

## **DEL MAR UNION SCHOOL DISTRICT**

### **Budget Committee Meeting**

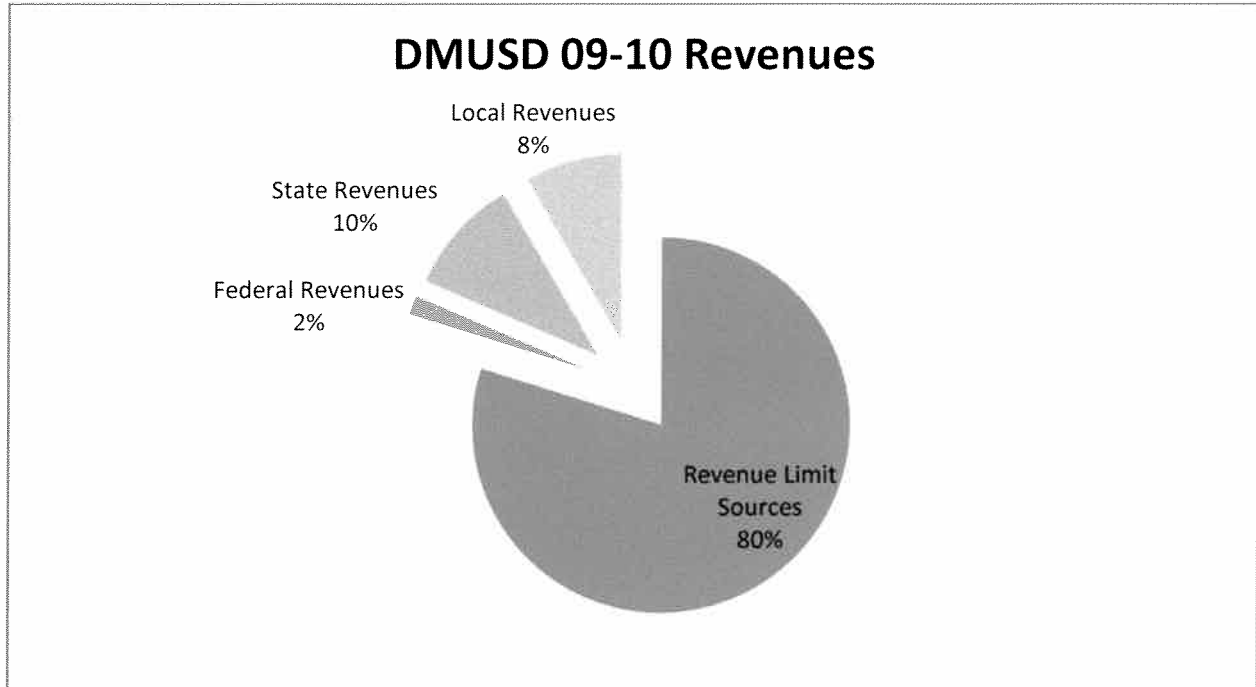
*Thursday, October 22, 2009*

*3:00 p.m.*

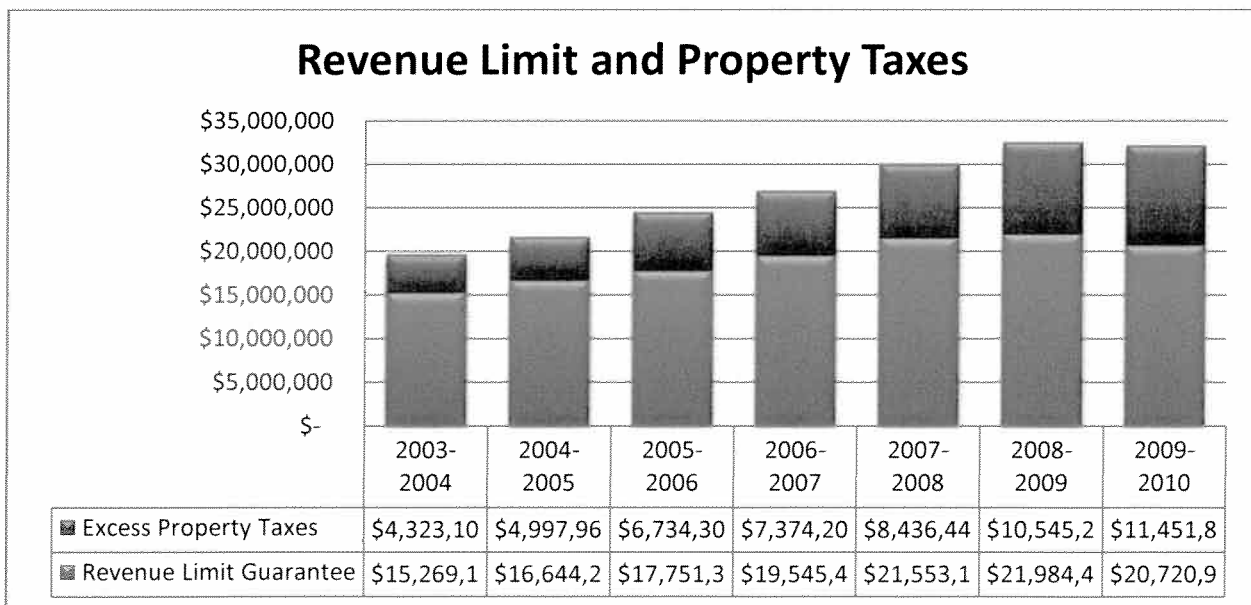
*Ashley Falls School, Room 305*

### **AGENDA**

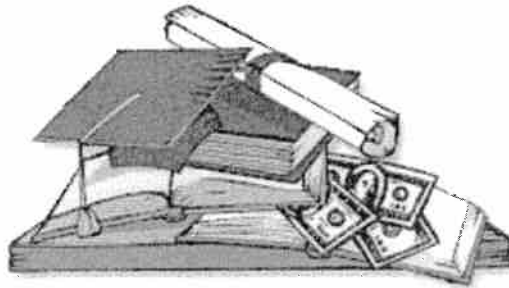
1. Overview of DMUSD 2009-2010 Revenue
2. The Uniqueness and Vulnerability of Basic Aid Funding
3. What State Receivership Means and Why It's Best to Avoid It
4. Real Estate Sales Activity
5. September Revenues Fall Short \$810 Million
6. DMSEF
7. Meeting Schedule



Year	Revenue Limit				Total Revenues
	Sources	Federal Revenues	State Revenues	Local Revenues	
2006-2007	\$ 27,037,752	\$ 677,187	\$ 4,759,592	\$ 3,629,291	\$ 36,103,822
2007-2008	\$ 30,105,081	\$ 748,617	\$ 4,366,333	\$ 3,672,803	\$ 38,892,834
2008-2009	\$ 32,663,325	\$ 718,321	\$ 4,223,737	\$ 3,319,526	\$ 40,924,909
2009-2010	\$ 32,291,136	\$ 672,802	\$ 4,067,927	\$ 3,399,777	\$ 40,431,642



**School Funding in California**  
**And**  
**The Uniqueness and Vulnerability of Basic Aid Funding**



**By**  
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**Field Report submitted to**  
**University of Southern California Rossier School of Education**  
**Ken Hall, Field Report Supervisor**  
**May 2009**

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# History of School Funding in California and The Uniqueness and Vulnerability of Basic Aid Funding

## 1. Introduction

The California School Finance System is complex and constantly changing. The current funding structure has been in place for over 35 years with changes and additions ranging from voter and judicial decision to annual modifications by lawmakers, factors that make it difficult to understand.

There are approximately 1,000 school districts in California and the majority of these districts are funded by the state's education funding formulas, which distribute a per-pupil dollar amount to each district known as the revenue limit. Each district's Average Daily Attendance (ADA) is the basis for calculating how much money school districts receive from the state (ADA x revenue limit). According to the California Department of Education, in 2008-2009 the state average revenue limit per pupil was \$5,567 for elementary districts, \$6,690 for secondary districts, and \$5,821 for unified school districts. The revenue limit funds that the districts receive are unrestricted and may be used at the discretion of the respective school district board. A small number of school districts are funded outside the revenue limit funding method where property taxes exceed the state's targeted funding level. The state allows these districts called "basic aid" or "community funded" districts to keep all of their property taxes, so they might have higher than average per-pupil funding. Revenue limit, as well as basic aid districts, are eligible to receive categorical Federal and State funds that are earmarked for certain purposes and are to be used only for certain student categories. The amount each district receives varies depending on the programs that the district offers, the number of students enrolled and the socioeconomic and demographics of the student population.

The purpose of this report is to help interested stakeholders including administrators, parents and board members understand the history of the current California school funding structure and the difference between revenue limit and basic aid funding. Obtaining an understanding of school funding, and specifically of the uniqueness and vulnerability of basic aid funding, will assist board members and administrators make informed decisions regarding the allocation of district funds and see the importance of building and maintaining a robust reserve.

The California Legislative Analyst projections on April 2008 included a \$27 billion operating shortfall in the state budget by 2009-2010. This financial crisis inevitably affects funding to education as cuts have been imposed and further reductions are proposed. Basic aid funding is very likely to be under attack once again as the economic crisis worsens and legislators desperately seek funds. Understanding the school funding structure is of utmost importance in this era of unprecedented cuts to education.

## **2. Methods and Procedures**

The information presented in this report was compiled from research, personal and written communication with authorities in school funding including Mr. Ken Hall, founder of School Services of California and Revenue Limit architect and School Services of California (SSC) experts such as Mr. Ron Bennett, CEO, and Mr. John Gray, Vice President. Written communication, telephone or face to face interviews were also conducted with Jim Cerretta and Joel Montero of Fiscal Crisis and Management Team, various basic aid districts chief business officials including Mr. Chuck Hagstrom of Taft School District, a former basic aid district, Ms. Julie Wood of Hope School District, a district new to basic aid, and Mr. Dick Douglas, Schools for Sound Finance President and Superintendent of Montecito Union School District a long time basic aid district. In addition, thorough research was conducted from SSC Fiscal Reports, written by SSC staff and Revenue and Revenue Limits a book written by Paul Goldfinger and Janelle Kubinec. Various websites were also used in this research including *Serrano vs. Priest* archives, Ed Source, California Department of Education and the University of Southern California Rossier School of Education.

## **3. History of School Funding in California:**

Before the current structure of school funding was in place, school districts were funded by their district's property tax base and as a result the per pupil expenditures varied greatly. The allocations the schools received were based on the tax amounts paid by the district's residents and the school board decided how to best utilize the money to educate students. This funding structure resulted in different funding levels for each district. Some had a surplus of funds while others barely had enough to meet obligations or were in a deficit. For example in the late sixties, the variation in per pupil expenditures was very significant. The Baldwin Park School District spent \$577 per pupil, Pasadena spent \$847 and Beverly Hills spent \$1,231. This funding disparity between districts also meant that low property tax district had to tax themselves at a higher rate. Baldwin Park was taxed twice the rate as Beverly Hills. It was impossible for low property wealth districts to match the expenditures of high property wealth districts.

As a result of the school funding inequity, lawyers from the Western Center on Law and Poverty approached John Serrano, a father who had to move his family to high property wealth districts so that his children's educational needs would be met, and asked him to lend his name for a class action law suit that challenged California's method of school financing.

### 3A. *Serrano vs. Priest* Chronology

Following is the chronology of the *Serrano vs. Priest* lawsuit and the events that followed as a result of the *Serrano vs. Priest* ruling, its effects on the current California school funding structure, and the exception to *Serrano* for some districts commonly known as basic aid. (also see attachment A)

In 1968 the *Serrano vs. Priest* lawsuit was filed in Los Angeles to challenge the funding inequities resulting from widely disparate property values and tax bases for funding K-12 education. It alleged that this funding structure violated the Equal Protection Clause of the California Constitution.

In 1971 the California Supreme Court ruled that the existing school funding method was unconstitutional and that it violated the Equal Protection Clause of the state Constitution and discriminated against the property poor districts because it made the quality of a child's education a function of the property wealth of his parents and neighbors and education cannot be conditioned on wealth related disparities.

**SB90 and AB 1267:** As a response to the *Serrano* lawsuit, bills SB90 and AB1267 were designed, the legislature passed and Governor Ronald Reagan signed them. These bills established what we know today as revenue limits. Revenue limit is a limit on the amount of general purpose money that each school district may receive. The revenue limit funding was based on an amount for each district's average daily attendance, ADA. (ADA x revenue limit = the district's funding allocation from the state)

**SB 90's** purpose was to equalize the funding differences between districts over time, mainly through a differential inflation increase that granted a larger dollar increase to low-revenue districts than to high-revenue districts. In addition, the low revenue districts were given increases in the initial year of up to 15%. These formulas leveled-up low revenue districts toward the statewide average and high-revenue districts were held to an inflation increase (Cost Of Living Adjustment or COLA) less than the real inflation increase (most often these districts received just about 50% of the COLA). This leveling restriction became known as the "squeeze formula" because it restricted the growth rate of high-revenue districts.

In addition, until Proposition 13 was adopted in 1978, there was a statutory provision that allowed districts to increase their revenue limit income through voter override. Districts were able to get these voter revenue limit increases approved by obtaining a majority vote of the electorate.

### 3A. *Serrano vs. Priest Chronology* (continued)

In 1974 the *Serrano* case was heard at the Superior Court level and Judge Jefferson ruled that while SB 90 was a step in the right direction, it did not equalize education funding either sufficiently or fast enough. The decision set a six-year deadline for compliance and required that the new school-funding system contain differences of no more than \$100 per pupil in expenditures financed from property taxes. This became known as the *Serrano Band*. A built in inflation factor was deemed appropriate by subsequent legal conclusion and thus the allowable difference increased to about \$300 per student by the time the final *Serrano* case was heard in 1983. The current allowable difference is approximately \$430 per student.

In 1976 the Supreme Court upheld the lower court's decision in *Serrano II* and the legislature enacted a comprehensive package of equalization formulas in 1977 to take effect for the 1978-79 school year.

In 1977 AB 65 was passed. AB 65 was a long term funding bill as an attempt to equalize school finance and improve school programs in response to the *Serrano* court decision. AB 65 provided additional state assistance to increase per pupil expenditures in low wealth districts and established new limits on the growth of expenditures in districts with high per pupil property values.

1978: Just weeks before the AB 65 equalization formulas took effect, **Proposition 13, Property Tax Amendment**, was approved by voters. Proposition 13 equalized total property tax rates statewide. It limited property tax rates to no more than 1% of full cash value and increases in assessed value per year were capped at 2% or the percentage growth in Consumer Price Index whichever is less.

Proposition 13 resulted in large cuts in statewide property taxes. The state then imposed funding cuts on all local government agencies including school districts. School funding cuts ranged from 9 – 15 percent based on the districts' revenue limit amounts.

1979 – AB 8 established the funding method for schools after Proposition 13, with a new formula for dividing property taxes between local cities, counties and school districts. It granted larger inflation increases to low spending districts.

1979- **The Gann Limit** was a Constitutional amendment adopted by the electorate that placed a limit on governmental spending at all levels, including school districts.

1980 – *Serrano* was in court again. The plaintiffs claimed that equalization had not been accomplished as required by the 1974 ruling and that the deadline for the \$100 band had not been met.

### 3A. *Serrano vs. Priest Chronology* (continued)

**1981-1982** – The squeeze formula continued. Due to the 1982-1983 recession there was no inflation increase and in lieu of COLA the State provided a flat inflation adjustment of \$11.90 per student and as an added protection, school districts received funding for decline in A.D.A.

The declining enrollment guarantee allowed districts to continue to count and be funded for a portion of the A.D.A. that had declined (phantom A.D.A.). This was a significant benefit to districts with declining enrollment as it gave them time to make the proper staff and fiscal adjustment due to less students.

**1983** – *Serrano* was back in court. Judge Olsen ruled that the \$100 band must be adjusted for inflation and that the State was in compliance with the *Serrano* standard. Since 93% of the State's students were in districts that had revenue limits within the set range. At this time the trial court also thoroughly considered the issue of districts that continued being funded by their local property taxes, basic aid districts and Judge Olsen concluded that the number of basic aid districts outside the *Serrano* range was insignificant in the total state funding scheme and therefore could continue with their unique funding structure.

**In 1983 SB 813** was passed. This bill is the school finance and school reform bill that ended the squeeze factor. Beginning with 1983-1984 school year, all districts of the same type, elementary, high school, and unified received the same dollar inflation increases. SB 813 also implemented major school improvement laws including mentor teachers, longer school day, longer year, minimum teacher salary reform programs, more rigorous graduation requirements and statewide curriculum standards. SB 813 finally implemented full revenue limit equalization for the first time.

**In 1984** a Constitutional amendment was passed that created the California State **Lottery**, with a designated percentage of earnings for education.

During the years 1985 – 1990, the State continued to be mindful of the importance of equalization and provided significant equalization aid in 1985-1986, 1986-1987 and 1989-90 and again in 1995-96. These three rounds of equalization resulted in about 98% of the students in the State to be within the allowable *Serrano* range of the original \$100 standard, adjusted for inflation.

**In 1988 Proposition 98** was passed. Proposition 98 is a Constitutional amendment that guarantees a minimum level of funding for K-14 education. The four provisions of Proposition 98 are:

### 3A. *Serrano vs. Priest* Chronology (continued)

- a guarantee of minimum funding for K-12 schools and community colleges based on a specific calculation. (ADA x Revenue Limit)
- an allocation to K-14 education of 50% of the difference when state tax revenues exceed the Gann limit, with the remaining 50% rebated to taxpayers,
- annual School Accountability Cards (SARCs) with at least 13 specific items for each school and
- a prudent state budget reserve

With a two-thirds vote of the Legislature and signature of the governor, Proposition 98 may be suspended for one year. (Ed. Data)

The Proposition 98 allocation is a complex calculation. In years of normal or strong state revenue growth, the K-14 guarantee is the larger of:

**Test 1** – the same share of the General Fund for K-14 education as the base year, 1986-87 (adjusted for changes in the share of property taxes)

**Test 2** – the prior year’s funding from state and property taxes adjusted for inflation (growth in per capita personal income) and increases in the student population (average daily attendance).

The guarantee when General Fund tax revenues grow more slowly than per capita personal income is:

**Test 3** the same criteria at Test 2 except inflation is defined as the growth per capita General fund revenues plus ½ percent.

**Test 3b** – same as test 3 except education may suffer cuts no deeper than other portions of the state budget.

The difference between the amount under Test 3 and what would have been the amount under Test 1 or 2 must be restored to education in years of stronger revenue growth. This provision is known at the maintenance factor or “safety net.”

**1996 – SB 1777 – Class Size Reduction.** This bill created funding incentives for districts to reduce class sizes in grades K-3 (20-1).

**2000 – Proposition 20.** Proposition 20 is a constitutional amendment requiring half of the growth in lottery money to be used for instructional materials.

**2000- Proposition 39.** Proposition 39 is a constitutional amendment permitting a 55% yes vote for approval of local general obligation bonds.

### 3A. *Serrano vs. Priest* Chronology (continued)

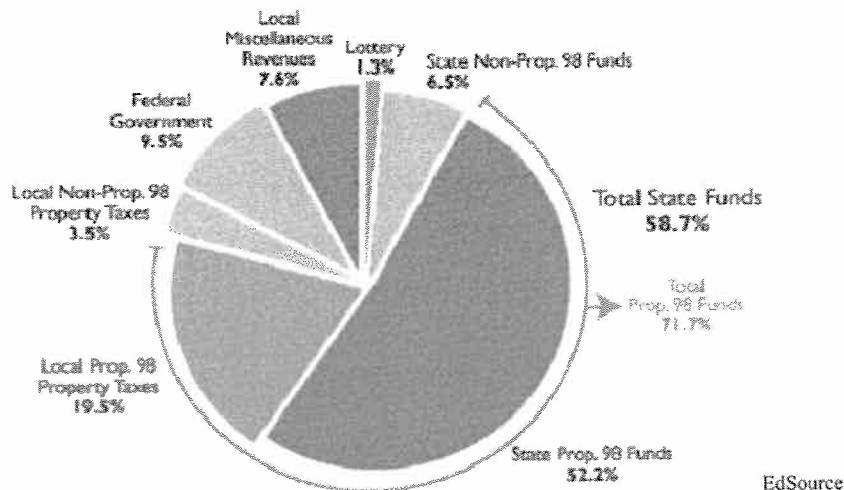
2000 – *Williams vs. California* – a lawsuit to ensure that California schools are providing all students with appropriate basic educational necessities.

*Serrano vs. Priest* was the catalyst for the current California School Funding structure. In years when no special school finance laws are passed, funding for education is written into the Budget Act and follow-up legislation.

### 4. School Funding Comes From Several Sources

The largest portion of school funding comes from the state’s general fund. The State general fund revenues are generated primarily from sales, income taxes and corporate taxes. Local school districts also receive income from property tax, Federal funds, lottery funds, local revenues such as donations, fees on commercial or residential construction; special elections for parcel taxes; cafeteria sales; and interest on investments. Districts may also sell voter approved general obligation bonds and impose developer fees on new construction or reconstruction within district boundaries. The developer fees funds may only be used for construction, acquisition, or major improvement of school facilities. The following chart shows the sources of K-12 education funds during the 2008-2009 school year:

### 2008-2009 revenues sources for K-12 education based on the enacted budget



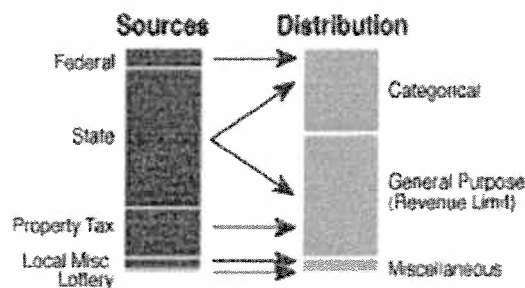
## 5A. Distribution of the Money for K-12 Education

About two-thirds of the total school district funding is for general purposes and the other one third is for special purposes or categories of students. Each district's income is based on three factors:

1. **ADA:** Average Daily Attendance. This is the average number of students attending school during the year.
2. **The revenue limit.** These are general purpose funds the district receives from the state based on ADA.
3. **Categorical Aid** are special support funds from the state and federal government earmarked for particular purposes and to serve specific student categories.

## 6. School Funding is a State Centralized System

Proposition 13 removed schools districts' ability to exert control over their revenue. Proposition 98 provides a measure of security to K-12 schools by guaranteeing a minimum amount of support from the State of California. The State collects revenue from the sources mentioned above and distributes the funds to school districts for general purposes and restricted uses according to each district's revenue limit, student population and/or demographics:



## 7. School Funding Outside of Revenue Limits

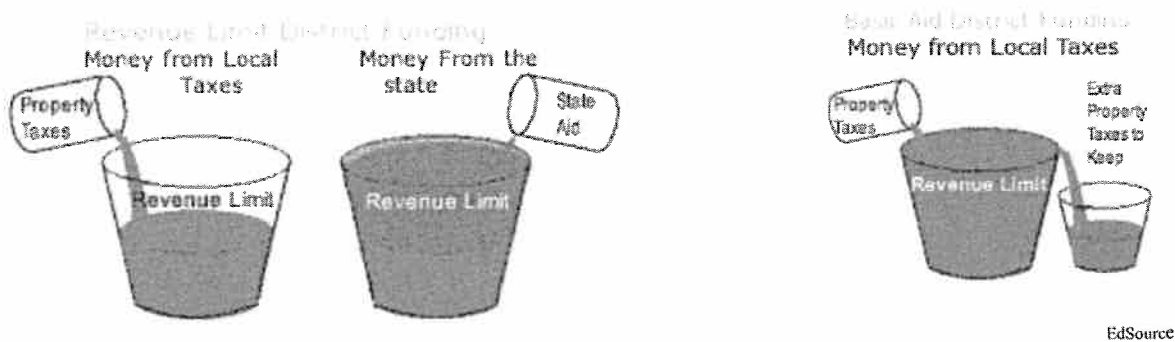
### 7A. Basic Aid School Funding is a Local System

Under the California Constitution, each school district must receive minimum State funding of \$120 per ADA or \$2400 whichever is greater. This constitutional guaranteed minimum amount is called basic aid. A small number of school districts receive property tax revenue that equals or exceeds their revenue limit and these districts have been historically called "basic aid."

In 2002-2003 due to budgetary constraints, the legislature eliminated the \$120 per ADA to basic aid districts and stated that it met its constitutional obligation to these districts with categorical funding. Even though the "basic aid" was taken away, these districts are still referred to as basic aid or "excess

## 7A. Basic Aid School Funding is a Local System (continued)

revenue” or “community funded” districts. Basic aid districts were discussed during the *Serrano* court case and in 1983 Judge Olsen ruled that the number of districts outside the *Serrano* band was insignificant and therefore could continue with their funding structure. As the chart below illustrates, the funding difference between basic aid districts and revenue limit districts is that basic aid districts are the exception to *Serrano* as their funding is not based on ADA, but are primarily funded by their local property taxes and are allowed to keep the property taxes that exceed their revenue limit funding.



Basic aid districts do not receive any general purpose Proposition 98 State funds; their revenue limit is funded strictly from local property taxes. These districts receive only property taxes from the secured roll and unsecured roll. They do not receive any property taxes from the supplemental secured roll, nor from property taxes shifted from local governments known as Education Revenue Augmentation Fund. They do receive categorical state and federal funds like revenue limit districts based on student population and demographics.

The extra property taxes kept by basic aid districts or the amount in excess of their computed revenue limit, does not count towards the Proposition 98 funding. If these property taxes were recaptured by the State it would merely offset state aid under Proposition 98 formulas, resulting in no additional funding for other school districts.

Unlike revenue limit districts, basic aid districts' financing is similar to that of California cities. The district income is determined by growth or decline of property tax revenues not by the population served. The total revenue received is a result of property tax income change and not as a result of an increase or decline in student population.

## **7B. How a District Becomes Basic Aid**

There is no application process to become basic aid. Basic aid funding is strictly based on the formula when property tax revenues per student equal or exceed the revenue limits per unit of average daily attendance (ADA). It is a matter of computing which provides more revenue per ADA, the State calculation for determining revenue limits or local property tax collection. When a district collects more property tax than its computed revenue limit income, the district is deemed to be “basic aid.”

## **7C. Basic Aid Districts Growing**

Out of the 1000 school districts in California, there were about 50 basic aid districts five years ago and per the Department of Education, there were 95 as of September 2008. This growth is a result of past years of slow revenue limit growth and faster growth in property taxes. Because local property tax revenues and enrollments fluctuate from year to year, some districts fall in and out of basic aid. They may be basic aid one year but not the next. At the time of the second principal apportionment (which is made in June), the California Department of Education (CDE) officially certifies which districts are basic aid for the school year that is ending. See attachment B for CDE’s list of 2008 basic aid districts.

**There are three factors than can lead to a district being basic aid:**

*First*, a school district can be basic aid as a result of having a very low revenue limit calculation and it is easy for property tax income to exceed the state revenue limit threshold. For example, Fallbrook Elementary School District in years past has been both basic aid and also eligible for equalization aid since its revenue limit was so low.

*Second*, a district can be basic aid as a result of a decline in the district’s enrollment and growth in district property tax income. If a district’s enrollment declines quickly, the authorized total revenue limit will also decline quickly. If the district property tax values grow, the dollar amounts from property tax income can exceed the computed revenue limit.

*Third*, a district can be basic aid as a consequence of high property tax values. A district that has oil wells, large power plants, large commercial real estate property or high residential property wealth within the district may become basic aid due to the high property tax collections.

As state revenue limits decrease, it is very likely that more districts will fall in the basic aid status. School Services of California calculates that over the past ten years school district revenues have increased by an average of about 4.2% per year while property taxes have increased at a much faster rate which moves more districts into basic aid. In addition, the tremendous real estate market growth during the past decade,

turnover of existing properties and new construction have greatly contributed to the growth in property tax pushing districts into basic aid.

Due to their low revenue limit funding, some districts take measures to qualify for basic aid and expediting their drop in enrollment by not accepting inter-district student transfers and therefore reaching an enrollment figure that generates lower total revenue limit income. Under such conditions a district's property tax revenue is more likely to exceed its total revenue limit income and thus the district will more likely be basic aid.

Even though the majority of basic aid school districts are small, as more districts enter basic aid status the variation in size also increases, ranging from very small districts of 200 or less up to over 21,000+ student population.

## **8. Characteristics of Basic Aid Districts**

### **8A. Basic Aid Districts' Students and Residents**

It is a common belief that the students served by basic aid districts are a homogenous and affluent group. This is not necessarily the case as basic aid status is determined by the property tax revenues not by the school district's residents' personal wealth. Students served by basic aid school districts in California are from various ethnic and economic backgrounds. The following basic aid districts are examples of the student demographics variety that exists at basic aid districts:

- In **Belridge Elementary School District** in Kern County, 96% of the students participate in the free or reduced meal program and 70% are English Learners.
- In **Horicon Elementary School District** in Sonoma County, over 50% of students are minority and more than 70% of students participate in the free or reduce meal program.
- In **Sausalito Marin City School District** in Marin County, about 80% of the students are minorities.
- In **Calistoga Joint Unified School District** in Napa County, almost half of the students are English Learners.
- In **Fremont Union High School District** in Santa Clara County, more than 66% of the students are minorities.
- In **Vista del Mar Union Elementary District** in Santa Barbara County about 50% of the students receive free or reduced price meals and about 30% of the students are English Learners.

### **Characteristics of Basic Aid Districts (continued)**

Although, basic aid districts are often referred to as high wealth this term is not a description of its residents but of the assessed value of property behind each pupil educated in the district. For example, Taft Union High School District was a basic aid district for a number of years. Taft had one of the lowest per capita personal income levels in the state, but due to the oil bearing property it qualified for basic aid status. Beverly Hills on the other hand, has one of the highest per-capita incomes for its residents, but it is estimated that it will not be basic aid until 2010-2011 due to their recent declining enrollment and not because of the personal wealth of its residents. In addition, due to the wide variation in actual revenue limits between districts, basic aid districts are not necessarily higher-funded than revenue limit districts.

### **8B. Additional Characteristic of Basic Aid Funding**

While some neighboring districts might see with envy that basic aid districts obtain more revenue from local property taxes than revenue limit districts, there are more factors involved to basic aid funding than there are in revenue limit funded districts. For example, basic aid districts must pay constant and close attention to local property assessments. The district administration and board must keep up to date with local assessments and valuations levels, property tax trends, new construction permits, changes in the city's general plan, zoning changes, and low-income housing projects. Basic aid districts must always maintain close relationships with the city and county governments to forecast revenues accurately. They must also know and be in close contact with local legislators and state representatives as basic aid funding is often the target of funding cuts.

### **8C. Falling In and Out of Basic Aid**

Basic aid districts must also be mindful that basic aid funding is vulnerable and due to the continuous fluctuations in enrollment and property values, districts may fall in and out of basic aid. The state's revenue limit funding structure is based on the district's prior year ADA. In the event that a district falls out of basic aid, the district would receive minimum general funding from the state. The significant loss of revenue forces the district to make drastic cuts to accommodate for the loss of basic aid status.

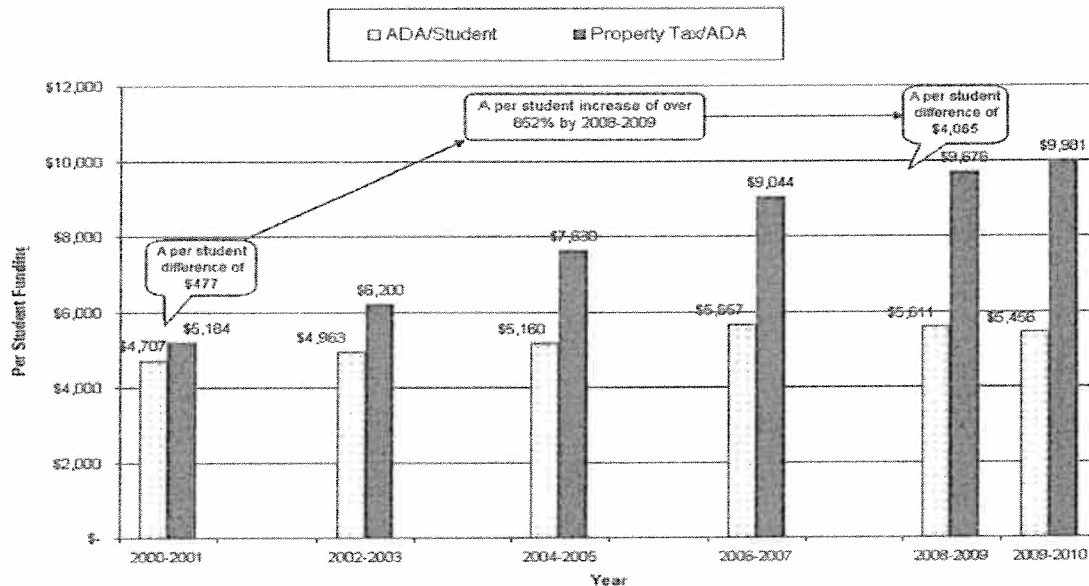
When a district becomes basic aid, the district could be cut off from the state's growth funding/COLA increases. Becoming basic aid is not necessarily an automatic windfall of wealth. In some cases many districts are barely into basic aid even as low as \$8 per pupil above their revenue limit. It may take years before a district is deep enough into basic aid to be able to have the resources needed to restore programs previously cut due to funding reductions.

## 9. The Good and the Bad of Basic Aid

### 9A. The Positive Side of Being Basic Aid:

When a district becomes basic aid it receives funding above its revenue limit per ADA that results in additional revenues. In most basic aid districts, property taxes per pupil grow faster than revenue limits cost of living adjustments (COLA) which may add up to a considerable funding difference over the years as shown below:

Sample of Revenue Limit vs. Property Tax Funding, per Student\*



\*Per Student = Average Daily Attendance (ADA)

Reed School District

**Mitigating Cuts:** Becoming a basic aid district means districts will be able to retain their local property tax income. For example, Carlsbad Unified School District was recently faced with projected cuts of over 5 million dollars due to the State budget funding reductions. As a result of falling into basic aid the district is now funded from property taxes and will receive about \$1.6 million in additional revenues which will help the district to reduce the anticipated cuts.

**State Budget Fluctuations:** The State budget is driven by sales and income taxes which are subject to major fluctuations. Basic aid districts on the other hand, are not dependant on State funding and may suffer less financial cuts during State budget crisis and Proposition 98 funding reductions.

**ADA:** Although attendance is very important in basic aid districts, property tax funding is not affected by ADA.

## **9A. The Positive Side of Being Basic Aid (continued)**

**Enrollment:** Declining enrollment does not negatively affect basic aid districts as the property tax funding remains the same regardless of the number of students. Categorical funding is however, affected by enrollment.

**Reserve:** Basic aid districts may be able to build reserves greater than the State required reserve level for school districts due to the surplus in funds from property tax revenue.

**Educational Programs:** Basic aid districts generally have the funding necessary to offer additional educational programs to support student achievement.

## **10. The Negative Side of Basic Aid:**

**Projections:** It is very hard to make long term funding projections because basic aid districts are at the mercy of local property tax values. They have no control over the revenues they receive from the local property tax. Property tax collections don't always grow and can vary from year to year, depending upon local economic conditions, sales of commercial, industrial and residential properties. Conversions of property to higher value parcels, and reassessments including downward reassessments during down markets, or fewer tax collections due to residents defaulting in their property tax payments or tax relief due to natural disasters also affect property tax revenue. For example, in the early 1990s a long time basic aid district, Pacific Grove, was receiving property tax funding from a golf course that sold for \$200 million. A few years later, the golf course was sold for \$50 million. The District's revenue fell unexpectedly and the District had to find a way to deal with such a significant funding loss.

**Other Funding Fluctuations:** Basic aid districts' dependence on property tax revenue also leads to difficult financial times as there is no proposition 98 funding guarantee like revenue limit districts. The recent wide swing in property values is an example of the negative sides of basic aid. These swings in property tax values are especially evident in those districts that are supported by the price of oil. With a wide fluctuation in oil values and the resulting changes in property tax values, oil and energy dependent districts can have fast declines in income and still have to meet obligations for growing ADA, honor labor contracts and cover other rising expenses. A decline in property values can impose a precipitous and very difficult budget squeeze on basic aid school districts.

**Meeting Payroll:** It might be difficult for districts that are barely into basic aid to meet payroll and other expenditures between tax funding times (April and December). The districts in this situation may be forced to borrow from their local county offices of education or tax treasurer office until they receive the property tax payments.

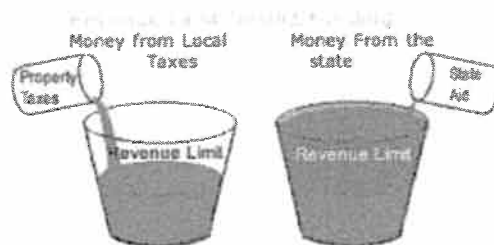
## 10. The Negative Side of Basic Aid (continued)

**Enrollment:** Unlike revenue limit districts, basic aid districts do not receive funding based on district enrollment. Property tax revenue has no direct relationship with district enrollment. There may be times when basic aid districts experience years of flat or falling property taxes at the same time as enrollment may increase. In these situations, the district must find ways to accommodate the enrollment growth including hiring new staff even though it has declining revenues.

**Interdistrict Transfers:** Unlike revenue earning districts whose funding is based on average daily attendance and the more students the school has the higher the funding, for basic aid districts it is unfavorable to accept students from outside the district because they represent additional expenditures rather than additional revenues.

**Elimination of Funds:** Basic aid districts must constantly be on the lookout for changes in State laws that affect their funding. The State eliminated the \$120 per pupil general purpose apportionment in 2003-2004 with no restoration. Basic aid districts only receive state aid through various categorical programs that prescribe how funds may be spent and which students may be served. (Due to the poor current economic situation, the state has recently made cuts in categorical funding and given some temporary flexibility to districts to decide how to best utilize the funds of certain categorical programs for general fund purposes.)

**No Back Fill:** Basic aid districts lose the backfill of the Education Revenue Augmentation Fund (ERAF) that revenue limits district receive. Although in some instances, basic aid districts do have more money than revenue earning districts, there is no safety net for basic aid districts and their finances are much more volatile. Basic aid districts are bracing themselves for tougher times ahead due to the sinking real estate market. Unlike revenue limit districts, basic aid districts funding is not offset by the State as shown in the graph below. In the event that enrollment grows or the property tax revenue decreases, the district is on its own and must find solutions to deal with the decline in funds.



## 10. The Negative Side of Basic Aid (continued)

**Charter Schools:** Charters can have a negative financial impact on basic aid schools. Basic aid schools are required to make money transfers to charter schools “in lieu of property tax” without being backfilled by the State. In the case of out of district students attending the charter school, the sponsoring basic aid district will only receive 70% of the district of residence base revenue limit. If the student is from another basic aid school district, the amount of reimbursement for the sponsoring district is zero.

**Increased Accountability:** Since basic aid districts receive the “incremental dollar” from local property tax and the schools are a major factor in determining local property values, the link between the local community and its schools is strengthened which allows local tax payers to have higher expectations.

**Bad Publicity:** Basic aid districts are often the target of bad publicity and often portrayed as immune from statewide budget cuts and as insulated from bad economic times. There is little or no sympathy for basic aid districts. (In an article, *The Sacramento Bee* referred to three rural Kern County basic aid schools as “The Three Little Pigs”.)

**Additional Funding Cuts:** Similar to all other districts in California, basic aid districts suffer cuts in categorical funds such as Special Education, class-size reduction and after-school programs. Basic aid districts that rely on categorical funds to serve their English-language learners or underprivileged students will see significant cuts just like all the revenue limit districts.

In addition to the cuts in categorical funding, basic aid districts will see a decrease in the property-tax revenues due to the current real estate slump and unlike revenue limit districts, basic aid districts will not be eligible for the 2009 Fiscal Stabilization Fund Portion of the Federal Economic Stimulus Package because it was last reported that these funds will be distributed to districts on a revenue limit basis.

**Proposition 98 Pay Back:** Proposition 98 guarantees a Maintenance Factor payback to revenue earning districts when the State does not fully fund districts per Proposition 98 guidelines. In this instance, the State “owes” the district the difference between what they were actually funded and what they should have been funded and will eventually pay the districts back during stronger revenue growth. Basic aid districts do not qualify for any pay back of decrease in revenues.

## 11. Basic Aid Districts' Vulnerability and Threats

The California Education Coalition was formed to protect Proposition 98 funding which does not include basic aid districts. As a result of having no advocacy, basic aid districts formed Schools for Sound Finance (SF)2; a coalition of Basic Aid Districts located throughout California dedicated to serve the interest of basic aid districts. SF2 hired School Services of California starting in 1975 to lobby on behalf of basic aid districts and address their varied needs.

In addition to the funding volatility that basic aid districts experience due to the fluctuation of property tax revenue because of changes in the real state market, downturn reassessments, impounds, defaulting in property tax payments and tax relief due to natural disasters, the following are additional threats that basic aid districts face:

**The Growth in Basic Aid Districts** presents a threat to all basic aid districts because as more districts enter basic aid status the insignificance factor that was used by Judge Olsen in the *Serrano* case to allow basic aid districts to continue being funded by local property taxes may become a significant percentage and provoke new legal action.

**School Funding Restructuring** has been a common topic among California Governors and legislators. Studies such as *Getting Down to Facts* and others are a loud bell regarding the idea of school funding inequity which may be the catalyst of major school funding restructuring that will inevitably target basic aid districts.

**Unification:** Due to the funding crisis facing the State, the legislature may decide to unify neighboring school districts. Basic aid districts like Montecito and Cold Spring in Santa Barbara County could be unified or absorbed by larger districts and basic aid funding would either go away or be stretched further to cover all the students in the unified district.

**Threats From The Legislature:** Basic aid districts are frequently singled out and in the forefront of threats by the State legislature. In January 2003 Governor Gray Davis proposed the following:

1. Eliminate the constitutionally required \$120 per student basic aid funding.
2. Seize the local property taxes above the amount required to fund each basic aid district's revenue limit.

It is interesting to note, that while revenue limit districts were facing as 6% funding cut, basic aid districts were targeted to lose the majority of their funding in some instances.

## **11. Basic Aid Districts' Vulnerability and Threats (continued)**

The seizure of these funds meant the destruction of many basic aid districts. Since these funds are not considered part of the Proposition 98 funding model, they would be used by the legislature to offset not augment the funding to other school districts and it would ultimate benefit the State not education. This action would be contrary to the historical practice of “leveling up” as it would cause irreparable damage to some of the States’ finest schools.

In the awakening of such threat, the basic aid districts with the assistance of Schools for Sound Finance, formed an organized arduous defense by contacting local and State representatives, holding town hall meetings and educating the public of the dangerous precedent that the capturing of property taxes would set for all of California citizens and the detrimental impact on school districts.

As California’s financial crisis continues and legislators desperately try to find funds to help the tremendous budget deficit, basic aid districts’ tax revenue become more desirable and basic aid districts are very likely to once again be the targets of attacks. Reserves are of utmost importance to basic aid districts due to the above mentioned funding vulnerability and the fact that there is no back fill or safety net for basic aid districts and thus they must create their own. The deeper a district is into basic aid the more difficult the reentry to revenue limit will be and therefore the prudent planning and reserves are even more important.

## **12. The Importance of Building and Protecting Reserves**

The State of California requires that school districts’ board of education adopt the “Criteria and Standards Review” report along with their annual budget. One criterion in this report is that the district budget appropriate a specific percentage of total budgeted expenditures and that amount be placed in a Reserve for Economic Uncertainties (REU). The statewide minimum reserve requirement for districts with over 1000 ADA is 3% of a district’s budget to be allocated for economic uncertainties.

Due to the property tax funding volatility, the legislative threats to seizure property taxes and the fact that there is no safety net for basic aid districts, robust reserves are extremely important for all basic aid districts.

## The Importance of Building and Protecting Reserves (continued)

Ron Bennett of School Services of California<sup>1</sup> recommends that basic aid districts maintain higher than average reserve levels and that the districts' board of education establish a board policy on reserves including the following:

- "First, the Board may wish to increase the level of the Reserve for Economic Uncertainty above the minimum level established by the state. If so, the Board should discuss and specify the reserve level that is comfortable given the circumstances of the district. Growth, decline, charter schools, opening or closing schools and other areas that affect all districts should be considered in this category."
- "Second, the Board may want to create a formal designation for a Basic Aid Reserve within the general fund. A separate Basic Aid Reserve recognizes the volatility of local property tax revenues. The size of the reserve depends on how far above the revenue limit the basic aid funding is and how volatile it is judged to be. A third of the difference between the revenue limit and the basic aid funding is often a good place to start the discussion. This reserve is unique to basic aid and may be very large: 20%-30% of the budget is not uncommon and is defensible."
- "Finally, the policy should address other topics of sufficient concern to warrant a separate designation. For example, a reserve for computer or other technology replacement or amounts set aside for amounts formally offered at the bargaining table, but not yet accepted by the union might be designated here."

"Any amount not affected by the above categories will fall to the undesignated portion of the reserve. The important thing to remember is that, while a district has great flexibility in how it shows the reserve, it is trying to be transparent and paint an accurate picture of the potential exposures faced by the district and what protection exists if some of those exposures become real. A reserve policy that is well-considered before the crisis occurs is always helpful."

### 12A. How Large is Large Enough?

While it is difficult to state a specific reserve amount as each district needs are unique, it is important to consider several factors when designating reserve funds. Some basic aid districts maintain reserve funds

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<sup>1</sup>"How Should Basic Aid Districts Designate Excess Reserves? School Services of California Fiscal Report, April 25, 2009, Volume 28, No. 9

**12A. How Large is Large Enough? (continued)**

equal to an entire year’s operating budget in order to smooth the funding peaks that come with property tax revenue. Others keep an amount sufficient to fund a three-to five year reentry cushion into state funding. Others maintain separate reserves that are designated for specific purposes such as technology, a student reserve (to accommodate enrollment increases), facilities, collective bargaining or legal costs. These reserves would help to soften the budgetary cuts imposed due to loss of property tax revenue.

School Services of California states that a prudent contingency reserve that is at least equal to the current-year differential between a district’s basic aid revenue and the state’s revenue limit guarantee is a must for basic aid districts. For example, in the event that the budget suffers an abrupt decline in property tax revenue or a seizure of property taxes occur, two thirds of that reserve could be expended in year one to soften the impact within the remaining third being drawn upon in year two. The greater the difference between revenue limit and basic aid funding, the higher the contingency reserve needs to be.

**12 B. Sample District**

Pacific Coastal Elementary School District is a district with stable enrollment deep into basic aid due to high residential property values and with approximately \$900,000 surplus funds each year to build a reserve. Pacific Coastal may consider the following reserve sample to designate its reserves as basic aid reserves for a 5 year cushion in the event that they lost their basic aid status or experienced a dramatic loss in tax revenue. For sample purposes, it is assumed that the revenue limit and enrollment remains the same and that there is a 1% increase in property tax revenue. \*The reserve amount is a moving target and it may take years to reach the year one basic aid reserve amount. The calculation figures would have to be adjusted each year depending on tax revenues actually received and COLA adjustments to revenue limits.

**Reserves of a Sample of Basic Aid District**

Pacific Coastal Elementary School							
		2008		Operating Budget		IDEAL BASIC AID RESERVE	
	ADA	State Revenue Limit	Average Revenue Limit	Revenue Limit Entitlement	Property Revenue	Tax	
					Difference Between RL and Basic Aid		
year 1	416	\$5,882		\$2,446,912	\$10,000,000	\$7,553,088*	projected 1% increase in property tax revenue
year 2	416	\$5,882		\$2,446,912	\$10,100,000	\$7,653,088	
year 3	416	\$5,882		\$2,446,912	\$10,201,000	\$7,754,088	
year 4	416	\$5,882		\$2,446,912	\$10,303,010	\$7,856,098	
year 5	416	\$5,882		\$2,446,912	\$10,406,040	\$7,959,128	

It will take years to build the reserve to an amount equal to the difference between the amount of the revenue limit and basic aid funding. Once the year one basic aid reserve goal is reached, Pacific Coastal School will annually add an amount, based on their income growth, to the basic aid reserve. Providing the basic aid funding continues at the same or higher level and that expenditures remain under control, the Board of Education might also consider establishing other reserves designated for specific purposes. Establishing and protecting adequate reserves during years of healthy funding is a long-term project that takes courage and prudent planning.

### **13. Collective Bargaining**

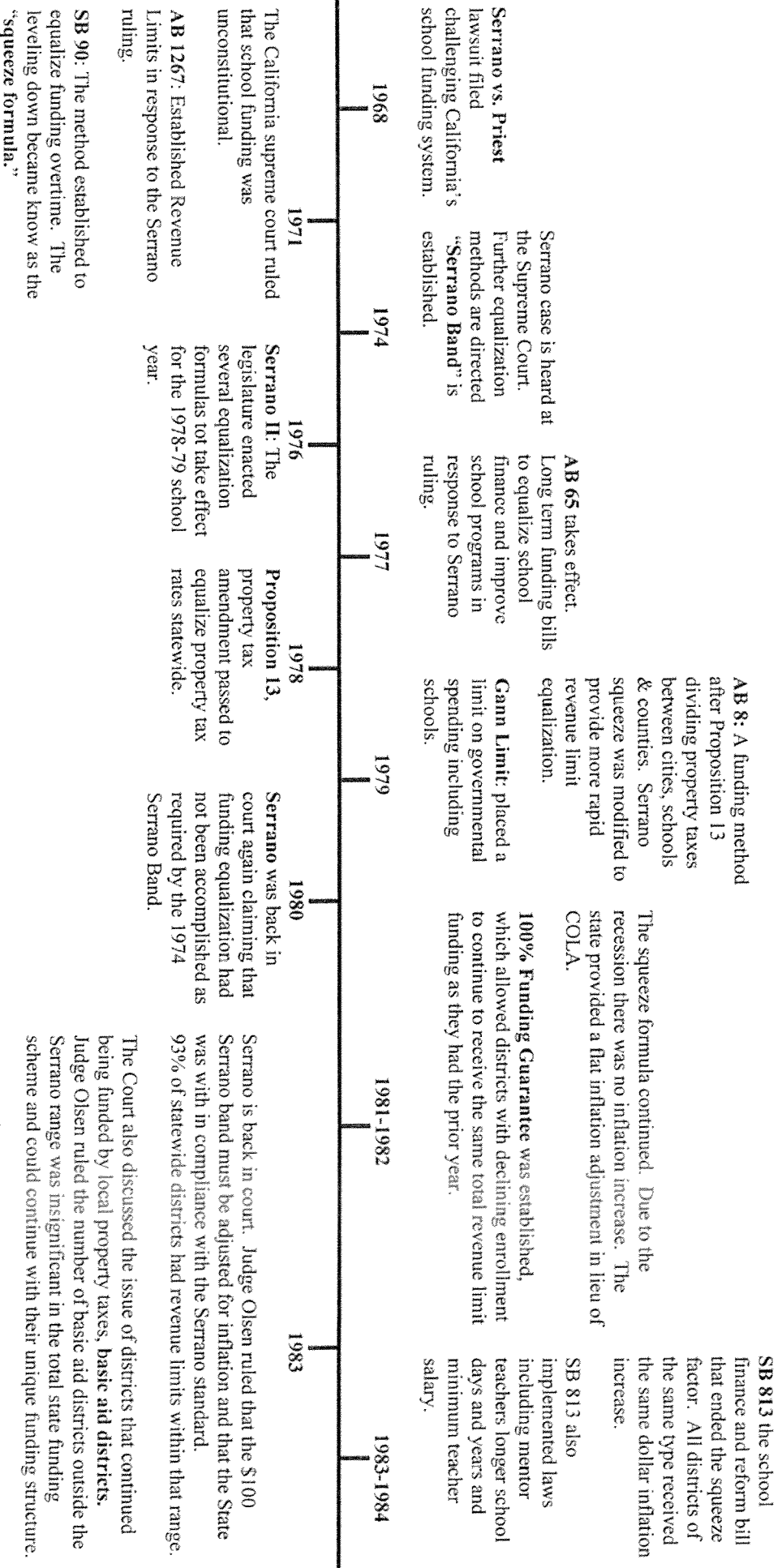
Districts deep into basic aid that have built reserves find themselves in difficult situations at the bargaining tables. The larger the reserve the bigger the target it becomes for the State and employees' unions. Labor unions are interested in negotiating salaries, benefits and working conditions for their membership, not necessarily in the financial well-being of the district. As the reserve grows, so does the desire to obtain higher salaries. As long as basic aid districts keep a fair and equitable compensation methodology, reserves are one-time funds that must be replenished if used and safeguarded to be used during tumultuous economic times.

### **14. Conclusion:**

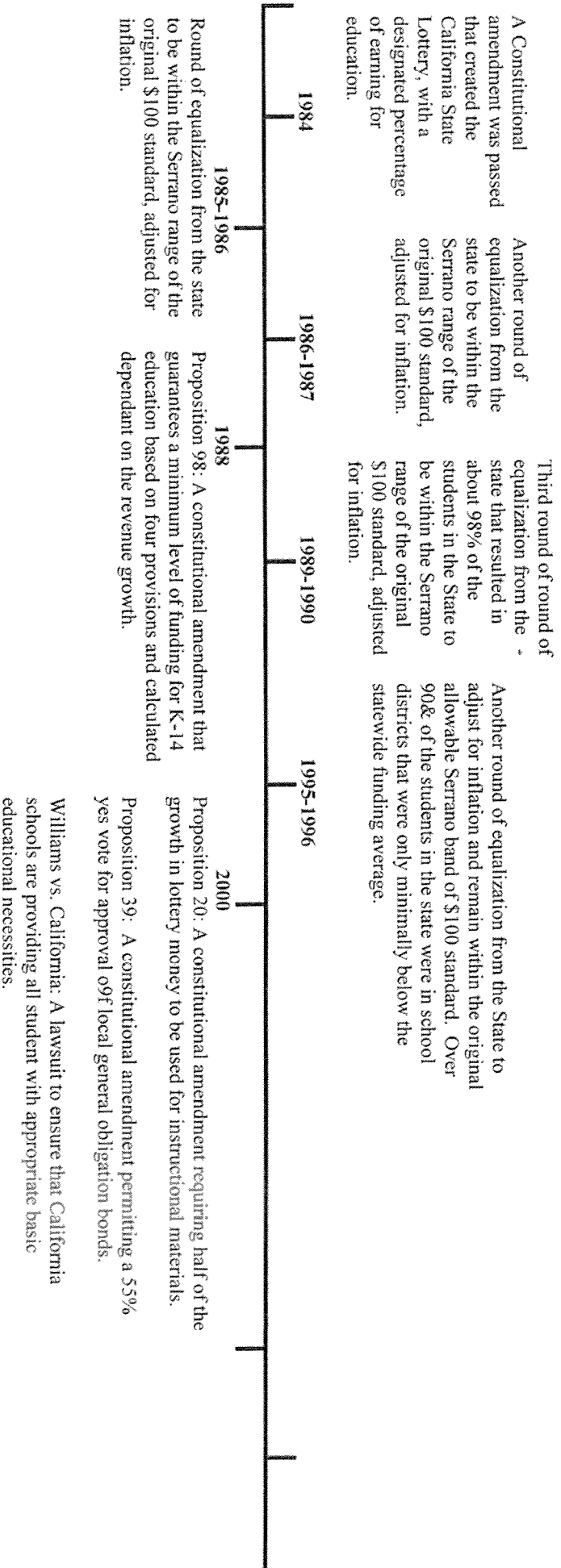
*Serrano vs. Priest's* intent was to level up and establish equity in funding in the California school system. Unfortunately, California currently ranks 48<sup>th</sup> in the nation in school funding and the current State economic crisis will most likely push it even lower. Basic aid districts are very vulnerable due to the fluctuations in local property tax revenues, the fact that unlike revenue limit districts there is no safety net from the State and the eminent attacks from legislators to seize the property tax above the districts' revenue limit funding. These districts have schools that rank among the best in the State of California and represent what education funding should be for every child. It is incumbent upon all legislators, parents and educators to keep a mentality of leveling up education and bring all school districts to funding levels similar to that of basic aid schools.



## Serrano vs. Priest and California's School Funding Structure 1968-1984



## Serrano vs. Priest and California's School Funding Structure 1984 - 2000



**2008-09 ADVANCE ADA FOR SECTION 75.70 OF THE REVENUE AND TAXATION CODE**  
DEPARTMENT OF EDUCATION LIST OF BASIC AID DISTRICTS AS OF SEPTEMBER 2008

<b>02</b>	<b>Alpine County</b>	
<b>UNIFIED</b>		
02 61333	Alpine County Unified	BASIC AID
<b>Total</b>	<b>Alpine County</b>	
<b>05</b>	<b>Calaveras County</b>	
<b>ELEMENTARY</b>		
05 61580	Vallecito Union Elementary	BASIC AID
<b>HIGH</b>		
05 61556	Bret Harte Union High	BASIC AID
<b>09</b>	<b>El Dorado County</b>	
<b>ELEMENTARY</b>		
09 61911	Latrobe Elementary	BASIC AID
09 61986	Silver Fork Elementary	BASIC AID
<b>10</b>	<b>Fresno County</b>	
<b>ELEMENTARY</b>		
10 62026	Big Creek Elementary	BASIC AID
10 62372	Pine Ridge Elementary	BASIC AID
<b>14</b>	<b>Inyo County</b>	
<b>ELEMENTARY</b>		
14 63305	Round Valley Joint Elementary	BASIC AID
14 63248	Big Pine Unified	BASIC AID
14 63289	Lone Pine Unified	BASIC AID
<b>15</b>	<b>Kern County</b>	
<b>ELEMENTARY</b>		
15 63347	Belridge Elementary	BASIC AID
15 63651	McKittrick Elementary	BASIC AID
15 63689	Midway Elementary	BASIC AID
<b>21</b>	<b>Marin County</b>	
<b>ELEMENTARY</b>		
21 65300	Bolinas-Stinson Union Elementary	BASIC AID
21 65318	Dixie Elementary	BASIC AID
21 65334	Kentfield Elementary	BASIC AID
21 65359	Lagunitas Elementary	BASIC AID
21 65367	Larkspur	BASIC AID
21 65391	Mill Valley Elementary	BASIC AID
21 65409	Nicasio	BASIC AID
21 65425	Reed Union Elementary	BASIC AID
21 65433	Ross Elementary	BASIC AID
21 65474	Sausalito Elementary	BASIC AID
<b>HIGH</b>		
21 65466	San Rafael City High	BASIC AID
21 65482	Tamalpais Union High	BASIC AID
<b>UNIFIED</b>		
21 73361	Shoreline Unified	BASIC AID
<b>23</b>	<b>Mendocino County</b>	
<b>ELEMENTARY</b>		
23 65557	Arena Union Elementary	BASIC AID
23 65573	Manchester Union Elementary	BASIC AID
<b>HIGH</b>		
23 65599	Point Arena Joint Union High	BASIC AID
<b>UNIFIED</b>		
23 65581	Mendocino Unified	BASIC AID

**2008-09 ADVANCE ADA FOR SECTION 75.70 OF THE REVENUE AND TAXATION CODE**

DEPARTMENT OF EDUCATION LIST OF BASIC AID DISTRICTS AS OF SEPTEMBER 2008

<b>26</b>	<b>Mono County</b>	
<b>UNIFIED</b>		
26 73668	Eastern Sierra Unified	BASIC AID
26 73692	Mammoth Unified	BASIC AID
<b>Total</b>	<b>Mono County</b>	
<b>27</b>	<b>Monterey County</b>	
<b>ELEMENTARY</b>		
<b>UNIFIED</b>		
27 65987	Carmel Unified	BASIC AID
27 66134	Pacific Grove Unified	BASIC AID
<b>28</b>	<b>Napa County</b>	
<b>ELEMENTARY</b>		
28 66258	Howell Mountain Elementary	BASIC AID
28 66282	Pope Valley Union Elementary	BASIC AID
<b>UNIFIED</b>		
28 66241	Calistoga Joint Unified	BASIC AID
28 66290	St. Helena Unified	BASIC AID
<b>29</b>	<b>Nevada County</b>	
<b>ELEMENTARY</b>		
29 66340	Nevada City Elementary	BASIC AID
29 66399	Ready Springs Union Elementary	BASIC AID
<b>30</b>	<b>Orange County</b>	
<b>ELEMENTARY</b>		
30 66555	Laguna Beach Unified	BASIC AID
30 66597	Newport-Mesa Unified	BASIC AID
<b>31</b>	<b>Placer County</b>	
<b>ELEMENTARY</b>		
31 66944	Tahoe-Truckee Joint Unified	BASIC AID
<b>32</b>	<b>Plumas County</b>	
<b>UNIFIED</b>		
32 66969	Plumas Unified	BASIC AID
<b>Total</b>	<b>Plumas County</b>	
<b>33</b>	<b>Riverside County</b>	
<b>ELEMENTARY</b>		
33 67041	Desert Center Unified	BASIC AID
<b>37</b>	<b>San Diego County</b>	
<b>ELEMENTARY</b>		
37 68007	Cardiff Elementary	BASIC AID
37 68056	Del Mar Union Elementary	BASIC AID
37 68080	Encinitas Union Elementary	BASIC AID
37 68312	Rancho Santa Fe Elementary	BASIC AID
37 68387	Solana Beach Elementary	BASIC AID
37 73551	Carlsbad Unified	BASIC AID
<b>40</b>	<b>San Luis Obispo County</b>	
<b>ELEMENTARY</b>		
40 68726	Cayucos Elementary	BASIC AID
40 75465	Coast Unified	BASIC AID

**2008-09 ADVANCE ADA FOR SECTION 75.70 OF THE REVENUE AND TAXATION CODE**  
**DEPARTMENT OF EDUCATION LIST OF BASIC AID DISTRICTS AS OF SEPTEMBER 2008**

<b>41</b>	<b>San Mateo County</b>	
<b>ELEMENTARY</b>		
41 68866	Belmont-Redwood Shores Elementary	BASIC AID
41 68874	Brisbane Elementary	BASIC AID
41 68908	Hillsborough City Elementary	BASIC AID
41 68957	Las Lomas Elementary	BASIC AID
41 68965	Menlo Park City Elementary	BASIC AID
41 68981	Portola Valley Elementary	BASIC AID
41 69088	Woodside Elementary	BASIC AID
<b>HIGH</b>		
41 69047	San Mateo Union High	BASIC AID
41 69062	Sequoia Union High	BASIC AID
<b>UNIFIED</b>		
41 68940	La Honda-Pescadero Unified	BASIC AID
<b>42</b>	<b>Santa Barbara County</b>	
<b>ELEMENTARY</b>		
42 69104	Ballard Elementary	BASIC AID
42 69161	Cold Spring Elementary	BASIC AID
42 69179	College Elementary	BASIC AID
42 69195	Goleta Union Elementary	BASIC AID
42 69211	Hope Elementary	BASIC AID
42 69252	Montecito Union Elementary	BASIC AID
42 69344	Vista del Mar Union Elementary	BASIC AID
<b>HIGH</b>		
42 69328	Santa Ynez Valley Union High	BASIC AID
<b>UNIFIED</b>		
42 69146	Carpinteria Unified	BASIC AID
<b>43</b>	<b>Santa Clara County</b>	
<b>ELEMENTARY</b>		
43 69492	Lakeside Joint Elementary	BASIC AID
43 69500	Loma Prieta Joint Union Elemen	BASIC AID
43 69518	Los Altos Elementary	BASIC AID
43 69526	Los Gatos Union Elementary	BASIC AID
43 69567	Montebello Elementary	BASIC AID
43 69682	Saratoga Union Elementary	BASIC AID
43 69890	Sunnyvale	BASIC AID
<b>HIGH</b>		
43 69401	Campbell Union High	BASIC AID
43 69468	Fremont Union High	BASIC AID
43 69534	Los Gatos-Saratoga Joint Union High	BASIC AID
43 69609	Mountain View-Los Altos Union High	BASIC AID
<b>UNIFIED</b>		
43 69641	Palo Alto Unified	BASIC AID
43 69674	Santa Clara Unified	BASIC AID
<b>44</b>	<b>Santa Cruz County</b>	
<b>ELEMENTARY</b>		
44 69732	Bonny Doon Union Elementary	BASIC AID
44 69757	Happy Valley Elementary	BASIC AID
44 69815	Santa Cruz City Elementary	BASIC AID
<b>HIGH</b>		
<b>45</b>	<b>Shasta County</b>	
<b>ELEMENTARY</b>		
45 70037	Indian Springs Elementary	BASIC AID
45 73700	Mountain Union Elementary	BASIC AID

2008-09 ADVANCE ADA FOR SECTION 75.70 OF THE REVENUE AND TAXATION CODE  
DEPARTMENT OF EDUCATION LIST OF BASIC AID DISTRICTS AS OF SEPTEMBER 2008

<b>47</b>	<b>Siskiyou County</b>	
<hr/>		
<b>ELEMENTARY</b>		
47 70359	Hornbrook Elementary	BASIC AID
<b>49</b>	<b>Sonoma County</b>	
<hr/>		
<b>ELEMENTARY</b>		
49 70599	Alexander Valley Union Elementary	BASIC AID
49 70763	Horicon Elementary	BASIC AID
49 70789	Kenwood Elementary	BASIC AID
49 70813	Monte Rio Union Elementary	BASIC AID
49 70821	Montgomery Elementary	BASIC AID

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School Fiscal Services Division  
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1. Mr. Ken Hall, University of Southern California Rossier School of Education Executive in Residence, School Services of California Founder, SB90 Architect.
2. Mr. Jim Cerretta and Mr. Joel Montero, Fiscal Crisis Management Assistance Team (FCMAT)
3. Mr. Dick Douglas, Superintendent, Montecito Union School District and Schools for Sound Finance President.
4. Mr. Chuck Hagstrom, Chief Business Official, Taft Union High School District, Taft, California.
5. Mrs. Julie Wood, Business Manager, Hope School District, Santa Barbara, California.
6. Mr. John Gray, Vice President, School Services of California.

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# *The* FISCAL REPORT an informational update

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No. 22

## **What State Receivership Means and Why It's Best to Avoid It**

*[Editor's Note: It is probably just coincidence, but we have had quite a number of inquiries recently about the consequences of just turning over the keys to the district to the state if the state doesn't stop cutting education. Since the Fiscal Crisis and Management Assistance Team (FCMAT) has responsibility for assisting districts in their efforts to avoid or deal with financial problems, we asked Joel Montero, FCMAT's Deputy Executive Officer, to author this article.]*

Last spring, California had the highest number of districts ever with qualified or negative certifications on their Second Interim budgets, reflecting the growing number of districts in fiscal distress. When a district gets to the point where it no longer has the cash to pay its bills, it must apply for a state loan, which means state receivership. Unfortunately, as a sign of the times, we have received many questions from districts about what state receivership looks like. What follows is some information on current law and, for a practical matter, what we have seen most recently in the districts that have required a state loan.

### **Budget Reserves vs. Cash Reserves**

A school district receives a qualified or negative certification generally because of its inability to maintain the state-required level of reserves in all three years of its multiyear projections. Running out of reserves by itself, however, does not cause a school district to require a state loan; running out of cash does.

The distinction between reserve levels and cash levels becomes clearer when looking at your General Fund balance sheet. Reserves are the (hopefully positive) difference between assets and liabilities, some of which are cash and some of which are not. On the assets side, there are several cash accounts that are obviously cash—Cash in County Treasury, Cash in Bank, Cash with Fiscal Agent, etc. Not all cash is accessible to pay bills—for example, Cash with Fiscal Agent is set aside for a specific purpose and the district may not have the legal authority to draw on that cash to pay for operations. Other assets are not cash—for example, Stores Inventory and Prepaid Expenses. Most liabilities are not cash, but one notable exception is Deferred Revenues, since this represents cash that has been received by the district. It is set up as a liability because it cannot be recognized as revenue until it has been spent on the specific purpose of the grantor agency.

It has generally held true that low reserve levels are an indicator of low cash levels and vice versa. However, with the recent state cash deferrals, this has become less true. School districts with prudent reserves are still having to manage their cash actively and borrow to get through the negative cash months. And districts with inadequate reserves are having an even tougher time ensuring that the cash is there to meet the obligations when due.

### **Cash Borrowing Options**

There are several options available to a school district to borrow cash locally—from its other funds, using tax and revenue anticipation notes (TRANS), from the county office of education, or from the county treasurer (Education Code Sections [E.C.] 42621, 42620). However, all of these options are temporary, short-term borrowing—they generally require that the district pay back the borrowing within a year or less. For each of these types of borrowing, the district is required to prepare a cash flow projection that indicates that the borrowing can be paid back from the district's future revenues in the time frame required.

If the cash flow projection, however, shows that the district will be unable to pay back the local borrowing, it means that the cash balance is trending downward with no end in sight—that the future revenues are not enough to keep up with operational obligations plus pay back the borrowing. If the district is unable to borrow locally, then the only other option is to request a loan from the state.

### State Loan

A loan (technically referred to in the Education Code as an emergency appropriation) from the state requires that one of the district's local representatives to the State Legislature sponsor a bill through the legislative process. This is typically an urgency bill, meaning that it requires at least a two-thirds vote of each house of the Legislature so that it can become effective upon the Governor's signature. The legislative process takes many months, so a state loan should be initiated early enough to ensure that the cash is there when the district needs it, and the timing needs to work within the legislative calendar. Typically, the bill has to be introduced in January in order to work its way through all of the legislative committees and the floors of both houses by the summer or early fall.

A loan from the state results in the state taking control of the school district. The degree of state control is determined by the size of the loan relative to the district's budget. Specifically, per E.C. 41326(a), if the loan is less than twice the size of the district's required reserve level, a State Trustee is assigned and assumes authority over the financial aspects of the school district's activities. If the size of the loan exceeds twice the size of the district's required reserve level, the following takes place:

- The school Board loses its powers and becomes advisory only [E.C. 41326(c)(1)]
- The Superintendent is no longer employed by the district [E.C. 41326(c)(2)]
- A State Administrator is assigned and assumes the powers of the Board and Superintendent [E.C. 41326(b)]

State loans are typically set up for repayment over 20 years. In both situations above, state control remains over the school district until the loan is fully repaid. The State Trustee or State Administrator reports directly to the Superintendent of Public Instruction—the state of California—not the local school Board or community.

The state loan is sized to accommodate the anticipated shortfall in cash that the district will need during the life of the loan in order to meet its obligations. In addition, all of the costs of ensuring a fiscal recovery are the responsibility of the district (E.C. 41328) and are added to the amount of the state loan. The cost of recovery when a State Administrator is assigned includes:

- The cost of the compensation package for the State Administrator (E.C. 41326[(b)][(8)])
- The cost of additional staffing as determined by the State Administrator to be necessary for ensuring fiscal recovery (E.C. 41326[(b)][(9)])
- The cost of management reviews and developing a recovery plan, including the cost of the initial comprehensive review and follow-up reviews every six months encompassing these five areas of the district (E.C. 41327.1):
  - Community relations and governance
  - Pupil achievement
  - Financial management
  - Personnel management
  - Facilities management
- Any other expenditures deemed necessary by the State Administrator to help ensure fiscal recovery

On the natural, a state loan will be much larger than what the district would otherwise need to borrow locally if it had been able to solve its own fiscal crisis. Therefore, a district that receives a state loan needs to make more expenditure cuts and/or take longer to pay the loan back.

The comprehensive review and six-month follow-up studies measure the district's progress in meeting the standards established. In the areas where the district has progressed enough in meeting the standards, the Board receives its powers back and a Superintendent is hired to administer those areas. It normally takes several years before the Board regains any of its powers. State control remains, either in the form of a State Administrator or State Trustee, with stay or rescind power over certain Board actions until the state loan is paid off.

The State Administrator's mission is to restore fiscal solvency as soon as possible so that the loan can be paid back to the state. This will be done by reducing expenditures to a level that is lower than revenues so that the reserves can be rebuilt over time while the state loan is being paid back. This means that all possible avenues for balancing the budget are pursued. The State Administrator cannot set aside any contractual obligations that the district has already entered into, including vendor contracts and bargaining unit contracts, without renegotiating them. If modifying provisions of these contracts is critical to gaining fiscal solvency, the State Administrator has the power to invoke the timelines available in the contracts or by law, including the ability to use the impasse/factfinding process to unilaterally impose changes in collective bargaining agreements.

### **Conclusion**

A district in financial trouble will regain fiscal solvency. If the district and the Board, while it has the power, do not take the necessary actions locally to restore fiscal solvency, the same actions and more will be imposed by the state. The typical state loan is established to be a 20-year payback. The district remains under some level of state control until that payback is complete. Generally, recovery costs more and takes longer if a state loan is required.

In the long term, taking the necessary actions locally and avoiding a state loan will result in greater local control, less outside intervention, and better long-term outcomes for students, employees, and the community.

—*Joel Montero*

posted 10/20/2009

Real Estate Sales Activity												
	2009 Sales Total	Average Sales Price	Average Value Increment (SP - 2008 AV)	Total Added Value Increment	2010 Sales Activity YTD Total (Est)	Average Sales Price	Average Value Increment (SP - 2009 AV)	Estimate Value Increment based on Total	# of Sales % Change	Sales Price % Change		
Cardiff	103	\$815,707	\$255,078	\$26,273,034	65	\$739,024	\$144,917	\$14,056,949	-5.83%	-9.40%		
Del Mar Union	620	\$1,069,811	\$386,230	\$239,462,600	333	\$967,033	\$268,591	\$134,295,500	-19.35%	-9.61%		
Encinitas Union	725	\$825,831	\$196,228	\$142,265,300	478	\$693,810	\$138,121	\$99,032,757	-1.10%	-15.99%		
Rancho Santa Fe	113	\$3,012,161	\$709,300	\$80,150,900	51	\$2,676,710	\$109,665	\$8,334,540	-32.74%	-11.14%		
Solana Beach	566	\$1,264,531	\$919,381	\$520,369,646	312	\$1,053,204	\$153,365	\$71,774,820	-17.31%	-16.71%		
Carlsbad Unified	899	\$629,171	\$121,364	\$109,106,236	586	\$522,287	\$83,139	\$73,079,181	-2.22%	-16.99%		

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# *The* FISCAL REPORT *an informational update*

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Volume 29

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No. 22

## September Revenues Fall Short \$810 Million

The Department of Finance (DOF) reported that state General Fund revenues for the key month of September were short of projections by \$810 million, with the biggest deficit in the personal income tax. Coupling the 2008-09 year-end deficit with the 2009-10 year-to-date shortfall of \$948 million, General Fund revenues are off almost \$1.9 billion from the budgeted level.

The October *Finance Bulletin* shows state revenues through the month of September, which is an important month for revenue collections because quarterly prepayments are due for corporate and individual income tax filers. The report includes a \$3 billion downward adjustment, which was not part of the Governor's May Revision, but was nevertheless included in the final Budget agreement. This downward adjustment, however, has not been distributed to the individual taxes, making it difficult to gauge the strength or weakness of each tax.

The *Finance Bulletin* shows that the personal income tax shortfall was \$1.043 billion in September, or 19.4% from what was forecast at the May Revision. After adjusting for the post-May Revision \$3 billion reduction, we estimate the personal income tax to be off about 16.5%. The DOF report indicates that the shortfall is due primarily to underperformance of nonwage income tax liabilities, such as capital gains. This tax has been notoriously difficult to accurately forecast.

The corporation tax was short \$189 million, or about 10.8%, but after distributing the \$3 billion adjustment, we estimate that this tax was off an estimated 7.7%. By comparison, the sales and use tax was essentially on target, falling short about 2% after the adjustment.

The *Finance Bulletin* reports employment data through the month of August; however, we would note that a more recent employment report was issued by the Employment Development Department (EDD) the week of October 12, 2009, which displays labor market trends through September. (See "[California's Job Losses Increase in September](#)," in the current issue of the *Fiscal Report*). The EDD report showed that California's unemployment rate dropped slightly from 12.3% in August to 12.2% in September. The number of jobs lost, however, increased from 7,200 to 39,300 over the same period.

The DOF also reported that nonresidential construction permitting was off 47% in August compared to August of 2008. Residential permitting, by comparison, was off 35% from one year ago. This development is consistent with the view of many economists that weakness in commercial real estate will be a drag on the economy even as residential construction turns the corner.

Finally, the bulletin noted that, while home prices rose statewide for the sixth consecutive month, increasing to \$292,960, the pace of sales slowed in August to 527,000 units seasonally adjusted.

—Robert Miyashiro

posted 10/19/2009

**Del Mar Union School District  
09-10 ESC Site Funding**

**Reconciliation of Positions Filled**

October 13, 2009

Site	Hired Certificated FTE	Hired Classified FTE	Certificated Dollar Value	Classified Dollar Value	Combined Purchased Staff
Ashley Falls	2.40	0.00	\$ 216,000	\$ -	\$ 216,000
Carmel Del Mar	2.00	0.00	\$ 180,000	\$ -	\$ 180,000
Del Mar Heights	2.00	0.00	\$ 180,000	\$ -	\$ 180,000
Del Mar Hills	1.80	0.00	\$ 162,000	\$ -	\$ 162,000
Ocean Air	2.60	0.00	\$ 234,000	\$ -	\$ 234,000
Sage Canyon	1.85	0.50	\$ 166,500	\$ 15,000	\$ 181,500
Sycamore Ridge	2.10	0.00	\$ 189,000	\$ -	\$ 189,000
Torrey Hills	1.70	0.00	\$ 153,000	\$ -	\$ 153,000
	16.45	0.50	\$ 1,480,500	\$ 15,000	\$ 1,495,500

Site	DMSEF Deferred from 2008-09	DMSEF Check dated 4/29/2009	DMSEF Check dated 6/15/2009	DMSEF Check dated 10/13/2009	Total DMSEF Donations
Ashley Falls	\$ 72,568.80	\$ 143,431	\$ -		\$ 216,000
Carmel Del Mar	\$ 10,987.00	\$ 168,918	\$ 95		\$ 180,000
Del Mar Heights	\$ 6,575.00	\$ 173,425	\$ -		\$ 180,000
Del Mar Hills	\$ 2,600.00	\$ 143,582	\$ 1,477	\$ 14,341	\$ 162,000
Ocean Air	\$ 9,269.32	\$ 242,021	\$ 710		\$ 252,000
Sage Canyon	\$ 25,020.50	\$ 222,612	\$ 3,045	\$ (3,045)	\$ 247,633
Sycamore Ridge	\$ 49,325.00	\$ 139,675	\$ -		\$ 189,000
Torrey Hills	\$ 29,641.14	\$ 115,879	\$ 26,388	\$ 8,092	\$ 180,000
	\$ 205,986.76	\$ 1,349,543	\$ 31,715	\$ 19,388	\$ 1,606,633

Site	Balance
Ashley Falls	\$ -
Carmel Del Mar	\$ -
Del Mar Heights	\$ -
Del Mar Hills	\$ -
Ocean Air	\$ 18,000
Sage Canyon	\$ 66,133
Sycamore Ridge	\$ -
Torrey Hills	\$ 27,000
	\$ 111,133

# DMSEF

Update #1

October 2009

Have you made your donation yet? If you have, Thank You! Our deadline for donations is February 15, 2010. Our goal? \$2 million dollars and 100% participation. With the new donation deadline of February 15th, we are able to give the district a clear picture of how we can support our Extended Studies Curriculum (ESC) programs and, as a result, the district is able to minimize layoffs.

**[Click Here to Donate Now](#)**

To date we have received \$200,000 with approximately 15% participation. Without your support our ESC programs are in jeopardy of being cut.

Mark your calendars:

November 16th The Phone a Thon. 6 - 8 p.m. Parent Volunteers will be helping us call families in the district. Please help support our district by donating generously to the ESC programs. (Music, Art, Science, Technology and P.E.)

To learn more please visit our website at [delmarkids.org](http://delmarkids.org)

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**DEL MAR UNION SCHOOL DISTRICT**  
Budget Committee Committee

Meeting Schedule

<b>Month</b>	<b>Date</b>
October	Thursday, October 22, 2009
November	Thursday, November 19, 2009
December	NO MEETING
January	Thursday, January 21, 2010
February	Thursday, February 18, 2010
March	Thursday, March 18, 2010