

Senate Budget and Fiscal Review—John Laird, Chair

SUBCOMMITTEE NO. 1

Agenda

Senator Sasha Renée Pérez, Chair

Senator Bob Archuleta

Senator Rosilicie Ochoa Bogh



Thursday, March 12, 2026
9:30 a.m. or Upon Adjournment of Session
1021 O Street, Room 2100

Consultant: Yong Salas and Diego Lopez

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Public Comment

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6100 DEPARTMENT OF EDUCATION

Issue 1: State of Education

Panel.

- Tony Thurmond, California State Superintendent of Public Instruction

Background.

The Superintendent of Public Instruction will provide an update on the state of K-12 education in California. This item is informational only.

Issue 2: Proposition 98 Overview and Structure**Panel.**

- Alex Shoap, Department of Finance
- Ken Kapphahn, Legislative Analyst’s Office

Proposition 98.

California serves approximately 5.8 million public school students in kindergarten through twelfth grades (K-12) and 2.2 million students in community colleges. There are 58 county offices of education, approximately 1,000 local K-12 school districts, nearly 10,000 K-12 schools, and nearly 1,300 charter schools throughout the state. Of the K-12 students, approximately 3.8 million are low-income, English learners, or foster youth students or some combination of those categories. Approximately one million of the K-12 students served in public schools are English learners. There are also 73 community college districts, 116 community college campuses, and 72 educational centers. Proposition 98, which was passed by voters as an amendment to the state Constitution in 1988, and revised in 1990 by Proposition 111, was designed to guarantee a minimum level of funding for public schools and community colleges.

For 2026-27, the proposed budget includes \$125.5 billion in Proposition 98 funding. The Governor’s budget proposes to provide total Proposition 98 funding for 2024-25 of \$123.8 billion. For 2025-26, while the Governor calculates the Proposition 98 Guarantee (Guarantee) to be \$121.4 billion, the budget appropriates \$115.9 billion, creating a “settle-up” amount of \$5.6 billion that will be paid when Proposition 98 is certified for 2025-26. The certification process is described in further detail later on in this agenda. These adjustments are primarily the result of higher than anticipated General Fund revenues than projected at the 2025 final budget act.

Proposition 98 Funding. State funding for K-14 education—primarily K-12 local educational agencies and community colleges—is governed largely by Proposition 98. The measure, as modified by Proposition 111, establishes minimum funding requirements (referred to as the “minimum guarantee”) for K-14 education. General Fund resources, consisting largely of personal income taxes, sales and use taxes, and corporation taxes, are combined with the schools’ share of local property tax revenues to fund the Proposition 98 minimum guarantee. These funds typically represent about 80 percent of statewide funds that K-12 schools receive. Non-Proposition 98 education funds largely consist of revenues from local parcel taxes, other local taxes and fees, federal funds and proceeds from the state lottery. In past years, there have been two statewide initiatives that increased General Fund revenues and therefore, the Proposition 98 minimum guarantee. Proposition 30, passed by the voters in 2012, raised sales and income taxes, but was designed to phase out over seven years. Anticipating the expiration of the Proposition 30 taxes, Proposition 55 was passed by voters in 2016, extending the income tax portion of Proposition 30 through 2030.

The Great Recession that began in 2008 impacted both General Fund resources and property taxes. The amount of property taxes has also been impacted by a large policy change since then—the elimination of redevelopment agencies (RDAs) and the shift of property taxes formerly captured by the RDAs back to school districts. The guarantee was adjusted to account for these additional property taxes, so although Local Educational Agencies (LEAs) received significantly increased property taxes starting in 2012-13, they received a roughly corresponding reduction in General Fund.

The table below summarizes overall Proposition 98 funding for K-12 schools and community colleges in 2007-08, or just prior to the Great Recess, and 2018-19, prior to the COVID-19 pandemic.

**Proposition 98 Calculated Funding
Sources and Distributions
(Dollars in Millions)**

	Pre- Recession 2007-08	Pre- Pandemic 2018-19	Revised 2024-25	Revised 2025-26	Proposed 2026-27
Sources					
General Fund	42,015	54,505	91,197	87,473	89,877
Property taxes	14,563	23,942	32,636	33,9497	35,604
Total	56,577	78,448	123,833	121,420*	125,480
Distribution					
K-12	50,344	69,253	105,859	102,197	111,732
CCC	6,112	9,195	14,129	12,999	14,156
PSSSA	N/A	N/A	3,845	664	-407

* The Governor's Budget proposes the funded level of Proposition 98 to be \$115.9 billion.

Source: Legislative Analyst's Office

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

2 and Test 3, the lower of which is applicable. This applicable test is then compared to Test 1; and the higher of the tests determines the Proposition 98 minimum guarantee. Generally, Test 2 is operative during years when the General Fund is growing quickly and Test 3 is operative when General Fund revenues fall or grow slowly.

The Governor's proposal assumes that in 2024-25, 2025-26, and 2026-27 the Proposition 98 minimum guarantee is calculated under Test 1.

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

The Test 1 percentage is historically-based, but is adjusted, or "rebenched," to account for large policy changes that impact local property taxes for education or changes to the mix of programs funded within Proposition 98. In the past few years, rebenching was done to account for property tax changes, such as accounting for the loss of property taxes due the Los Angeles wildfires, and program changes, such as removing childcare from the Proposition 98 minimum guarantee and expanding transitional kindergarten. For 2025-26, Proposition 98 is rebenched to account for \$1.94 billion for universal transitional kindergarten expansion and \$66.5 million for property tax losses. For 2026-27, the Governor's budget Proposition 98 Test 1 percentage is 39.34 percent.

Suspension of Minimum Guarantee. Proposition 98 includes a provision that allows the Legislature and Governor to suspend the minimum funding requirements and instead provide an alternative level of funding. Such a suspension requires a two-thirds vote of the Legislature and the concurrence of the Governor. To date, the Legislature and Governor have suspended the Proposition 98 minimum guarantee three times; in 2004-05, 2010-11, and 2023-24. While the suspension of Proposition 98 can create General Fund savings during the year in which it is invoked, it also creates obligations in the out-years, as explained below.

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

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

- In a Test 2 year, the rule of thumb is that roughly 55 percent of additional revenues would be devoted to Proposition 98 to pay off the maintenance factor.
- In a Test 1 year, the amount of additional revenues going to Proposition 98 could approach 100 percent or more. This can occur because the required payment would be a combination of the 55 percent (or more) of new revenues, plus the established percentage of the General Fund—roughly 38 percent—that is used to determine the minimum guarantee.

Due to the suspension of Proposition 98 in 2023-24, a maintenance factor obligation of \$8 billion was created. The General Fund revenue conditions in the Governor’s budget requires a maintenance factor payment in 2024-25 of \$7.8 billion, with no payments estimated in 2025-26 or 2026-27. The remaining maintenance factor balance is \$584.6 million at the end of 2026-27.

Proposition 98 Certification. The 2018 budget included a new process for certifying the Proposition 98 guarantee and the 2019 budget made additional changes to this process. Under current statute, certification of the guarantee is a process by which the Department of Finance (DOF), in consultation with the Department of Education and the Chancellor’s Office of the Community Colleges and based on actual data, verifies the factors for the calculation of the Proposition 98 guarantee and the appropriations and expenditures that count towards the guarantee level. Certifying the guarantee results in a finalized guarantee level for the year, as well as finalizing any settle-up owed as a result of changes in the guarantee level. Adjustments will be made to increase the guarantee after the fiscal year is over if the calculation results in an increase in a prior year, but makes no changes in the event of a decrease in a prior year. Prior to this new process, the guarantee was last certified for 2008-09. The most recently certified year is 2023-24.

Proposition 98 Accrual. In 2023, 55 of the 58 California counties were granted a delay for the year 2022 tax filing deadlines from the typical spring deadline to November 16. As a result, without the most recent tax data, the budget overestimated the revenue projections adopted at the June 2023 budget enactment. When actual tax revenue data became available during the 2024-25 budget development, tax revenues fell significantly short for the 2022-23 fiscal year, and the 2022-23 Proposition 98 Minimum Guarantee significantly dropped.

Stakeholders at the time argued that existing law prevents any reduction in appropriations credited for that particular fiscal year when certifying that year for purposes of Proposition 98, even if revenues fall below what was projected, citing Education Code Section 41206.03, which states that when “the state has applied moneys for the support of school districts and community college districts in an amount that exceeds the minimum required pursuant to Section 8 of Article XVI of the California Constitution for the fiscal year being certified, the excess money shall be credited to the fiscal year being certified.”

The 2022-23 Proposition 98 funding level was certified in 2024-25 Budget Act to be \$103.7 billion, which was \$6.2 billion above the state’s revised calculation of the guarantee and served as the basis for future calculations of the Proposition 98 minimum guarantee. However, for accounting purposes, the state will not recognize the \$6.2 billion as a state-level expenditure until 2027-28, and will be counted on the non-Proposition 98 side of the General Fund.

Settle-Up. Every year, the Legislature and the Governor estimate the Proposition 98 minimum guarantee before the final economic, fiscal, and attendance factors for the budget year are known. If the estimate included in the budget for a given year is ultimately lower than the final calculation of the minimum guarantee, Proposition 98 requires the state to make a "settle-up" payment, or series of payments, in order to meet the final guarantee for that year.

The 2025 Budget Act created \$1.9 billion in settle-up in what was then the current year 2024-25, representing the difference between what was originally funded in the 2024 Budget Act and what was calculated for Proposition 98 in the 2025 Budget Act. The Governor's budget proposes to fully appropriate the calculated level of Proposition 98 in 2024-25, representing an increase of \$3.9 billion, the amount of which repays the \$1.9 billion settle-up balance that was created in the 2025 Budget Act.

According to the Department of Finance, due to persistent uncertainty in revenue projections, the Budget proposes to create \$5.6 billion in settle-up in 2025-26. This means that the funded level of the Guarantee in 2025-26 is \$115.9 billion, compared to the calculated amount of \$121.4 billion. This is intended to mitigate the risk of potentially appropriating more resources to the Guarantee than are ultimately available in the final calculation for 2025-26. The final Proposition 98 calculation for 2025-26 will occur during the certification process for this fiscal year in Spring and Summer 2027.

Public School System Stabilization Account (PSSSA). The state's Proposition 98 Rainy Day Fund was established with the passage of Proposition 2 in 2014. The 2026-27 proposed budget requires a mandatory payment of \$3.8 billion into the Proposition 98 Rainy Day Fund in 2024-25 (an increase from the 2025 Budget Act of a payment of \$455 million), with another mandatory payment of \$424.3 million in 2025-26, and a mandatory withdrawal in 2026-27 of \$407.1 million. The budget also proposes a discretionary deposit of \$240 million in 2025-26. At the end of the 2026-27, the budget proposes a balance in the Rainy Day Fund of \$4.1 billion.

Under current law, there is a cap of 10 percent on school district reserves in fiscal years immediately succeeding those in which the balance in the account is equal to or greater than three percent of the total TK-12 share of the Guarantee. The balance of the Proposition 98 Rainy Day Fund during the three-year budget window triggers school district reserve caps in 2025-26 and 2026-27; however, discussions are ongoing to have the school district reserve cap only in effect in 2026-27.

Proposition 98 K-12 Proposals:

TK-12 Local Control Funding Formula. The bulk of funding for school districts and county offices of education for general operations is provided through the Local Control Funding Formula (LCFF) and is distributed based on the number of students served and certain student characteristics. The state fully funded the LCFF in 2018-19 and has annually adjusted the grant amounts by a cost-of-living adjustment (COLA). The Governor's budget proposes an LCFF COLA of 2.41 percent, and when combined with growth adjustments, results in \$2 billion in increased discretionary funds for local educational agencies.

Necessary Small Schools. The Governor’s budget proposes an ongoing increase of \$30.7 million Proposition 98 General Fund to provide a 20 percent increase in LCFF for Necessary Small Schools, which is the funding formula for the smallest schools in the state.

Special Education. The Governor’s budget proposes an increase of \$509 million ongoing Proposition 98 General Fund to increase special education base rates.

Student Support and Discretionary Block Grant. The Governor’s budget proposes a one-time \$2.8 billion Proposition 98 General Fund block grant to address rising costs and declining revenue due to attendance and enrollment decline. These funds are also proposed to support professional development for English Language Arts/English Language Development and Mathematics instruction, teacher recruitment and retention strategies, and career pathways and dual enrollment expansion efforts.

Community Schools. The Governor’s budget proposes \$1 billion ongoing Proposition 98 General Fund to expand the community school model.

Expanded Learning Opportunities Program. The Governor’s budget proposes \$62.4 million ongoing Proposition 98 General Fund to guarantee \$1,800 per pupil for Rate 2 local educational agencies. This brings total program funding of \$4.7 billion Proposition 98 General Fund.

Learning Recovery Emergency Block Grant. The Governor’s budget proposes to augment the Learning Recovery Emergency Block Grant by \$757.3 million one-time Proposition 98 General Fund. This allocation is proposed to be the final allocation of the program.

Teacher Residency. The Governor’s budget proposes \$250 million one-time Proposition 98 General Fund to continue educator residency programs through 2029-30, administered by the Commission on Teacher Credentialing.

Child Nutrition. The Governor’s budget continues to fund universal access to school meals with an ongoing decrease of \$67.9 million Proposition 98 General Fund, to fully fund the universal school meals program and for students who want a meal will have access to two free meals each day. These adjustments reflect a reduction in 2025-26 estimates compared to the 2025 Budget Act projections and an increase in meal reimbursement rates.

Kitchen Infrastructure and Training. The Governor’s budget proposes a one-time \$100 million Proposition 98 General Fund investment for specialized kitchen equipment, infrastructure, and training to support schools in providing more freshly prepared meals made with locally grown ingredients.

Dual Enrollment and Career Pathways. The Governor’s budget proposes \$100 million one-time Proposition 98 General Fund to increase access to college and career pathways for high school students, including expanded access to dual enrollment and dual credit opportunities.

Los Angeles County School Wildfire Recovery. The Governor’s budget proposes one-time \$22.9 million Proposition 98 General Fund to support local educational agencies that are continuing to recover from the January 2025 Los Angeles County wildfires, including \$4 million for Pasadena Unified School District.

Arts and Music in Schools-Funding Guarantee and Accountability Act (Proposition 28). The Governor’s budget includes \$1.06 billion to fund arts and music in schools pursuant to Proposition 28.

Literacy Screener Implementation. The Governor’s budget proposes \$40 million one-time Proposition 98 General Fund in 2026-27 to support the continued implementation of the reading difficulties screener for students.

Fiscal Crisis and Management Assistance Team (FCMAT). The Governor’s budget proposes \$994,000 in ongoing Proposition 98 General Fund to support increased FCMAT workload.

California School Information System (CSIS). The Governor’s budget proposes \$966,000 in additional ongoing Proposition 98 General Fund to support increased CSIS costs.

Cost-of-Living Adjustments. The Governor’s proposed budget provides \$228.2 million ongoing Proposition 98 General Fund to support a 2.41 percent COLA for categorical programs and the LCFF equity multiplier. These programs include special education and child nutrition, State Preschool, Youth in Foster Care, Mandates Block Grant, Adults in Correctional Facilities Program, Charter School Facility Grant Program, American Indian Education Centers, and the American Indian Early Childhood Education Program.

County Offices of Education. The Governor’s budget proposes \$13.3 million additional ongoing Proposition 98 General Fund, for a total of \$131.9 million, for county offices of education to provide universal and targeted support to school districts and charter schools, including those eligible for differentiated assistance. This funding will align with updates to local educational agency assistance and intervention performance criteria that the State Board of Education is required to adopt pursuant to AB 121 (Committee on Budget), Chapter 8, Statutes of 2025. The budget also proposes an ongoing decrease of \$15.6 million Proposition 98 General Fund to reflect ADA changes applicable to county office of education LCFF and a 2.41 percent cost-of-living adjustment.

Home-to-School Transportation. The Governor’s budget proposes \$322 million one-time and \$239.2 million ongoing Proposition 98 General Fund to reflect higher costs in the Home-to-School Transportation program.

K-12 High Speed Network. The Governor’s budget proposes an increase of \$629,000 ongoing Proposition 98 General Fund to support the K-12 High Speed Network program.

Legislative Analyst's Office.

The LAO's recent publication, *The 2026-27 Budget: Proposition 98 Guarantee and K-12 Spending Plan*, included an analysis of the Governor's Proposition 98 Proposals. Below are comments provided by the LAO.

School Funding Requirement Grows, but Underlying Revenue Estimates Are Risky. The state calculates an annual "minimum guarantee" for school and community college funding based upon the formulas established by Proposition 98 (1988). Compared with the June 2025 enacted budget, the Governor's budget estimates the guarantee is up \$3.9 billion (3.2 percent) in 2024-25, \$6.9 billion (6 percent) in 2025-26, and \$10.9 billion (9.5 percent) in 2026-27. These estimates depend on revenue projections that do not account for the current elevated stock market risks. A major downturn could reduce revenues by tens of billions of dollars—reducing the guarantee by about 40 cents for each \$1 of lower revenue.

Recommend an Alternative to the Governor's Proposed Funding Delay. The Governor proposes delaying a \$5.6 billion payment associated with the higher estimate of the 2025-26 guarantee. This delay shifts costs to the future when the state must "settle up" and meet this obligation. We recommend an alternative that would set aside funding to cover the full cost of the guarantee while holding some or all of the additional funding in the Proposition 98 Reserve. This alternative would address the Governor's concern about inadvertently exceeding the guarantee and avoid worsening future budget deficits. It would also require additional solutions for the non-Proposition 98 side of the budget this year.

Governor's School Spending Plan Has Some Prudent Features. After accounting for higher guarantee estimates, delayed payment, and other adjustments, nearly \$9.7 billion is available for new school spending. The Governor's budget allocates \$3.7 billion for ongoing programs and \$5.9 billion for one-time activities. It uses \$4 billion in ongoing funds to pay for the one-time activities. This approach is prudent because it creates a cushion to protect ongoing programs if the guarantee declines in the future. Separate from the new spending proposals, the Governor's budget adds \$4.1 billion to the Proposition 98 Reserve. Most of this amount is required by constitutional formulas, but a small portion reflects a discretionary deposit.

Recommend Adopting Several of the Larger Proposals. The largest ongoing proposal provides \$2.3 billion for a 2.41 percent cost-of-living adjustment (COLA). We recommend funding the final statutory COLA rate unless revenue estimates drop significantly by May. The budget also provides \$1 billion in ongoing funds for community schools, a proposal we plan to analyze in a forthcoming report. Regarding one-time proposals, the Governor proposes \$2.8 billion for a discretionary block grant, \$1.9 billion to eliminate previous payment deferrals, and \$757 million to restore the Learning Recovery Emergency Block Grant. These proposals would help sustain local programs and fund previous commitments, and we recommend adopting them.

Legislature's Core Budget Decisions Revolve Around Risk and Resiliency. As the Legislature reviews the Governor's budget and makes adjustments, we recommend that it plan for scenarios

where the guarantee decreases. In practical terms, this approach means being cautious about new spending commitments, building reserves and other tools to protect existing school programs, and identifying proposals that it would be willing to delay, reduce, or reject if the guarantee were to drop. The Legislature cannot predict the timing or magnitude of the next downturn, but it can use the upcoming hearings to identify actions that would stabilize the budget, shore up programs that benefit students, and preserve its core priorities.

Suggested Questions.

- DOF: How did the Department of Finance determine the Proposition 98 settle-up amount of \$5.6 billion?
- LAO: The LAO recently released its updated revenue projections with its report, *Updated “Big Three” Revenue Outlook*, and identified at least an additional \$6 billion in revenues above the Governor’s budget. How will the additional revenues impact Proposition 98 for the current year (2025-26 fiscal year) and beyond?

Staff Recommendation. Hold open.

Issue 3: Local Control Funding Formula (LCFF)

Panel.

- Katie Lagomarsino, Department of Finance
- Patrick Rochelle, Department of Finance
- Michael Alferes, Legislative Analyst's Office
- Dean Patterson, Department of Education

Background.

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

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

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

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

- **Base Grants** are calculated on a per-student basis (measured by student ADA) according to grade span (K-3, 4-6, 7-8, and 9-12) with adjustments that increase the base rates for

grades K-3 (10.4 percent of base rate) and grades 9-12 (2.6 percent of base rate). The adjustment for grades K-3 is associated with a requirement to reduce class sizes in those grades to no more than 24 students, unless other agreements are collectively bargained at the local level. The adjustment for grades 9-12 recognizes the additional cost of providing career technical education in high schools. For school districts, funded ADA is equal to the greater of current, prior, or the average of the three most recent prior years' ADA.

- **Supplemental Grants** provide an additional 20 percent in base grant funding for the percentage of enrollment that is made up of unduplicated students.
- **Concentration Grants** provide an additional 65 percent above base grant funding for the percentage of unduplicated students that exceed 55 percent of total enrollment.
- **Categorical Program** add-ons for Targeted Instructional Improvement Block Grant and Home-to-School Transportation provide districts the same amount of funding they received for these two programs in 2012-13. The transportation funds must be used for transportation purposes. Charter schools are not eligible for these add-ons.
- **Necessary Small School (NSS) Allowance** provides funding for school districts with qualifying schools that serve a small population of students and are geographically isolated. NSS funding is provided in lieu of LCFF base grant funding. In 2024-25, over \$101.3 million funded approximately 144 necessary small schools across 108 school districts in the state.
- **LCFF Economic Recovery Target** add-on ensured that districts receive, by 2020-21, at least the amount of funding they would have received under the old finance system to restore funding to their 2007-08 level adjusted for inflation. Districts are not eligible for this add-on if their LCFF funding exceeds the 90th percentile of per-pupil funding rates estimated under the old system.
- **Hold Harmless Provision** ensures that no school district or charter school will receive less funding under the LCFF than its 2012-13 funding level under the old system.
- **Transitional Kindergarten Add-On** is equal to the TK Add-on Rate multiplied by the current year TK ADA to meet the lower adult-to-student ratios. For 2025-26, this rate is \$5,545.

Budget Appropriations. The LCFF established new “target” LCFF funding amounts for each LEA, and these amounts are adjusted annually for COLA and pupil counts. When the formula was initially introduced, funding all school districts and charter schools at their target levels was expected to take eight years and cost an additional \$18 billion, with completion by 2020-21. However, Proposition 98 growth exceeded expectations and LCFF was fully funded in the 2018-

19 fiscal year for school districts and charter schools. COEs reached their target funding levels in 2014-15, which adjusts each year for COLAs and ADA growth. With full-funding of the formula, LEAs and stakeholders can see how much funding is received through base, supplemental, and concentration grants on the CDE website and reported through each LEA's local control and accountability plan (LCAP).

The 2022-23 budget included a 6.28 increase to the LCFF base grant, in addition to a 6.56 percent COLA, and smoothed out the year-to-year funded average daily attendance by allowing LEAs to be funded by either their current year, past year, or average of the three prior years' average daily attendance. The 2022-23 budget also provided a "boost" for the funded 2021-22 average daily attendance for LEAs that provided independent study offerings to students. In the 2023-24, 2024-25, and 2025-26 budgets, the COLA was 8.22 percent, 1.07 percent, and 2.3 percent, respectively.

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

Attendance Recovery. The 2024 Budget Act established the Attendance Recovery program, where school districts, county offices of education and classroom-based charter schools can earn additional ADA in classroom-based programs during before or after school, during weekends, or on intersession breaks. Local educational agencies can claim up to 10 days or the number of absences, whatever is lesser, through attendance recovery programs. The first year of implementation for attendance recovery programs is in the 2025-26 school year.

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

Similar to the LCFF formula for school districts and charter schools, COEs were also guaranteed that they would not get less funding than was received in 2012-13. In addition, COEs were held harmless for the amount of state aid (essentially the value of the categorical funding) received in

2012-13. Unlike school districts, for COEs this minimum state aid amount floats above their target, meaning that as local property tax revenue grows in a county over time and funds their LCFF allocation, the minimum state aid allotment for that COE becomes a new bonus in base funding on top of their LCFF level.

Governor’s Budget Proposal.

The proposed budget includes a COLA of 2.41 percent, and combined with growth adjustments, results in an increase of roughly \$2 billion Proposition 98 General Fund for LCFF.

The budget also includes a 20 percent increase in LCFF for necessary small schools, which reflects an ongoing increase of \$30.7 million Proposition 98 General Fund.

Legislative Analyst’s Office.

The Legislative Analyst’s Office recommends funding the final statutory COLA rate unless revenue estimates drop significantly by May.

Necessary Small Schools. The Governor’s budget proposes \$30.7 million ongoing Proposition 98 General Fund to apply a 20 percent increase for necessary small schools—additional funding provided for geographically isolated schools. The Governor’s proposal has some merit given it would target districts that likely face greater cost pressures from operating very small schools in geographically isolated parts of the state. However, the proposed 20 percent increase is not aligned with any particular assessment of cost and results in a significant difference in per-student funding rates between schools above or below the upper thresholds of eligibility. If the Legislature is interested in adopting the proposal, it could consider providing a different level of funding based on its priorities. We also recommend modifying the proposal to avoid large differences in funding above and below the eligibility thresholds.

Suggested Questions.

- CDE/LAO: Are there any preliminary indicators for how local educational agencies are implementing, or contemplating implementation for, attendance recovery programs
- LAO: What should the Legislature consider as possible tradeoffs if the cost-of-living adjustment is increased in LCFF?

Staff Recommendation. Hold open.

Issue 4: Fiscal Health of School Districts**Description.**

The Fiscal Crisis and Management Assistance Team (FCMAT) provides a statewide resource to help monitoring agencies in providing fiscal and management guidance and helps local education agencies (LEAs) - school districts, county offices of education (COEs), and charter schools, as well as community college districts - fulfill their financial and management responsibilities. Lead FCMAT staff will provide a general overview of the fiscal health of school districts.

Panel.

- Mike Fine, Chief Executive Officer, FCMAT
- Megan Reilly, Chief Administrative Officer, FCMAT

Background:

Assembly Bill 1200 (Eastin), Chapter 1213, Statutes of 1991, created an early warning system to help LEAs avoid fiscal crisis, such as bankruptcy or the need for an emergency loan from the state. The measure expanded the role of COEs in monitoring school districts and required that they intervene, under certain circumstances, to ensure districts can meet their financial obligations. The bill was largely in response to the bankruptcy of the Richmond School District, and the fiscal troubles of a few other districts that were seeking emergency loans from the state. The formal review and oversight process requires that the county superintendent approve the budget and monitor the financial status of each school district in its jurisdiction. COEs perform a similar function for charter schools, and the California Department of Education (CDE) oversees the finances of COEs. There are several defined "fiscal crises" that can prompt a COE to intervene in a district: a disapproved budget, a qualified or negative interim report, or recent actions by a district that could lead to not meeting its financial obligations.

Beginning in 2013-14, funding for COE fiscal oversight was consolidated into the Local Control Funding Formula (LCFF) for COEs. COEs are still required to review, examine, and audit district budgets, as well as annually notify districts of qualified or negative budget certifications, however, the state no longer provides a categorical funding source for this purpose.

AB 1200 also created FCMAT, recognizing the need for a statewide resource to help monitoring agencies in providing fiscal and management guidance. FCMAT also helps LEAs fulfill their financial and management responsibilities by providing fiscal advice, management assistance, training, and other related services. FCMAT also includes the California School Information Services (CSIS). LEAs and community colleges can proactively ask for assistance from FCMAT, or the Superintendent of Public Instruction (SPI), the county superintendent of schools, the FCMAT Governing Board, the California Community Colleges Board of Governors or the state

Legislature can assign FCMAT to intervene or provide assistance. Ninety percent of FCMAT's work is a result of an LEA inviting FCMAT to perform proactive, preventive services, or professional development. Ten percent of FCMAT's work is a result of assignments by the state Legislature and oversight agencies to conduct fiscal crisis intervention. The office of the Kern County Superintendent of Schools was selected to administer FCMAT in June 1992.

Interim Financial Status Reports. Current law requires LEAs to file two interim reports annually on their financial status with the CDE. First interim reports are due to the state by December 15 of each fiscal year; second interim reports are due by March 17 each year. Additional time is needed by the CDE to certify these reports.

As a part of these reports, LEAs must certify whether they are able to meet their financial obligations. The certifications are classified as positive, qualified, or negative.

- A positive certification is assigned when an LEA will meet its financial obligations for the current and two subsequent fiscal years.
- A qualified certification is assigned when an LEA may not meet its financial obligations for the current and two subsequent fiscal years.
- A negative certification is assigned when an LEA will be unable to meet their financial obligations in the current year or in the subsequent fiscal years.

AB 1200 states the intent that the legislative budget subcommittees annually conduct a review of each qualifying school district (those that are rated as unlikely to meet their fiscal operations for the current and two subsequent years), as follows: "It is the intent of the Legislature that the legislative budget subcommittees annually conduct a review of each qualifying school district that includes an evaluation of the financial condition of the district, the impact of the recovery plans upon the district's educational program, and the efforts made by the state-appointed administrator to obtain input from the community and the governing board of the district."

First Interim Report. The first interim report has been published by CDE, and eight LEAs (two of which share a joint administration) have negative certifications for the first interim report. For comparison, seven LEAs were identified with negative certifications at this same time last year. These LEAs that have negative certifications will not be able to meet their financial obligations for 2025-26 or 2026-27, based on data generated by LEAs in Fall 2025, prior to release of the Governor's January 2026-27 budget. The first interim report has also identified 45 LEAs with qualified interim report certifications. These LEAs with qualified certifications may not be able to meet their financial obligations for 2025-26, 2026-27, or 2027-28. For comparison, the first interim report in fiscal year 2024-25 identified 32 LEAs with qualified certifications.

Second Interim Report. The second interim report, which covers the period ending January 31, 2026, is due March 17th.

State Emergency Loans. A school district governing board may request an emergency apportionment loan from the state if the board has determined the district has insufficient funds to meet its current fiscal obligations. Existing law states the intent that emergency apportionment

loans be appropriated through legislation, not through the budget. The conditions for accepting loans are specified in statute, depending on the size of the loan. For loans that exceed 200 percent of the district's recommended reserve, the following conditions apply:

- The county superintendent shall assume all the legal rights, duties, and powers of the governing board of the district.
- The county superintendent, with concurrence from both the SPI and the president of the state board of their designee, shall appoint an administrator to act on behalf of the SPI.
- The school district governing board shall be advisory only and report to the state administrator.
- The authority of the county superintendent and state administrator shall continue until certain conditions are met. At that time, the county superintendent, with concurrence from both the SPI and the president of the state board of their designee, shall appoint a trustee to replace the administrator.

For loans equal to or less than 200 percent of the district's recommended reserve, the following conditions apply:

- The county superintendent, with concurrence from the SPI and the president of the state board or their designee, shall appoint a trustee to monitor and review the operation of the district.
- The school district governing board shall retain governing authority, but the trustee shall have the authority to stay and rescind any action of the local district governing board that, in the judgment of the trustee, may affect the financial condition of the district.
- The authority of the county superintendent and the state-appointed trustee shall continue until the loan has been repaid, the district has adequate fiscal systems and controls in place,
- and the SPI has determined that the district's future compliance with the fiscal plan approved for the district is probable.

State Emergency Loan Recipients. Ten school districts have sought emergency loans from the state since 1991. The table below summarizes the amounts of these emergency loans, interest rates on loans, and the status of repayments. Seven of these districts: Coachella Valley Unified, Compton Unified, Emery Unified, West Fresno Elementary, Richmond/West Contra Costa Unified, Vallejo City Unified, and Oakland Unified have paid off their loans. Three districts have continuing state emergency loans: Plumas Unified, South Monterey County Joint Union High (formerly King City Joint Union High), and Inglewood Unified School District. The most recently authorized loan was to Plumas Unified School District in 2025 in the amount of \$20 million from the General Fund, of which \$8.5 million is drawn down. Of the three districts with continuing emergency loans from the state, Inglewood Unified School District and Plumas Unified are the only two districts operating under an administrator. At first interim in 2025-26, Inglewood Unified has a positive certification and Plumas Unified has a negative certification.

Currently Outstanding Emergency Loans to School Districts

District	Tenure of Administrators and Trustees	Amount of State Loan	Interest Rate	Outstanding Balance of I-Bank and General Fund Loans	Amount Paid By District Including Principal & Interest	Pay Off Date
Plumas Unified	Administrator 10/06/25– Present	\$8,500,000 (\$20 million authorized)	6.411%	\$8,500,000 as of 9/01/25	\$0	November 2055 GF
Inglewood Unified	Administrator 10/03/12– Present	\$7,000,000 \$12,000,000 \$10,000,000 = \$29,000,000 (\$55 million authorized)	2.307%	\$16,837,002 as of 07/01/25	\$18,319,840	11/01/34 GF
South Monterey County Joint Union High (formerly King City Joint Union High)	Administrator 07/23/09– 06/30/16 Trustee 07/01/16– Present	\$2,000,000 \$3,000,000 \$8,000,000 = \$13,000,000	2.307%	\$3,727,273 as of 07/01/25	\$15,596,357	October 2028 I-bank

Source: California Department of Education

Suggested Questions.

- Is there a common trend or economic factors among the school districts with a qualified and negatively certified budget?

Staff Recommendation. This item is informational.

6120 CALIFORNIA STATE LIBRARY

Issue 5: Increased Building Rental Expenses for Library and Courts I and II

Panel.

- Mary Halterman, Department of Finance
- Greg Lucas, California State Library
- Florence Bouvet, Legislative Analyst’s Office

Request. The Governor’s budget proposes \$1.1 million General Fund in 2026-27 and ongoing for the State Library to address increased building rental expenses.

Background. According to the Administration, rental charges are fixed, mandatory costs outside of the California State Library’s control. Budget Act of 2022, Chapter 43, Statutes 2022, provided \$2.2 million ongoing General Fund appropriations to address increased costs in building rental expenses for Library and Courts II, but the existing facilities operation appropriations have not kept pace with escalating rent obligations for California State Library’s buildings.

TABLE C – Building Rent Invoice Totals for Library and Courts I and Library and Courts II
(Dollars in thousands)

Building Name	Price Book Category	2022-23	2023-24	2024-25	2025-26 (Projected*)	2026-27 (Projected*)
Library and Courts I	Office Space	\$2,602	\$2,618	\$2,627	\$2,624	\$2,624
Library and Courts I	Storage Area	\$265	\$265	\$265	\$265	\$265
Library and Courts I	Portfolio Management Surcharge	\$19	\$20	\$20	\$20	\$20
Library and Courts I	Central Plant Usage Fee	\$178	\$187	\$187	\$187	\$187
Library and Courts II	Office Space*	\$4,419	\$4,628	\$4,757	\$4,757	\$4,757
Library and Courts II	Portfolio Management Surcharge	\$30	\$31	\$32	\$32	\$32
Library and Courts II	Central Plant Usage Fee	\$916	\$964	\$964	\$964	\$964

*2025-26 and 2026-27 expense projections based on 2025-26 published Price Book rates

This proposal, according to the Administration, is intended to resolve the ongoing structural deficit between the actual building rental expenses billed by DGS and the funding levels currently appropriated to the California State Library. Absent corrective action, the Library must absorb these escalating costs by redirecting resources away from critical programmatic and operational needs, thereby undermining service delivery and long-term fiscal sustainability. The requested

funding augmentation is therefore intended to align the Library's baseline appropriation with its rent obligations, ensuring compliance with state facility cost requirements while preserving resources for mission-driven priorities.

The additional authorized appropriation will be applied directly to cover the DGS quarterly rental invoices, beginning in 2026-27. This funding ensures that all mandated facility costs are fully funded within the Library's 2026-27 appropriation, outyears subject to additional increases, eliminating the need to redirect resources from core operations and programs.

Staff Recommendation. Hold Open.

Issue 6: Imagination Library

Panel.

- Mary Halterman, Department of Finance
- Greg Lucas, California State Library

Background.

Dolly Parton’s Imagination Library is a book-gifting program operated by the Dollywood Foundation, which partners with local nonprofits or local governmental entities to deliver books to children from birth to age 5. Local affiliates are responsible to raise funds in order promote programs, enroll children, and work with Dolly Parton’s Imagination Library to coordinate monthly book orders and fulfillment. The Dollywood Foundation/Imagination Library covers the overhead and administrative costs.

Senate Bill 1183 (Grove and Atkins) was signed and chaptered in 2022 by Governor Gavin Newsom, which established the Statewide Imagination Library under the State Librarian. This bill primarily did two things:

1. Created the Imagination Library of California Fund in the State Treasury, which was to be administered by the California State Library in order to support: (1) providing age-appropriate books through Dolly Parton’s Imagination Library, and (2) qualified local entities (defined as “any existing or new local Dolly Parton’s Imagination Library affiliate”) that agree to a dollar-for-dollar match for the program, which can be waived.
2. The bill also required the State Librarian to administer a California iteration of Dolly Parton’s Imagination Library, and coordinate with a nonprofit entity that is organized solely to promote and encourage reading by the children of the state.

In tandem with the legislation, the Legislature also included \$68.2 million to the California State Library in the 2022 Budget Act to establish the Statewide Imagination Library, and further support local California partners by covering half the cost of the books with a dollar-for-dollar match. The California State Library was intended to be the statewide partner that is responsible for the outreach and the administration of the dollar-for-dollar match (unless it is waived) to local partners to distribute books to children, with the Dollywood Foundation covering additional program costs. The stated goal at the time the funding was secured was to reach the goal of enrolling 65 percent of eligible children in California by the end of the five-year program period. 10 percent of these funds, or \$6.8 million, were allowed for the State Library’s administrative costs. These funds were available until June 30, 2028.

California State Library establishes Nonprofit. Articles of Incorporation for a nonprofit organization called “Imagination Library of California Strong Reader Partnership” were filed with the Secretary of State on April 18, 2023. An amended Articles of Incorporation were subsequently

filed on July 18, 2025, dropping the “Imagination Library of California” part of the name to “Strong Reader Partnership.” This nonprofit will be referenced in this agenda item as the Strong Reader Partnership. Both the Articles of Incorporation and the Statement of Information documents filed with the Secretary of State for the Strong Reader Partnership lists the Deputy State Librarian as the Agent for Service of Process, with addresses associated with the California State Library.

By July 2024, two years after the initial \$68.2 million investment, the program and funding were not being implemented. The Imagination Library of California Fund in the State Treasury was not administratively established. Instead, the California State Library executed a contract valued at \$19.2 million between the California State Library and the Strong Reader Partnership on August 6, 2024. The contract required the Strong Reader Partnership to, among other things, administer the dollar-for-dollar match, and provide quarterly financial and activities reports every three months.

Subsequent Budget Actions. In order to streamline and expedite the program administration after two years of inaction and delay, the 2024 Budget Act (AB 157, 2024) re-appropriated at least 90 percent of the \$68.2 million to the Dollywood Foundation no later than 45 days after enactment of the budget bill, with the expectation that the Dollywood Foundation would oversee the outreach to local program partners and the administration of the book-gifting program. The budget bill went into print on August 24, 2024 and the bill was enacted on September 30, 2024.

However, the California State Library allocated \$4.8 million to the Strong Reader Partnership, and bank statements show that the Strong Reader Partnership deposited these funds into a business checking account on August 26, 2024. Contrary to the budget bill language in AB 157, the California State Library only allocated approximately 37 percent, or \$25 million, to the Dollywood Foundation in a contract that was executed on February 9, 2025.

To reinforce the 2024 budget agreement, the 2025 budget reverted the remaining funds from the California State Library, including the remaining funds held by the nonprofit Strong Reader Partnership, so that the Department of General Services could properly allocate the funds to implement and expedite the Statewide Imagination Library.

The California State Library ultimately reverted the remaining unencumbered balance of \$36,884,933, and abated \$3,863,947.40 (of which \$78,932.41 was comprised of interest) from the Strong Reader Partnership. According to the State Controller’s Office, this reversion was processed in December 2025.

Fiscal details of Strong Reader Partnership murky. In September 2025, Senate budget committee staff requested the quarterly reports by the Strong Reader Partnership that were required in the August 6, 2024 contract between the Strong Reader Partnership and the California State Library, which totaled four required reports by the time these were requested. Instead, the committee received one report that consolidated financial and narrative reporting for the period between July 2024 and August 2025 (see Attachment).

In addition to requests for quarterly reporting, budget committee staff requested bank statements, receipts and invoices to corroborate expenses related to the implementation of the Imagination Library. To date, the committee has only received bank statements between August 2024 and August 2025. The bank statements showed that the Strong Reader Partnership transferred \$4 million to a money market account, where it accrued approximately \$132,000 in interest between August 2024 and August 2025.

The Strong Reader Partnership's expenditures between August 2024 and August 2025, including bank fees and accounting software fees, totaled \$555,871.40. The total balance in the money market account as of August 2025 was \$4,131,932.39. However, in an undated report provided to the committee by the California State Library on February 27, 2026, the Strong Reader Partnership reported that it ultimately spent \$1,205,222.76. Despite repeated requests for additional information, the California State Library has not been able to account for \$649,351.36, or the difference between the expenditures as of August 2025 and the final expenditure amount reported by Strong Reader Partnership, or produce corroborating documentation for these expenditures.

Budget committee staff has requested from the California State Library corroborating receipts, invoices, and final bank statements from the Strong Reader Partnership to understand the expenditures with the stated activities in its report, and requested the additional information on the following dates:

1. November 5, 2025
2. November 13, 2025
3. December 3, 2025
4. January 5, 2026
5. January 22, 2026
6. February 17, 2026

To date, the California State Library has not provided these documents. Staff notes that the executive director of the Strong Reader Partnership also serves as the principal of one of its vendors, a Sacramento-based consulting firm that has received at least four checks dispensing \$208,652.75 as of August 2025.

Dolly Parton's Imagination Library of California. The Dollywood Foundation received approximately \$25 million on February 18, 2025 from the California State Library. In the reporting period between July 1, 2025 and December 31, 2025, the Dollywood Foundation reports 683,636 books being distributed, with 52,034 new children enrolled into the programs. During this reporting period, the Imagination Library expanded into seven new counties, with five counties/region of counties getting ready to launch in Spring/early Summer 2026.

In comparison, the Strong Reader Partnership has only provided one \$5,000 grant to a Sacramento-based local partner serving Yolo County. The California State Library could not share information

with the committee on how many children have been enrolled or how many books have been distributed with this grant.

Recommended Questions.

- Why did the California State Library establish its own nonprofit? What was its vision for the Strong Reader Partnership?
- What are the challenges that prevent the California State Library from producing backup documentation, including bank statements, invoices, and receipts, for the Strong Reader Partnership and its stated activities related to the Imagination Library to the Legislature? What can the California State Library tell us with absolute certainty about how \$1.2 million was spent?
- The contract between the California State Library and the Strong Reader Partnership gives authority to the California State Library, the Department of General Services, the State Auditor, or their designated representatives to review, audit, inspect and copy any records and supporting documentation pertaining to the nonprofit's performance. The contract also provides authority to the California State Library to require the nonprofit to forfeit unexpended funds or repay any funds improperly expended. What has the California State Library done, or will do, in order to enforce its contract with the Strong Reader Partnership?

Staff Recommendation. This item is informational.