) provide the segments with unallocated base increases, (2) combine UC's and CSU's capital and support budgets, and (3) allow the universities to restructure their debt-service payments. In contrast to these proposals, we think the Governor's proposal relating to CSU retirement costs has merit but are concerned with the absence of a proposal relating to UC retirement costs. Lastly, we think the Governor's interest in rethinking how the state allocates funding to the community colleges also has merit, but we offer the Legislature an alternative that we think is much more likely to foster the state's dual goals of providing student access and promoting student academic success.

Unallocated Base Increases

Given High Costs and Mixed Outcomes, Justification for More Funding Unclear. The Governor provides $427 million in unallocated base funding increases to the institutions, with only a vague connection to undefined performance expectations. (Including additional funding provided in exchange for not raising tuition last year, cumulative new unallocated funding for the segments is $677 million.) Why the state would invest more in a system that is high cost and has poor outcomes without requiring explicit improvement is unclear.

Unallocated Increases Allow Segments to Pursue Own Interests Rather Than Broader Public Interests. For the universities, the Governor's budget lumps virtually all of each segment's funding into one pot and allows the segment to determine how best to spend the entire pot. For the community colleges, the Governor also provides an unallocated base augmentation linked neither to enrollment growth nor to any other identified public purpose. Rather than encouraging the segments to address state-identified problems and priorities, such an approach gives the segments much broader authority to pursue their top priorities. For example, the segments might decide to focus on more research, their law and medical schools, or administrative support, even if at the expense of broader public interests. Moreover, based on the segments' own budget plans, the segments likely would use augmentations primarily for employee compensation. As a result, the augmentations would increase the cost per student. Given the almost complete removal of funding requirements and the associated weakening of the incentives segments have to focus on broader public interests, the Governor's approach could end up exacerbating existing problems rather than improving the system.

Some Problems Can Be Addressed by Redistributing Rather Than Increasing Funding. Furthermore, most of the Governor's proposals involve substituting more efficient or effective activities for existing ones. For example, increasing the availability of required courses while reducing the amount of excess course-taking could be done within existing resources. Likewise, the segments could leverage an existing repository of online courses developed by faculty and enable students more easily to access those courses largely, if not entirely, within existing resources. As these examples illustrate, the segments likely could achieve many of the goals set forth by the Governor using funds the state already provides.

If Additional Funding Provided, Use to Meet Highest Priorities. We recommend the Legislature reject the Governor's unallocated base increases, as they would be very unlikely to promote systemic change. We also recommend the Legislature reject the Governor's approach of providing equal dollar amounts to each university segment irrespective of its needs. Instead, we recommend the Legislature allocate any new funding to meet the state's highest priorities. As a first priority, we recommend the state meet existing higher education obligations, including debt service, employee pension costs, and paying down community college deferrals.

Set Specific Improvement Targets and Review Performance Annually. If more funding is provided than needed to meet these existing funding obligations, then we recommend the Legislature link the additional funding with an expectation that the segments develop and implement strategies to improve *legislatively specified* student outcomes and meet identified cost-containment goals. Broad consensus already exists on some key outcome goals, including improving student persistence, transfer, and graduation; reducing costs; and maintaining quality. Moreover, the Legislature last year passed legislation outlining a process that would enable the state to measure progress and promote improvement in these areas through budget and policy decisions. Building on this foundation, the Governor and Legislature could establish specific improvement targets and a system for reporting on the segments' performance relative to these targets. We also recommend the Legislature establish enrollment targets for all three segments to ensure that student outcome improvements do not come at the expense of existing student access. These performance and enrollment targets would send a clear signal to the segments regarding the state's priorities and expectations. Compared with unallocated increases of seemingly arbitrary amounts, this approach would be far more likely to result in improved performance of the higher education system.

Combining Capital and Support Budgets

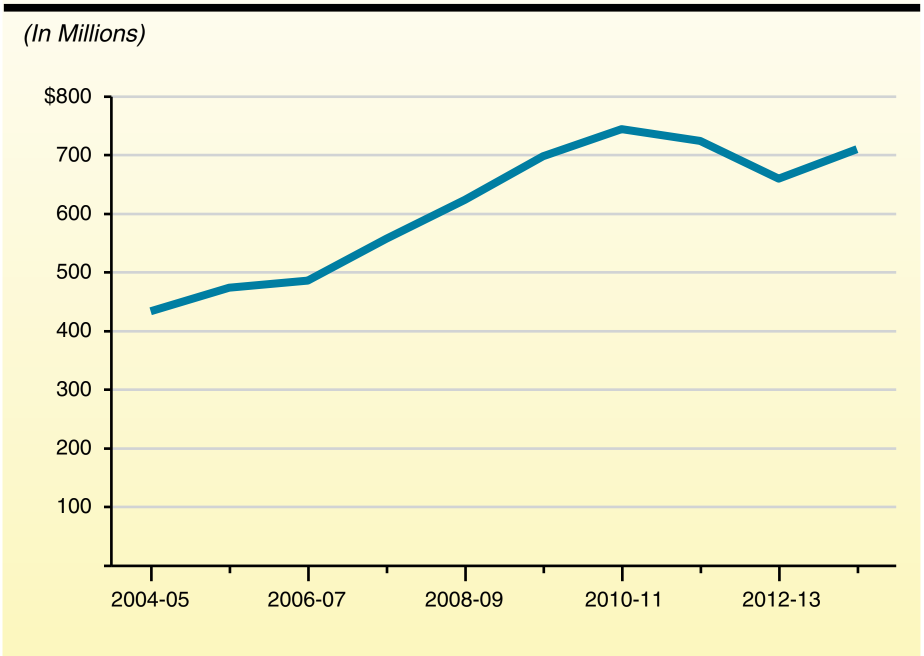
Weak Rationale for Proposed Changes to Capital Outlay Budget Process. The administration indicates the motivation for combining the universities' capital and support budgets is to provide the universities with more flexibility, given limited state funding. The administration, however, has not identified specific problems associated with the current process used to budget the segments' capital projects, nor identified any specific benefits the state might obtain from the proposal. As a result, both the problems the proposal is intended to address and the benefits that the proposal offers are difficult to ascertain. (How the administration proposes funding CCC facilities moving forward also is unclear.)

Legislature Would Lose Control of Key Budget Decisions. Not only does the Governor's proposal not identify any benefits for the state, we find that the proposal has several serious drawbacks. Most troubling, the Governor's approach is predicated on the Legislature relinquishing its role in capital decisions for the universities. That is, the Governor takes the Legislature out of the business of approving state buildings at the universities and gives it no role in determining the shares of higher education funding to be used for infrastructure and operations. As a result, the Legislature would have less oversight over the segments' use of state funds and the segments would have even greater incentive to pursue their own institutional interests, instead of those benefiting the state more broadly. In addition, the Governor's proposal would make planning for infrastructure spending statewide more difficult, as the state would not be able to prioritize funding as easily among the segments and/or other program areas.

Funding Provided Under Proposal Not Linked With Any Assessment of Ongoing Needs. Another concern with the Governor's proposal relates to the amount of funding he plans to provide the segments for their ongoing infrastructure needs. Specifically, the proposal presumes the amount of debt service funding related to one fiscal year (2013-14) is an appropriate amount upon which to base ongoing needs yet offers no evidence to this effect. It may be, for instance, that the current debt service amounts are too high. As shown in Figure 10, the state's total debt service costs (general obligation bonds and lease-revenue bonds) for UC, CSU, and Hastings have increased significantly over the last decade—growing from

Figure 10

Debt Service Costs for Universities Have Increased Signficantly



$434 million ten years ago to $711 million today (an increase of 64 percent). The Governor's proposal nonetheless effectively rolls into each of the three segments' base budget a relatively high point in debt service, without attempting to determine how this amount relates to the segments' ongoing needs.

Future Need for Infrastructure Spending Likely to Decrease. A related problem with the Governor's proposal is that it does not take into account that the segments' infrastructure needs likely will decrease significantly in the near future. One reason for this is demographic changes. The state projects that the 18 to 24 year-old population (the traditional college-age population at universities) will start to decline by about 1 percent annually starting in 2015. This means the segments may not require as many new buildings to accommodate enrollment as they have in past years when this age group was growing at a rapid pace. Moreover, the Governor's proposal to change the delivery model for higher education would result in a significantly reduced need for infrastructure spending. In particular, moving more courses online and increasing summer sessions would reduce the demand for new, traditional facilities (as would other strategies that increased space utilization). Thus, even if the current debt service amounts were somehow reflective of the segments' capital outlay needs at present, they could seriously overstate future needs.

Recommend Rejecting Proposal to Combine Capital and Support Budgets. Given the lack of a compelling policy rationale for the proposal, along with the serious concerns regarding the loss of the Legislature's ability to plan and oversee infrastructure projects, we recommend the Legislature reject the Governor's proposal. If the Legislature is interested in developing a new process for funding the segments' capital projects, then it would need to grapple with several fundamental issues. Most importantly, the Legislature would need to (1) identify the specific problems with the current capital outlay process and (2) develop a new method for allocating and overseeing funding that addresses these problems. As part of this process, if the Legislature did decide to combine capital and operational funding, then the Legislature would need to assess annual ongoing capital priorities, identify a reasonable initial amount to transfer, decide how to adjust that amount moving forward, and decide whether the segments should be able to pledge their state appropriations to issue debt. Without addressing such fundamental issues, we think moving to a new process as proposed by the Governor is premature.

Debt Service Restructuring

UC's Proposal Would Increase Future Costs Significantly in Exchange for Relatively Minor Short-Term Savings . . . In response to the Governor's proposal to allow the universities to restructure state infrastructure-related debt, UC has developed one potential restructuring plan. (The CSU has not yet presented a proposal.) Under UC's plan, it would restructure the existing lease-revenue debt over a 40-year period. Under the state's current repayment schedule, this debt would be retired fully in half that time. Because the university would extend the repayment period so far into the future, UC estimates it could lower the annual debt service payment by about $80 million in the short term. After ten years, however, the university would begin paying a few million dollars more in debt service annually than under the current repayment schedule. This difference would increase significantly in later years, such that, over the life of the restructured debt, UC estimates it would pay an additional $2.1 billion. In today's dollars, this means the restructuring would cost nearly $400 million.

. . . Which Could Make Investing in UC Facilities More Difficult in the Future. The university asserts that extending the repayment term to 40 years matches the life span of the buildings built with the bonds. By pushing debt out to years in which there otherwise would be no debt service, this approach, however, risks making investments in future facilities more difficult. For example, the university may have difficulty undertaking as many new capital projects 30 years from now as it otherwise could because it still would be paying off debt issued over 30 years earlier. (Though the demographic projections and policy proposals discussed earlier could mitigate the need for facilities in the near term, making similar judgments about facility needs several decades from now is more difficult.) Faced with such a situation, the university likely would have to (1) forgo capital projects it otherwise would have undertaken, (2) redirect funding that otherwise would have gone to support instruction or research, (3) seek additional funding from the state, and/or (4) increase student tuition.

Other Restructuring Proposals Also Would Not Be Worth Pursuing. The example above reflects one scenario provided by UC as to how it could restructure the state's lease-revenue debt. The universities could develop other proposals with different repayment periods and financial assumptions. These proposals potentially could have lower costs compared to the proposal discussed above. By definition, however, restructuring typically means extending out debt repayments into the future. As a result, debt restructuring typically means paying more in interest. For this reason, the state does not restructure its debt to longer repayment periods. (The state routinely refinances its debt, however, to take advantage of lower interest rates. In these transactions, the state keeps the same repayment schedule or shortens it and saves money on interest costs.)

Recommend Rejecting Restructuring Proposal. Given that restructuring debt would cost more money in the long term and constrain future budget choices, we recommend the Legislature reject the Governor's debt restructuring proposal for the universities. If the Legislature is concerned that the universities would lose the short-term savings associated with the debt restructuring, it could consider other strategies for the universities to increase revenue or reduce costs.

University Retirement Costs

Proposal for CSU Provides Some Benefits, Recommend Adopting. The Governor's proposal to modify the way the state budgets for CSU retirement costs offers some minor benefits. Specifically, the proposal would provide an incentive for the university to consider retirement costs in its hiring decisions. Right now, the university likely ignores these costs since they are automatically covered by the state. Because the university no longer would receive automatic budget adjustments above the current payroll level, the Governor's approach would incentivize CSU to be more cautious in its hiring and use its existing resources more efficiently. This could reduce both payroll costs and future retirement costs. At the same time, the proposal reasonably allows for future budget adjustments related to the university's existing payroll to account for rate changes made by CalPERS. For these reasons, we recommend the Legislature adopt the proposal.

Governor Does Not Directly Address UC Retirement Costs. Unlike for CSU, the Governor does not have a proposal to address retirement costs at UC. (He also does not have a proposal for Hastings—which participates in UC's plan.) In the 2012-13 budget, the state provided $89 million to UC (and nearly $900,000 to Hastings) specifically to cover increased retirement costs. For 2013-14, UC has identified additional retirement costs of $67 million, due to an increase in employer contribution rates and an increase in payroll. (Hastings has identified $455,000 in additional costs.) The Governor's budget does not identify any funding for these costs. The university could cover them, however, with a portion of the Governor's proposed base augmentations. (Hastings could cover all but $63,000 of its costs with its proposed base augmentation.)

Three Budget-Year Considerations Related to UC Retirement Costs. In deciding how best to address UC's retirement costs, we think the Legislature has three main issues to keep in mind.

- ***Cost Control.*** One major issue is that UC, unlike other state agencies, administers its own retirement plan. This means that UC determines its contribution rates, employee benefits, and investment options—all of which affect the plan's costs. Given this, the state needs to assess UC's retirement costs and benefits to ensure they are reasonable. For example, at the moment, UC employees contribute less to their pension plan than most state workers. Both the state and UC, however, have been undertaking many changes in their retirement programs and phase-in issues are making comparison of the two programs somewhat more difficult. Our best assessment today is that UC's increased costs in 2013-14 appear reasonable.

- ***Payment Obligation.*** The state is not legally obligated to provide funding for the university's retirement costs. Nevertheless, current retirement costs are largely unavoidable obligations for the university. Not addressing them means the university would incur significantly greater costs in the future. Addressing them without state funding means the university would have to cover the costs in some other way—such as by redirecting from its instructional program or increasing student tuition.

- ***Transparency.*** The Governor's approach to provide UC with a base augmentation but not designate any of it specifically for retirement costs lacks transparency. For other state agencies, the state typically makes a baseline funding adjustment to cover retirement costs. This makes identifying how much funding is going toward this purpose possible and provides clarity for both the agency and the state. For UC, identifying retirement costs would show how much of its base augmentation is available for this and other purposes. For the state, identifying retirement costs would prevent the university from asserting in the future that it did not receive funding for this purpose.

Recommend Designating $67 Million for UC Retirement. For these reasons, we recommend the Legislature specify $67 million of UC's proposed 2013-14 base budget increase for pension costs. (For Hastings, we recommend the Legislature increase the Governor's proposed base augmentation from $392,000 to $455,000 and designate the full amount for retirement.) In addition, consistent with the approach taken by the state in 2012-13, we recommend the Legislature include language in the budget reiterating that the state is not obligated to provide any additional funding for this purpose moving forward. Such language is intended to reinforce that the state is not liable for these costs.

Future Considerations for Universities' Retirement Costs. The Legislature recently enacted pension-related legislation that could significantly reduce long-term retirement costs for nearly all public employers. In the future, the Legislature may want to consider the universities' retirement costs in light of this legislation. This consideration would be useful since UC was specifically exempt from the legislation, while the applicability of some provisions to CSU is still being determined. In the future, the Legislature could consider providing the universities with funding for retirement costs comparable with costs incurred by other public employers. Under this approach, the universities would be responsible for any costs beyond that level. Alternatively, the Legislature could consider encouraging the universities to change their retirement plans to conform with other public employers by linking such changes with their state appropriation.

Higher Education Funding Reform

Current Funding Model Pays CCC for Providing Student Access, Not Promoting Success. Like any other organization, the way community colleges are funded drives their priorities and behavior. Because they are funded on enrollment at census, a top priority of the colleges is to ensure enough students are enrolled early in the term to meet their enrollment targets. While funding community colleges this way creates a positive incentive for colleges to provide students with access to instruction, the funding approach has been criticized for not creating a strong incentive for colleges to help students fulfill their broader academic objectives. For example, some community colleges have acknowledged that they have been reluctant to require new students to participate in assessment and orientation—support services that are strongly correlated with student success—for fear of "turning off" potential students. As a result, students may enroll in courses for which they are academically unprepared and have little chance of successfully completing. The need to meet enrollment targets also can create an incentive for colleges to offer popular instruction that "fills seats" but is primarily recreational in nature and outside of CCC's core educational mission.

Legislature Has Shown Interest in New Funding Approaches That Improve Incentives. In recent years, the Legislature has expressed interest in modifying CCC's funding model to address these issues. During the 2009-10 legislative session, AB 2542 (Conway) would have created a voluntary pilot program allowing up to five community colleges to be funded based on the number of students who successfully completed their courses (with bonus payments for increasing student graduations) rather than the traditional census method. Also during the 2009-10 legislative session, SB 1143 (Liu) sought to base CCC funding in part on successful course completions. After its passage in the Senate, this bill was amended to require the BOG to convene a task force to study "alternative funding options" and other strategies designed to improve student success at the community colleges. The legislation was signed by the Governor in fall 2010.

CCC Task Force Recommends Ongoing Study of Outcome-Based Options. In response to the legislation, the BOG created the Student Success Task Force. The task force was comprised of 21 members from inside and outside the CCC system. After meeting for nearly one year, the task force released *Advancing Student Success in California Community Colleges* in December 2011. The report contains a number of recommendations, including creation of a common assessment test for new students and development of a "scorecard" that measures student success rates at each college. While members did not reach consensus on whether to endorse funding outcomes in the report, the task force recommended the CCC Chancellor's Office "continue to monitor implementation of outcomes-based funding in other states and model how various formulas might work in California." The BOG formally adopted the Student Success Task Force's recommendations in January 2012.

Some Advantages of Funding Course Completions Over Current Approach . . . Though the Governor's proposal is not tied to a specific recommendation of the Student Success Task Force, funding course completions would have a couple of advantages over how CCC's are currently paid. By not providing funding for students who fail to complete their courses, the proposed change could result in colleges providing more guidance to students regarding their readiness for collegiate instruction. For example, colleges would have a stronger incentive to assess more students and require students to demonstrate a minimum level of proficiency in reading, writing, and mathematics before attempting certain transfer-level courses. The Governor's proposal also would help eliminate the current public perception that the state is paying for many students who are no longer enrolled. (We recognize, however, that colleges incur upfront costs to compensate instructors for teaching a course—costs that do not change if a student drops the course later in the term.)

. . . But Governor Misses Opportunity for More Meaningful Reform. Though funding course completions has some advantages over the current funding model, course completion is actually quite high at CCC—the systemwide average course retention is about 85 percent. Program completion, on the other hand, is low. According to the Institute for Higher Education Policy and Leadership, only about one-third of all CCC students seeking to transfer to a four-year institution or earn a certificate or associate degree actually do so. Whereas course retention is not a major problem, research has shown that students do tend to struggle to achieve *other* milestones on their educational path, such as returning the following year, completing their basic skills (remedial) sequences, passing transfer-level math and English courses, and reaching 30 units of college credit (one full academic year of coursework). By addressing only course retention, therefore, we believe the Governor is focused too narrowly on only one type of outcome—when instead the focus should be on several other more meaningful outcomes of student success.

Funding Course Completions Could Create Perverse Incentives for CCC. In addition, we are concerned that, if implemented, the Governor's proposed funding model could create perverse incentives for community colleges. While average course retention rates are 85 percent, rates vary considerably by discipline and program. For example, mathematics and economics courses tend to have lower retention rates than fine arts and sociology courses. If the CCC system were to be funded based on course completions, colleges would have a perverse incentive to de-emphasize core programs with relatively low retention rates and increase offerings of noncore programs (such as physical education) with relatively high retention rates. Moreover, the Governor's budget seeks to create incentives for CCC to offer "quality programs." Yet if the state were to adopt his proposal, we are concerned that faculty would feel pressure to reduce course rigor or inflate grades so as to reduce the number of students who drop classes before the end of the term.

Proposed Funding Reallocation Mechanism Could Impair CCC Improvement Efforts. The Governor's proposal also has a weak justification for redirecting any reduction in a districts' apportionment funds relating from the shift to course retention to that districts' Student Success and Support categorical program. In effect, the Governor presupposes that students do not complete their courses because of inadequate assessment or counseling services, but course-retention problems also can stem from a poorly designed or taught class. Yet, if the Governor's proposal were adopted, the primary funds that support local professional development (apportionments) would be automatically shifted to a categorical program that has an unrelated purpose. Such a redirection of funds actually could serve to undermine a college's efforts to improve student outcomes.

Consider Funding Approach That Supports Access and Success. For all these reasons, we recommend the Legislature reject the Governor's proposal to change the census date. We believe the Legislature could achieve the overarching objective of improving college and student outcomes by developing a more robust funding model that balances student access (enrollment) with student success (as measured by specific performance indicators). In effect, a disconnect exists today between the state's message to community colleges and its funding mechanism—value both access and achievement but only get compensated for successfully providing access. We envision a better funding model that continues to place an important emphasis on enrollment and access but also creates stronger incentives for colleges to focus on student achievement by linking a portion of state funding to colleges' ability to improve outcomes.

Building an Effective Funding Model. Currently, a number of other states (such as Pennsylvania, Ohio, and Washington) have adopted funding models that fund colleges for enrollment as well as student achievement. Other states (such as Illinois, Missouri, and South Carolina) adopted such an approach before abandoning it a few years later. Given all of these experiences to date, many best practices and lessons learned have been identified. We believe an effective funding model for the CCC system would include the following components.

- ***Specific Outcome Measures.*** The new system could have program-completion measures (such as graduations and transfers) as well as intermediate measures that influence program completion (such as reaching a certain unit threshold).
- ***Rules for Tracking Progress.*** The new system could measure year-to-year changes for each college. Colleges' performance could be compared against themselves (rather than other colleges within the system) to account for differences in student demographics among colleges.
- ***An Integrated Allocation Mechanism.*** The new system could allocate a portion of base as well as new funds on performance results. Remaining funding could continue to be allocated based on enrollment. Over time, a larger share of funding could be linked to performance.

We believe building this type of funding model would be a significant improvement over both the current system and the Governor's course-completion funding approach. States' experiences with more robust outcome-based funding models indicate that such systems can play an important role in focusing institutional efforts on student success.

University Funding Model Also Has Basic Problems. The state's approach to funding the universities also has a number of problems. Historically, the universities' funding model similarly has emphasized access over success. That is, funding for UC and CSU traditionally has been based largely on the number of full-time equivalent (FTE) students the state expects each segment to enroll, multiplied by an estimated marginal cost per student. The marginal cost formula has been an important way to guide the segments' student-faculty ratios, faculty salaries, and allocation of resources between research and instruction. Over the last five years, however, a series of unallocated budget reductions and augmentations has disconnected state funding from enrollment. By removing enrollment targets for the universities and delinking base augmentations from enrollment expectations for all three segments, the Governor's budget effectively funds neither access nor success at the universities.

Consider Dual Enrollment and Achievement Funding Model for Universities Too. As the state's budget stabilizes, the Legislature has an opportunity to establish a new basis for funding UC and CSU that balances access, student outcomes, and other state priorities. For example, instead of basing funding entirely on expected enrollment, the Legislature and Governor also could establish targets for degrees earned, research activity, and cost reductions. When determining funding allocations to each segment, the Legislature could consider the segment's performance in these areas. In addition, the Legislature could direct the universities to include incentives for improving student achievement (analogous to those described above for CCC) in their internal allocation of state funds across campuses. In these ways, the state could promote both student access and success through its support of the universities.

Delivery Model Could Be Improved At Lower Cost Than Governor

In an effort to expand access to instruction at a lower cost, the Governor's budget includes several related technology and efficiency proposals. We think these proposals can help place even greater attention on how best to open up new college opportunities. However, as discussed in more detail below, we believe many of the improvements sought by the Governor through these proposals could be accomplished largely within existing resources.

Online Education

Online Education Can Promote Access, Efficiency, and Student Learning. Online education has been found to have numerous benefits, including making coursework more accessible to students who otherwise might not be able to enroll due to restrictive personal or professional obligations and allowing campuses to serve more students without a commensurate need for additional physical infrastructure. Moreover, research suggests that, on average, postsecondary students who complete online courses learn at least as much as those taking the same courses solely through in-person instruction (though students tend to drop online courses at higher rates than face-to-face courses). Recently, massive open online courses (MOOCs) also appear to be paving the way for open-access instruction—often taught by the country's most distinguished professors—at minimal or no cost to students.

Need for New Funding to Create More Courses Is Questionable. We do not see a justification, however, for earmarking $10 million each for UC and CSU and up to $16.9 million at CCC for the development of additional online courses. Each year the state provides funds to UC, CSU, and CCC to support their operational costs. The segments use these monies to pay faculty to develop and deliver instructional content, and campuses generally decide on their own whether that content is offered through face-to-face or online courses. The segments have chosen to use their general-purpose monies to fund a considerable amount of online education. In 2011-12, the CCC system spent approximately $500 million serving over 100,000 FTE students through online education (about 10 percent of total instruction provided that year). Though CSU does not separate out costs by instructional type, online education is commonly used, with each of the segment's 23 campuses providing such instruction (primarily to undergraduate students). And, while historically UC has offered very little state-supported online instruction, over the past couple of years UC has expanded its online program—with plans to continue adding courses in the near future. Among the three segments, we estimate that more than 20,000 undergraduate courses (and more than 30,000 course sections) were offered online in 2011-12. It is unclear to us, then, why the segments require ongoing augmentations to develop more online courses.

Need Does Exist for Segments to Share Existing Online Curriculum With Each Other. While we do not believe additional monies are warranted as proposed by the Governor, we do believe significant opportunities exist for the segments to share more of their current inventory of online courses. Traditionally, faculty that develop curriculum for face-to-face courses do not share it with faculty at other campuses (either within their segment or across the segments). Generally, we find this practice has carried over to online courses at the segments—despite the relative ease with which such coursework can be made available to colleagues. Notably, while CSU and CCC are partners in administering Multimedia Educational Resource for Learning and Online Teaching (MERLOT)—a repository of free online course curricula developed by faculty and researchers throughout the world—faculty from these two segments generally borrow from (rather than contribute to) the collection of online presentations, assignments, tests, and other learning material. This lack of sharing across campuses and segments has several disadvantages, including duplicative spending of state resources (courses can cost tens of thousands of dollars each to develop) and forgone opportunities to share thoughtful coursework with other educators.

Recommend Using Competitive Grants to Build Repository of Online Courses. A more cost-effective approach than the Governor's would be for faculty to make their content available to colleagues for reuse. To facilitate sharing, we recommend the Legislature provide one of the segments with a small portion of one-time funding to administer a competitive grant program that would provide grants to faculty (from any of the segments) to modify, as needed, their existing online curricula (or, to the extent a need is identified by the Academic Senates of the three segments, to create a new online course). To assure quality, courses would be reviewed by other faculty in the field. As a condition of receiving the grant monies, faculty would agree to make the learning materials available on MERLOT. (The intellectual property rights would remain with the original developer.) These online materials would be available to all of the state's educational segments—including K-12 teachers who may wish to adapt the coursework for their Advanced Placement or precollegiate courses. Assuming an average grant amount of $20,000, a $1 million augmentation would fund the modification or development of 50 open online courses. Such an approach would result in a large number of online courses becoming available to students and faculty throughout the state.

Opportunities Exist to Create Streamlined Online Student Pathways. As part of his online initiative, the Governor also has expressed an interest in increasing opportunities for students to enroll in online courses offered at other campuses, though he does not provide the segments with specific direction as to how to achieve this goal. We agree with the Governor that the state should address this issue, as the current cross-campus enrollment process is disjointed and overly cumbersome for students. For years, the state has funded California Virtual Campus (CVC), a website featuring a catalog of online courses offered by CCC, CSU, and UC, as well as by various private colleges and universities. While CVC can be helpful, its utility is limited. For example, CCC students who identify a course of interest at another college in the system have to apply for admission at that college, receive a new student identification number and password, and register for the class. Students also are responsible for transferring credits earned from the course back to the home campus (typically by petitioning an academic counselor). Community college students interested in transferring to CSU can face even more difficulties, as they must navigate among CSU's degree requirements, CVC's online catalog, and potentially numerous campus registration websites.

Recommend the Segments Report on Cross-Campus Enrollment Projects. A more convenient system would allow students to plan their education using a single website, enroll directly in online classes they need, and immediately determine whether the course is accepted for credit at the home campus. Currently, all three segments are investigating new systems to facilitate a more streamlined process of cross-campus enrollment in online courses. A joint project involving CSU East Bay, CVC, and several community colleges in the San Francisco Bay Area is seeking to improve this process for students who are attending college online. This project—the California Online Program Planner—would allow transfer-seeking CCC students to select an online program at CSU East Bay and identify (1) what courses they will need to earn the degree (lower-division courses at CCC and upper-division courses at CSU) as well as (2) participating pilot campuses where transferable courses are offered (and whether a seat is available). Students then would be able to register for these courses from one website (using the same identification number and password) and "check off" their academic progress against degree requirements as they successfully complete their courses. The intent is to eventually expand beyond the handful of participants in the pilot project and include other CCC and CSU campuses throughout the state. The UC also is studying the possibility of a "cross-campus hub" that could include UC as well as non-UC students. To better assess the potential of these projects for streamlining online pathways, we recommend the Legislature request CVC and the three segments to provide updates at spring budget hearings on their implementation plans and estimated costs.

Common Learning Management System (LMS)

Proposes to Fund Common LMS for All Colleges to Use. As part of his CCC technology initiative, the Governor proposes using some of the new $16.9 million to purchase a common LMS for the entire CCC system. Though a precise amount had not been provided by the administration at the time this report was being prepared, the CCC Chancellor's Office estimates the annual cost would be about $10 million, with an additional one-time up-front cost of about $2 million. A LMS allows faculty to post information about a course (such as the syllabus), instructional content (such as video presentations), assignments, and other material. Students use the LMS to perform functions such as submitting their assignments, taking tests, and participating in online discussions with classmates. Several vendors create and sell these systems and community colleges currently decide on their own which LMS to use. Colleges typically use apportionments (general-purpose monies) to acquire the software. By purchasing centrally and making the LMS available to community colleges at no cost, the Governor anticipates that colleges would discontinue use of their current LMS format (assuming it is different from the LMS that is selected) and use their freed-up monies for other purposes. To the extent colleges adopted the same

LMS, students across the CCC system would no longer have to spend time learning to navigate different LMSs.

Recommend CCC Adopt Common LMS Using Existing Funding. We agree that a common LMS would have some benefit to students who take courses at more than one college. A common LMS also could make sharing digital instructional content among colleges easier. We do not believe however that a funding augmentation for this purpose is necessary. By purchasing their LMS on an individual basis, colleges pay much more than they would if they were to buy "in bulk" from one vendor and divide the total cost of the LMS among themselves. In fact, the Chancellor's Office estimates that colleges could save on average roughly $100,000 each per year if they were to leverage economies of scale in this way. We recommend the Legislature direct the Chancellor's Office to report this spring at budget hearings on opportunities for community colleges to collaborate in such a manner, including the role the Chancellor's Office might play in facilitating the procurement of a common systemwide LMS using community colleges' existing funding.

Credit by Examination

"Challenge Tests" Provide an Alternative Way for Students to Earn CCC Credit. In an attempt to create greater efficiencies, the Governor also seeks to increase the number of students who can earn CCC credit for prior learning. Typically, students earn CCC credit by enrolling in courses, completing required coursework, and receiving a passing grade. Community college regulations, however, allow for students to obtain course credit using an alternative method. Specifically, districts may grant course credit to students who—despite never taking the course—pass a challenge test. (The resulting CCC credit is known as credit by examination.) By allowing students to earn credit for material they learned through self-study or other experiences, colleges can help students accelerate their time to a degree.

Credit by Examination Accounts for Small Amount of Overall Credit Granted. Little statewide data are available on the prevalence of credit by examination at the community colleges. Based on the limited information that is available, we estimate that only a very small percentage (less than 1 percent annually) of CCC students request to take a challenge test. (Of those students who do take a challenge test, less than half pass the examination and earn course credit.)

Campus Policies Can Limit Credit-by-Examination Opportunities for Students. Based on our review of various CCC catalogs, a number of potential limitations to students seeking to obtain credit by examination appear to exist. For example, not every course a college offers typically is available for students to earn credit in this manner. Rather, departments generally designate which courses, if any, may be challenged. Colleges also often limit the total number of units a student may earn by examination (typically about 12 units). While many colleges allow new students to take a credit by examination, others require students to wait until they successfully complete at least 12 units of regular coursework at the college before being permitted to take a challenge test. (Still others allow new students to take a challenge test but do not post any credit earned on students' academic record until they successfully complete 12 units of regular coursework.)

Important Issue to Raise but Legislature Needs More Details on Governor's Proposal. Like the Governor, we believe opportunities exist to expand the usage of credit by examination and improve certain students' time to degree. This is particularly true given the many opportunities today for individuals to acquire knowledge and skills outside the traditional collegiate environment, including students who enroll in MOOCs and veterans returning to civilian life having learned material that is comparable to the content in CCC courses (such as in electronics, computer programming, and various health care fields). To date, however, the Governor had not provided any detail on his proposal to expand credit-by-examination options and what he is requesting the Legislature specifically to do remains unclear. We thus withhold recommendation pending additional information from the administration.

Mixed Review of Governor's Tuition and Fee Proposals

As the Legislature considers funding and tuition levels each budget cycle, it grapples with the share of cost to be borne by the state and students. As part of his budget package, the Governor has several proposals relating to share-of-cost issues. As discussed in more detail below, we have serious concerns with the Governor's tuition freeze proposal, as it very likely would result in steep tuition increases during the next economic downturn and reduced accountability in the near term. In contrast, we recommend the Legislature adopt some variant of the Governor's unit-cap proposal, as we believe it would create positive incentives for both students and the segments. We also recommend the Legislature adopt the Governor's two CCC financial aid proposals.

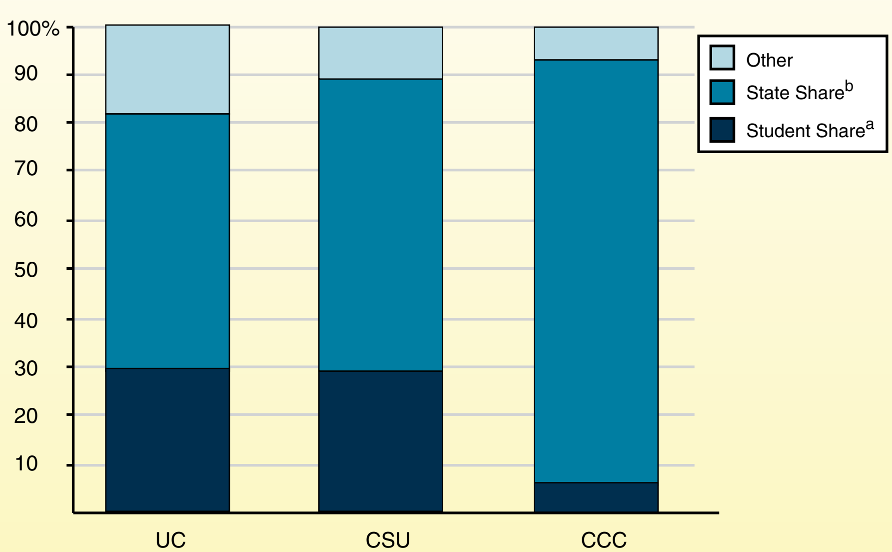
Tuition and Fees

Current Student Share of Cost Relatively Low. The full tuition level currently reflects about 55 percent of education costs at UC, 46 percent at CSU, and 24 percent at CCC. Because of financial aid, however, fewer than half of students pay the full tuition rate. After accounting for state and institutional financial aid, the average net amount paid by students currently covers about 30 percent of education-related spending at the universities and 6 percent at the community colleges, as shown in Figure 11. (When federal and private grants are included, the student shares are even lower.) These shares are very low compared with other states.

Figure 11

Student Share of Cost Is Low

Share of 2011-12 Education and Student Services Spending From Various Sources



[a] Reflects net tuition and fees paid by students after waivers, discounts, and grants.
[b] Reflects base funding for segment as well as Cal Grant funding.

Governor's Proposal to Freeze Tuition Levels Likely Would Have Negative Long-and Near-Term Consequences. The Governor's proposal would extend for four more years UC and CSU tuition levels that already have been in place for two years. While this would help current students, it likely would increase volatility for future students. As shown in Figure 12, extended tuition freezes at California's public institutions have been followed by periods of high annual tuition increases. The proposal also would have the negative near-term effect of reducing the incentive students and their families have to hold higher education institutions accountable for keeping costs low and maintaining quality. Given the important role of tuition in higher education budgets, a relatively low share of cost now borne by students and their families, and likely negative consequences of an extended tuition freeze, we do not see a strong justification for having the state bear all higher education cost increases for the next four years.

Recommend Share-of-Cost Fee Policy. For these reasons, we do not think an extended tuition freeze would be in the public's best longer-term interests. Instead of an extended tuition freeze, we recommend the Legislature adopt a policy that bases tuition and fee charges at each of the public higher education segments on a share of educational costs. Such a policy would provide a rational basis for fee levels and a simple mechanism for annually adjusting them. It would recognize explicitly the partnership between students and the public. It also would strengthen accountability by giving students and their families an incentive to hold institutions accountable for keeping costs low and maintaining quality. Though such a policy would depend on the state providing its share of funding, we believe it would be more likely than the Governor's proposal to result in moderate, gradual, and predictable tuition increases over time.

Caps on State-Subsidized Units

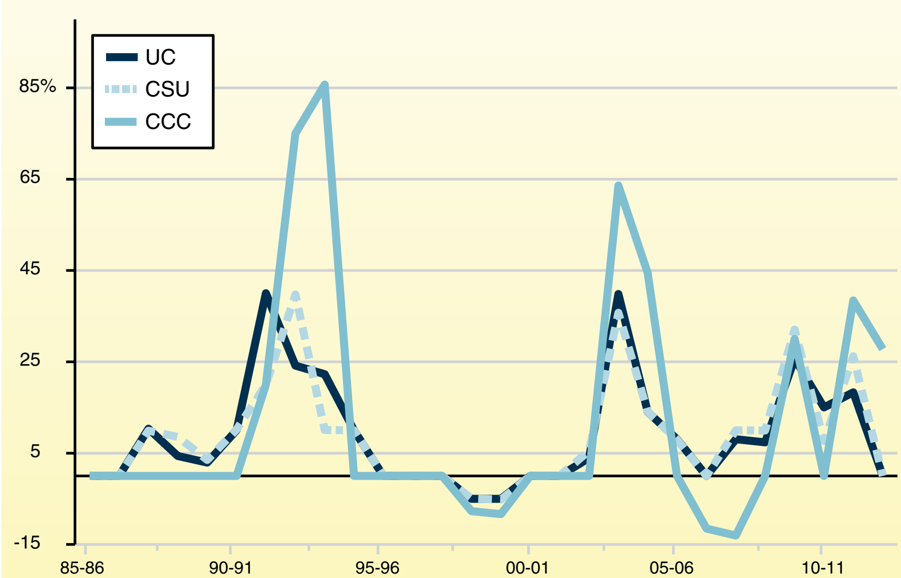
Proposal Creates Positive Incentives for Students . . . If they work as intended, caps on state-subsidized units encourage students to seek academic advising and develop academic plans in their first year of college. Unit caps also discourage repeated changes of major and other student choices that result in excess unit-taking yet still providing some room for students to explore other subjects and add new skills. By promoting more efficient course-taking, unit caps likely would reduce costs and improve on-time graduation rates.

. . . Also Could Improve Institutional Practices. In addition to encouraging efficient student choices, unit caps could improve campus practices that contribute to excess unit-taking.

Figure 12

Extended Tuition Freezes Followed by Periods of Steep Increases

Annual Percent Change in Systemwide Tuition and Fees



The proposed policy would create pressure for campuses to enhance academic advising and ensure availability of required courses. It also would focus attention on course articulation (the formal recognition of specified courses at one institution to meet equivalent course and program requirements at another institution). Campuses also would need to track student progress toward degrees under the proposed policy, providing valuable information for course scheduling as well as student advising.

Recommend Adopting Unit-Cap Policy. Because it creates positive incentives for students and motivates institutions to improve the efficiency of their academic programs, we recommend the Legislature adopt a cap on the number of state-subsidized units students can accrue. As discussed in the nearby box, a unit-cap policy would complement existing institutional efforts to improve academic efficiency. The Governor's unit-cap proposal is vague, however, and needs to be further developed. The administration has provided a few details as to which types of courses would be excluded from the cap and how the cap would be applied across the segments but leaves out numerous details that typically are included in unit-cap policies.

Several Specific Issues to Address in Developing Unit-Cap Policy. In designing a unit-cap policy, the Legislature will need to work through several specific issues including:

- ***Credits Earned Through Other Agencies.*** The Governor's proposal would exclude from the cap credits earned for Advanced Placement and other courses students complete for college credit while they are in high school. The proposal, however, does not address credits earned through other types of external validation (such as programs coordinated by the Department of Defense to help active duty and veteran students earn credit for prior learning) or standardized exams (such as the College Board's College Level Examination Program and the national licensing exam for nurses).

- ***Credits Earned by Evaluation.*** In addition to relying on external agencies, colleges and universities award credit within their departments by evaluating students' mastery of subjects through various types of assessments including challenge exams, portfolios, and skills demonstrations. While credits awarded by evaluation count toward meeting degree requirements, they are excluded from the calculation of FTE students. It is unclear whether these units count toward the caps under the Governor's proposal.

- ***Prior Unsubsidized Courses.*** The Legislature also will need to decide whether to exclude from the caps any units not paid by the state, such as those transferred from unsubsidized extension programs and private and out-of-state colleges.

- ***Higher Unit Requirements for Double Majors.*** The Governor's proposal is unclear as to whether additional requirements for a student to complete a double major would count toward the cap. Although double majors have increased course requirements, they typically can be completed within 125 percent of the units required for one major because several courses may count as electives for both majors.

- ***Courses Attempted but Not Completed.*** The Legislature also may wish to consider how to treat courses attempted but not completed for credit. These include courses that students fail or drop. Because students

Some Efforts Already Underway to Reduce Excess Course-Taking

The proposed unit cap would complement the following existing efforts to improve on-time graduation rates.

New California Community College (CCC) Regulations. In recent years, the CCC Board of Governors (BOG) has adopted several new regulations intended to reduce excess course-taking by students. In July 2011, the BOG approved a regulation that limits the number of times community colleges are eligible to receive state support for students who fail to pass a course (or enroll but then drop the course). In July 2012, the BOG adopted another regulation that prohibits community colleges from receiving state support for student re-enrollments in certain "activity" courses (such as physical education). The BOG also has adopted a regulation that establishes a systemwide enrollment policy. Under the new regulation, which goes into effect in fall 2014, community colleges are no longer permitted to give enrollment priority to students who have accumulated 100 or more degree-applicable CCC units.

Various California State University (CSU) Initiatives. The CSU campuses have adopted numerous strategies to improve course availability. These include block scheduling (assigning a fixed course schedule to entering freshmen) and "four-year pledge programs" (which guarantee to full-time students who follow a specified academic plan that they will be able to get the necessary classes to complete a degree within four years). In January 2013, the CSU Board of Trustees also adopted a policy capping the number of units that campus programs may require for a bachelor's degree to 120, with limited exceptions. (Currently about 20 percent of CSU bachelor's degree programs require more than 120 units.) While required units above 120 would not be considered excess units, capping degree requirements achieves a similar objective as the excess unit policy—it reduces student and state costs to complete an academic program and makes room for additional students at CSU. In addition, last fall, CSU administration proposed three new incentive fees to be assessed on (1) excess units (similar to the Governor's proposal), (2) high unit load in a given term, and (3) course repeats. Discussion of these three proposals has been deferred to a future board meeting, but all three proposals would reduce excess unit-taking by students.

Joint CCC-CSU Transfer Initiative. In 2010, the Legislature adopted Chapter 428, Statutes of 2010 (SB 1440, Padilla), to improve the efficiency of transfer from CCC to CSU. The legislation requires community colleges to create two-year (60 unit) degrees (known as "associate degrees for transfer") that are fully transferrable to CSU. A student who earns such a degree is automatically eligible to transfer to the CSU system as an upper-division (junior) student in a bachelor's degree program. Though these students are not guaranteed admission to a particular CSU campus or into a particular degree program, SB 1440 gives them priority admission to a CSU program that is "similar" to the student's CCC major or area of emphasis, as determined by the CSU campus to which the student is admitted. Once admitted, SB 1440 students need only to complete two additional years (60 units) of coursework to earn a bachelor's degree. By guaranteeing full credit for courses taken at the CCC and limiting the number of additional units students may be required to complete, this legislation also reduces excess unit-taking.

often repeat failed and dropped courses—sometimes over and over—they contribute to excess course-taking. The Governor's proposal excludes these courses.

- ***Case-by-Case Waivers.*** The Governor's proposal authorizes the governing board of each segment to approve waivers on a case-by-case basis for students who exceed the cap "due to factors beyond their control." (The Governor cites lack of access to required courses as one example of a factor beyond a student's control.) The Legislature may wish to weigh in on the general types of factors that may justify a waiver.

Recommend Adopting Certain Provisions Not in Governor's Proposal. Given all these considerations, we recommend the Legislature adopt three specific provisions as part of a unit-cap policy that would encourage efficient student choices while protecting students from undue penalties.

- We recommend excluding from the caps units earned through other agencies, by internal evaluation, and for unsubsidized courses as long as they do not contribute to FTE student counts. Units earned in these ways reduce costs for students and the state on the natural. Including them in unit caps could create a disincentive for students to use these approaches for fear of accumulating too many units.

- We also recommend that students not be allowed additional state-subsidized units for double majors. This would encourage students to use their electives efficiently while still allowing students to expand their academic horizons.

- We further recommend a cap on the number of failed and dropped courses the state subsidizes.

- Lastly, we recommend providing additional guidance regarding waivers. We think the vagueness of the waiver criteria could result in an excessive number of appeals and weaken the unit-cap policy. For example, students might claim that they took excess units because they could not get into required courses. Given the difficulty of retroactively assessing whether required courses could have been taken on time, we recommend a policy requiring up-front verification that required courses are unavailable. This would ensure that students seek advising if they are having difficulty enrolling in courses, increasing the likelihood of finding solutions for many students, and avoiding numerous appeals.

Recommend Implementation in 2015-16. Instead of implementing the unit caps in 2013-14, we recommend the Legislature delay implementation for two years to (1) provide adequate notice to students and (2) permit the segments to develop systems to identify and monitor excess units as students enroll. With adequate notice, the phase-in beginning with 150 percent of required units for UC and CSU students would be unnecessary. Current students and new students entering after enactment would have sufficient time to develop and adjust their academic plans to graduate within the tighter unit limit. Accordingly, we recommend forgoing the Governor's proposed unit caps for 2013-14 and 2014-15 but implementing his proposed caps for 2015-16 and thereafter.

CCC Financial Aid

Recommend the Legislature Approve Proposed Changes to FAFSA and CCC Fee Waiver. As noted earlier, certain community college students currently can apply for a BOG fee waiver using either a FAFSA or separate BOG form. We agree with the Governor that allowing students to complete only the BOG form works at cross-purposes with both student and state interests. We thus recommend the Legislature approve the Governor's FAFSA proposal. (While undocumented immigrants are not eligible to submit a FAFSA, CSAC has recently developed a new FAFSA-like form so that financially needy students covered under the Dream Act can be considered for the full range of state financial aid funds, including BOG fee waivers and Cal Grants.) In addition, we recommend the Legislature approve the Governor's proposal to require CCC to count dependent students' income for purposes of determining eligibility for a BOG fee waiver. This would bring CCC policy in line with federal financial aid policy for dependent students, which includes both the parents' and students' income for purposes of determining financial need.

SUMMARY OF RECOMMENDATIONS

LAO Recommendations

Unallocated Base Increases

- ✓ ***Unallocated Base Increases.*** Reject the Governor's approach to base increases. Fund obligations (including debt service, employee pension costs, and deferral pay downs) as a first priority. If more funding is provided, link with specific expectations.
- ✓ ***Enrollment Targets.*** Set enrollment targets for all three segments to ensure that improvements in student outcomes do not come at the expense of existing student access.
- ✓ ***Combining Universities' Capital and Support Budgets.*** Reject Governor's proposal.
- ✓ ***Restructuring Universities' Debt.*** Reject Governor's proposal.
- ✓ ***Universities' Retirement Costs.*** Adopt Governor's proposal to lock in current base for CSU retirement costs. For UC, designate $67 million of base increase for retirement costs. For Hastings College of the Law, increase base augmentation from $392,000 to $455,000 and designate for retirement costs. Adopt budget language specifying the state is not obligated to provide additional funding for UC and Hastings.
- ✓ ***CCC Funding Reform.*** Reject the Governor's proposal to fund community colleges based on course completions. Consider an alternative funding approach that balances student access with student success.

Technology Initiatives

- ✓ ***Online Education.*** Reject the Governor's proposals to provide $10 million each to UC and CSU and up to $16.9 million to CCC for the development of new online courses. Instead, provide one segment with a small amount of one-time funding (such as $1 million) to provide competitive grants to faculty who modify their existing online courses (or, as needed, create new online courses) and share the courses among all three segments as well as K-12 faculty. Further recommend the Legislature request the three segments to provide updates at spring hearings on their plans to implement cross-campus enrollment processes for online students.
- ✓ ***Common Learning Management System (LMS).*** Recommend the Legislature encourage CCC to adopt a common LMS using existing resources.
- ✓ ***Credit by Examination.*** Withhold recommendation on the Governor's proposal to expand opportunities for students to earn credit by examination pending further information.

Tuition, Fees, and Aid

- ✓ ***Tuition.*** Reject proposal for extended tuition freeze at the universities. Adopt share-of-cost fee policy.
- ✓ ***Caps on State-Subsidized Units.*** Modify Governor's proposal to exclude certain types of credits earned and provide additional guidance regarding waivers. Provide no special treatment for double majors. Allow two-year implementation lag.
- ✓ ***CCC Board of Governors (BOG) Fee Waiver Program.*** Approve the Governor's proposals to require students to (1) complete a federal financial aid application to obtain a BOG fee waiver and (2) count dependent students' income for purposes of determining eligibility for the BOG fee waiver.

RELATED LAO PUBLICATIONS

Faculty Recruitment and Retention at the University of California (December 2012). Examines recent trends in faculty recruitment, retention, and compensation at the university. Discusses implications of recent trends for state budget decisions.

Improving Higher Education Oversight (January 2012). Presents a conceptual model of how the state can improve higher education oversight and provides specific short-term and long-term recommendations.

The Master Plan at 50: Improving State Oversight of Academic Expansions (December 2009). Evaluates the efficacy of the state's approval process for new programs and schools at the state's public universities and colleges.

The Master Plan at 50: Using Distance Education to Increase College Access and Efficiency (October 2010). Provides an overview of online education—including its prevalence, data on learning outcomes, and funding—as well recommendations to improve state oversight and overall program efficiency and effectiveness at UC, CSU, and CCC.

Public Pension and Retiree Health Benefits: An Initial Response To the Governor's Proposal (November 2011). Provides background on the state's retirement policy issues and our initial response to the Governor's 12-point plan to change pension and retiree health benefits.

Reforming the State's Transfer Process: A Progress Report on Senate Bill 1440 (May 2012). Discusses SB 1440 (Padilla), which was enacted in 2010 with the intent to fundamentally reform the transfer process between CCC and CSU. Provides an overview of key issues and concepts pertaining to transfer education, assesses each segment's progress to date in implementing the legislation, and makes recommendations designed to ensure that CCC and CSU stay on track and meet the Legislature's intent.

Restructuring California's Adult Education System (December 2012). Contains background on adult education in California, identifies five major problems with the current system, and provides a package of recommendations for improving the state's adult education system.

"Rethinking the Community College Fee Waiver Program to Better Promote Student Success and Assess Need," in *The 2012-13 Budget: Analysis of the Governor's Higher Education Proposal* (February 2012). Reviews the CCC Board of Governors fee waiver program and identifies several opportunities to change the program in ways that promote student achievement while ensuring that state resources are targeted to actual student need.

A Ten-Year Perspective: California Infrastructure Spending (August 2011). Examines recent trends in state infrastructure spending (including for higher education) and discusses issues for the Legislature to consider moving forward.

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Higher Education – Multi-Year Plan

BACKGROUND:

California's public higher education system involves three "segments": the University of California, the California State University, and the California Community Colleges. It also includes the Hastings College of the Law. The state's Master Plan for Higher Education, originally adopted in 1960, ascribes distinct missions to each of the segments and expresses a set of general policies for higher education in the state, including the state's intent that higher education remain accessible, affordable, high-quality, and accountable.

University of California (UC). Drawing from the top 12.5 percent of the state's high school graduates, the UC educates approximately 239,500 undergraduate and graduate students at its ten campuses and is the primary institution authorized to independently award doctoral degrees and professional degrees in law, medicine, business, dentistry, veterinary medicine, and other programs. UC manages one U.S. Department of Energy national laboratory, partners with private industry to manage two others, and operates five medical centers that support the clinical teaching programs of the UC's medical and health sciences schools and handle more than 3.9 million patient visits each year.

The UC was written into the State Constitution of 1879 as a public trust, to be administered by an independent governing board, the Regents of the University of California, which includes 28 members: seven ex officio; 20 appointed by the Governor subject to Senate confirmation; and one student appointed by the Board. The UC is headed by a President who is responsible for overall policy development, planning, and resource allocations. Chancellors are responsible for the management of individual campuses. The Regents have delegated authority to the Academic Senate to determine conditions for admission, degree requirements, and approval of courses and curricula.

California State University (CSU). Drawing students from the top one-third of the state's high school graduates, as well as transfer students who have successfully completed specified college work, the CSU provides undergraduate and graduate instruction through master's degrees and independently awards doctoral degrees in education, nursing practice, and physical therapy, or jointly with UC or private institutions in other fields of study. With 23 campuses and approximately 410,300 students, the CSU is the largest and most diverse university system in the country.

The CSU is administered by an independent governing Board of Trustees that includes 25 members: five ex-officio; 16 appointed by the Governor to four-year terms (subject to Senate confirmation); and four members appointed to two-year terms (two student representatives, one voting and one non-voting, and one representative each from faculty and alumni). The Trustees appoint the Chancellor, who is the chief executive officer of the system, and the Presidents, who are the chief executive officers of the respective campuses. The Trustees, the Chancellor, and the Presidents develop systemwide policy, with actual implementation at the campus level taking place through a broadly based consultative process. The Academic Senate, made up of elected faculty representatives from each campus, recommends academic policy to the Board of Trustees through the Chancellor.

California Community Colleges (CCC). The CCC are publicly supported local educational agencies that provide educational, vocational, and transfer programs to approximately 2.4 million students. The CCC system is the largest system of higher education in the world, with 72 districts, 112 campuses, and 70 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 through basic skills courses and adult non-credit instruction.

The Board of Governors of the CCC was established in 1967 to provide statewide leadership and technical assistance and allocate funding to the 72 districts and 112 colleges that constitute the system. The Board has 17 members appointed by the Governor subject to Senate confirmation. Twelve members are appointed to six-year terms, and two student members, two faculty members, and one classified member are appointed to two-year terms. Locally elected Boards of Trustees work on the district level with Presidents who collectively are responsible for the operation of individual college districts and campuses.

Hastings College of the Law (Hastings). Hastings was founded in 1878 and on March 26, 1878, the Legislature provided for affiliation with the UC. Hastings is the oldest law school and one of the largest public law schools in the West. Its mission is to provide an academic program of the highest quality, based upon scholarship, teaching, and research, to a diverse student body of approximately 1,100 students.

The Hastings Board of Directors establishes policy that is carried out by the Chancellor, Dean, and other officers. The Board has 11 directors serving 12-year terms: one is an heir or representative of S.C. Hastings and the other ten are appointed by the Governor subject to Senate confirmation.

Higher Education Funding from 2008-09 thru 2011-12. From 2008-09 through 2011-12, the state reduced funding for UC, CSU, CCC, and Hastings by $2.65 billion General Fund. The most notable consequences of these reductions were significant student tuition increases (as illustrated in the chart on the next page), effectively increasing the share of total education costs being shifted to students, and declining course offerings, which made it difficult for students to complete their certifications and degrees in a timely manner. In 2012-13, and with the passage of Proposition 30, higher education budgets were held flat and mandatory systemwide tuition fees remained at the 2011-12 level.

Higher Education Annual Tuition/Fees: 2008-09 through 2012-13

Full-Time Resident Students							Change from 2007-08	
	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	Amount	Percent
University of California								
Undergraduate	$ 6,636	$ 7,126	$ 8,373	$ 10,302	$ 12,192	$ 12,192	$ 5,556	84%
Graduate	7,440	7,986	8,847	10,302	12,192	12,192	$ 4,752	64%
California State University								
Undergraduate	2,772	3,048	4,026	4,440	5,472	5,472	$ 2,700	97%
Teacher credential	3,216	3,540	4,674	5,154	6,348	6,348	$ 3,132	97%
Graduate	3,414	3,756	4,962	5,472	6,738	6,738	$ 3,324	97%
Doctoral	7,380	7,926	8,676	9,546	10,500	10,500	$ 3,120	42%
California Community Colleges	600	600	780	780	1,080	1,380	$ 780	130%
Hastings College of the Law	21,303	26,003	29,383	36,000	37,747	43,486	$ 22,183	104%

Source: LAO

GOVERNOR'S PROPOSAL:

Higher Education Funding. The budget provides $11.9 billion in General Fund support for higher education in 2013–14 (*including funding for financial aid programs administered by the California Student Aid Commission described in a separate chapter of this report*). This is $1.4 billion (13 percent) more than the revised 2012-13 level. The bulk of the new funding is for base increases at the universities, a general purpose increase for the community colleges, adult education restructuring, and increased participation in the Cal Grant program. A portion of the total ongoing General Fund increase is due to Budget Act of 2012 appropriations of $125 million each to UC and CSU if student tuition fee levels were held flat in 2012–13.

Higher Education General Fund Support
(Dollars in millions)

	2011–12 Actual	2012–13 Revised	2013–14 Proposed	Change From 2012–13	
				Amount	Percent
UC	$2,504	$2,567	$2,846	$279	11%
CSU	2,228	2,492	2,809	317	13
CCC	3,612	3,802	4,503	701	18
Hastings	8	9	10	—	3
CSAC	1,533	1,624	1,722	98	6
Totals	**$9,885**	**$10,494**	**$11,890**	**$1,396**	**13%**

For UC, CSU, and Hastings, amounts include general obligation bond debt service in each year. For CCC, amounts include general obligation bond debt service and funding for the CCC Chancellor's Office. For the California Student Aid Commission, amounts include federal Temporary Assistance for Needy Families and the Student Loan Operating Fund support that directly offset General Fund costs.

Source: LAO

Multi-Year Funding Plan and Increased State Support for Base Budgets. The budget proposes a multi-year funding plan across all segments of higher education, including increased state support. UC, CSU, and Hastings budgets will increase by roughly five percent per year in 2013-14 and 2014-15, and by four percent in each of the subsequent two years. CCC funding will also increase by roughly five percent in 2013-14, and then grow significantly over the subsequent years of the multi-year plan. These increases translate to an additional $125.1 million each for UC and CSU, $392,000 for Hastings, and $197 million for the community colleges (an additional $179 million for the community colleges is directed to the buydown of inter-year deferrals and is discussed further in the "*Issues to Consider*" section below).

Assumes No Tuition Fee Increases Over Extended Period. The budget expects the segments to maintain current tuition fee levels for the life of the plan. No increases are necessary because any need is negated by the year-over-year General Fund increases coupled with savings from expected reforms from the improved deployment of teaching resources and from current segmental efforts to increase efficiencies. The reforms related to improved deployment of teaching resources include: (1) making available the courses students need and help them progress through college efficiently; (2) using technology to deliver quality education to greater numbers of students in high demand courses (with $37 million in designated funding for UC, CSU, and CCC as described further below); (3) improving course management and planning; (4) using faculty more effectively; and (5) increasing the use of summer sessions.

Expects Performance on Certain Priorities. The budget directs each segment to use the increased funding to achieve the following priorities: (1) provide high quality instruction at lower cost; (2) decrease the time it takes to earn a degree; (3) increase graduation rates; (4) increase the CCC transfer rate; and (5) improve credit and basic skills course completion.

Variety of Segment-Specific Proposals. The budget proposes various segment-specific "tools" to assist the segments in achieving the priorities of the multi-year plan. In addition, and in order to require the segments to factor these costs into their fiscal forecasting and decision-making, the budget proposes to shift certain costs onto the segments' budgets, such as for debt service and retiree benefits, that have been historically borne by the state's budget.

- <u>*UC, CSU, and CCC – Funding for On-Line Education*</u>. To expand the number of courses available to matriculated undergraduate students through the use of technology, the budget provides $10 million each to UC and CSU as part of their $125.1 million General Fund increases and a separate augmentation of $16.9 million Proposition 98 General Fund to the CCC. For all segments, the focus is on courses that have the highest demand, fill quickly, and are prerequisites for many different degrees. For UC and CSU, the budget bill earmarks the funding and requires that the courses be available to all undergraduates systemwide, regardless of the campus where they are enrolled, and that student tuition is the same as for regular academic year state-subsidized courses. For the CCC, the budget bill earmarks the funding and requires the Chancellor's Office to submit an expenditure plan to the Administration by July 1, 2013. The *Budget Summary* indicates the CCC initiative will include three key elements: (1) creation of a "virtual campus" to increase state student access to 250 new courses delivered through technology; (2) creation of a single, common, and centralized delivery and support infrastructure for all courses delivered through technology and for all colleges; and (3) expansion of options for students to access instruction in other environments and earn college credit for demonstrated knowledge and skills through credit by exam. Budget trailer bill language will also be submitted to implement this proposal.

- <u>*UC, CSU, and CCC – Unit Caps*</u>. To shorten students' time-to-degree, reduce costs for students and the state, and increase access to more courses for other students, the budget proposes trailer bill language to cap the number of General Fund subsidized-units students can take during the life of the plan. For UC and CSU in the first two years, the limit would be 150 percent of degree requirements (for example, 180 units for a standard bachelor's degree and 90 units for an associate's degree). The limit would be reduced in year three to the equivalent of about one extra year of full-time attendance (for example, 150 units for a bachelor's and 90 for an associate's). For CCC, starting in 2013-14, students will be allowed to take no more than 90 semester credit units (150 percent of the standard required to earn an associate's degree or credits for transfer).

- *UC, CSU, and Hastings – Bond Debt Service Costs and Capital Outlay*. The budget shifts roughly $400 million in debt service costs for general obligation bond financed capital improvements at UC, CSU, and Hastings into each segment's budget. The budget also makes one last adjustment to UC and CSU budgets for lease-revenue bond debt service costs. No further augmentations will be provided for either form of debt service payment. The budget further proposes that any new capital expenditures will be subject to approval by the Administration and there will be limits on the amount of the budget that can be spent on capital expenditures. Budget trailer bill language will be submitted to implement this proposal as well as to authorize UC and CSU to restructure their respective lease-revenue debt obligations to create budgetary savings.

- *CSU Employer Contribution to CalPERS*. The budget provides a $51.4 million General Fund increase to fund the annual increase in costs for CSU's required employer pension contribution to CalPERS. In future years, CSU will continue to receive annual General Fund adjustments based on current payroll; however, if CSU chooses to increase expenditures beyond the 2012-13 payroll level, CSU would be responsible for the associated pension costs.

- *CSU Employer-Employee Share of Cost for Health Premiums*. The budget proposes budget trailer bill language to provide CSU with the same statutory authority to negotiate or set employee health care benefit rates that is provided to the California Department of Human Resources for other state employees. Currently, CSU pays 100 percent of the health care premiums for its employees and 90 percent for employees' family members. However, for most other state employees, the state pays either 80 or 85 percent of employees' health care premiums and 80 percent for family members.

- *CCC Board of Governor's Fee Waiver Program Reform*. The budget proposes trailer bill language to require all students seeking financial aid, including Board of Governor's (BOG) Fee Waivers, to fill out a Free Application for Federal Student Aid (FAFSA) form. This change is proposed to ensure that only financially needy students are determined eligible for the BOG fee waiver program and to ensure program integrity. Any savings will be reinvested to further increase course offerings and student services.

- *CCC Funding Incentive Initiative*. The budget proposes trailer bill language to change community college census accounting practices by adding a second census date at the end of each academic term. Over a five-year-period, the earlier census date (which is currently in the third or fourth week of the each semester) would gradually be phased-out.

Any enrollment monies that districts "lose" due to this policy change would be transferred to district categorical programs that fund student support services (such as counseling). This proposal is intended to apportion funding by focusing on completion at the end of the term, thereby incentivizing districts to focus on outcomes.

T*he Governor's proposals related to K-14 Adult Education and expenditure of Proposition 39 Energy Efficiency funds are discussed in other sections of this report.*

ISSUES TO CONSIDER:

Overall Theme to the Higher Education Budget. The Governor has identified several important areas of focus for the state's higher education system, including the need for increased productivity, a lower cost per degree for students and the state, and improved student success and outcomes. The Governor has also highlighted that continued increases in costs are not necessarily adding value or productivity. Rather, to achieve long-term financial sustainability and to fund future initiatives, higher education segments will have to lower their cost structures. The Governor also acknowledges the significant budget reductions that have been made in recent years and proposes to begin reinvesting in the higher education system.

While there will be questions raised about some of the specific reforms and tools the Governor proposes as part of his multi-year plan, the areas of focus identified therein are generally shared by the Legislature. At this juncture, many aspects of the Administration's multi-year plan remain undefined or under-defined. This will remain the case until budget trailer bill language is transmitted and subcommittee hearings begin in early March. However, the overall approach contained in the multi-year plan presents a broad threshold question about the role of the Legislature, as well as a number of other questions on specific components of the plan, as delineated below.

What is the Legislature's Role in the Multi-Year Plan? Last year, the Governor proposed a similar long-term funding plan for UC, Hastings, CSU, and the CCC that promised stable and increasing state funding and fiscal incentives to allow the segments to better manage their resources. The plan was dependent upon the passage of Proposition 30 and on the segments achieving certain performance metrics as specified by the Administration. While the Legislature expected to be provided with further details of the plan, no specific or complete plan ever materialized.

In the interim, Proposition 30 passed. In the 2013-14 budget, the Governor again proposes a multi-year funding plan for higher education but with increased funding. Similar to last year, the multi-year plan proposes a new approach to capital outlay (discussed below) and the elimination of earmarks and enrollment targets (also discussed below), all of which effectively decrease legislative oversight and remove key budget tools that the Legislature uses to guide higher education agencies. Finally, the multi-year plan identifies several performance expectations.

In short, the multi-year plan significantly increases the segments level of autonomy but does not link to any specific outcome targets or means to hold the segments accountable for meeting those expectations. This approach raises important questions for the Legislature to consider: What role should the Legislature play in making key high level decisions about the $4.5 billion spent each year on higher education, including regarding capital outlay and determining the outcomes and the metrics used to measure performance of the segments? Is the Legislature's role simply to appropriate state funding absent any earmarks and/or enrollment targets and leave it to the Administration and the segments to determine priorities and progress? If this is the funding level that the state is going to provide for higher education, what does the Legislature expect the segments to achieve? Does the Legislature want to provide even greater autonomy to the segments?

Legislature's Consistent Message on Higher Education Accountability. On a bipartisan basis, the Legislature has been developing, supporting, and refining proposals to create greater accountability for higher education since 2002. These provisions are consistent with recent LAO recommendations on the need for a public agenda and improved oversight of the higher education segments, and reflect the findings of the most recent review of the state's Master Plan for Higher Education – that there is a need for clearly articulated goals in order to enable increased accountability across the entire higher education system. This is especially true in the current fiscal climate; the state needs to be clear about priorities for the use of the public funding provided to the segments. Being clearer about the goals and the measures will highlight and drive the budget and policy decisions necessary to support the state's higher education system in meeting the state's goals.

The most recent iteration of this effort was Senate Bill 721 (Lowenthal). Passed by wide margins in both houses, this bill established goals for higher education and laid out a process for establishing metrics and targets and for assessing progress in meeting California's educational and workforce needs. The Governor vetoed SB 721, stating, "*This bill sets three goals for our colleges and postsecondary institutions and orders the Legislative Analyst to create a committee to establish metrics that measure progress towards these goals. The bill also requires annual reports. Questions about who should measure, what to measure, and how to measure what is learned in college are way too important to be delegated to the Legislative Analyst*."

The Governor's stated reason for the veto is process-orientated. Therefore, it would appear that the broad objectives of the Administration and the Legislature about goal setting and establishing metrics to measure progress are consistent. Further, SB 721 and preceding bills were approved by the Legislature in the leanest of fiscal times. This raises a key question for the Legislature to consider: now that the state is reinvesting in higher education, to be consistent with prior legislative intent and action shouldn't that reinvestment and overall higher education budget be linked directly to an accountability framework?

The State Lacks a Higher Education Oversight Structure. In 2011, the Governor vetoed funding for the California Postsecondary Education Commission (CPEC), citing the agency's ineffectiveness in higher education oversight. In light of this action, the future of higher education oversight remains unclear. While the public segments have stepped in to assume some roles previously performed by CPEC, there are concerns about how institutional and public interests will be balanced. In its January 6, 2012, report entitled, "*Improving Higher Education Oversight*," the LAO focused on the need for oversight that enables policymakers and others to monitor how efficiently and effectively the postsecondary system is serving the state's needs, and make changes to improve its performance. The specific recommendations of that report include that the Legislature: (1) define the state's postsecondary education needs, such as setting specific goals; (2) use performance results to inform policy decisions; and (3) establish an independent oversight body with limited and clear responsibilities.

Noting the difficulty of creating a new public organization in the current fiscal environment, the LAO offered a number of short-term measures to strengthen oversight in the interim: (1) amending statute to ensure pertinent data remain available to policymakers and researchers; (2) increasing direct legislative oversight and limiting new long-term funding commitments until an effective oversight structure is in place to support the legislature's decision-making; and (3) monitoring segments' allocation decisions, including investment in new programs and other major program changes, until mechanisms are in place for outcome review. The LAO's short-term measures warrant further consideration by the Legislature as it begins its review of the Governor's multi-year plan.

Online Education at the Higher Education Segments. A key component of the multi-year plan's focus on improved deployment of teaching resources is the proposal to use technology to deliver quality education to greater numbers of students in high demand courses; e.g., bottleneck courses that slow time to degree while students await a "seat" in the required course. If the reform bears fruit, the net result will be increased productivity and lower cost per degree for students and the state, as well as increased access for other students. While budget trailer bill language has not been transmitted, the *Budget Summary* and budget bill language provide insight into the Governor's vision: the focus is matriculated undergraduate students and for high demand courses. For UC and CSU, the courses will be available systemwide regardless of a student's "home" campus and tuition will be the same as for regular courses. For the CCC, a "virtual campus" will be created and credit by exam options will be expanded.

While the state's colleges and universities have been providing distance education for decades through university extension programs, online instruction for credit towards undergraduate and graduate degrees has become a much more prominent part of postsecondary education in recent years. At the same time, debates have been sparked about quality assurances. Recent media reports have been focused on the rapid rise of MOOCs (massive open online courses), which are online courses aimed at large-scale participation and open access via the web. Though the design of and participation in a MOOC may be similar to college or university courses, MOOCs typically do not offer credits awarded to paying students at schools. However, that aspect is changing as universities here, and nationally, are now examining opportunities to use the MOOC platform for credit instruction, including the recently announced pilot at San Jose State using a MOOC platform for introductory and remedial classes.

In its October 2010 report entitled, "*The Master Plan at 50: Using Distance Education to Increase College Access and Efficiency*," the LAO found that while distance education is not, and is not intended to be, suitable for everyone (students as well as faculty), it offers an important alternative means of providing instruction that can complement existing formats and expand options for the state's students and segments. In order to take fuller advantage of this potential, the LAO recommended that the Legislature guide a clearer statewide vision that specifies data which the segments should collect and report on distance-education students and clarifies expectations concerning intercampus collaborations and other partnerships. Specific LAO recommendations included: (1) streamlining educational pathways for online students; (2) promoting the sharing of curriculum across campuses; and (3) encouraging collaborative academic programs.

There are several other key questions for the Legislature to consider: (1) What is online credit instruction? Should it be more than simply taking the traditional classroom model and moving it online without any change in approach? (2) How much are the segments currently spending for online credit instruction and can supplanting be prevented? (3) What will move the needle? Should the focus be systemwide, for projects that can ease taking courses across campuses and/or support the development of courses to be used across campuses? (4) What is the appropriate balance between investing funds in proven methods versus new and emerging methods? (5) How can the quality of instruction be ensured?

Unit Caps on State-Subsidized Courses at UC, CSU, and CCC. The budget proposes caps on the number of units the state will subsidize at UC, CSU, and CCC. While budget trailer bill language has not been transmitted, the Administration has indicated that the cap would apply to both new and continuing students beginning in the 2013-14 academic year and be in place over the life of the multi-year plan. The budget would allow the universities and colleges to grant waivers and allow students to take additional units above the cap; however, the state would provide no subsidy so either the student pays full freight or the institution bears the entire cost of providing the instruction. This approach raises important considerations for the Legislature.

The initial limit for UC and CSU (150 percent of standard requirements) likely would not have a significant impact, but the eventual limit to be imposed at the universities after two years (125 percent of standard requirements) would impact more students primarily at CSU. For the community colleges, however, the impact is much more immediate and significant. For instance, in 2009-10, nearly 120,000 students had earned 90 units or more.

The cap is intended to create an incentive for students to shorten their time-to-degree, reduce costs for the state, and increase access to more courses for other students. This is a legitimate goal, but ignores some of the realities of the current situation. Students should be able to take appropriate courses and earn degrees in a timely fashion, but there needs to be shared responsibility for doing so. However, this proposal penalizes only students and ignores the reasons why students may accrue excess units, including the unavailability of courses, inconsistent transfer requirements, and requirements of particular majors, and to what degree those reasons are within the control of students.

A one-size-fits-all approach is potentially punitive to those who have a double major and those who may be returning to college to train for a new job. For the community colleges specifically, the cap would also apply to so-called freeway fliers, who are students that, largely out of necessity, enroll and take classes at multiple colleges and/or districts. It is not clear that the community colleges have the data capabilities to track those students and the number of accumulated units. This raises a legitimate question about enforcement of the cap within the community college system.

A New Approach to UC and CSU Capital Outlay. The *Budget Summary* indicates the Administration is considering some changes to the state's infrastructure spending practices, including identifying alternatives to limit future bond authorizations backed by the General Fund, currently the state's main source of infrastructure funding. Some alternatives mentioned include identifying new funding sources and creating new mechanisms to prioritize and limit capital spending.

For higher education, and consistent with the above direction, the budget proposes a new approach to UC and CSU capital outlay, including how debt service costs are budgeted and structured as well as how future projects are approved and funded. While many details remain outstanding, including what, if any, role the Administration envisions for the Legislature in approval of new higher education capital outlay expenditures and the impacts of the proposal to authorize UC and CSU to restructure their respective lease-revenue bond debt to create budgetary savings, the approach raises important considerations for the Legislature.

The approach is a departure from how UC and CSU capital outlay has been historically addressed. Under prior practice, and in the last ten years, the LAO reports that the state spent an estimated $10.1 billion on higher education infrastructure; 80 percent of that support came from general obligation (GO) bonds and an additional 19 percent from lease-revenue bonds. Associated higher education debt-service costs more than doubled during this same time period, from about $516 million in 2000-01 to an estimated $1.1 billion in 2010-11. Most of the GO bond spending was from bonds approved by the voters in 1998, 2002, 2004, and 2006. In general, the state provides less funding for higher education projects when the balance of GO bonds is exhausted. In the case of UC and CSU, the state has typically offset some of this reduction by funding some projects with lease-revenue bonds. All of these projects were presented as part of the annual budget process, thereby ensuring the segments requested approval from the Administration and Legislature for any projects funded with either GO bonds or state-issued lease-revenue bonds.

At this point, the remaining higher education GO bond authority has all but been exhausted. This Administration has not advanced any new lease-revenue bond financed projects. To wit, the Budget Act of 2012 included very limited new funding for capital outlay. For UC, $4.75 million (2006 GO bond funds) was appropriated for preliminary plans and working drawings for a new building at UC Merced. For CSU, $10.995 million (GO bonds) and $11.155 million (federal funds) to fund all phases of five seismic upgrade projects at the Los Angeles, San Luis Obispo, Bakersfield, and Humboldt campuses.

Looking ahead to 2013-14, both the UC and CSU governing boards adopted extensive state-funded capital outlay programs, with 39 projects totaling $788.5 million and 38 projects totaling $520 million, respectively. The request submitted to the Administration was much smaller: UC advanced three projects totaling $73 million and CSU advanced 21 projects totaling $390.3 million. The budget includes no capital outlay projects for UC; for CSU, the budget includes $3.637 million (GO bonds), for equipment phases of already constructed projects at the San Jose, Maritime Academy, Bakersfield, and Fresno campuses.

By shifting the debt service payments into the segments' base budgets, the Administration asserts that this would limit the segments' capital spending by highlighting the trade-offs between spending on infrastructure versus operations. As it stands now, these debt service costs are borne by the state's budget providing no incentive for the segments to limit the number and scope of capital projects they submit to the Administration and Legislature. Yet, this change in approach raises several questions for the Legislature to consider, including: (1) Is the 2013-14 funding provided adequate to annually service the segments' existing bond debt in the coming years? (2) Is the proposed total base funding (which could grow by up to five percent annually over the life of the multi-year plan) reasonable to cover the UC's and CSU's various operational and bond-related costs? (3) To what extent, and in what ways, will the Legislature have a role in approval of higher education capital outlay projects?

Elimination of UC and CSU Budgetary Earmarks. Typically, the annual budget act includes a number of conditions on UC's and CSU's General Fund appropriations. These earmarks for UC and CSU funding have varied over the years in keeping with the Legislature's and Governor's particular concerns at the time and have covered such programs as nursing and medicine, student financial aid, and science and math teaching initiatives. Due to Governor's vetoes, the Budget Act of 2012, for the first time, included minimal earmarks in UC's and CSU's budgets. The budget contains no earmarks except for a new one to address the Governor's priority, namely the $10 million provided to each segment to increase the number of courses available through the use of technology.

The UC and CSU are governed by independent boards that make various decisions about how the universities will spend their resources, including the number of faculty, executives, and other employees on the payroll and those employees' salary and benefits; student tuition levels; and the amount of tuition revenue redirected to financial aid, among other fiscal decisions. Further, UC has constitutional autonomy afforded by the California Constitution, under which the Regents have "*full powers of organization and governance*" subject only to very specific areas of legislative control, such as budget act appropriations.

Given this dynamic, where significant budget authority has already been delegated to UC and CSU, the Legislature has relied on earmarks to ensure key concerns are addressed within the funding appropriated to the universities. The inclusion of earmarks in the budget bill provides a clear public record of budgetary allocations and expectations. The Governor's approach effectively eliminates this budgetary tool for Legislative priorities, but creates a new earmark for his priority.

The LAO has recommended that rather than simply abandoning all earmarks in the universities' budgets, the Legislature should reevaluate budgetary earmarks on a case-by-case basis. In some cases, the Legislature may decide that a particular earmark is no longer a priority. In others, the Legislature may wish to keep or change or add an earmark. To help in evaluating potential earmarks, the Legislature may wish to develop guidelines such as approving only those earmarks that serve a broader state purpose.

Elimination of UC and CSU Enrollment Targets. The *Budget Summary* states that "*enrollment based funding does not promote innovation and efficiency or improve graduation rates. It does not focus on critical outcomes, affordability, timely completion rates, and quality* *programs. Instead, it builds on the existing institutional infrastructure, allowing public universities and colleges to continue to deliver education in the high-cost, traditional model*." Therefore, the budget does not include enrollment targets for either UC or CSU, effectively allowing UC and CSU to make their own decisions about how many students to enroll with the funding available to them.

Historically, UC's and CSU's budget have been tied to a specified enrollment target. To the extent that the segments failed to meet those targets, the state funding associated with the missing enrollment reverted to the General Fund. Beginning with the Budget Act of 2011, enrollment targets were included but without any penalty should a segment fail to meet its target in recognition of the overall reductions to higher education budgets.

Enrollment levels are irrefutably a fundamental building block of higher education budgets. The number of students enrolled is a direct measurement of the "access" provided to higher education. Further, enrollment levels are a central cost driver for the segments and drive other costs, such as state financial aid. For these reasons, enrollment targets have been a major legislative concern in recent years. With no target, as proposed by the Governor, the segments would have wide discretion as to their enrollment levels. For example, they could significantly reduce the number of students served, thus raising the amount of funding available per student. Or UC and CSU could reduce the number of undergraduates served, and use the funding to add a smaller number of higher-cost graduate students. Certainly choices here link back to the multi-year plan and its expectations for segmental performance on certain priorities. For instance, it is unlikely the segments would decrease the acceptance of community college transfer students, as that is an identified priority of the multi-year plan. Nevertheless, enrollment decisions have implications not just for educating students, but they also have a profound effect on the level of access provided at each segment.

In the past, the LAO has recommended the rejection of any proposal to eliminate enrollment targets. Further, to the extent that the Legislature chooses to significantly increase a segment's budget, it may wish to modify the enrollment targets. Alternatively, the Legislature may wish to require the segments to achieve greater efficiencies without reducing enrollment. In addition, this proposal raises other key questions for the Legislature's consideration: With no enrollment target, what assurances does the Legislature have that UC and CSU will continue to serve all students eligible for their institutions under the Master Plan? What recourse would be available if the segments fail to do so?

CSU Employer Costs for Retirement. CSU's required employer contribution to CalPERS has been historically borne by the state's budget. Each year, the annual budget act provided an adjustment for either the increase or decrease in the required contribution level as determined by the CalPERS Board of Administration. CSU's base budget of $1.9 billion contains $460 million for this purpose. The budget proposes an annual adjustment of $51.4 million General Fund and a substantive change in approach going forward. In future years, CSU will continue to receive annual General Fund adjustments for CalPERS costs based on 2012-13 payroll; however, if CSU chooses to increase payroll expenditures above the 2012-13 level, CSU would be responsible for the associated pension costs. CSU could be concerned that under the budget proposal, it and its employees will have little flexibility and few tools beyond salary/benefit setting authority to manage unfunded liabilities and higher costs that could result in the future. For instance, the CalPERS Board sets the employer contribution rate. However, this is not unique to CSU as an employer; this also applies to the state as well as every other public employer who contracts with CalPERS. Absent the Governor's proposal, the alternative is that the state's budget will continue to bear these costs yet have no control over the salary/benefits and resulting pension costs (above the 2012-13 expenditure level) that CSU negotiates with its employees.

CSU Employee Health Care Benefit Rates. The budget proposes trailer bill language to provide CSU with the same statutory authority to negotiate or set employee health care benefit rates that is provided to the California Department of Human Resources (CalHR) for other state employees. A similar proposal was included as part of the 2012 May Revision but was not part of the final budget. Last year concerns were raised about timeliness given that CSU was actively bargaining with the majority of its represented employees. At present, all of CSU's bargaining units are under contract. While the actual trailer bill language has not been transmitted, the Governor is raising a legitimate point about providing CSU with the same tools as CalHR to better manage and negotiate the entirety of its personnel costs, including employee health care benefit rates.

Community College Base Budget Increase. The budget provides $197 million in Proposition 98 General Fund support for the community colleges. Unlike other state funds in the community college budget, the budget would allow the Chancellor's Office to make its own decisions about how the funds would be distributed and for what purpose. This is a broad departure from past practice, whereby any increase in base budget funding was provided for a specific purpose, such as for growth (unfunded FTES) or a cost-of-living-adjustment (increase in the per FTES amount). The LAO has raised concerns about whether the Governor's approach would ensure that the state's highest community college priorities would be addressed. For instance, the Legislature has enacted several pieces of legislation specifying a number of priorities to fund once new resources become available, such as a common assessment instrument to place incoming students into appropriate coursework, additional academic counselors to help students identify and make progress toward their educational goals, and a system for electronic student transcripts to improve campus record-keeping and efficiencies. In addition, the state has a number of outstanding community college-related liabilities, including over $300 million that is owed for past mandate claims.

Buydown of Community College Inter-Year Deferrals. The Governor's budget proposes an increase of approximately $1.9 billion in Proposition 98 General Fund to reduce inter-year budgetary payment deferrals for K-14 education in 2013-14. Of that total, $179 million is for community colleges reducing the deferral debt owed to the community colleges to $622 million (the Budget Act of 2012 reduced the debt to $801 million from a total of $961 million). The level of deferral "buy down" is consistent with, and proportional to, the payment of deferred funding in K-12 education; e.g., basically a 50-50 split of new funding versus deferral buydown. The Governor further plans to eliminate all inter-year payment deferrals to schools and community colleges over the next few years. From a fiscal and policy standpoint, it is prudent to reduce these inter-year deferrals, as they remain outstanding obligations on the state's books. The deferrals also were an agreed-upon solution to avoid more draconian cuts to K-14 budgets. They also come with borrowing costs for districts, in order to address cash flow concerns caused by the delayed state payments. It remains unclear if there are any advantages to delaying repayment of inter-year deferrals for K-12 schools and community colleges to future years.

Board of Governor's Fee Waiver Program Reform. The budget proposes to require all community college students seeking financial aid, including Board of Governor's (BOG) Fee Waivers, to fill out a Free Application for Federal Student Aid (FAFSA) form.

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 General Fund monies, has grown rapidly in recent years with waiver costs projected to total $855 million in 2012-13. Under current law and regulation, there are three means of eligibility: (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 $1,104 or more; $1,104 is the amount of annual fees charged to a full-time student taking 24 units). Students can apply for a fee waiver by completing: (1) the 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. The Chancellor's Office indicates that 80 percent of students currently receiving aid filled out a FAFSA.

The LAO has previously recommended that the Legislature enact the statutory changes necessary to add satisfactory academic progress requirements to the BOG Fee Waiver program (Chapter 624, Statutes of 2012). The LAO also recommended that the Legislature enact the statutory changes necessary to 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. In considering this proposal, an important consideration is to avoid creating a new reimbursable state mandate.

Community College Funding Incentives Initiative. The budget proposes to change the basis on which districts are funded for credit instruction by phasing in a second census date at the end of each academic term to focus on completion at the end of the term. While the Governor raises a fair point about the benefit about moving to a funding model that is more outcome-oriented, legitimate concerns can be raised about unintended consequences in the classroom, such as grade inflation or reductions in course rigor. The LAO has also noted that by redirecting any "lost" funds to a district's categorical program, the budget presupposes that students do not complete their coursework because of inadequate support services. This may be a contributing factor, but it ignores the many other factors that could be at play such as a poorly designed or taught course. The LAO has suggested the Legislature consider changes to the funding model that would place greater emphasis on more meaningful outcomes, such as rewarding colleges for student learning gains and program completions (such as obtaining a degree or skills certificate) rather than course completion. Given that the Student Success Task Force (SSTF), which is discussed below, considered and rejected a similar proposal, the Legislature should consider the interaction of this proposal with the work of the SSTF, such as establishing enrollment priorities, which is already underway and could accomplish the same goal.

Interaction with the Priorities of the Student Success Task Force. Pursuant to Chapter 409, Statutes of 2010, the Board of Governors (BOG) created the Student Success Task Force (SSTF) to research, study and debate the best methods to improve student outcomes. The SSTF final report was unanimously adopted by the BOG in January 2012. The SSTF efforts resulted in 22 specific recommendations, to be accomplished through regulatory changes, system-wide administrative policies, local best practices, and legislation. Major recommendations address linkages with K-12 schools, student intake and support, instructional programs, and accountability. Seven of the 22 recommendations are in the implementation phase, as follows: (1) Common Core State Standards; (2) Common Assessment; (3) Statewide Enrollment Priorities; (4) BOG Fee Waiver Requirements, contained in Chapter 624, Statutes of 2012; (5) Student Success Score Card; (6) Longitudinal Student Record System; and (7) Student Support Initiative, also contained in Chapter 624. With all of this work related to the SSTF recommendations underway, the conversation has effectively moved from “what” recommendations to “how” the recommendations are implemented. The Legislature has been a full partner in this process as evidenced by Chapter 624.

There is, however, an interesting juxtaposition between the SSTF recommendations and the budget reforms. The SSTF is an example of local control that the Governor supports, yet some of the budget reforms would supersede the SSTF work done to date and planned for the future. For instance, there is overlap between the SSTF recommendations and the budget reforms (such as differing policy changes regarding BOG waiver requirements and unit caps), other SSTF recommendations address issues not identified in the budget reforms (such as establishing registration priorities, including allowing students who participate in orientation and academic assessment programs and have 100 units or less to enroll in classes first), and some of the budget reforms go well beyond the SSTF recommendations (such as the proposed funding incentives initiative). Given these intersections, and prior legislative support for the SSTF process and recommendations, careful legislative consideration is warranted of all related budget proposals.

Higher Education

Each year, millions of Californians pursue degrees and certificates and enroll in courses to improve their knowledge and skills at the state's higher education institutions. More are connected to the system as employees, contractors, patients, and community members. California's system of higher education consists of three segments. Drawing from the top 12.5 percent of the state's high school graduates, the University of California (UC) educates approximately 239,500 undergraduate and graduate students and is the primary institution authorized to independently award doctoral degrees and professional degrees. Drawing students from the top one-third of the state's high school graduates, the California State University (CSU) provides undergraduate and graduate instruction to approximately 410,300 students. The California Community Colleges are publicly supported local educational agencies that provide open-access educational and vocational programs to approximately 2.4 million students. The state also provides financial aid to students attending all institutions of public and private postsecondary education through the Cal Grant program. Over 99,000 students received new Cal Grant awards, and over 150,000 students received renewal awards, in 2011-12.

Beginning with the Master Plan in 1960, California's approach to higher education has been to heavily subsidize the public segments and keep costs low for university students (and even lower for community college students). California's higher education system is relatively affordable to students because of California taxpayers' investment in that system. California institutions have some of the lowest published tuition and fee levels in the country. In addition to providing direct support to the higher education system, California fully reimburses all UC, CSU and community college tuition and fee costs for students with family incomes below $96,000 through the Cal Grant and the California Community Colleges Board of Governors Fee Waiver programs. In total, California taxpayers provide approximately $13 billion of annual General Fund support to California's higher education system through a combination of general-purpose, categorical program, and Cal Grant Program funding.

As a result of the taxpayers' investment in higher education, California public college and university graduates carry some of the lowest student loan debt burdens when compared to graduates from other states. California students in public and non-profit colleges rank 46th in student debt levels — half of California undergraduates have student debt, averaging $18,800, compared to two-thirds of graduates nationally, averaging $26,600.

The recent economic downturn and resulting shortfalls in state revenues required reductions in the state's subsidies of public higher education. During this period of fiscal constraints, state and local public agencies throughout California reexamined their cost structures and refocused limited resources on the most essential functions. UC and CSU pursued administrative efficiencies that have yielded from the low-to-mid hundreds of millions of dollars of savings for each segment. However, from 2007-08 to 2012-13, when other public agencies were retrenching, UC expenditures increased by 15 percent and CSU expenditures increased by 3 percent. These expenditure increases were funded by approximately $1.4 billion in tuition revenue increases at UC and $1 billion at CSU, a near doubling of tuition and fees from 2007-08 to the present. Specifically, UC's tuition and fees increased by $5,556 over that period. CSU's tuition and fees increased by $2,700 over that same period (see Figure HED-01). These rapid tuition increases have been a significant hardship for students and their families, particularly middle-income families who do not qualify for Cal Grants.

The rising cost of higher education not only threatens affordability, it also threatens the quality of California's system of higher education as it relies on a model that is not sustainable. Historically, California's public higher education institutions have led the world in terms of quality, innovation, and affordability for students. However, California is beginning to lose its lead in these areas in large part because of a higher education cost structure that continually increases without necessarily adding productivity or value. While this is a problem nationwide, California's higher education system is more expensive than other states' systems because (1) spending is very high in UC compared to other public research universities, and (2) completion and transfer rates are very low in CSU and the community colleges, resulting in great inefficiencies.

Figure HED-01

UC and CSU Expenditures and Undergraduate Tuition and Fees

(Dollars in Millions)

	2007-08	2008-09	2009-10	2010-11	2011-12	2012-13	2013-14 [4]	Change from 2007-08 Dollars	Change from 2007-08 Percent
UC									
General Fund	$3,257.4	$2,418.3	$2,591.2	$2,910.7	$2,272.4	$2,377.3	$2,644.1	-$613.3	-19%
Tuition and Fee Revenue	1,593.1	1,676.8	2,054.4	2,212.7	3,022.6	3,000.6	3,029.2	1,436.1	90%
Federal Funds - ARRA [1]	-	716.5	-	106.6	-	-	-	-	-
Total Funds [2]	$5,453.3	$5,453.4	$5,298.1	$5,948.2	$6,117.2	$6,263.6	$6,526.6	$1,073.3	20%
Systemwide Tuition and Fees	$6,636	$7,126	$8,373	$10,302	$12,192	$12,192	$12,192	$5,556	84%
CSU									
General Fund [3]	$2,970.6	$2,155.3	$2,345.7	$2,577.6	$2,002.7	$2,063.6	$2,333.0	-$637.6	-21%
Tuition and Fee Revenue	1,176.3	1,406.1	1,630.6	1,681.9	2,187.0	2,129.9	2,129.9	953.6	81%
Federal Funds - ARRA [1]	-	716.5	-	106.6	-	-	-	-	-
Total Funds [2] [3]	$4,487.1	$4,616.9	$4,279.9	$4,674.5	$4,612.0	$4,633.2	$4,902.7	$415.6	9%
Systemwide Tuition and Fees	$2,772	$3,048	$4,026	$4,440	$5,472	$5,472	$5,472	$2,700	97%

[1] The second round allocations of American Recovery and Reinvestment Act (ARRA) funding from the State Fiscal Stabilization Fund are shown in 2008-09 to more accurately reflect segmental expenditures between the two fiscal years and intent of federal law to backfill 2008-09 reductions.

[2] Total funds for UC and CSU include offsetting general purpose income, but exclude self-supporting functions such as auxiliary enterprises and extramural programs among others.

[3] Beginning in 2012-13, health benefits provided for CSU retired annuitants are included in CSU's main General Fund and Total Funds budget, rather than in the main statewide item for retired annuitant benefits, as reflected in Figure HED-02. However, for purposes of this figure, to compare 2007-08 to 2013-14 funding, these expenditures are not reflected in CSU's funding levels in 2012-13 or 2013-14.

[4] Beginning in 2013-14, the general obligation bond debt service payments are included in UC and CSU's main General Fund and Total Funds budgets. However, for purposes of this figure, to compare 2007-08 to 2013-14 funding, the GO bond debt service amounts are not reflected in the segments' 2013-14 expenditures.

UC and CSU have proposed budgets that call for increases in state funding of about 12 percent and 18 percent, respectively, from the preceding year. By comparison, over the past three years, personal income growth in California has averaged slightly less than 4 percent per year. California taxpayers cannot sustain institutions whose cost growth greatly outpaces the state's income growth. Furthermore, the rapidly growing numbers of college graduates who are unable to repay their student loans is an indication that these costs cannot be forever pushed onto students through tuition and fee increases.

Even while the California higher education system demands more funding, it produces transfer and completion rates that need improvement. Less than 30 percent of degree seeking students at community colleges complete a degree, earn a certificate, or transfer within six years. For CSU, only 16 percent of students complete their degree within four years, and just 60 percent of students earn a degree in four years at UC. A significant obstacle to timely completion is the unavailability of courses. When students are turned away from courses, time to completion increases and students enroll in courses they do not need for their degree, generating excess costs to the student and the state, and crowding out other students in the process.

Until recently, the state has funded higher education based on enrollment targets. However, enrollment-based funding does not promote innovation and efficiency or improve graduation rates. It does not focus on critical outcomes—affordability, timely completion rates, and quality programs. Instead, it builds the existing institutional infrastructure, allowing public universities and colleges to continue to deliver education in the high-cost, traditional model.

Investing in Higher Education

The state must begin to reinvest to improve the quality and affordability of California's system of higher education. This investment is critical to provide all Californians—regardless of their financial circumstance—access to high-quality post-secondary instruction, improve educational attainment, and support civic engagement and critical thinking—thereby strengthening the foundation for sustainable growth. While continued state support of the Cal Grant program will maintain access for low-income families, additional state support for UC, CSU and community colleges alone will not be sufficient to stabilize tuition and fee costs for middle-income students or maintain the quality of these institutions. The UC, CSU and community colleges need to move aggressively to implement reforms to provide high-quality instruction at lower cost, decrease the time it takes to earn a degree, and increase graduation rates, by deploying their teaching resources more effectively.

There are many immediate demands for state funding. The Budget chooses to invest new, discretionary General Fund resources in higher education because the Administration believes that maintaining a quality, affordable system is critical to the future of the state. The Budget aims to enhance the quality of California's higher education institutions by making them more affordable, decreasing time to completion, improving overall completion rates in all higher education segments, and improving the transfer rate of community college students to four-year colleges and universities.

The Budget proposes total funding of $25.8 billion, reflecting an increase of $1.3 billion, or 5.3 percent, above 2012-13. The Budget proposes funding of $13.2 billion in General Fund and Proposition 98 related-sources reflecting an increase of $1.2 billion above 2012-13.

See Figure HED-02 for a summary comparison of individual institution funding totals reflecting the budget proposal and prior year appropriations.

Figure HED-02

Higher Education Expenditures

(Dollars in Millions)

	2011-12	2012-13	2013-14	Change from 2012-13 Dollars	Change from 2012-13 Percent
University of California [1/]					
Total Funds [2/]	$6,348.7	$6,453.0	$6,728.3	$275.3	4.3%
General Fund	2,503.9	2,566.7	2,845.8	279.1	10.9%
California State University [1/]					
Total Funds [2/ 3/]	$4,840.3	$5,069.0	$5,379.6	$310.6	6.1%
General Fund [3/]	2,231.0	2,492.4	2,809.3	316.9	12.7%
Community Colleges [1/]					
Total Funds	$10,674.6	$11,263.7	$11,880.3	$616.6	5.5%
General Fund & P98 [4/]	5,594.7	6,166.2	6,784.0	617.8	10.0%
Student Aid Commission					
Total Funds	$1,578.6	$1,654.3	$1,752.6	$98.3	5.9%
General Fund	1,486.2	735.6	719.6	-16.0	-2.2%
Other Higher Education [5/]					
Total Funds	$55.8	$58.9	$57.8	-$1.1	-1.9%
General Fund	9.1	9.2	9.5	0.3	3.3%
Total Funds	**$23,498.0**	**$24,498.9**	**$25,798.6**	**$1,299.7**	**5.3%**
General Fund	**$11,824.9**	**$11,970.1**	**$13,168.2**	**$1,198.1**	**10.0%**

1/ UC, CSU, and CCC General Fund and Total Funds include general obligation bond debt service.

2/ For purposes of this table, expenditures for the UC and CSU have been adjusted to include the offsetting general purpose income, but exclude self-supporting functions such as auxiliary enterprises and extramural programs among others. This provides consistency in comparing magnitudes and growth among the various segments of education.

3/ Beginning in 2012-13, the health benefits provided for CSU retired annuitants are reflected in CSU's budget, rather than in the statewide total.

4/ For purposes of comparing with UC and CSU General Fund, CCC includes property tax revenue as a component of the state's obligation under Proposition 98.

5/ The Other Higher Education amount includes Hastings College of the Law, including Hastings' GO bond debt service, and the California Postsecondary Education Commission.

Multi-Year Stable Funding Plan

The state's General Fund contribution to UC, CSU, and Hastings will increase by 5 percent per year in 2013-14 and 2014-15 and by 4 percent in each of the subsequent two years. Community colleges funding will also increase by 5 percent in 2013-14. It is expected that community colleges funding will grow significantly over the next several years. All institutions will be expected to use these increases to implement reforms that will make available the courses students need and help them progress through college efficiently, using technology to deliver quality education to greater numbers of students in high-demand courses, improving course management and planning, using faculty more effectively, and increasing use of summer sessions. With savings achieved in this way, in combination with the General Fund increases and realizing the savings of current efficiency efforts (e.g. UC's Working Smarter Initiative and CSU's Systemwide Administrative Efficiencies), the Administration expects the colleges and universities to maintain current tuition and fee levels over the next four years. The Administration will continue to engage UC, CSU, and community colleges administration, faculty, staff, and students in this effort to maintain the quality of education at these institutions while, at the same time, controlling costs and preventing further increases in tuition and student fees for motivated and focused students.

Expand the Delivery of Courses through Technology

The Budget provides $16.9 million to the community colleges to increase the number of courses available to matriculated undergraduates through the use of technology. The focus should be on the courses that have the highest demand, fill quickly, and are prerequisites for many different degrees. Priority will be given to development of courses that can serve greater numbers of students while providing equal or better learning experiences, but only if those courses are aimed at advanced students who are likely to succeed in these types of courses. This initiative will include three key elements: (1) the creation of a "virtual campus" to increase statewide student access to 250 new courses delivered through technology, (2) the creation of a single, common, and centralized delivery and support infrastructure for all courses delivered through technology and for all colleges, and (3) the expansion of options for students to access instruction in other environments and earn college credit for demonstrated knowledge and skills through credit by exam.

In addition, the Budget provides UC and CSU $10 million each to increase the number of courses available to matriculated undergraduates through the use of technology, specifically those courses that have the highest demand, fill quickly, and are prerequisites for many different degrees. Priority will be given to the development of courses that can serve greater numbers of students while providing equal or better learning experiences.

Student Success

The plan provides annual General Fund augmentations and expects each institution to direct those funds to the achievement of the following priorities: improvements in time-to-completion, improvements in graduation and completion rates in all segments, increases in transfer students enrolled at CSU and UC, and successful credit and basic skills course completion. Not all students matriculating in higher education have the common goal to earn a degree in four years. Both CSU and community colleges have significant populations of students who are earning their degrees or certificates on a part-time basis (e.g. full-time employment and family commitments). Higher education systems should provide all students the opportunity to access the courses needed to complete their degrees or certificates within the students' intended timelines. This applies to students whether they complete their undergraduate coursework in a traditional four-year period or over a longer timeframe.

Student Incentives

To shorten students' time-to-degree, reduce costs for students and the state, and increase access to more courses for other students, the number of units students can take while receiving a state General Fund subsidy at any of the segments will be capped.

- For UC and CSU, in the first two years of the proposal, students will be allowed to accrue no more than 150 percent of the standard units needed to complete most degrees (270 quarterly units at UC and 180 semester units at CSU); in later years, students will be allowed to accrue units equivalent to no more than about one additional year of coursework (225 units at UC and 150 units at CSU). If students enroll in courses that exceed these unit caps, students will be required to pay the full cost of instruction. However, the universities may grant case-by-case waivers to students who exceed the cap due to factors beyond their control, allowing them to continue to pay the subsidized tuition level. The universities would not receive any additional state funding for these students.

- For community colleges, students will be allowed to take no more than 90 semester credit units (150 percent of the standard 60 semester credit units required to earn an associate's degree or credits for transfer) starting in 2013-14. If students enroll in credit courses that exceed these unit caps, students will be required to pay the full cost of instruction. Community colleges may grant case-by-case waivers to students who exceed the cap due to factors beyond their control, allowing them to continue to pay the subsidized tuition level. However, the community colleges will not receive any state funding for these students.

This policy will encourage students to identify an educational goal and reach it in a timely and efficient way, focusing on the courses necessary to complete their educational goals, while still allowing for some exploration of other subject areas.

University of California

Drawing from the top 12.5 percent of the state's high school graduates, the University of California (UC) educates approximately 239,500 undergraduate and graduate students at its ten campuses and is the primary institution authorized to independently award doctoral degrees and professional degrees in law, medicine, business, dentistry, veterinary medicine, and other programs. UC manages one U.S. Department of Energy national laboratory, partners with private industry to manage two others, and operates five medical centers that support the clinical teaching programs of UC's medical and health sciences schools that handle more than 3.9 million patient visits each year.

Significant Adjustments:

- General Fund Increase — As discussed above, an ongoing increase of $125.1 million General Fund for core instructional costs. This includes the $10 million to increase the number of courses available to matriculated undergraduates through the use of technology. This funding should obviate the need for UC to increase student tuition and fees and can be used by the university to meet its most pressing needs. This increase is in addition to the $125 million General Fund that UC will receive in 2013-14 for not increasing tuition and fees in 2012-13, as required by the 2012 Budget Act.

- Debt Service Costs — Currently, the state separately funds general obligation and lease revenue debt service for UC capital improvement projects. The Budget proposes to shift these appropriations into UC's budget, which will require UC to factor these costs into the university's overall fiscal outlook and decision-making process. Any new UC capital expenditures will be subject to approval by the Administration to ensure the funds are used for academic facilities to address seismic and life safety needs, enrollment growth, modernization, or for cogeneration and energy conservation projects. Further, there will be limits on the amount of the budget that can be spent on capital expenditures. If UC elects to restructure its debt as a result of this proposal, it is expected that it will make resources available for instruction.

California State University

Drawing students from the top one-third of the state's high school graduates, the California State University (CSU) provides undergraduate and graduate instruction through master's degrees and independently awards doctoral degrees in education, nursing practice, and physical therapy, or jointly with UC or private institutions in other fields of study. With 23 campuses and approximately 410,300 students, CSU is the largest and most diverse university system in the country. CSU plays a critical role in preparing the workforce of California; it grants more than one-half of the state's bachelor's degrees and one-third of the state's master's degrees. CSU prepares more graduates in business, engineering, agriculture, communications, health, and public administration than any other California institution of higher education. It also produces over 50 percent of California's teachers.

Significant Adjustments:

- General Fund Increase—As discussed above, an ongoing increase of $125.1 million General Fund for core instructional costs. This includes the $10 million to increase the number of courses available to matriculated undergraduates through the use of technology. This funding should obviate the need for CSU to increase student tuition and fees and can be used by the university to meet its most pressing needs. This increase is in addition to the $125 million General Fund that CSU will receive in 2013-14 for not increasing tuition and fees in 2012-13, as required by the 2012 Budget Act.
- Debt Service and Retirement Contribution Costs—Currently, the state separately funds general obligation and lease revenue debt service for CSU capital improvement projects. The state also annually adjusts funding for CSU's retirement obligations. The Budget proposes to fold debt service appropriations into CSU's budget. Any new CSU capital expenditures will be subject to approval by

the Administration to ensure the funds are used for academic facilities to address seismic and life safety needs, enrollment growth, or modernization. Further, there will be limits on the amount of the budget that can be spent on capital expenditures. The Budget also proposes that the state continue to fund retirement contributions for CSU employees, based on the number of 2012-13 employees. If CSU chooses to add employees or increase wages beyond 2012-13 levels, CSU will be responsible for the associated costs. These two changes will require CSU to factor these costs into the university's overall fiscal outlook and decision-making process.

- Provide CSU the Authority to Negotiate and Set Employee Health Benefit Rates with Represented and Non-Represented Employees—CSU will be provided the same statutory authority to negotiate or set employee health care benefit rates that is provided to the California Department of Human Resources for other state employees. Currently, CSU pays 100 percent of the health care premiums for its employees and 90 percent for employees' family members. However, for most other state employees, the state pays either 80 or 85 percent of employees' health care premiums and 80 percent for family members. This proposal will provide CSU a tool to better manage and negotiate the entirety of its personnel costs.

California Community Colleges

The California Community Colleges are publicly supported local educational agencies that provide educational, vocational, and transfer programs to approximately 2.4 million students. The California Community College system is the largest system of higher education in the world, with 72 districts, 112 campuses, and 70 educational centers. In addition to providing education, training, and services, the community colleges contribute to continuous workforce improvement. The community colleges also provide remedial instruction for hundreds of thousands of adults across the state through basic skills courses and adult non-credit instruction.

Significant Adjustments:

- Expand the Delivery of Courses through Technology—As discussed above, an augmentation of $16.9 million to increase the number of courses available to matriculated undergraduates through the use of technology.

- Reforms to Census Accounting Practices—Currently, community colleges are provided state funding based on the number of students enrolled at the 20-percent mark of the term. Under this construct, the fiscal incentives for community colleges are to enroll students and not to ensure that students complete the term. When students withdraw after the 20-percent mark, the state is unnecessarily paying community colleges for students who are no longer in class. Enrollment-based funding lacks incentives for the colleges to focus on critical outcomes—affordability, timely completion rates, and quality programs. This proposal will more appropriately apportion funding by focusing on completion at the end of the term, as opposed to counting attendance at the early weeks of the term. It will be phased in over several years to help colleges adjust their policies and practices in a way that encourages appropriate student placement and good course management. This proposal will reinvest savings into higher apportionment rates for students that complete their courses and for student support services in those communities with higher non-completion rates.

- Board of Governor's Fee Waiver Program Reform—The Board of Governor Fee Waiver program provides hundreds of millions of state financial aid dollars annually to community colleges and their students. Approximately 60 percent of all credit course fees are waived annually by the community colleges, and the state backfills this lost community college revenue source with state funds. The fee system is designed to charge fees to those who can afford to pay them and provide waivers to students who need them. The current fee waiver program provides financial aid to students with limited verification of financial need. To ensure that only financially needy students are determined eligible for the fee waiver program and to ensure program integrity, students seeking financial aid will be required to fill out a Free Application for Federal Student Aid and include both parent and student income when determining fee waiver eligibility. Any savings that result will be reinvested to further increase course offerings and student services and allow students to move through the system more quickly. Additionally, this proposal will generate additional federal financial aid resources for students and colleges.
- Adult Education Realignment—As referenced in the K Thru 12 Education Chapter, K-12 school districts and community colleges are both currently authorized to provide adult education instruction. However, there is no statewide requirement or mechanism to coordinate the efforts of these two systems. As a result, the state has an inefficient and redundant system that is not always structured in the best interest of adult learners. Further, funding for the K-12 adult education program is currently flexible and available for any educational purpose. Many districts are eliminating their programs and redirecting this funding to support their core instructional programs.

- To create a more accountable and centralized adult education learning structure, the Budget proposes $315.7 million Proposition 98 General Fund to fund a comparable K-12 adult education service delivery system. It proposes an increase of $300 million to support the program within the community colleges. It also shifts $15.7 million and the responsibility for the Apprenticeship Program from school districts to the community colleges. The proposal eliminates the current bifurcated system and places community colleges in a position to improve coordination at the regional and statewide levels. Community colleges are better positioned to address the needs of adult learners because that is their core function. However, the colleges will be encouraged to leverage the capacity and expertise currently available at the K-12 district adult schools.

- Funding for adult education will be allocated from a new block grant based on the number of students served and only for core instructional areas such as vocational education, English as a Second Language, elementary and secondary education, and citizenship. This proposal will refocus apportionments away from non-mission areas and reinvest savings for additional courses in mission areas such as basic skills and workforce training. If community colleges offer non-mission courses, students will be required to pay the full cost of instruction. The funding level will be reassessed in the future based on program participation and effectiveness.

- Clean Energy Efficiency Projects—An increase of $49.5 million Proposition 98 General Fund for community colleges to undertake clean energy efficiency projects. Like school districts, community colleges are well positioned to undertake projects that reduce their current utility requirements and expand the use of renewable energy resources. Moreover, community colleges are in the unique position to make a substantial energy efficiency imprint throughout the state in terms of their scope (112 colleges and their related facilities) and emphasis on employment training. As a result, the Budget proposes to allocate all Proposition 39, the California Clean Energy Jobs Act, funding to schools and community colleges (see the K Thru 12 Education Chapter for further details on Proposition 39). Community colleges can use the funds to expand career technical educational training and on-the-job work experience training in partnership with the California Conservation Corps and participating community conservation corps programs.

- Deferrals—At the beginning of 2011-12, the state had accumulated $961 million of deferral debt owed to community colleges. The state successfully reduced the deferral balance to $801 million in 2012-13 and the Budget will reduce that balance to $622 million through an increase of $179 million Proposition 98 General Fund in 2013-14. This funding is consistent with, and proportional to, the payment of deferred funding in K-12 education. The increase will reduce the substantial borrowing costs borne by the community colleges as a result of funding deferrals. Every dollar that colleges must now spend on borrowing is a dollar taken out of the classroom.

- Apportionments—An increase of $196.9 million Proposition 98 General Fund to base apportionments. This represents a 3.6-percent increase to general purpose community college funding.
- Property Tax Adjustment—An increase of $133.2 million Proposition 98 General Fund in 2013-14 to reflect reduced property tax estimates. Current law intends that property taxes offset Proposition 98 General Fund costs for community college apportionments. Because property taxes are estimated to decline, General Fund costs are increased by a like amount. Additionally, the Budget includes an increase of $47.8 million Proposition 98 General Fund for 2012-13 to offset lower-than-anticipated property tax revenues from the elimination of redevelopment agencies.
- Student Fee Adjustment—A decrease of $12.6 million Proposition 98 General Fund to reflect revised estimates of student fee revenue, primarily resulting from lower-than-anticipated Board of Governors' fee waivers. Similar to property taxes, student fees are intended to offset the costs of apportionments.

Hastings College of the Law

Affiliated with the University of California, the Hastings College of the Law is the oldest and one of the largest public law schools in the West, providing instruction annually to approximately 1,100 students.

Significant Adjustments:

- General Fund Increase—An ongoing increase of $392,000 General Fund for core instructional costs. This funding will mitigate the need for Hastings to increase student tuition and fees and can be used by the college to meet its most pressing needs.
- Debt Service Costs—Currently, the state separately funds general obligation debt service for Hastings. The Budget proposes to shift these appropriations into

Hastings' budget, which will require the college to factor these costs into its overall fiscal outlook and decision-making process.

California Student Aid Commission

The California Student Aid Commission administers state financial aid to students attending all institutions of public and private postsecondary education through a variety of programs including the Cal Grant High School and Community College Transfer Entitlement programs, the Competitive Cal Grant program, and the Assumption Program of Loans for Education. Over 99,000 students received new Cal Grant awards, and over 150,000 students received renewal awards in 2011-12. These programs are a key way in which the state supports the public higher education infrastructure and does so to make college more affordable to the state's lower-income students.

Prior to 2001, the program offered a capped number of awards to students and award amounts were specified in the Budget. The program is now an entitlement and has been one of the fastest growing programs in the Budget. Costs for the program have increased dramatically due to an increased number of students participating in the program and UC and CSU tuition and fee increases in recent years. Over an eight-year period, participation in the program and costs have increased by 79,000 students and $915 million, from 177,000 students and $688 million in 2004-05 to an estimated 288,000 students and $1.7 billion in 2013-14. Absent tuition and fee increases at UC and CSU, the rate of growth in the program is expected to slow somewhat in future years.

The Cal Grant program is one of the most generous entitlement financial aid programs in the country. Only New York, Pennsylvania, Illinois, and Texas have need-based student financial aid programs comparable in size to California.

Significant Adjustments:

- Offset Cal Grant Costs with Federal Temporary Assistance for Needy Families (TANF) Reimbursements—A decrease of $139.2 million General Fund in 2013-14 to reflect increased TANF funds available through an interagency agreement with the Department of Social Services. This adjustment will bring the total TANF funds expended on the Cal Grant program to $942.9 million in 2013-14.
- Cal Grant Program Growth—An increase of $61 million General Fund in 2012-13 and $161.1 million General Fund in 2013-14 to reflect increased participation in the

Cal Grant program. Of the 2013-14 amount, $19.5 million is attributable to the first year of implementation of the California Dream Act.

- Offset of Cal Grant Program Costs with Student Loan Operating Fund—An increase of $60 million Student Loan Operating Fund and an offsetting decrease of $60 million General Fund to support Cal Grant program costs.

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