CALIFORNIA STUDENT AID COMMISSION[SM]

CSAC Responses to the Legislative Analyst

Analysis of the 2004-05 Budget Bill

March 2004

March 19, 2004

The Honorable Wesley Chesbro, Chair, Senate Budget and Fiscal Review Committee
The Honorable Darrell Steinberg, Chair, Assembly Budget Committee
The Honorable Dede Alpert, Chair, Senate Appropriations Committee
The Honorable Judy Chu, Chair, Assembly Appropriations Committee
Budget Committee Vice Chairs
Members of the Senate and Assembly Budget Subcommittees

Dear Members:

On behalf of the California Student Aid Commission (Commission), I would like to take this opportunity to thank you for the thoughtful consideration that is given to higher education funding issues, generally, and for the Legislature's past and current support of the Commission's budget and the Cal Grant programs. As you know, the Commission's mission is to *make education beyond high school financially accessible to all Californians*.

The following information has been prepared by the Commission in response to several issues related to the Commission's budget and programs that were raised by the Legislative Analyst in the *Analysis of the 2004-05 Budget Bill*. Our responses are designed to assist you, your colleagues and your staff in making decisions on the 2004-05 Budget.

In September 2000, the State took the historic step of enacting SB 1644 (Chapter 403, Statues of 2000), vastly improving the opportunities available to California students pursuing a higher education. Through the creation of the Cal Grant Entitlement and Competitive Programs, the state reaffirmed its historic commitment to provide educational opportunity for students pursuing a higher education by ensuring both student access and choice for students with financial need and who meet academic criteria. With your help, over the past three years, we have been able to provide over 240,000 Cal Grant awards to financially needy students under the new Entitlement and Competitive programs (as of December 2003).

While we may differ with some of the Legislative Analyst's specific recommendations, the Commission agrees with the Analyst's view that the integrity of the Cal Grant program should be preserved during this challenging fiscal and economic environment. Furthermore, we believe the Governor and the Legislature should continue to support the long-term policy outlined in SB 1644 and its commitment to California's financially needy students, and their families, to put a higher education within their reach. Doing so will ensure that all Californians have an opportunity to be productive participants in the workforce needed to fuel California's economic recovery.

Thank you in advance for reviewing this document and giving us an opportunity to share our perspective with you. Should you have any questions regarding any of the information presented in this document, please feel free to contact me at (916) 526-8271.

Sincerely,

Diana Fuentes-Michel

Diana Fuentes-Michel
Executive Director

cc: Ms. Elizabeth G. Hill, Legislative Analyst
Ms. Donna Arduin, Director, Department of Finance
Commissioners

The California Student Aid Commission Response to the
Analysis of the 2004-05 Budget Bill

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Guiding Principles for the 2004-05 Budget Discussions

California statute (Education Code §66021.2) adopted as part of the Ortiz-Pacheco-Poochigian-Vasconcellos Cal Grant Program (SB 1644, Chapter 403, Statutes of 2000) affirms the state's historic commitment to provide educational opportunity to students pursuing a higher education by ensuring both student access and choice for students with financial need and who meet academic criteria.

The California Student Aid Commission (Commission) has a long-standing commitment to increased resources for student financial aid. Therefore, the Commission continues to support the policies adopted by the Ortiz-Pacheco-Poochigian-Vasconcellos Cal Grant Act and opposes any changes which would undermine them. Consequently, the following policy principles are the priorities of the Commission, and the Commission urges the Governor and Legislature to support them:

- **PRESERVE THE CAL GRANT ENTITLEMENT PROGRAM**

  - **Maintain Current Cal Grant Eligibility Requirements**
    - Maintain statutory GPA requirements
    - Maintain statutory income ceiling

  - **Preserve the Value of Award**
    - Continue to cover University of California (UC)/California State University (CSU) systemwide fees – oppose "decoupling"
    - Retain at current levels the award amount for nonpublic postsecondary institutions
    - Support the development of a statutory formula that adjusts the maximum award amount for nonpublic postsecondary institutions and would not be subject to the annual budget process

- **PRESERVE THE COMPETITIVE PROGRAM**

  - **Maintain Current Cal Grant Eligibility Requirements**
    - Maintain statutory GPA requirements
    - Maintain statutory income ceiling

  - **Preserve the Value of Award**
    - Continue to cover UC/CSU systemwide fees – oppose "decoupling"
    - Retain at current levels the award amount for nonpublic postsecondary institutions
    - Support the development of a statutory formula that adjusts the maximum award amount for nonpublic postsecondary institutions and would not be subject to the annual budget process

  - **Maintain, at a minimum, the current number of awards**

Introduction

On February 18, 2004, the Legislative Analyst released its analysis of the Governor's Budget Proposal.

The following analysis was prepared by Commission staff and focuses only on those issues which directly affect the Commission and its programs.

Page E-197 – E-213: Higher Education: Intersegmental – Student Fees

Analyst's Recommendation: *The Analyst recommends an overall policy of moderate fees and moderate aid with reasonable and predictable fee increases. The Analyst asserts that such a policy would help students and families to plan for and save for their children's higher education.*

Commission Comments: The Administration proposes to cap UC and CSU fee increases at 10 percent per year for undergraduate students, and 40 percent for graduate students.

The Commission supports a fee policy that would allow California students to plan for, save for, and achieve a postsecondary education. It is clear that the state's current boom and bust approach to funding higher education and raising student fees is counter-productive. Therefore, if the State finds it necessary to raise fees, the Commission firmly believes that the Governor and the Legislature must also ensure that there is adequate financial aid for low-income and disadvantaged students.

Page E-216 – E-218: Higher Education: Intersegmental – Financial Aid – Projections

Analyst's Recommendation: *The Analyst recommends the Legislature adopt more realistic Cal Grant budget assumptions. The Analyst asserts that, rather than another likely reversion, the Legislature should use "overbudgeted" monies for identified Cal Grant Needs. As a result, the Analyst recommends reducing item 7980-101-0001 by $20 million.*

Commission Analysis: Since the implementation of the Cal Grant Entitlement and Competitive programs, the Commission and Administration have worked together to develop assumptions on: 1) the number of students who would be financially eligible for an Entitlement award, 2) the number of new recipients who would actually receive the award, and 3) the number of continuing recipients who would receive renewal payments. The model for projecting the Cal Grant Entitlement program funding has included assumptions for program growth.

The Commission requests that adequate funding be appropriated for the Cal Grant Program in the annual budget act to avoid a potential deficiency request later when funding may be unavailable. The budget act language reflects this process by requiring immediate reversion of the funds not encumbered by the Commission at the end of the fiscal year. Each spring, the Commission staff revises the funding projections for the Entitlement awards to reflect a more accurate number of new awards offered in the current year. Funding changes are provided to the Administration and reflected in the Governor's Proposed May Revision.

In developing the 2004-05 Cal Grant budget projections, Commission staff had only one completed year of new Entitlement award data (2001-02), one nearly completed year of data (2002-03) and preliminary 2003-04 award data. With limited data, trends cannot be established. Commission staff continued to use the growth model for new Entitlement awards for 2004-05 and used 2002-03 projected data on renewal rates for renewal recipients.

At the time the 2004-05 budget year projections were provided to the Administration, Commission staff were aware of some factors that could potentially affect the number of students attending postsecondary institutions, but did not have any specifics to include in the model. Given the General Fund deficit and the subsequent proposals affecting higher education enrollment and financial aid, the Commission acknowledges that it may be prudent to revise the model to reflect less growth in the number of new Entitlement awards. The Competitive and Entitlement renewal recipient pools would also need to be reviewed to determine whether or not to adjust the assumptions regarding renewal attrition. In revising the Cal Grant projections, special care must be taken in ensuring that the Commission is not in a deficiency situation.

The Commission will have more reliable 2003-04 award data in early May and recommends that final decisions on redirecting any available excess funding in the Cal Grant program to identified Cal Grant needs be made at that time.

Commission Recommendation: Consistent with the Legislative intent in providing access to all academically qualified students with financial need who are pursuing the dream of higher education, the Commission recommends that any available excess funding in the projected budget for the Cal Grant program be redirected to preserve the current Cal Grant eligibility requirements and to maintain the value of the awards.

Page E-218 – E-222: Higher Education: Intersegmental – Financial Aid – Income Ceilings

Analyst's Recommendation: *The Analyst recommends that the Legislature adhere to its existing statutory policy for annually adjusting the income and asset ceilings. Unlike the Governor's proposal, which reduces the number of students eligible for entitlement benefits, the Analyst recommended the Legislature retain the existing entitlement eligibility pool. In the budget year, this would help many middle-income students cover likely increases in student fees and tuition and would prevent some of California's financially neediest students from being denied entitlement benefits.*

Commission Analysis: The Administration recommends saving $11.2 million by reducing the maximum allowable income for Cal Grant recipients by 10 percent. This proposal would result in approximately 4,450 otherwise qualified entitlement students being denied a Cal Grant award and would reduce the eligible pool for the competitive program by 19,000 students.

In accordance with current law (SB 1644, Chapter 403, Statutes of 2000), the Commission approved the 2004-05 Income Ceilings at its November 2003 meeting. The 2004-05 income and asset ceilings were calculated based on the 2003-04 income ceilings plus a 1.26 percent increase, based on the September 2003 estimated increase (the most current information available) in per capita income for 2003 from the Department of Finance (DOF). The following table outlines the Commission's approved 2004-05 income ceilings based on the most recent information available at that time:

2004-2005 INCOME CEILINGS
APPROVED BY THE COMMISSION NOVEMBER 21, 2003

Dependent and independent students with dependents other than a spouse		
Family Size	Cal Grant A, C, T	Cal Grant B
Six or more	$78,100	$42,900
Five	$72,400	$39,700
Four	$67,600	$35,500
Three	$62,200	$31,900
Two	$60,700	$28,300
Independent students		
Family Size	Cal Grant A, C, T	Cal Grant B
Single, no dependents	$24,800	$24,800
Married	$28,300	$28,300

In order to prepare for processing the next award year applications:

1. Commission staff proposed income and asset ceilings for the next award year to the Commission's Grant Advisory Committee (GAC) in October.

2. The Commission took action on the GAC recommended income and asset ceiling changes at its November meeting.

3. Grant Delivery System programs were updated to reflect the approved amounts in order to determine eligibility for the Cal Grant programs.

During the 2004-05 budget preparation process, DOF asked Commission staff to estimate the savings associated with a 10 percent reduction in the income ceilings. Since the Commission had already approved the 2004-05 Income Ceilings, Commission staff used those amounts in calculating the proposed 10 percent reduction. The following table outlines the Governor's proposed 2004-05 income ceilings:

2004-2005 GOVERNOR'S BUDGET
PROPOSED CAL GRANT BUDGET REDUCTIONS

Dependent and independent students with dependents other than a spouse		
Family Size	Cal Grant A & C	Cal Grant B
Six or more	$70,290	$38,610
Five	$65,160	$35,730
Four	$60,840	$31,950
Three	$55,980	$28,710
Two	$54,630	$25,470
Independent students		
Family Size	Cal Grant A & C	Cal Grant B
Single, no dependents	$22,320	$22,320
Married	$25,470	$25,470

Using the 2003-04 entitlement award pool, approximately 4,450 students would be denied Cal Grant awards if this reduction is enacted. The $11.2 million estimated savings included in the Governor's budget is based on these amounts. In addition, the Governor's proposed income ceiling change would reduce the eligible pool for the competitive program by approximately 19,000 students (using the 2003-04 competitive applicant pool). The Governor's proposed income ceiling changes would not affect recipients who received an award issued before 2004-05.

Commission Recommendation: The Commission recommends that the Governor and the Legislature continue to honor the long-term policy set in SB 1644 and maintain the current eligibility criteria. In order to recover from the current economic downturn, California must continue to educate its future workforce to fuel the economic engine that has helped California recover from economic downturns in the past. Denying students choice and access to a postsecondary education will only serve to obstruct California's economic recovery.

Page E-222 – E-223: Higher Education: Intersegmental – Financial Aid – The Private University Cal Grant

Analyst's Recommendation: *The LAO recommends that the Legislature adopt a long-term Cal Grant policy through legislation that would link the private university Cal Grant to the weighted average General Fund subsidy the state provides for financially needy students attending the University of California and the California State University. For 2004-05, this policy actually would result in a slight increase in the private university Cal Grant (raising it to $9,906).*

Commission Analysis: The Administration proposes to reduce the maximum Cal Grant award for students at non-public postsecondary institutions from $9,708 to $5,482 per year, representing a 44 percent decrease in the value of the award. According to the Governor's budget proposal, $5,482 represents the amount of the undergraduate fee after the proposed 10 percent increase for UC in 2004-05. This proposal would not affect awards issued prior to 2004-05.

Reducing Cal Grant maximum award for new students at non-public institutions would affect approximately 9,700 students. While the Commission has no historical data to predict the effect of such a reduction, award recipients who plan to attend non-public institutions may face more limited choices such as borrowing more, attending out-of-state schools or postponing their postsecondary education.

Commission Recommendation: The Governor and the Legislature should continue to support the ideals of access and affordability which have always been central to the Cal Grant program and were reaffirmed in SB 1644. The Commission seeks support from the Governor and Legislature to maintain the maximum Cal Grant award for non-public institutions at no less than its current level of $9,708. Any decrease in the value of the awards will leave many students with financial need unable to fill the gap in education financing.

The Commission believes that a policy framework for setting the maximum private university award needs to be established in statute and should not be subject to the annual budget process. A formula should be developed, and the financial commitment of private sector institutions (as compared with those of public institutions) should be taken into consideration when setting the maximum award amounts.

Page E-226 – E-235: Higher Education: Intersegmental – Financial Aid – The Public University Cal Grant

Analyst's Recommendation: *The Legislature should adhere to existing law and existing budgeting practice and increase the grant to cover the entire systemwide fee. This would send the clear and consistent message that the financially needy students at all three public higher education segments will continue to receive full student fee coverage.*

Commission Analysis: The Administration proposes to "decouple" Cal Grant awards from the systemwide fees at UC and CSU. Otherwise, following current policy would require that Cal Grant awards be increased to cover the undergraduate fee increases proposed for UC and CSU. The Administration estimates that this policy change would avoid approximately $23.6 million in additional General Fund costs in 2004-05.

Decoupling systemwide fees from financial aid will impact the ability of students from low-income backgrounds to afford an education and attend the state's public institutions. In addition, decoupling will only serve to widen the funding gap that already exists for up to 90,000 CSU and UC students who qualify for Cal Grant awards. This gap is exacerbated by the impending fee increases at the UC and CSU as well as proposed reductions to the funding provided for campus-based aid. Additionally, federal student loan limits have not increased for more than a decade. The cumulative impact of this and other proposed cuts will force students and families to use higher cost alternative loans or credit card financing. Many students and families who do not have access to alternative financing will simply decide not to pursue a higher education.

Even prior to the creation of the Cal Grant Entitlement program, the state's long-term statutory policy had been to link the public university Cal Grant with systemwide student fees at UC and CSU. However, students' cost of attendance and actual fees are much higher than what is covered by the maximum Cal Grant award. For example, not since the 1991-92 academic year have Cal Grant awards been used to cover *all* UC/CSU fees including campus-based student fees. Historically, students' educational fees have been viewed as the major fiscal hurdle to attending college. Thus, the state's primary goal has been to cover all systemwide student fees. The Commission's recommendation to maintain the integrity of the public university Cal Grant by linking it to the 2004-05 systemwide fee level therefore is consistent with the state's overall Cal Grant policy.

Commission Recommendation: The Governor and the Legislature should continue to support the access and affordability established under SB 1644 which allows the state's low-income and disadvantaged students to obtain and complete their postsecondary education even in the face of increasing fees. Any decrease in the value of the awards will leave many students with financial need unable to fill the gap in education financing.

Page E-270 – E-271: Higher Education: Student Aid Commission – Retain existing APLE Priorities

Analyst's Recommendation: *The Analyst recommends that the Legislature retain the existing eligibility criteria for the Assumption Program of Loans for Education (APLE), and give highest priority for new warrants to those individuals teaching in a critical subject shortage area in a very low-performing school.*

Commission Analysis: The APLE is a competitive teacher incentive program designed to encourage outstanding students, district interns, and out-of-state teachers to become California teachers in subject areas where a critical teacher shortage has been identified, or in designated schools meeting specific criteria established by the Superintendent of Public Instruction. The APLE program currently assumes loans for participants who agree to teach in a subject shortage area or in a disadvantaged school (defined as low-income, low-performing, or having a high percentage of uncredentialed teachers). Through statute, the State of California has already defined its high priority teaching areas (determined annually by the Superintendent of Public Instruction). As a result, APLE teachers are serving where the State needs them the most.

The Governor proposes to reduce allowable APLE warrants from 7,700 to 3,500 in the current year and the budget year. In addition, the Administration proposes corresponding trailer bill language that changes the existing APLE eligibility criteria. Specifically, the changes would involve eliminating the general disadvantaged-school component and replacing the subject-shortage-area component with specific allowable subject areas (mathematics, science, reading, and instruction for students with visual impairments). Of the individuals teaching in one of these four areas, those working in a school within the bottom two deciles of the API would be given first priority for new warrants.

Over the last eight years, the State incorporated changes to the APLE program that tightened the eligibility criteria and teaching service requirements. Since then, the program has grown from 400 new participants per year to 7,700 new participants annually. The program is extremely cost-effective; the State incurs very minor initial costs prior to a participant actually providing required teaching service. Moreover, participants who do not complete their postsecondary education and/or do not provide the required teaching service in a California public school are not eligible to receive student loan assumption benefits.

At what may be its near-peak level of student participation, the approximately 12,000 APLE participants who are teaching in California public schools during the 2003-04 academic year will receive up to $34 million in student loan assumption program benefits in 2004-05. Of these APLE participants, about 900 of the participants are teaching mathematics; more than 800 are teaching science; and over 1,600 are teaching in Special Education, including 7 who are providing service in the state's school for the blind. Approximately 2,400 of these participants (who could be eligible for their first year of APLE benefits) have agreed to teach in a designated low-income school. The remaining participants are currently expected to teach in disadvantaged schools. A recent APLE participant survey revealed that many APLE participants who never thought about teaching in a disadvantaged school, but did because of APLE, have committed themselves to continue teaching in these schools.

Changing the selection and participation criteria would permit students to perform their service in *high-performing schools* while very few participants would be allowed to serve in the underserved special education classrooms. Furthermore, the demand for Special Education teachers, in all areas, has increased from year to year.

The Commission is aware that the Administration is in the midst of revising its original proposal.

Commission Recommendation: The Commission recommends that the Legislature support the existing statutory eligibility criteria and standards.

Page E-271 – E-274: Higher Education: Student Aid Commission – The EDFUND Surplus

Analyst's Recommendation*:* *The Analyst recommends the Legislature use a portion of EDFUND's Student Loan Operating Fund (Loan Operating Fund) to relieve the General Fund of a current obligation. Specifically, the Analyst recommends the Legislature designate $66 million in monies from the Loan Operating Fund for financial aid administration at the University of California and the California State University - reducing General Fund support by a like amount. The Analyst recommends reviewing the condition of the Loan Operating Fund annually to determine the viability of future swaps.*

Commission Analysis: EDFUND is a nonprofit public benefit corporation that is an auxiliary to the Student Aid Commission. EDFUND administers the Federal Family Education Loan (FFEL) program on behalf of the state. Colleges and universities that are interested in participating in the FFEL program may choose to work with EDFUND or one of several other independent guaranty agencies. Alternatively, colleges and universities may participate in the Federal Direct Student Loan program, in which case their student loans are guaranteed and administered directly by the federal government.

The California Student Aid Commission and EDFUND have achieved strong annual growth in the federal student loan guarantee program in the past five years. The Commission/ EDFUND's loan volume now totals more than $4.42 billion annually. In turn, the Commission and EDFUND have recognized significant growth in the Loan Operating Fund, with the annual operating surplus totaling $104 million in fiscal year 2002-03. EDFUND, however, projects an annual operating surplus of just $30 million for its 2003-04 fiscal year ending September 30, 2004. Overall, the cumulative surplus balance in the Loan Operating Fund was approximately $266 million as of September 30, 2003.

At the direction of the Legislature, revenues from the Loan Operating Fund already provide major public benefits to students and their families, postsecondary institutions and the State of California. The Loan Operating Fund currently is used to pay state costs of approximately $25 million for Commission administrative operations and for the California Student Opportunity and Access Program (Cal-SOAP). In addition, the Commission is devoting from the Loan Operating Fund an additional $25 million to support statewide financial aid outreach functions.

By the end of the current 2003-04 fiscal year, the Loan Operating Fund will have funded the following:

- $12,960,000 for administrative costs of the Commission, including the Cal Grant Program, and policy and oversight of the Federal Family Education Loan (FFEL) program.
- $7,100,000 awarded to campuses and classroom-based academic support programs to reach underrepresented students and inform and instruct them to apply for financial aid. This amount also funds a technology initiative and Fill-Out-the-FAFSA activities.
- $3,000,000 to fund a public awareness/media campaign to educate the public about Cal Grant Entitlement.
- $8,567,000 for Cal-SOAP, which provides local college readiness programs. The local consortia match state funding, further leveraging the state's investment.

At this time, the Commission and EDFUND believe that a major redirection of revenues from the Loan Operating Fund would not only eliminate the Commission's ability to provide public benefits in the very near future, it also would place the continued viability of the Commission and EDFUND in jeopardy.

The Analyst itself issued a cautionary note in recommending that $66 million from the Loan Operating Fund be redirected to fund UC and CSU financial aid offices in fiscal year 2004-05. The Analyst cautioned that the Loan Operating Fund would need to be reviewed annually to determine the viability of any such future uses due to the uncertainty over federal law and policies regarding loan guarantee agency revenue retention and usage. In fact, approximately 40% of EdFund revenues in 2002-03 derived from a voluntary federal revenue-sharing agreement that is subject to annual renewal and is likely to generate less revenue in future years.

Furthermore, it should be noted that the UC and the CSU largely participate in the federal direct student loan program and as a result do not contribute fully to EDFUND's Loan Operating Fund. According to a recent estimate by EDFUND staff, the amount of revenue lost to direct lending in California from 1997-98 to 2002-03 totaled $150.9 million.

Finally, the Commission in February 2004 already has adopted a Capital Utilization Plan (CUP) to designate use of redirected revenue from the Loan Operating Fund. In adopting a CUP, the Commission stated its commitment to ensure college access and affordability, both today and in the future. To that end, the Commission and EDFUND are committed to the following actions:

- To identify ways to fully fund Cal Grants without draining the Loan Operating Fund, thereby ensuring the "integrity" of the Cal Grant Program as recommended by the Analyst;
- To pursue business diversification to generate additional revenue that will be used to help reduce the unmet financial needs of middle- and low-income students via low-cost loans and better loan services, and to provide increased public benefits in the future.

Under the CUP, the Commission has taken a prudent approach to the use of the accumulated Loan Operating Fund to provide optimal educational benefits to students and to further enhance the Commission/ EDFUND's revenue-generating capacity over the long run while maintaining adequate reserves.

Commission Recommendation: The Commission opposes the Analyst's specific recommendation that the Legislature designate $66 million in monies from the Loan Operating Fund for financial aid administration at the UC and the CSU.

The Commission, however, recognizes the magnitude of the General Fund budget deficit and that the Loan Operating Fund may be utilized to help bring temporary relief. In that regard, the Commission recommends that any revenue that may be redirected from the Loan Operating Fund in fiscal year 2004-05 be limited to non-recurring, one-time expenditures, and that such expenditures be permissible under the Higher Education Act of 1965, as amended. The Commission stands ready to work with the Administration and Legislature to determine these expenditures.

Finally, the Commission recommends that the Commission and EDFUND receive the necessary legislative flexibility to pursue business diversification to generate additional revenues to sustain and increase public benefits to students, postsecondary educational institutions and the State of California.

The Commission makes these recommendations in accordance with its mandate to provide college access and affordability and to ensure that the Commission and EDFUND continue as the self-sustaining guarantor of student opportunity in California. The Commission strongly believes that sustaining and not draining the Loan Operating Fund is critical if the Commission and EDFUND collectively are to serve as the "annuity" for college opportunity in California.