

July 28, 2005

Hon. Bill Lockyer
Attorney General
1300 I Street, 17th Floor
Sacramento, California 95814

Attention: Ms. Tricia Knight
Initiative Coordinator

Dear Attorney General Lockyer:

Pursuant to Elections Code Section 9005, we have reviewed the proposed initiative entitled the "Preschool for All Act" (File No. SA2005RF0088). This measure would establish a constitutional entitlement to statewide voluntary preschool services for all children one year prior to entering kindergarten, hereafter generally referred to as four-year-olds, to be funded by revenues from a new personal income tax explicitly dedicated to this purpose.

BACKGROUND

The state currently provides preschool services for low-income children through its state preschool program, which is administered by the State Department of Education. In 2004-05, a combination of state General Fund (Proposition 98) and federal monies totaling \$207 million funded preschool services for approximately 66,000 four-year-olds. Federal Head Start funds (in 2004-05) totaling \$500 million supported preschool services for 59,000 four-year-olds. Finally, available data suggest that approximately two-thirds of the state's four-year-olds are enrolled in some type of "nursery school," of which slightly less than half of those enrolled are in privately run programs.

PROPOSAL

This initiative, the Preschool for All Act (PFA), includes constitutional and statutory provisions that would generate additional government revenues and expenditures for preschool services. The initiative would create a one-year entitlement to voluntary preschool services for all children born on or after June 6, 2006, and eligible for preschool beginning in the fall of 2010. (While the entitlement begins in the 2010-11 school year, the state could use revenues raised between 2007 and 2010 for early implementation of PFA, with priority given to children residing within the attendance boundary of low performing schools.) These services would be offered free of charge to the participant unless the PFA program experienced a funding emergency, in which case the Legislature could, with a two-thirds vote and the approval of the Governor, institute a parent contribution.

The Superintendent of Public Instruction (SPI) would have overall responsibility for PFA, and the program would be administered at the local level by county offices of education (COEs). However, the initiative would make an allowance for an alternative local administrator to the COE in the case that a countywide voluntary preschool program is already underway by January 1, 2006 and receives public funds of at least \$200 million. A program managed by an alternative local administrator would have all the same responsibilities that would be required of COEs.

A ten-year phase-in period would be provided for the requirements of this initiative. When fully implemented in 2016-17, PFA preschool programs must consist of: (1) a minimum three-hour per day instructional program offered at least 180 days each year; (2) a curriculum based on state preschool learning standards and guidelines, and aligned to the state's academic standards for kindergarten through third grade; and (3) classes of no more than 20 children taught by at least one credentialed teacher and one instructional aide.

Revenue Provisions

The initiative includes provisions that would generate additional income tax revenue and designate it solely for the new preschool program.

Personal Income Tax Provisions. Under current law, the maximum marginal personal income tax rate is 9.3 percent, and it generally applies to individuals with taxable income over \$40,000 and to married couples with taxable income over \$80,000. In addition to this rate, a further 1 percent rate is levied on taxable incomes in excess of \$1 million, with the proceeds used for mental health services. This initiative would impose an additional 1.7 percent tax rate on individuals with taxable income over \$400,000, head of household filers with taxable income over \$544,457, and married couples with taxable income over \$800,000. (The additional 1 percent rate would still apply to taxable incomes in excess of \$1 million.)

Revenue generated by the higher tax rate would be deposited directly in a PFA fund. These revenues would not be considered "proceeds of taxes" under the state's appropriations limit or any other limit on state expenditures, and thus would not be subject to any associated limitations. The tax revenue also would not be considered when calculating the Proposition 98 minimum funding guarantee for K-14 education.

These changes to the revenue statutes would take effect on January 1, 2007, unless the Legislature imposed the same or higher personal income tax rate on the same group of high income earners prior to June 6, 2006. In the event of such legislative action, the taxes specified in this initiative would not take effect until January 1, 2010. (At that time, the 1.7 percent additional rate would go into effect in addition to the tax rates, that were already in effect.) This delay would also commensurately delay the other timeline requirements of the initiative.

Education Expenditure Provisions

Under this initiative, the SPI would have overall authority to administer the program, and would determine the disbursement of PFA funds to COEs, institutions of higher education, and the California Commission on Teacher Credentialing (CTC). The SPI would distribute monies from the PFA fund to support the following activities:

- Program administrative costs at the state and local levels.
- Operation of a preschool program for eligible children.
- Purchase, construction, renovation, and leasing of facilities.
- Training of the preschool workforce, including higher education costs and financial aid.
- Transfers into and maintenance of operations and facilities reserve funds.

The SPI would determine a uniform statewide per-pupil rate for distribution of funds to COEs. In the early years of implementation, funds would be distributed based on the number of four-year-olds in each county. Starting in 2016-17, funds would be distributed based on the number of children actually *enrolled* in PFA programs. Funds would also be allocated to the state public college and university systems based on an evaluation of their funding needs (as further discussed below). Before allocating PFA funds, the SPI would also determine, on an annual basis, the amount of funds to be set aside in state-level PFA operating and facilities reserve funds (also discussed below).

State and County Administration. The SPI and COEs would be authorized to use up to 6 percent of the PFA funds for state and local administration costs. Administrative activities would include: oversight and monitoring; planning and needs assessments; data collection; development of standards, regulations, and guidelines; and development, approval, and processing activities related to the proposed new early learning teaching credential. The SPI and COEs would also have some additional oversight responsibilities, regarding audits, evaluations, and conducting community outreach, among others.

Program Operation Requirements. The COEs would use PFA funds to support the provision of preschool services to eligible children. By July 1, 2007, each county superintendent of schools would be required to submit a five-year implementation plan for PFA to the SPI. While the entitlement for preschool services is established in the constitutional provisions of the initiative, these COE plans would serve as detailed descriptions and guiding documents for how each county would implement the PFA program. Major requirements of the plan would include the provision of:

- ***Access.*** The plans must guarantee each four-year-old child equal access to PFA programs. This includes ensuring preschools are located near students' homes, and ensuring that children with special and/or language needs are accommodated. The COEs must also permit parental choice among PFA schools.

The initiative explicitly states, however, that it would not create an obligation or right to fund or provide transportation.

- **Coordination.** The plans must ensure that PFA programs coordinate with local elementary schools and existing child care programs to maximize the extent to which the needs of families are met, including the need for full-day child care. The initiative stipulates, however, that it would not create an obligation or right to full-day care, and that PFA funds may not be used to subsidize full-day care.
- **Comparable Salaries.** The plan must ensure that full-time preschool teachers and aides who have met the full qualification standards established by the initiative would be compensated similarly to teachers and aides in their county's K-12 public schools. (In order to be considered full-time, teachers and aides must teach two three-hour PFA sessions each day.)
- **Community Outreach.** The plan must propose community outreach activities to ensure that families know about the program and how to access PFA services.
- **Phase-In to Serve Lower-Achieving Areas First.** The COEs that choose to offer PFA programs before the entitlement takes effect in 2010-11 must begin by serving children who live in elementary attendance areas that contain schools where student achievement is ranked in the lowest three deciles (as measured by the most recent California Academic Performance Index).

Once the SPI has approved their plans, COEs would receive PFA monies to fund qualified program providers including COEs, school districts, public higher education institutions, charter schools, and both non- and for-profit providers. Although they would receive funding from the SPI based on a statewide per-pupil rate, the COEs would be required to include in the county's plan a schedule for the distribution of the county's PFA funds to program providers based on a tiered payment system that provides an incentive to providers who make progress toward meeting the statewide quality standards and that takes into account other factors relevant to quality and access.

Facilities. The initiative would provide a maximum of \$2 billion to meet facility needs resulting from an anticipated increase in the number of preschool programs and enrolled children. These funds could be used to support construction, purchase, lease, or renovation of facilities. The SPI would distribute some funding to counties based on the number of four-year-olds in the county, and then would maintain a state facilities reserve to provide additional financial support to counties that demonstrate additional facilities needs.

Preschool Workforce Development. Currently, state preschool teachers are required to hold a permit issued by the CTC, which requires 40 college-level units (including 24 units in early childhood development) or roughly one and one-half years of college full-time. This initiative would require all PFA teachers to have a baccalaureate degree by July 1, 2014. By 2016-17, preschool teachers would also need to hold a new early learning credential to be

developed and issued by CTC, which would likely require an additional year of college beyond a baccalaureate degree.

Currently, there is no existing minimum educational requirement for instructional aides working in state preschools. By July 1, 2014, the initiative would require that aides complete 48 college-level units (approximately two years of full-time schooling), including 24 units in early childhood education.

The initiative would provide up to \$700 million to address the workforce needs expected to result from the training requirements that would be imposed by this measure. Specifically, it provides grants to students and institutions of higher education.

- ***Student Grants.*** Provides up to \$200 million in financial aid (scholarships or forgivable loans) to support full- or part-time students pursuing the additional training required for preschool teachers and aides. Costs would be spread across a maximum ten-year period, beginning in 2007-08. The program would give priority to individuals who: (1) commit to working in geographic areas that have teacher shortages, (2) have worked in the early childhood education field, or (3) have financial need. All students receiving aid would have to commit to working in the PFA program for an amount of time commensurate with the total amount of state assistance they received.
- ***Grants to Institutions of Higher Education.*** The initiative would provide up to \$500 million in PFA funds to be used during the first ten years of the program for workforce development at the post-secondary level. These funds would support grants to public colleges and universities to develop, expand, and provide curriculum and courses in early learning, including a new post-baccalaureate teacher education program in early learning.

Reserves. The measure states that during the first ten years after the effective date of the initiative, the state must establish a PFA operating reserve account. Each year, the SPI would make annual contributions to this account using the revenues generated for the PFA program, with the requirement that by the end of the tenth year, the account must contain funds equal to one year of operating expenses for full implementation of PFA. Subsequently, the SPI would annually determine the amount needed to ensure PFA is self-sustaining, with the goal of maintaining a balance equal to one year's operating expenses. The SPI could access the reserve in any year that the statewide per-student funding level would decline without using the reserve.

Other Provisions

Funding Emergency. If, after accessing the reserve fund, its balance is projected to fall below 10 percent of the average annual operating costs of the program, the initiative would require the SPI to declare a funding emergency. In the case of a funding emergency, the Legislature may enact legislation with a two-thirds vote of each house to institute a parent

contribution for PFA services for a single year. The SPI would then set the level for that contribution.

Interaction With Other Funds. The initiative states that no funds that would be provided by this measure may be used to supplant state child development funds. Thus, the amount the state is now spending for state preschool and child care would need to be maintained. In addition, COEs would be required to demonstrate that PFA funds would not be used to supplant state or federal funding for children with special needs.

Collective Bargaining. The measure provides all PFA employees with the right to representation and collective bargaining.

FISCAL EFFECTS OF THE INITIATIVE

Effects on State Revenues

Increases in Personal Income Taxes for Certain Income Brackets. The increase in personal income taxes on individuals with taxable income over \$400,000, head of household filers with taxable income over \$544,467, and married couples with taxable income over \$800,000 would begin to generate additional revenues starting in 2007. We estimate that revenues for the 2006-07 fiscal year (a one-half-year amount) would be roughly \$800 million. These estimates would increase to about \$2 billion in 2007-08, and then grow with the economy to \$2.4 billion by 2010-11 when the preschool entitlement begins. However, past trends show that the group of income-earners who would pay this additional tax have demonstrated significant year-to-year variability in taxable income. This suggests that the amount of revenue generated for PFA on a year-to-year basis may be somewhat unpredictable. (The initiative would create the aforementioned reserve fund and contains a fiscal emergency clause to address potential revenue volatility.)

No Impact on Revenues that Determine Proposition 98 Guarantee. The required minimum guarantee for Proposition 98 would not be affected by the revenues generated from this initiative because the initiative stipulates that revenues derived from the new tax would not count as proceeds of taxes in the Proposition 98 calculation for K-14 education.

Effects on Expenditures

This measure would develop and implement a new statewide voluntary preschool program resulting in numerous state and local costs—including costs for facilities, funding for higher education to develop a more highly trained and expanded workforce, and for actual PFA services. We estimate that the expenditures needed to meet the requirements of the measure could be fully funded by the revenues generated from the additional tax described above.

Limited-Term Expenditures

The PFA would necessitate expenditures related to the initial preparation and implementation of the act. These start-up costs, which can be considered as short-term and/or one-time, relate primarily to facilities and workforce development needs. As noted above, the initiative would provide a total of up to \$2.7 billion over ten years for these purposes, to be allocated in the following manner:

- \$2 billion for construction, purchase, lease, or renovation of facilities.
- \$500 million for the state's public institutions of higher education to develop and offer coursework in early education.
- \$200 million in financial assistance grants for students seeking to meet the requirements necessary to become PFA teachers and aides.

Ongoing Expenditures

The ongoing costs of implementing PFA would be driven primarily by expenditures related to program administration and instruction. The initiative would provide funding for these activities as follows.

Program Administration. As described previously, the initiative would cap expenditures on state and county administration at 6 percent of the amount distributed from the PFA Fund. The measure does allow for some program support activities, including evaluation and outreach, to be funded with additional monies beyond the 6 percent cap. We anticipate overall administrative and program support expenditures would total approximately \$175 million a year in 2010-11, growing over time in proportion to overall program expenditures.

Instruction and Operations. Most of the PFA funds would be distributed to COEs on a per student basis for operating costs of the program. This funding would support the new preschool program, including costs related to teachers, teacher aides, other classroom support, and special education. Based on participation rates in other states that offer universal preschool, we have assumed that approximately 70 percent of the state's eligible children would choose to enroll in a PFA program once the program is fully implemented.

The program would generate enough funds to provide between \$6,000 and \$8,000 per participating pupil in 2010-11 for instruction and operations. This estimate assumes the aforementioned revenue projections and reflects deductions for limited-term costs, costs of program administration, and required annual contributions to the state PFA reserve fund. It also reflects funding offsets from existing programs, as described below. The estimated per pupil amount is almost double the funding currently provided for state preschool, and approximately 75 percent of the estimated spending for each K-12 student. We anticipate this would be more than sufficient to fund the minimum requirements set forth in this initiative.

Funding Rate Dependent on Potential Cost Offsets. The estimated level of per pupil spending noted above assumes that the PFA program would take advantage of offsets from certain existing state and federal programs. The measure prohibits the state from using PFA funds to supplant funds for special education and childcare, including state preschool. Different interpretations of this language, however, would affect the level of PFA per pupil funding provided.

SUMMARY OF FISCAL EFFECTS

The measure would have the following major fiscal effects:

- Increased personal income taxes on high-income earners beginning in 2007, with revenues reaching approximately \$2.4 billion annually in 2010-11.
- Revenues would support an entitlement to one year of preschool for four-year-olds beginning in 2010-11. Revenues in the early years of the program could be used for facilities, teacher training, student financial aid, and early implementation of preschool services.

Sincerely,

Elizabeth G. Hill
Legislative Analyst

Tom Campbell
Director of Finance