

Key Policies Considered but Not Recommended

During two years of deliberations, the Committee examined a wide array of issues related to its charge areas — especially finance — for which the Committee ultimately either remained unresolved or determined to pursue an alternative approach. In this appendix, the Committee documents some of the key policy ideas discussed but not pursued as affirmative recommendations. Because some of these difficult issues must be resolved for implementation of other changes recommended by the Committee, and because the Governor, Legislature, and other stakeholders likely will need to conduct a similar examination, the Committee provides some of the context of its deliberations here.

Determining a Viable Base Funding Level and Issues of Transitioning to the New Funding Model

What is the appropriate base?

As discussed in the Finance chapter of this report, research tells us little about the level of overall funding needed in the state’s education system. And, while the Committee recommended additional investments to support economically disadvantaged students and English learners, the Committee was unresolved on the funding needs of “base” students (those students not economically disadvantaged, English learners, or in special education). The Committee concluded that the available research did not lead to a definitive determination of the base and that, ultimately, the question of the appropriate base funding level for the new finance system was more of a political question than a research/policy question. Ideally, a strong relationship would exist between the financial inputs of the education system and the academic outcomes of students, but as adequacy studies have shown — with proposed costs ranging from \$1 billion to \$1.5 trillion — such a relationship either does not exist or can be identified only by methodologies that have not been applied.

Economists have had difficulty establishing a link or relationship between funding and outcomes. This is not surprising to those in the education system. In simplest terms, the state, districts, and schools provide the highest level of resources to those students who have the greatest needs, and historically, students with greater needs have had lower academic achievement. Thus, when economists look at the relationship between the level of funding spent and student outcomes, it is not surprising that they have difficulty finding a direct relationship. Of course, this by no means implies that money does not matter, but simply that the academic literature cannot say much about *how much funding* is necessary for California’s school system.

In this report, the Committee has set forth short-term and medium-term recommendations that have significant cost implications. The Committee believes that the state first must make the type of fiscal investments outlined in this report to

transition the finance system to a local control-driven, continuous improvement model. Once these short-term and medium-term goals have been accomplished, the Committee recommends that the state re-examine the question of the appropriate base level of funding for the system. At that point, under the proposed student-centered funding model, any adjustment to the new base for the finance system will automatically adjust the funding level for the entire system.

Issues of transition must be addressed

Because this new student-centered funding system will recognize the need to target substantial additional resources to economically disadvantaged students and English learners, it is unlikely that the state will be able to immediately implement the new finance system in full. For this reason, the Committee recommends transitioning to the new funding system over a multiyear period, making additional investments as state revenues permit. The Committee recognizes that the state will face political barriers in transitioning from the current funding system to the new one. To make this transition viable, the state likely will have to ensure that districts are, to some extent or at least for some time period, held harmless compared to the funding allocation that the districts currently receive through the existing finance system, to provide districts with the time they need to adjust to the new funding system. The state could smooth the transition to a new finance system with any of several hold-harmless mechanisms, some of which are presented here, in order of cost to the state.

- **Hold districts harmless for some time period to accommodate adjustments.** The state could ensure that for the first three years of the transition, a school district would receive at least as much as under the current system. After this adjustment period, a district's funding level would transition to the new formula-driven finance system. This approach has been used previously in California to make transitions in the state's special education funding model.
- **Hold harmless at current dollar level.** The state could ensure that districts receive at least the same dollar amount as they receive under the current system. This type of hold harmless could be calculated on a per-pupil basis or could provide some relief for declining enrollment districts by having the state hold the total funding constant, even if the district were declining in enrollment. Under this model, the benefits of the hold-harmless provision would be eroded over time by inflation.
- **Hold harmless adjusted for growth and cost of living adjustments (COLA).** Because education funding generally grows over time as costs increase and attendance grows, the state could hold districts harmless by adjusting the funding level received under the current system by some COLA and growth factors. The state either could provide a differential COLA for those districts receiving funding in excess of the new funding model or provide all districts with growth and COLA, regardless of whether their current exceeds the new funding model.
- **Hold harmless to ensure level of service is maintained for sub-populations.** Since the proposed finance system makes comparatively larger investments in economically disadvantaged students and English learners, the new finance system may be seen by some to redistribute within a district's allocation the level of funding available to the base student compared to the targeted student. The state could develop a hold-harmless provision to ensure that such redistributions did not occur. The state could use the targeted student spending levels (see Finance chapter generally, and Recommendation 2.1.4) to determine the aggregate funding goal for each district. First, all districts would be provided the same level of total funding that they received in the prior year (adjusted for growth and COLA). Any additional revenues available above growth and COLA that are not designated for incentive purposes would be disbursed proportionally to those districts that have a funding gap between their funding goals and their prior-year funding levels. If, for example, statewide there is sufficient additional funding to close one-fourth of the aggregate funding gap between districts' funding goals and their current funding levels, each district would have one-fourth of its gap closed, irrespective of the actual gap size; those districts with larger gaps would receive larger increases in funding each year to help close the larger gaps more rapidly. This process would continue until the state achieves its new targeted funding level for each district. Because the augmentations for low-income students (40 percent) and English learners (20 percent) will be higher than their implicit weighting in the current finance system (approximately 10 percent), over time school districts with large numbers of these targeted students will receive substantial additional funding beyond growth and COLA.

While the Committee recognizes that the state may face some issues in the transition from the current funding system to the proposed student-centered funding model, the issues raised in the transition process are basically political ones. Since the Committee had no basis to favor one political answer over another, it leaves this decision to the Governor, the Legislature, and stakeholders to determine within the political process.

Determining the Complexity of the New Finance System

After the Committee concluded that the current finance system was structurally flawed and needed to be overhauled, the Committee spent several meetings determining the appropriate characteristics of a new funding model. Early in that process, the Committee was faced with the difficult trade-off between incorporating substantial complexities into the finance system model to improve its accuracy and equity, on the one hand, and the benefits of transparency and ease of understanding that comes from a more simplistic funding model, on the other. Ultimately, the Committee determined that developing a funding model that educators, parents, taxpayers, and voters could easily understand and the accountability that comes with such transparency were more beneficial than the benefits that could result from adding many layers of complexity. Most of the additional complexities considered take the form of additional factors or adjustments in a student-centered funding model — many of which have been incorporated into the funding models of other states or are recommended in abstract models developed by academics. Some of those complexities, which were considered but rejected by the Committee included the following:

Complexity in targeting disadvantaged students

- **Using multiple measures of economically disadvantaged.** The Finance chapter of this report discusses important considerations regarding whether the state should use poverty data, eligibility for the federal free and reduced-price lunch program, or California Work Opportunity and Responsibility to Kids (CalWORKs) data to determine eligibility for and levels of additional funding for targeted students; the Committee resolved on a single criterion. Alternatively, the state could use a combination of measures. One approach would be to use all of these measures and assign different adjustments to each factor to create a “need index.” The new state funding model used in New York effectively does this, combining the percentage of the enrollment of English learners, the percentage of those eligible for a free or reduced-price lunch, the percentage of those living in poverty and other measures into one composite-need index that is then used to determine a district’s funding. Another, similar approach would be to establish different tiers of disadvantaged students: A state might, for example, provide 40 percent more funding for students living in poverty but only 20 percent more for students who are eligible for a free or reduced-price meal but whose families’ incomes are above the poverty line. This latter approach would allow districts and the public to know how much is available for each type of student.
- **Measures of concentration.** The cost of educating an economically disadvantaged student or English learner may differ depending on the demographics of the other students in the classroom or school. For example, it may be more difficult for a Spanish-speaking English learner to learn English if he or she is in a school where all of the other students also are Spanish-speaking English learners. The academic literature often refers to the impact that other students in the same class or school have on a specific student’s achievement as “peer group effects.” The finance system can address this peer group effect by providing additional funding to districts that have higher concentrations of economically disadvantaged students or English learners. This approach may make even more sense in a finance system that provides the funding directly to the school level because peer group effects are more likely to happen at the school and classroom level and not at the district level.
- **Other measures to target disadvantaged students.** Other states have additional factors in their finance systems for smaller populations with higher funding needs. These populations include, for example, students who are migrant, transient, in foster care, or pregnant or parenting.

Regional cost adjustment of salaries

School district budgets are predominantly comprised of personnel compensation, with teacher salaries usually accounting for more than half of the budget. As the Public Policy Institute of California (PPIC) determined in its “Getting Down to Facts” research paper, these teacher costs vary considerably across the more than 1,000 school districts across the state.¹ These variations should not be surprising given the size and diversity of California and the characteristics of its school districts in terms of geographic, ethnic, social, economic, and educational needs of the students they serve. Some districts in higher-cost areas often are forced to offer fewer educational programs in order to pay the higher teacher salaries in their region (often this translates into districts in high-cost areas having larger average class sizes). The PPIC paper develops a regional cost adjustment that would modify the base funding that a district receives to reflect the cost that these districts face to be competitive in the local labor market. Some of the models used to develop cost adjustments are discussed below, along with discussion of some of the problems Committee members found with them, that led the Committee to *not* include a regional cost adjustment in the proposed student-centered funding model.

The issue of regional cost adjustments is not new. The underlying question regarding teacher wage adjustments in state school finance policy may be expressed as follows:

How much more or less does it cost to recruit and employ similar school personnel (i.e., exhibiting similar discretionary factors) in different school districts (characterized by different sets of cost factors) at different points in time (i.e., in different school years)?

Three basic approaches have been used by states to address cost differences in wages across school districts: 1) Regional COLA; 2) comparable wage adjustments; and 3) an index that combines monetary and non-monetary characteristics.

- **Regional COLA.** These adjustments are intended to compensate teachers for differences in the costs of maintaining comparable quality of life across school districts or regions within a state. A regional COLA typically assumes some basket of basic amenities required for attaining a specific quality of life: Goods and services of a specific quality level are identified, and the price differences for purchasing those goods or services are estimated across regions in a state. The basket of goods typically includes items such as housing, food, clothing, child care, and health care.
- **Comparable wages.** These adjustments are estimated for teachers by evaluating the competitive wages of workers in other industries in a region that require similar education levels and professional skills as teachers. To the extent that competitive wages for similar work (at similar levels of experience, education, age, etc.) vary across regions within a state, it also is assumed that competitive wages for teachers must vary. The underlying assumption is that teachers’ wages must be competitive with other local industries requiring comparable skills, or teachers might choose to work in those industries instead. Because local labor markets vary, competitive teacher wages must vary.³

The PPIC research is based on this approach. It finds that in areas of the state with higher costs of living, districts need to compensate teachers with higher salaries. This generally leads to districts in high-cost areas of the state having larger class sizes. The PPIC paper proposes to multiply funding provided to districts by a comparable wage factor that would increase school funding in high-cost counties and decrease funding in low-cost areas of the state.

- **Use monetary and non-monetary factors to adjust district allocations.** A vast body of educational research indicates that teachers’ job choices are driven by both monetary factors (salary and other compensation) and non-monetary factors, including work conditions and local living conditions that are largely out of the control of the local district. For example, a teacher is more likely to want to work in a community considered a highly desirable place to live. This assessment may include factors such as the local job market, public safety, affordable housing, recreational activities, weather, air quality, healthcare facilities, culture and entertainment, proximity of a college or university, and transportation. This type of information is used to develop “best places to live” lists that find that communities like San Diego, San Luis Obispo, and San Francisco are highly desirable places to live, irrespective of the high cost of living there.

Similarly, such work environment factors as facilities, parental and community support, and student demographics, which are largely outside of district’s control, may be key factors. Better qualified teachers, in particular, often are predisposed to seek and obtain jobs based on these non-monetary factors. In order to equalize the ability of districts to attract and retain teachers, the state could adjust the funding allocation to account for these non-monetary factors as well as the monetary ones. Specifically, the state could create a wage index that would attempt to adjust funding allocations to districts to recognize that the availability of these factors has an inverse relationship to the need to augment salaries to attract teachers. Neither the regional cost nor the comparable wage adjustments methods address these factors directly. While more complicated than the comparable wage or cost of living indices, this combined index has the distinct advantage of reflecting the array of barriers a district encounters in hiring a teacher without unintended consequences of the other approaches.

Concerns with regional cost adjustments

Many Committee members were concerned that incorporating a regional cost adjustment in the student-centered funding model would further disadvantage some districts that appear to have the most difficulty attracting and retaining qualified and effective teachers. A comparable wage index would essentially increase salaries in high-cost counties and decrease them in low-cost counties. However, some of the districts that would benefit from a cost of living or comparable wage index have been able to overcome local cost pressures and still recruit quality personnel because of desirable quality of life and work environments. The chart “Teacher Credentialing Information for Select High- and Low-Cost Counties” shows the PPIC comparable wage index for sets of high-cost and low-cost counties, along with the percentage of teachers in each county who possess a full credential (while a full credential is not an ideal measure teacher quality, it is one of the only measures or proxies readily available). These data suggest that at least the listed high-cost counties do not appear to have problems recruiting and retaining qualified teachers. In all of the high-cost counties cited, approximately 97 percent of teachers possess a full credential, while the lower-cost counties — in which only 90 percent of teachers are fully credentialed — appear to have difficulty recruiting qualified teachers, even though salaries there go further. The chart suggests that incorporating a comparable wage index could further exacerbate the disparities among districts’ abilities to recruit teachers.

Teacher Credentialing Information for Select High- and Low-Cost Counties

High-cost counties			Low-cost counties		
County	Comp. wage index	Percentage full credentials	County	Comp. wage index	Percentage full credentials
Orange	1.11	97.3%	Imperial	0.95	87.5%
Ventura	1.09	97.2%	San Joaquin	1.01	88.9%
Marin	1.2	97.0%	Merced	0.93	90.5%
San Francisco	1.2	96.5%	Lassen	0.84	91.7%

Source: PPIC and the California Department of Education

The highest-cost county in the state, Santa Clara, does appear to have some difficulty attracting and retaining teachers. However, a closer look suggests that local costs are not the most important issue when it comes to recruiting and retaining teachers. Specifically, the higher-cost areas of the county do not appear to have a problem recruiting teachers, while the areas of the county with lower housing costs, such as East Side Union and Gilroy, do appear to have a problem. This again raises the question of the whether a cost adjustment could solve the recruitment/retention issues.

Proportion of Fully Credentialed Teachers in the Largest Districts in Santa Clara County

10 largest districts in Santa Clara	Number of teachers	Percentage fully credentialed
San Jose Unified	1,601	96%
East Side Union	1,222	88%
Cupertino Union	816	96%
Alum Rock Union	729	92%
Palo Alto Unified	720	98%
Santa Clara Unified	703	98%
Evergreen Elementary	628	96%
Oak Grove Elementary	566	96%
Gilroy Unified	516	91%
Franklin-McKinley Elementary	482	97%

Source: California Department of Education

The implementation of a regional cost adjustment in a student-centered funding model has potential benefits and disadvantages. Such an adjustment could help higher-cost areas of the state maintain class sizes similar to those in lower-cost areas of the state. However, a regional cost adjustment would likely exacerbate the difficulty that many districts in low-cost areas already experience in recruiting and retaining quality teachers. After reviewing all ramifications, the Committee decided not to implement an adjustment in its proposed funding model.

Other potential regional adjustments

Other factors that are included in the school finance systems of other states, but which the Committee opted not to recommend, include:

- **Transportation cost factors.** This usually takes the form of a measure of student density in a district or vehicle miles traveled to transport a student to and from school.
- **Average teacher experience level.** The more experience a teacher has, the more expensive it is for a district to employ that teacher. Some states make adjustments in their finance systems to provide additional funding to districts with more experienced teachers. This adjustment may be indirectly related to whether the district's enrollment is growing or declining; districts with declining enrollment often have a teaching staff with greater experience, due to hiring freezes.
- **Rural or small schools.** Systems may have adjustments for schools that are necessarily small because of their geographic location and, therefore, experience high costs while simultaneously being unable to realize efficiencies or economies of scale.

Should Student-Centered Funding Go Directly to Schools?

Across the nation, there is widespread support for streamlining education finance systems and increasing funding for disadvantaged students — consistent with the Committee's recommendations in this report. There is some interest in revising finance systems one step further, to provide revenues directly to school sites and allow them to decide how to spend the money, rather than maintaining fiscal control at the district. In its reviews of such finance models, both theoretical and in practice, the Committee examined this approach and determined not to recommend a school-level finance system for California. Because both

the Committee’s finance proposal and school-site budgeting models of this nature often are referred to as “weighted pupil funding” models, this discussion is provided to distinguish the Committee’s recommendations from school-site budgeting.

Proponents of school-site weighted pupil funding systems identify many of the same problems the Committee recognized in California’s current finance system. To resolve those issues of inequity, rigidity, complexity, and antiquity, they would both streamline state finance systems *and* delegate budget decision making to the school site.⁴ While the Committee obviously agrees with the need to streamline the finance system, the Committee believes that requiring the delegation of budgeting authority to schools can have many unintended consequences. The Committee determined that systemic problems could be overcome without those consequences through the combination of (1) streamlining the finance system to provide funding to districts in a transparent way, (2) providing easily accessible data on school-site budgeting, and (3) having districts voluntarily provide additional decision-making authority to schools as a performance incentive.

Arguments in support of school-site budgeting

Recently, William Ouchi from UCLA, the Thomas B. Fordham Institute, and others have proposed moving resource decision-making authority to the school level, and several districts have begun to implement related school-site management reforms.⁵ The following are the principal rationales generally offered in support of school-site budgeting:

- **Address intradistrict inequities.** Marguerite Roza and others have recently shed light on the funding inequities that continue to exist among schools within districts.⁶ Roza finds that in some states, the inequities within districts are larger than those across districts. Advocates believe that if school-site budgeting models were implemented, then districts would be forced to improve the equity of funding among their schools.
- **Improve resource use.** Ouchi and the Fordham Institute argue that funding schools directly can significantly improve the efficiency of how funds are used. They then note that districts that have pursued this type of funding allocation system generally reduce the size of the district central office staff. In Edmonton (Alberta, Canada), the school district distributes nearly 75 percent of its funding directly to schools through formulas that provide base funding plus additional resources to students with greater needs. Moreover, with decision-making authority, a school is able to purchase the bundle of goods and services it determines best meets its students’ needs, rather than accepting services the district provides to all schools but the particular school might deem unnecessary (or not the best use of its funds).
- **Support school choice.** Often schools of choice, especially charter schools, receive lower per-pupil funding than traditional public schools. A statewide evaluation by RAND found that California’s charter schools receive less funding than non-charter schools.⁷ That is because charter schools have significantly lower participation in categorical programs due to the combination of their not being eligible and their being deterred by the complexity of the categorical programs (without a district administrative structure to negotiate the details). Proponents argue that if the state moved to a school-site budgeting model, charter schools likely would receive more funding, at levels comparable to non-charter public schools.

Proponents’ arguments not persuasive

The Committee was not persuaded by these arguments. In the case of inequities within districts, since the proposed student-centered funding model makes the funding process transparent and is supported by a school-level accounting system, the state can ensure that large and inexplicable intradistrict inequities will not exist in the future — without requiring the expansion of administrative processes to every school. The Committee also questions whether requiring school-site budgeting supports a more efficient use of resources. Not all schools are prepared for school-site management: If a school is currently low-performing and largely dysfunctional, providing additional autonomy and more flexible resources to that school easily could be a recipe for (involuntary) misuse of funds. In general, principals may not have adequate training to put in place the type of internal controls necessary to ensure that funds are used effectively. A principal’s job is to be the instructional leader of the school, the curriculum

expert, the teacher evaluator, and a mentor, among many other roles. To mandate adding detailed budgeting responsibility on top of the existing ones without the necessary buy-in, training, and support is a recipe for disaster.

In terms of charter school equity, one of the tenets of the Committee’s proposed funding model is to ensure that charter schools receive an equivalent share of funding as non-charter schools; here again, a far simpler proposal exists, rather than expanding administrative structures at all schools statewide. Finally, the Committee notes that these proposals for mandated delegation of authority to school sites present significant operational and philosophical difficulties in California, where voters elect local school boards and entrust them with decision making and where many long-term contracts entered into at the district level would present significant impediments to *all* principals having the genuine autonomy this model envisions.

Committee supports experimentation in this area

While the Committee would not support California mandating that districts delegate budget responsibility to school sites, it does believe that the state should support further experimentation with expanded school-site autonomy, on a district-by-district basis, in which school-site budgeting is a part of the district’s overall reform strategy and the district provides the appropriate supports school leaders need. In fact, some of Committee’s recommendations would directly promote such experimentation:

- **Implementing a student-centered funding system.** Simply moving toward a student-centered funding model is an important first step to support districts that want to expand school-site autonomy. Among districts in California, San Francisco Unified has the most experience with providing greater school-site budgeting authority. However, because of the difficulty of ensuring that all categorical program requirements are fulfilled, San Francisco Unified only delegates decision-making authority over a portion of its general purpose funds. (Oakland Unified has recently implemented a similar structure.) This can make it difficult to ensure that categorical funding programs are well-aligned with the local decisions made about general purpose funds. Simplifying the categorical funding structure would allow districts already providing school-site budgeting autonomy to improve the effectiveness of their programs.
- **School-site inspections could support “earned autonomy.”** The new school inspection system proposed in the Governance and Accountability chapter of this report would provide school reports that will give districts information about the capacities of a specific school site. If a school inspection shows that the school has a strong principal who works collaboratively with teachers, well-documented goals, and an education plan that supports progress toward those goals, that school may be well-positioned to be granted greater budgetary discretion. Districts could use this new tool to voluntarily implement school-site budgeting, on a site-by-site basis, in those schools in which success and capacity warrant it.
- **Locally designed principal training programs could support local decision making.** Finally, as the state grants selected districts the authority to conduct principal training programs, districts could incorporate into their newly designed training programs specific elements that would support future principals’ development of the necessary skills to effectively carry out oversight of a school-site budget.

Why Not Categorical Block Grants Instead of Overhauling the Finance System?

In its earliest deliberations, the Committee determined that the current finance system needed to be streamlined to reduce the unnecessary complexity and related burdens. The Committee then turned to the question of whether to implement a student-centered funding model, as it ultimately recommended, or to take the less dramatic step of consolidating the existing categorical programs into various block grants. The Committee reviewed previous categorical reform proposals made by the current and prior administrations, the Legislature, the Legislative Analyst’s Office (LAO), and others. While the Committee saw merit in many of these proposals when compared to the status quo, Committee members did not believe that consolidation of categoricals alone would create the type of transparency and rationality that the Committee desires for California schools.

Should the State Offer Additional Declining Enrollment Relief?

Because of shifting demographics, California has reached a point at which 63 percent of its students attend school in districts with declining enrollment. Although the state has long employed a mechanism to offset some of the costs of enrollment declines, the scope of the related fiscal pressures on districts has become so great that there is much discussion of whether compensatory treatment should be increased.

Why the state provides relief for districts facing declining enrollment

Many factors over which a school district has no control may contribute to declines in student enrollment and the commensurate loss of operational funding. These losses can have great impact on a school district, since its operational costs may not be lessened much — or at all — in conjunction with the loss of funding. State policy recognizes that some buffer must be provided for districts that face a gap between levels of resource loss and expenditures. When school districts experience declining enrollment, they often have difficulty making adjustments to their budgets quickly enough to stay solvent. Moreover, if districts are not aware of a decline until it actually happens, then the district will have even more trouble adjusting. Among the issues that commonly contribute to districts' difficulties when their enrollments are declining are the following:

- **Marginal costs are less than average costs.** When a district's attendance declines slowly, it usually begins by invoking a hiring freeze; if the decline is significant enough, the district usually will lay off some teachers and other staff. However, the teachers that either were not hired or were laid off are generally junior teachers, who are paid at the lower end of the salary schedule. As a result, the average teacher salary *increases* in these declining enrollment districts even as their fiscal resources continue to erode. The combination of revenue loss and higher salary costs usually results in these districts being forced to eliminate programs to balance their budgets.
- **Districts do not see the decline coming.** Some districts do not invest in good enrollment projections to guide their longer-term planning (if they do any longer-term planning at all). These districts are often surprised when fewer students arrive than had been expected in a given year. By the beginning of that school year, staff has been hired for the year, and budgets quickly become strained. For districts that do not see it coming, declining enrollment will lead to significant fiscal difficulties and, potentially, to insolvency.
- **Closing schools is extremely difficult.** If the enrollment decline in a district continues, eventually the budgetary pressures likely will force a district to close some schools. Some superintendents say that closing a school is the most difficult thing a district can face, due to extreme community pressures to keep schools open in each neighborhood. Because of this extreme difficulty, districts often delay the inevitable, with the result that their budgets become even more challenged.
- **Declining enrollment may be more difficult for unified districts.** For unified districts, a districtwide decline may be even more difficult to address because the total district enrollment trends partially mask the grade-specific trends. In particular, over the last several years, the state has seen dramatic statewide declines in elementary school-aged children and significant increases in high school-aged populations. Between 2004–05 and 2006–07, statewide enrollment decreased about 0.5 percent. However, elementary school enrollment decreased almost 2 percent. So, while most elementary districts were benefiting from declining enrollment protection, unified districts received no relief for their elementary declines. Because districts are provided declining enrollment relief based on total average daily attendance (ADA), severe declines in elementary schools within a unified district may be masked by high school enrollment growth, generating little or no relief for the declining-enrollment schools, in addition to the budgetary pressures the district already faces due to the higher costs of educating students as more of them move into high school. Another exacerbating factor is the inability of unified districts to transfer elementary teachers to high schools and vice versa, since they have different credentials.

Current system provides one year of relief

The state provides some funding relief to offset the financial difficulties faced by districts experiencing declining enrollment. Currently, districts are provided relief for one year before revenue limit funding begins to decrease. Technically, this relief is provided by allowing a district to claim the higher of its current year or prior year ADA level — in effect, not recognizing that enrollment declines begin when they actually do. With so many districts now in decline, the cost under the current law has almost reached one-half billion dollars annually. The chart “Cost of the State’s Declining Enrollment Provision” shows Department of Finance estimates of the amount the state has spent on providing this relief for each of the last three years. The difficulty with the current declining enrollment provision is that for districts with multiple years of enrollment declines, the district’s budget is reduced every year following the first year of relief; yet, many districts are not able to take the necessary actions far enough in advance to avoid fiscal difficulty or severe cuts with a one-year buffer.

Cost of the State’s Declining Enrollment Provision

(In millions)

Year	Amount
2005–06	\$402
2006–07*	\$378
2007–08 estimated	\$488

*Department of Finance and LAO disagree on the cost of the declining enrollment provision in this year. LAO estimates that 2006–07 costs are \$50 million higher than Department of Finance’s estimate.
Source: California Department of Finance

Options to provide additional relief to declining enrollment districts

Several of the options used in other states or previously used by the California Community Colleges provide multiple years of relief from the impacts of declining enrollment:

- **Previous community college declining enrollment provision.** Prior to 2003–04, colleges received funding based on their highest enrollment in the prior three years. For those college districts experiencing steady decline, the benefits can be significant in amount, as well as longer in duration.
- **Multiyear average.** Several states provide financial relief beyond one year by averaging the support over several years. Wyoming, for example, provides funding based on the higher of current year attendance or a weighted average of attendance for the previous three years.
- **Provide additional funding to districts that are both declining and “low wealth.”** LAO recently proposed an option to resolve two fiscal pressures in concert with one another: declining enrollment and equalization.⁸ Specifically, LAO proposed that if a district were declining and also had a low revenue limit, then its budget would be maintained from the prior year, but as attendance fell, the district’s revenue limit would be raised by a similar amount — holding the district’s actual budget harmless while adjusting its revenue limit calculation upward. This process would continue until the district’s revenue limit met the state’s equalization target, at which point the additional declining enrollment relief would end.

Why not more relief for declining enrollment districts?

Many criticize expanding the benefits for declining enrollment districts for three reasons:

- **Relief is not a cost-effective investment.** The state already spends nearly one-half billion dollars annually on declining enrollment relief. While some students may benefit from reduced class size or smaller schools because of declining enrollment funding, this might not be the most effective use of additional resources.

- **Allows districts to delay the inevitable.** Providing additional funding to districts to allow them to delay making the difficult decisions that eventually they *must* make does not help districts in the long run, since it allows them to continue to delay closing schools, laying off staff, or making other program reductions. Declining enrollment relief has the effect of reducing districts' average costs rather than just their marginal costs.
- **Spend funding on students who are present.** Former California State Sen. John Vasconcellos summed up this argument well during a difficult budget in the early 2000s — "I would rather spend money on students who are there than on students who are not there." Policymakers in Sacramento continue to evoke this sentiment when discussion of enhanced compensation of declining enrollment is suggested.

Declining enrollment has some impact on a district's fiscal health

Even with the state's investment in the current approach, declining enrollment is a common characteristic among school districts facing fiscal difficulties. In its paper for the Getting Down to Facts research project, School Services of California (SSC) developed a broad measure of a district's fiscal health. Districts facing declining enrollment were statistically more likely to be fiscally unhealthy — although not by as much as one would expect. SSC determined that 16.3 percent of districts that were growing were fiscally unhealthy, compared to 21.2 percent of districts experiencing declining enrollment. While this differentiation is disturbing, it also is worth noting that most districts in decline (79 percent) were able to maintain fiscal health using, at least in part, the current hold-harmless provision.

Declining enrollment and special education

After revenue limits, the largest state funding source for schools is special education funding. Special education funding has its own declining enrollment provision. Funding for special education is provided to Special Education Local Plan Areas (SELPA) — agencies that are regional providers of education services — and the state provides a declining enrollment provision for the entire SELPA, rather than for the individual districts located within the SELPA. This would not be problematic if the SELPA hired *all* special education staff serving schools; however, SELPAs usually hire only those staff serving students with the most severe special education needs and pass funding through to districts to serve the lower-cost special education students; thus, district enrollments and district staffing patterns are critical even though the funding is generated on a regional basis.

Within a SELPA, some districts may be growing while others are declining. By applying the declining enrollment provision to the whole SELPA region, the state offsets the declines with the growth in the allocation of funds. As a result, the determination of whether one district receives a declining enrollment benefit depends on the enrollment changes of the other districts in the SELPA, so that a district experiencing significant enrollment decline may receive no offsetting funds. If, for example, within a SELPA, District A were growing by 100 students and District B were shrinking by 100 students, SELPA funding would be stagnant from one year to the next; however, the SELPA would have to increase District A funding and decrease District B funding from its stable pot of funds, and District B would receive no declining enrollment benefits. This has caused problems within SELPAs, since there is little alternative to redistributing funding as described in this example.

It should be noted that this condition generally does not impact California's largest districts because most of them (Los Angeles Unified, Long Beach Unified, San Diego City Unified, Fresno Unified, Oakland Unified, Santa Ana Unified, etc.) are single-district SELPAs and receive the declining enrollment benefit for their special education funding.

The Committee examined alternative approaches, including allowing each district within a SELPA to generate funding based on the higher of the current and prior year ADA. This would provide SELPAs serving a combination of growing and declining enrollment districts with additional funding needed to accommodate actual enrollment changes.

Conclusion: Good arguments on both sides

Reasonable arguments are made on both sides of the issue of enhancing relief for declining enrollment. There existed sufficient disagreement among Committee members that the Committee opted not to propose any expansion of the current state relief provided for declining enrollment districts. One important factor in this decision was the Committee's recommendation that additional resources be invested in the K–12 system. Districts can use these resources strategically to address some of the difficulty of declining budgets.

Reforming the State Mandate Reimbursement Process To Eliminate Inefficiencies and Inequities

California's constitution requires the state to pay for the fiscal impact that new laws have on schools and districts. The current process to meet this requirement is inefficient and inequitable. First, the process requires approximately five years for lawyers and accountants to determine whether a state mandate is reimbursable and what the rules for reimbursement will be. It requires schools and districts to spend significant time and resources documenting the costs of complying with a mandate — especially in those first five years, before they know what rules for the reimbursement process will apply. In fact, districts often hire high-cost consultants to maximize their mandate reimbursements, counting any conceivable expense as related to the mandate. Then, the state has auditors review these claims, and many of the claims are disallowed. For smaller districts, all of this work is often determined to outweigh the benefits of gaining the reimbursement, so most of them simply do not bother seeking mandates reimbursement. As a result, the distribution of mandate funding is highly inequitable. The current process creates jobs for lawyers, auditors, and high-paid consultants to process a lot of paperwork at the expense of schools. The state can do better.

Chapter 329, Statutes of 2007 (AB 1222, Laird) created an important first step by creating an alternative mandate negotiation process that bypasses the bureaucratic Commission on State Mandates. Cooperation between local governments and the Department of Finance will be needed to reap the benefits of this new option. This statute will provide improvements for some new mandate claims but does not address the inefficiencies with the current process that applies to some five or more years' worth of backlogged claims, as well as to many future claims.

As described in the Finance chapter, the Committee recommends consolidating the funding for most categorical programs into the new student-centered funding system. Ideally, the state would include funding for payment of state mandates within this consolidation process, for as many of the existing mandates as possible. While the Committee reached agreement on the goal of consolidating and/or reducing the number of mandates as part of a broader systemwide finance reform, the Committee did not develop a specific mechanism to achieve this goal.

Endnotes

¹ Rose, Heather, and Ria Sengupta (2007) *Teacher Compensation and Labor Market Conditions in California: Implications for School Funding*, Public Policy Institute of California, written for Getting Down to Facts, Institute for Research on Education Policy and Practice.

² Chambers, J.G. (1999) "Patterns of Variation in the Salaries of School Personnel: What Goes on Behind the Cost Index Numbers?" *Journal of Education Finance* 25.

³ For a more thorough discussion of Comparable Wage Indices, see Lori Taylor (2005) "Comparable Wages, Inflation and School Finance Equity," Working Paper No. 540, Bush School of Government and Public Service, Texas A&M University.

⁴ For example see William Ouchi (2003) *Making Schools Work: A Revolutionary Plan to Get Your Children the Education They Deserve*, Simon and Schuster, and Thomas B Fordham Institute (2006) *Funding the Child: Tackling Inequity and Antiquity in School Finance*.

⁵ Many prominent educators have sign on in support of the Fordham proposal including three former U.S. Secretaries of Education (William Bennett, Rod Paige, and Shirley Hufstedler), several former governors (John Engler, Michigan; James B. Hunt, North Carolina) and other leaders including Paul O'Niell (former Secretary of the Treasury), John Podesta (former Chief of Staff for President Clinton), Bill Goodling (former Chairmen, Committee on Education and the Workforce, U.S. House of Representatives), Eli Broad (Co-founder of the Broad Foundation), and numerous other prominent figures in the policy, education, and non-profit and private sector.

⁶ See Marguerite Roza, Kacey Guin, Betheny Gross, and Scott Deburgomaster (2007) "Do Districts Fund Schools Fairly?" *Education Next*, Hoover Institute; Stanford; Marguerite Roza (2006) "How Districts Short Change Low Income and Minority Students," *Funding Gaps* 2006, The Education Trust; Janet Hansen and Marguerite Roza (2005) *Decentralized Decisionmaking for Schools, A New Promise for an Old Idea*, RAND, Occasional Papers.

⁷ Zimmer, Ron, et al. (2003) *Charter School Operations and Performance: Evidence from California*, RAND.

⁸ Legislative Analyst's Office (2005) "Create a New Declining Enrollment Option" *Analysis of the 2005–06 Budget Bill*, page E-53.