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to the  
Governor's Commission on Educational Quality

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You have asked that I provide the Commission with a brief history of categorical funding in California. I have been asked to address three issues:

First, to provide you with a conceptual framework for reviewing categorical funding as it relates to the total of school funding;

Second, to provide a historical perspective as to why categorical funding has been used as one form of state revenue allocations; and,

Third, to try and link the laws and allocations of today back to their historical roots.

The Conceptual Framework

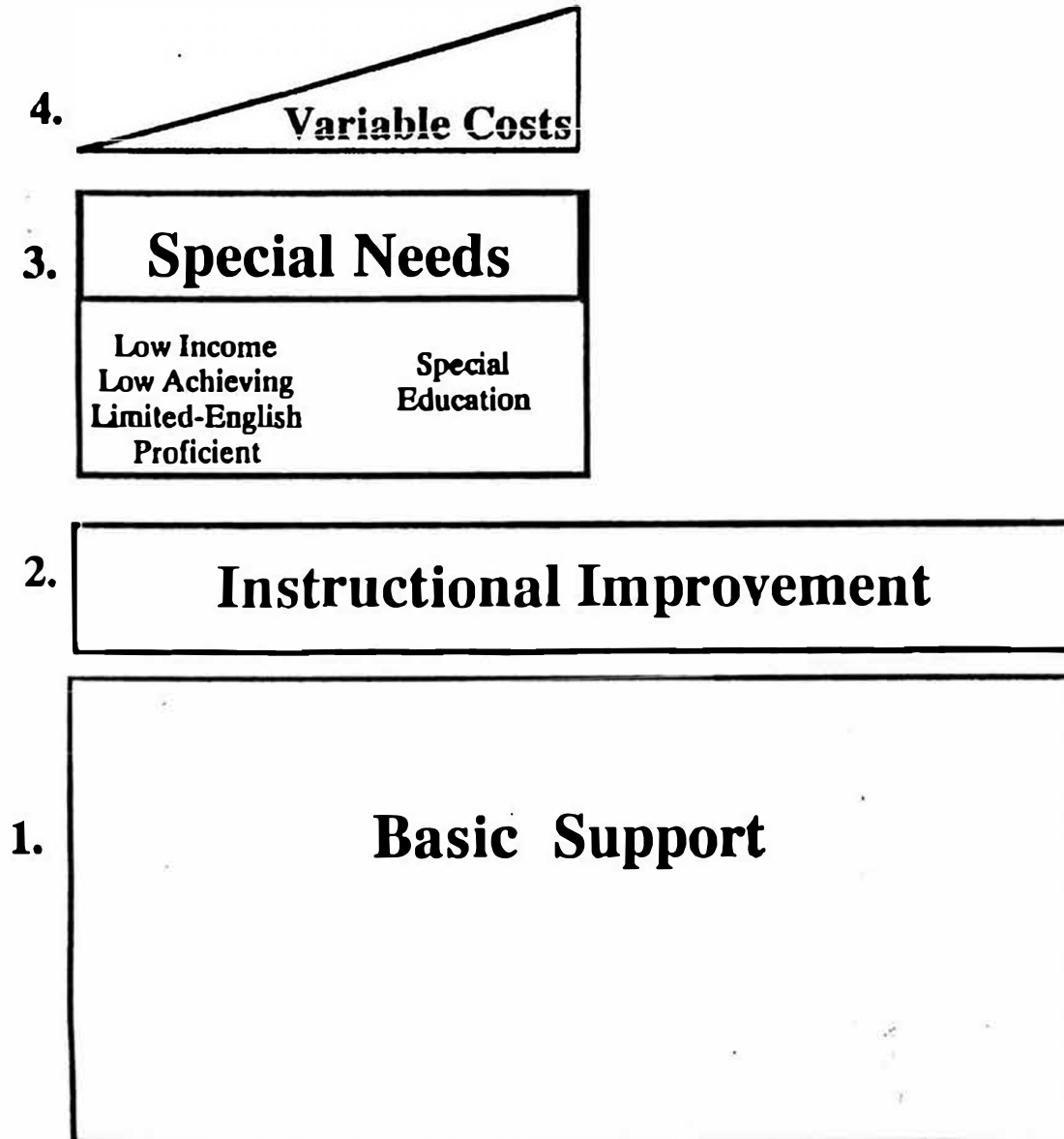
Categorical funding is really nothing more than constraints placed by the funding governing body upon the funded governing body. Categorical funding was created for a variety of different reasons, but in essence, these are created to ensure that the funds which are allocated for specified purposes are spent on those purposes.

In order to understand the history of categorical funding it will help if we take a conceptual look at all of the types of revenue allocations to schools used by the state and federal government. Like the blind men experiencing the elephant, when we only grasp a part of the beast, our limited knowledge can lead to misunderstanding the animal.

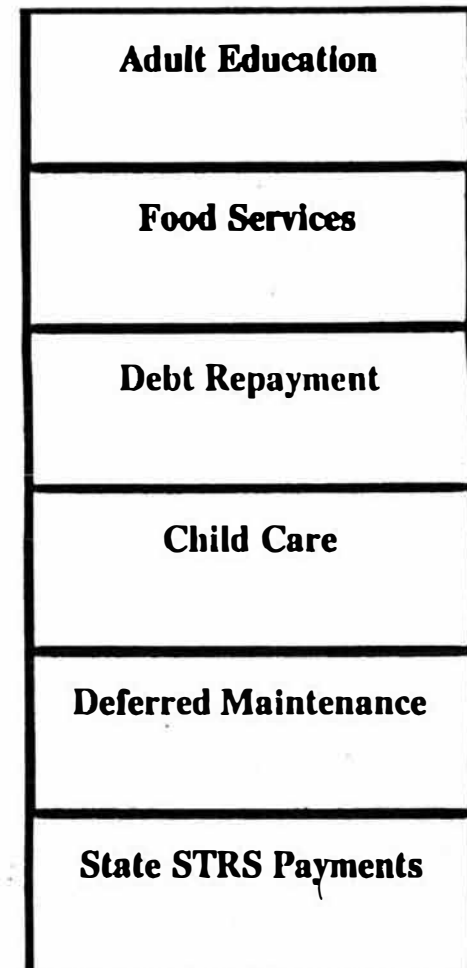
With a little force-fitting, the multitude of school finance mechanisms can be reasonably divided into five different types of revenue allocations. Four of the five are generally called categorical.

- These are:
1. Basic Support Revenues
  2. Categorical Instructional Improvement Revenues
  3. Special Needs Revenues
  4. Variable Cost Revenues
  5. Auxiliary Activity Revenues

# School District Resources



## 5. Auxiliary Activities of School Districts



[Page 2 provides a visual display of this division.

1) Basic Support Revenues: These are funds allocated to school districts to provide a typical educational program for the typical student in a typical school. They are often referred to as "general aid." Most of the basic support revenues are provided to districts through revenue limits. There is no particular magic regarding this funding. It has been derived over time based upon historical practices in local school districts. During the 1960's and 1970's several models were developed, but not used, to determine just how much money per student should be allocated for basic support revenues. Each year we have substantial arguments regarding just how much this should grow, whether each type of district is funded properly and whether this resource allocation system has been sufficiently "Serranoized."

2) Instructional Improvement Revenues: These are funds allocated to provide school and district activities to enhance activities for all students in a school or instructional area. Such funds may be spent on any student for additional services, but they must purchase more services -- they may not be used to cover increased costs of current services. Such allocations include school improvement funding, educational technology, staff development, and other instructional improvement efforts.

3) Special Need Revenues: These are funds allocated to districts and schools for the express purpose of providing more services to students and schools with defined needs. They are to supplement the basic program of the schools and to assist identified students in meeting basic educational goals. Such allocations include Special Education Funding, Economic Impact Aid, Gifted and Talented Education, demonstration programs in reading and mathematics, Miller-Unruh Reading, vocational education and Indian Education Programs. It is important to note that two major activities -- Special Education and services to limited-English proficient pupils -- are known as service mandates. That is, districts must, by state law, federal law, or court mandates, provide services to identified pupils. While state and federal resources are available to assist districts, the lack of revenues does not eliminate the requirement for services.

4. Variable Cost Revenues: These are funds allocated to districts because of real or estimated costs not controllable by the district which occur at a level that is higher than other districts. They include such revenues as desegregation funding, transportation funding, Urban Impact Aid, Small District Transportation Aid, and Meade Aid.

5. Auxiliary Activities Revenues: These are funds allocated to districts which are used for a variety of purposes that may be related to K-12 education but are generally auxiliary to the direct classroom instructional function. They include Adult Education, Food Services, debt repayment, child care, deferred maintenance and state obligations to fund the State Teachers' Retirement System. These types of allocations cause considerable confusion among districts, educators and taxpayers. This is because such activities in general do not provide revenues for the K-12 instructional program.

However, when they are increased, the public is led to believe that schools have increased revenues. It is interesting to note that every time school lunch prices are increased by a dime, school revenues are shown to have increased by some \$40 million. It's never noted that these millions of dimes must actually be spent upon providing lunches, not for additional instructional services.

This five-part model of school revenues may assist you in trying to understand the reasons behind the creation and use of categorical funding.

The questions regarding school finance are not very difficult. The first question is: Just how much do we want to spend on our children in the public schools? By any measure we now spend less than most other states.

Once we decide how much we want to spend on our children, we can ask what areas of revenue needs have the highest priority for our dollars. Within the five types of revenue allocation, each has merit, and so each allocation depends upon the underlying philosophy as well as an assessment of how the revenue needs of schools stack up next to existing resources.

Each person's answer is also strongly influenced by his or her beliefs as to where resources are needed and who should make decisions regarding their allocation.

#### A Historical Perspective

Each of the many categorical funding allocations presently existing in California (and for that matter in Washington D.C.), were created because some individual or group felt that schools would serve students better if more or less money was spent on a particular category. A review of the history of categorical funding indicates that California has actively intervened in the education of its children for a long time. Categorical funding allocations and state service mandates have been the primary means of intervening. A review of the history also finds that all reform movements began by trying to consolidate categoricals and ended up creating new categories as the reformers try to mold schools to fit the reform trends.

I will begin this brief historical prospective in the early 1960's, although the history of categoricals goes back to the Land Grant Colleges, federal set-asides of land for public schools, and the Smith/Hughes Vocation Education Act of 1917.

In the early 1960's, state intervention was concentrated in three areas.

For basic support, the state provided incentives for school district reorganization. Under instructional improvement, class size was reduced, the first state-wide testing program was created, and the Farr-Quimby Educational Television Act was adopted to move new technology into the classroom. For special needs revenues, the state continued an earlier trend by establishing a multitude of new categories of services to physically and mentally handicapped students.

The state also created the first state funded preschool program, and the McAteer State Compensatory Education Act was the state's first effort to assist low income and low achieving students. Remnants of these efforts exist today. A major new credentialing law (The Fisher Act) was also passed.

Parallel efforts by the federal government also began in the 1960s. In 1965, Congress passed far-reaching legislation for major federal funding of education. The Elementary and Secondary Education Act of 1965 created new federal interventions on a categorical basis. The major thrust of the effort was to provide new emphasis and revenue for low income and low achieving students. While it is not my task to trace the federal funding history, it is important to realize that much of the criticism of categoricals relates to federal issues not directly resolvable by the state of California.

By 1966, the host of state and federal categorical programs in place was staggering, and the first attempts to consolidate these efforts began. 1968 saw a fundamental move away from state control with the passage of SB 1, the so-called "magna carta" of local control. This legislation eliminated the then-existing specific directions in the education code as to the number of minutes each district must spend on each subject each week. In addition, the earlier state testing program created under the Miller-Unruh Reading Act was scrapped in favor of a movement towards a new state testing program. In effect, the legislature said we won't tell you how to educate students but we want to know the results of your efforts.

In 1969, the legislature passed two more major bills reflecting the concern over the legions of categorical aid programs. First, they passed AB 606 which required the Legislative Analyst to perform a major cost effectiveness study of state categorical programs. The second measure was Assembly Concurrent Resolution 127, which directed the Department of Education to consolidate the multitude of applications for state and federal categorical funding into one application. The legislature, by a nearly unanimous vote, had fired the first shot in the war against the complicated system of categorical funding. Some 20 years later, it is curious to note that the major application form used by school districts for state and federal aid is named the A-127 after this initial legislative direction.

The early 1970's saw a major new emphasis on state intervention in school revenue allocations for four important reasons. First, a new Superintendent of Public Instruction was elected on a reformist platform. Second, the Supreme Court ruled that the fundamental underpinnings of the school finance system were unconstitutional. Third, then-Governor Ronald Reagan vowed to cut property taxes for California citizens. And fourth, there was a very activist legislature.

In the brief four-year period from 1971 through 1974 state intervention and reform increased at a stunning pace. Schools and school districts were hard-pressed to keep up with the changes made during this period.

\* New basic revenue structures were enacted which placed total state control over basic revenues through revenue limits.

- \* A new state textbook law allowing more flexibility and choice in selecting books was enacted.
- \* The California Assessment Program (CAP) was created to test school achievement in grades 1, 2, 3, 6 and 12.
- \* The Ryan Act changed the way teachers were credentialed in the state.
- \* A new state teacher tenure law was enacted, which required not only semi-annual evaluations of all certificated personnel, but also that each district establish standards of pupil performance in every area of study.
- \* New consolidated school-level planning for use of categorical revenues was enacted to carry out the intent of ACR 127.
- \* There were major increases in categorical funding for low income, low achieving and limited-English proficient pupils.

The first bilingual education act became law

- \* Over 20 separate programs for physically and mentally handicapped students were eliminated and combined under the Special Education Master Plan.
- \* Numerous separate state advisory bodies were consolidated into four major commissions.

While such reformist and state interventions may have had exceptional merit, it is a wonder that schools and districts did not fall under the weight of these changes. Whenever you're inclined to believe that schools do not change, remember that they responded to these and other interventions.

The major categorical funding issues of the early 1970's reflected three separate concerns.

First, the implementation of the Serrano decision meant that most urban districts had their revenues reduced relative to suburban school districts. Because the majority of low income students went to school in school districts that were deemed "high wealth," the legislature and the governor decided to create and expand special funding to such districts to mitigate the effects of Serrano implementation. Thus, the Educationally Disadvantaged Youth Program (EDY) was made a part of SB 90, the bill that reduced property taxes and took the first major steps towards equalizing revenues per school district.

The United States Supreme Court ruled that students who do not speak English must be offered differentiated services. California had a large and growing number of limited-English-proficient students. Such services cost money. Thus, the educationally disadvantaged youth program dollars were targeted at districts with such students.

Second, the issue of school and district level instructional planning and consolidation of categorical resources were high on the reform agenda. Thus, the Early Childhood Education Act and its successor, the School Improvement Program, were to be the vehicles for providing new instructional services and planning. The Special Education Master Plan was the other major attempt to consolidate services into a single service delivery system with local planning as a major focus.

The third issue of the early 1970's , instructional materials reform, was an outgrowth of a governmental efficiency issue. The Constitution of the state of California contains few direct mandates for educational policy. However, one mandate requires that the state Board of Education adopt textbooks for use in grades 1 through 8, and that such books be provided free of charge to all such pupils. Prior to 1972, the state adopted a single book for each subject in each grade level. The state printed the books and sent them to each district. Studies determined that (1) such books were not being used by local districts; (2) that such books did not provide a diverse approach to learning; and, (3) the system of adoption just did not work.

Textbook reform provided that the state would adopt from five to 15 books per subject per grade level and that each district would be allocated a specified dollar amount per student to purchase such books. Districts would have more choice, but the Constitutional mandate would be met by a separate instructional materials fund for each district.

Thus, the early 1970's saw the beginnings of a build up of instructional improvement by school and district planning and consolidation. It was also the beginning of a major state effort to provide differential resources to schools and districts with high concentrations of low-income, low-achieving and limited-English proficient pupils and the beginning of major service mandates for handicapped pupils and pupils who did not speak English.

The period 1975 through 1980 saw the continuation of this early movement. However, a new dimension was added, and with it a new rationale for categorical efforts. A law requiring collective bargaining for school employees was passed. Some believed that if the schools simply received more general aid funding, it would go to increase the costs of current services rather than providing new services for students. Thus categorical funding, which required adding more services, took on a new meaning. In addition, the second Serrano decision specified that much greater efforts to provide equalized revenue were required, except where the legislature defined a special need. Urban districts, rural districts with high costs, and other districts which would be negatively affected by equalization efforts, sought additional categorical funding.

In 1976, the Legislature mandated that local districts must offer special services, including bilingual education, to each child who was identified as having insufficient skills in the English language. This mandate, along with emerging mandates from the federal government for services to mentally and physically handicapped students, was to dominate the categorical educational agenda for the next decade.

In 1977, the legislature passed AB 65, culminating a decade of reform and restructuring of school funding in California. AB 65 combined early childhood education and other instructional improvement efforts into a concept of school improvement for all grades thus expanding legislative efforts for instructional improvement. AB 65 consolidated four special need categorical funding allocation systems into what is known as Economic Impact Aid, thereby broadening the number of districts served and giving greater flexibility to local districts to allocate such funds to schools in need. It provided several new mechanisms to equalize funding, and it created two variable cost allocations to allow for the fact that some districts had higher costs for services than others. These were Urban Impact Aid and a general differential cost system. The latter provision was the only part of AB 65 vetoed by Governor Jerry Brown. Less than eight months after the passage of AB 65, the people of California made the effort moot by the passage of Proposition 13 and the issues resolved through AB 65 were back on the drawing board.

After the passage of Proposition 13, the legislature attempted to save as much as possible of the provisions of AB 65. But with reduced revenues, major cuts were made in all categorical programs as well as local district revenues. Once again, the best laid plans of consolidators and reformers were thwarted by fiscal conditions, and the school funding system was destabilized.

In 1979, the legislature began anew with the provisions of AB 8. AB 8 made permanent the basic thrust of the legislation implementing Proposition 13, enacted in 1978. In addition, it created a new general aid categorical program -- Small District Transportation Aid. The program was funded to provide extra revenues to small (fewer than 2,500 pupils) districts with high transportation costs. Politically, it was the rural version of the variable cost allocation made to urban districts as Urban Impact Aid.

AB 8 also contained the process for sunseting nearly all categorical programs. In essence, the sunset law calls for the review of a multitude of categorical aid programs. If, after the review, the legislature and the governor don't reauthorize the programs, the funds still flow to districts to be used for the same purposes, but the statutes and regulations affecting the programs are eliminated.

So in 1979 we created one new categorical and put most others on notice that they could be terminated.

In 1980, the legislature passed AB 777, which expanded funding for some programs. Of more importance, however, are the AB 777 waiver provisions. These provisions provide more flexibility to local school districts than any law ever passed before in California. This law allows local districts, with some exceptions, to seek from the State Board of Education waivers of any section of the education code which the district believes inhibits its ability to meet the needs of its pupils.



In addition, AB 777 provided direct statutory authority to merge most major categorical funding at multi-funded schools. Thus, the legislature addressed the categorical issue by creating broad new authority for local districts to manage their resources more effectively. Interestingly, although a large number of districts seek to waive provisions of the education code, very few have used the school-based consolidation of resources authority allowed for in AB 777. AB 777 also redefined the sunset provisions of AB 8 and realigned the dates of the proposed sunsets on each program.

From 1980 until 1983 the California public schools were under exceptional financial pressure. The only legislative action on funding consisted of freezing it, and local district spent these years trying to cope with dismal funding levels.

In 1983 the next wave of categorical funding began. Once again we had similar conditions to those which existed in 1971. A governor committed to holding the line on taxes, an activist legislature, and a new state Superintendent of Public Instruction committed to "reform."

SB 813, the Hughes/Hart Educational Reform Act, began this new reform effort.

The major difference between SB 813 and the reforms of previous decades was that its major categorical interventions were not based upon special needs of pupils. That is, the legislature and the governor used instructional improvement categoricals rather than special need categoricals to carry out its policies.

While many new categories were created, none of them directed special services to handicapped low-income, low-achieving or limited-English speaking students.

SB 813 did provide an 8% cost of living increase to the basic programs and a smaller cost of living adjustment to all existing categorical funds. Its new categorical provisions included:

- incentives for longer school days and school years
- incentives to increase beginning teacher salaries
- a new categorical funding for educational technology
- increased categorical funding for textbooks
- creation of categorical funding for a mentor teacher program
- expansion of school improvement at the elementary level
- expansion of authority and flexibility to consolidate existing categorical funding
- funding of summer school for up to 5% of pupils

expansion of Urban Impact Aid to non-unified school districts

- codification and expansion of funding for teacher education and computer centers

In addition, the state created several new service mandates to local school districts in the area of curriculum. These included minimum coursework for high school graduation, review of curriculum standards, training for school administrators and major changes in teacher tenure provisions.

The law had many other provisions including an additional change in the schedule for programs covered under the AB 8 sunset law.

In a sense, then, the legislature turned away from special need categoricals funding, continued to use instructional improvement categorical funding, and added incentive funding to move local schools in the direction legislators deemed appropriate. The curriculum flexibility granted by SB 1 in 1968 was terminated by 1983's SB 813. With this law, the state moved into curriculum and day-to-day local school decision-making with gusto.

This commission's review of categorical aid begins with this history. There are many reasons for the existence of categorical funding, and some of these are very good reasons. Special need revenues were made categoricals because careful reviews of expenditure patterns showed that it costs more to educate low income and non-English-speaking students and that costs are higher to provide educational services to handicapped students. Such students are not found equally in all schools and districts.

Variable cost allocations were created because it was determined that some districts have non-avoidable costs which are far higher than those of other districts. Instructional improvement categoricals were created to ensure that state policies on planning and accountability conformed to the wishes of state policy makers. Auxiliary activities were created because it was believed that K-12 public school districts have functions beyond educating elementary and secondary students.

History seemed to suggest that categorical intervention has been a major tool of state decision makers.

Your task is to take the best intentions of these efforts and make them work better for children.

I hope that this cursory review will assist you in your task