INTEROFFICE CORRESPONDENCE
Los Angeles Unified School District
Independent Analysis Unit

DRAFT INFORMATIVE

TO: Members, Board of Education
Vivian Ekchian, Interim Superintendent

DATE: February 28, 2018

FROM: Glenn Daley, Director, Independent Analysis Unit
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SUBJECT: **USES OF DISCRETIONARY IRREGULARLY OCCURRING FUNDS**

SUMMARY

This informative is one in a series of reports by the Independent Analysis Unit on budget-related topics. This report reviews a range of uses for discretionary irregularly occurring funds such as the **mandated cost reimbursements** included in the governor's budget for FY 2019, and provides decision-making guidance for budget development. The IAU uses an estimate here of $140 million for the reimbursement for FY 2019, although **the state's improving budget status may substantially increase the funds available to L.A. Unified**. The framework we describe does not depend on that estimate. These considerations can be useful even if the amount of similar funding turns out to be much larger or smaller, now or in the future.

Increased funding from the state such as increases in LCFF can be used in a variety of ways that create new ongoing budget obligations. Examples of such initiatives might include expansion to universal transitional kindergarten, expansion of after-school, summer, and Saturday enrichment programs, enhancement of school security, increasing maintenance workers, class size reduction in selected grades, and various ways to increase total compensation. Each of these involves creating an ongoing budget obligation with an indefinite lifespan. These are appropriate to consider when funding levels are increased in a somewhat permanent manner.

In contrast, the mandated cost reimbursements do not carry an assurance that they will be repeated. Indeed, the Legislative Analyst's Office recommends that a district's acceptance of these funds would mean waiving the balance of such costs remaining to be reimbursed in the future.[1] Although mandated costs occur regularly, the amount and timing of reimbursements for them depend on the Governor's and legislature's decisions and are less predictable. This presents

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[1] Legislative Analyst's Office (2018). Proposition 98 Education Analysis. Retrieved from http://www.lao.ca.gov/Publications/Report/3741

a different budgeting challenge from more consistent funding sources such as LCFF. It is best to avoid using cost reimbursements to create new permanent obligations for payment out of future general funds.

That guidance is not as restricting as it might sound. The District faces many unmet needs, and not all of them require permanent budget obligations to be addressed. The existence of funds such as this reimbursement, without strings attached, gives the District an opportunity to accomplish one or more goals in the short to medium term, which may have an enduring impact even without perpetual funding.

This report is not about what to do with increases in funding flows that are expected to continue into the future. The IAU is examining a variety of budget issues and will provide additional reports on District revenues and expenses on an ongoing basis. **This report is about what to do with discretionary funds that do not involve a continuing budget increase**.

We describe five general strategies for the use of such funds, and give examples of each:

Strategy	Examples
Strategy 1: Pay down debt or fund liabilities	One-time OPEB or Supplemental Pension Fund payment
Strategy 2: Save	Reinforce operating reserves
Strategy 3: Spend to improve student outcomes	Curriculum rollouts, digital textbooks
Strategy 4: Invest in enhancing revenue	Increase attendance or enrollment, develop underutilized property, expand legislative advocacy activities
Strategy 5: Invest to transform	Invest for financial return, then spend over time on an innovative school improvement initiative in selected high-need schools

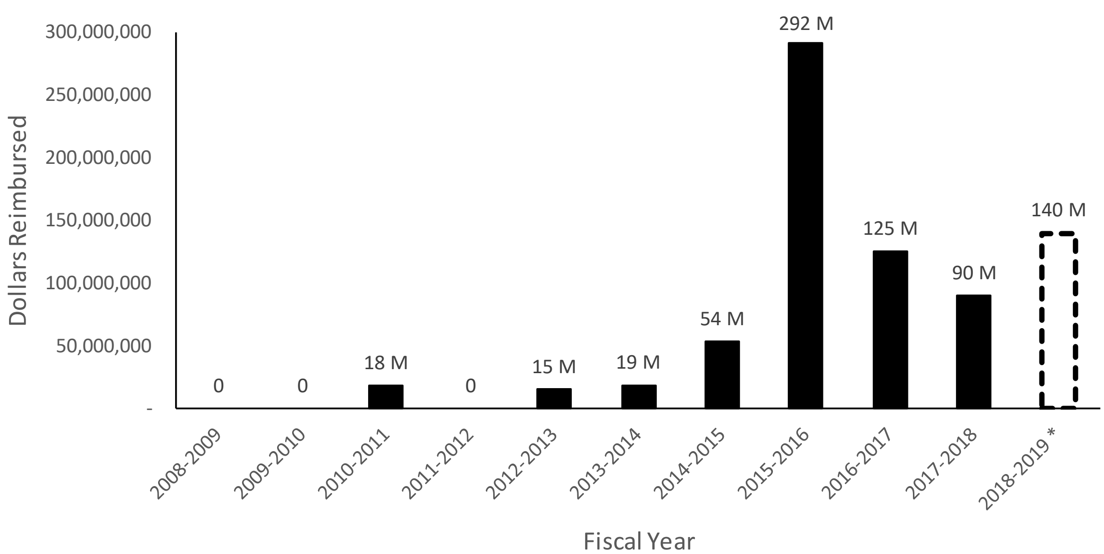
All five of these strategies have reasons to support them under certain conditions. All five involve tradeoffs, since it is not possible to do everything at once. The discussion in this report is intended to stimulate further thought and analysis of the possibilities, and not to recommend a final decision. However, we do urge careful consideration of strategy 5, invest to transform, as a creative way to use this funding opportunity to support a focused initiative — a “Marshall Plan” or “surge” — to make a meaningful difference in transforming a selected set of high-need schools.

BACKGROUND

The Governor's budget for FY 2019 contains good news for California schools. Due to increased income and property tax revenue, next year's education budget is over $3 billion higher than this year's, and discussions in Sacramento suggest that this number may go even higher. The Governor's budget proposal uses some of this money to accelerate funding of the Local Control Funding Formula (LCFF). In addition, nearly $2 billion previously allocated by the state for discretionary spending and programs that have expired is currently unassigned. The Governor has proposed to use this amount for "discretionary grants that support local needs and priorities" as well as reimbursing existing debt of districts for mandated costs. L.A. Unified stands to receive about $140 million in these payments ($295 per ADA, according to School Services of California[2]). This money will probably become available in the District's FY 2019 budget.

These special funds are above and beyond the "regular" income stream that flows—more or less dependably—from the state to the District every year under the Proposition 98 guarantee and the Local Control Funding Formula. The District often receives reimbursements and other irregularly occurring funds, but their amount differs from year to year. (See Figure 1.) They also may have strings attached depending on legislative priorities.

Figure 1. State Mandated Cost Reimbursements to L.A. Unified, 2009-2019



** Anticipated*
Note. Data were drawn from LAUSD Unaudited Actual reports through 2016-2017 and First Interim Report for 2017-2018. Projection for 2018-2019 was based on School Services of California (2018).

[2] School Services of California. (2018). Special Fiscal Report: Governor's Proposals for the 2018-19 State Budget and K-12 Education (Fiscal Report No. 1, Vol. 38). Retrieved from https://www.sscal.com/fiscal_reports.cfm.

Unlike the increases in LCFF funding in recent and current years, mandated cost reimbursements should be viewed as irregularly occurring rather than recurring, even though there are likely to be similar funding streams from time to time in the future. And these funds are discretionary, unlike categorical funds and most LCFF funds. The county or the legislature may indicate their priorities, but it is likely that the District will have broad latitude in how it chooses to use these funds.

Is $140 million in one year a small number or a large number? In the context of the District as a whole, it is a small number, representing about two percent of the overall District budget. However, to a school or a selected group of schools, it is a large number. The recent ACLU/CoCo settlement was **$172 million**, enough to give an additional $1 million a year to each of 50 secondary schools over the next three years. Another comparable amount is the cumulative **$85 million** donation made by Richard and Melanie Lundquist, which was used to create and support the Partnership for Los Angeles Schools (PLAS) and amounts to about $650 per student annually for 10 years.

Another way to look at the amount of money is that $140 million is enough to completely fund 10 comprehensive high schools or 28 elementary schools for one year. If invested and used over a 10-year period, it could produce a steady cash flow of $17 million per year or more, depending on the rate of return. This could provide an infusion of about **$330,000 annually for 10 years to each of about 50 priority schools**, over and above their existing budgets.

In deciding how to utilize these funds, the Board can look for guidance to District policy, the Superintendents strategic plan, the Local Control Accountability Plan (LCAP), and recommendations of the Instructional Technology Initiative Task Force (ITITF), the L.A. Unified Advisory Task Force and the Independent Financial Review Panel. In this informative, the IAU suggests some additional considerations and possibilities.

FROM OPPORTUNITY TO STRATEGY

Advice varies about what an *individual* should do upon receiving a sudden windfall of money from an inheritance, a settlement or a gift. Common personal finance advice is to pay down high-interest debt but not necessarily low-interest debt, invest in a way that balances risk and rate of return depending on the age and goals of the individual, or spend the money on a durable asset or a memorable experience. The one thing that is not recommended is to make permanent and costly changes to one’s lifestyle.

For a *business, nonprofit, or government agency*, the options are to reduce high-interest debts, to invest in a financial market, or best of all to invest in the organization’s activities with the expectation of making profits or achieving goals. The one thing that is not recommended is to increase spending in a way that creates long-term commitments unless there is a plan to pay for them out of expected future revenues.

For L.A. Unified, **paying down debt** would mean offsetting long-term liabilities—most likely making a large payment to the OPEB trust or the Supplemental Pension Set-aside/Reserve Fund. But the District's debts are not high-interest consumer debts and the amount they would decrease by applying the discretionary funds to them would be negligible given their size. Further, paying into trust funds for this kind of debt can backfire if unexpected needs or costs come up, since the money cannot be retrieved and repurposed for general expenditures.

For L.A. Unified, **saving** would mean increasing the reserves in the health and welfare fund, the worker's compensation fund, the liability self-insurance fund, or operating reserves (unassigned fund balance) to meet the five percent Minimum Reserve Threshold, which is the official policy of the District regarding reserves. All of these types of savings would help ensure against unexpected costs or decreases in revenue.

Using irregularly occurring funds in this way has its downsides too. One disadvantage of saving is psychological. Putting the funds into these reserves might temporarily relieve the pressure to take action to bring the District's revenues and expenditures into balance. In addition, saving has opportunity costs. By saving, the District may miss a timely opportunity to achieve one or more of its goals by spending strategically on assets or activities with positive outcomes for schools and students.

Thus, **spending** the funds on durable assets or short-term activities that promote the District's goals and improve student outcomes is an option to consider. But how to spend them is the question. District policy prohibits spending non-recurring funds on recurring costs such as salaries that require permanent sources of revenue[3], so using these funds to create obligations for ongoing costs does not appear to be an option, although there may be exceptions worth considering. The District can spend non-recurring funds on durable goods or services that can be paid for in one budget cycle. If there is strategic value in such an expenditure, it may be worth considering.

Another option is that the funds can be **invested**, by which we mean putting the money to use to generate new revenue as a return on the investment. For the District, investing might mean taking actions that would improve attendance or increase enrollment—thus increasing state and Federal revenue. It might also mean acquiring new assets or improving existing assets that can be

[3] District policy states that, to the extent feasible, non-recurring, or "one-time" revenues will be applied toward non-recurring expenditures. By definition, non-recurring revenues cannot be relied on in future budget periods. This policy on the use of non-recurring revenues provides guidance to minimize disruptive effects on services due to non-recurrence of these sources. The Chief Financial Officer shall be responsible for identifying one-time revenues and expenditures and for making recommendations regarding their use. (Source: LAUSD Budget and Finance Policy, approved by the BOE November 12, 2013.) **The IAU suggests revisiting the language of this policy** to provide more flexibility. It is important to account for the possibility that some revenues classified as non-recurring may actually be part of a mixed stream of funds with only slightly less predictability than so-called recurring funds.

used to generate revenue. Or it might mean funding a much larger effort to advocate for legislative and policy changes that would mean more revenue to the District in the future.

Finally, it is possible **to combine investing and spending in such a way as to fund a transformative initiative** over a predetermined period of time. One example of such an initiative would be to select a number of high-need schools for intensive support and partnership. Rather than spending the funds all at once, or setting them aside as savings or debt reduction, this approach would schedule the use of the funds, plus a financial return, over a period such as 10 or 20 years. Because the funds are discretionary, this creates an opportunity for the District and these schools to do something more innovative and transformational than might be allowed with categorical funds.

Deciding between these five strategies is a matter of assessing the tradeoffs involved in each option. Perhaps the most important consideration is the impact of the choice on the District's goals, not just in the period during which the funds are used, but in the long term. In considering this impact, the Board should ask, for each strategy, **whether the amount of discretionary funding is sufficient to make a lasting difference**.

It is easy to use new funds to do simply more of the usual activities or to spread the funds so thinly across a range of programs that none of them really lead to changes beyond the status quo. In contrast, receiving discretionary irregularly occurring funds presents an opportunity to do something different, something more focused, and something that might not happen without the catalyst of these funds.

So the most meaningful dimensions on which to evaluate this choice are not whether the funds and spending objects are recurring or non-recurring. The more important questions are whether the use of the funds is **strategic, enduring, and transformational**. In the following sections, we describe a number of options that appear to fit these criteria, some to a greater extent than others. These suggestions are intended to stimulate discussion, and do not constitute an exhaustive list. We finish with a suggestion that may be the most enduring and transformational of all.

STRATEGY 1: PAY DOWN DEBT/PREFUND LIABILITIES

According to the LAO Proposition 98 Outlook report from November, 2017, some districts in the past have used non-recurring allocations to pay down pension and other post-employment benefit (OPEB) liabilities. Along those lines, L.A. Unified could use the $140 million to make a **one-time OPEB trust payment.** Using $140 million to offset the OPEB liability would reduce the unfunded liability from $13.6 billion to $13.5 billion (using 2015 figures for the liability; the 2017 actuarial report is under review but appears to show a liability over $15 billion). Although there is currently no specific target for a funded ratio, if the target were 70%, this additional payment would reduce the target amount from $9.6 billion to $9.5 billion—a one percent reduction—and reduce the annual amount the District would have to prefund or save by about six million a year over 30 years (see Table 1).

Table 1. Details of strategy aimed at achieving 70% pre-funding of OPEB liability (dollars in millions)

	Current level of pre-funding without one-time payment	**Current level of pre-funding with one-time payment**
OPEB liability (2015)	$13,649	$13,649
Minus one-time payment		$140
70% of OPEB liability (pre-funding target)	$9,554	$9, 456
Currently budgeted pre-funding	$101/yr	$101/yr
Remaining balance of pre-funding target	$7,947	$7,849
Additional pre-funding and/or cost reductions needed to reach target	$499/yr	$493/yr

Note. Source for OPEB liability figure is the 2015 Actuarial Report; calculations from the IAU. See IAU Board Informative - Health and Welfare, 2017-11-17.

Offsetting liabilities in this way is low-risk, feasible, and consistent with the District's Budget and Finance Policy, Principle II, which includes prudent debt management. Other than that, however, making a payment to the OPEB trust is a relatively low-leverage strategy because by itself it would make little difference on the unfunded OPEB liability. Meaningful progress towards pre-funding the liability would still require a combination of cost reduction and additional set-asides of $493 million a year. Furthermore, offsetting the liability using the discretionary funds would preclude using these funds to pay for goods or activities that could yield immediate returns in terms of improved educational outcomes.

STRATEGY 2: SAVE

Another viable strategy for the use of these funds is to add them to the general fund, in effect saving them for current or future requirements. Sometimes doing nothing is a good idea because it leaves options open. In fact, it is the default option. Here, doing nothing means leaving the funds unassigned, which would in effect result in a **contribution of $140 million to operating reserves.**

Reserves are the portion of the general fund balance that is set aside to hedge against risk. L.A. Unified's policy is to maintain a 5% Minimum Reserve Threshold. In the last few years, the District has maintained that threshold, which is an indication that the organization's budget is balanced on a year-to-year basis. However, District reserves are projected to decline in the next few years because of a widening imbalance between revenue and expenditures. If the Board opts to play safe, this option would increase the reserves in 2018-2019 by 1.91% to 9.16% of revenue.

As shown in Table 2, in 2015-2016, the District's reserve balance (as stated in the original budget for that year) was 4.61% of total planned expenditures. In that year, the District's revenues, expenditures and other financing sources/uses summed to a positive balance, so the reserves remained untouched. In the next four budget years, however, expenditures were or are projected to be higher than income, which requires tapping into the reserves or adjusting revenues and/or expenditures to ensure that the ending balances are positive. Nevertheless, despite this shortfall, the total ending balances will remain above 5% until 2018-2019 and dip below that amount in 2019-2020 under the latest budget projections (which do not include full LCFF funding as announced by the Governor). By adding full LCFF funding, plus $140 million unassigned to the budget in 2018-2019, the 2019-2020 ending balance also remains about 5%. The 2020-2021 reserve likely falls below the threshold.

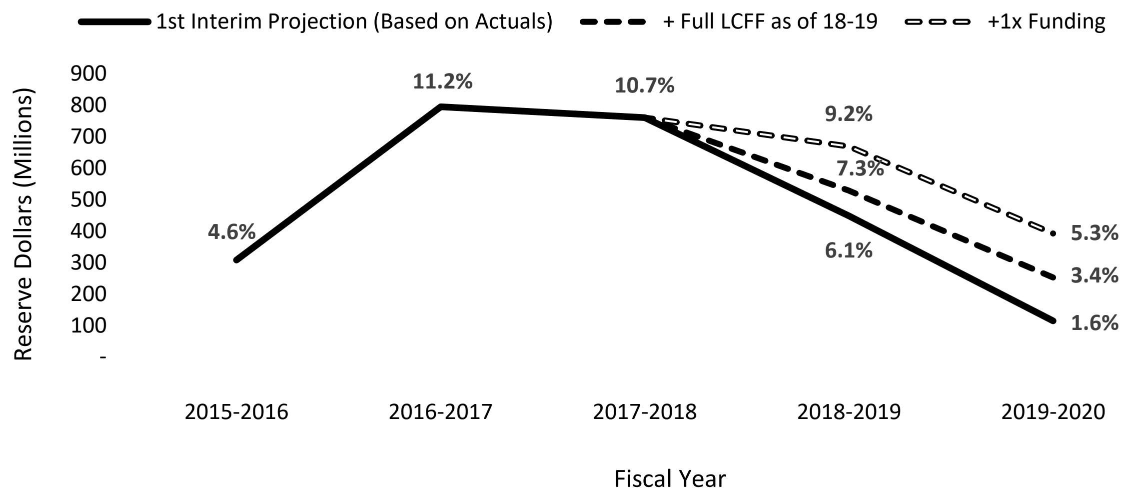
Table 2. L.A. Unified Year-End Reserve Balance 2015-2020 (dollars in millions)

	2015-2016	2016-2017	2017-2018	2018-2019	2019-2020
Original Reserve balance	308	795	761	448	114
Balance as % of expenditures	4.61%	11.20%	10.67%	6.14%	1.55%
+Full LCFF ($219 M over 2 yrs)				529	252
Balance as % of expenditures				7.25%	3.42%
+One-time funding ($140 M)				669	392
Balance as % of expenditures				9.16%	5.32%

Note. Data for the Original Reserve Balance were drawn from the following reports: For FYs 2016 and 2017, figures were retrieved from their respective LAUSD Unaudited Actual reports. Data for FYs 2018, 2019, and 2020 were drawn from the 2017-2018 LAUSD 1st Interim Financial Report. Other figures were generated by adding amounts derived by the IAU’s calculations of full LCFF funding and the LAUSD share of state surplus funding/reimbursements to existing LAUSD projections.

Figure 2 illustrates this reserve trend in graphical form. The solid line represents the actual reserve balance as of FY 2017 and projections from FY 2018 to FY 2020 as of the first interim report in FY 2018. The middle dotted line represents the effect of full LCFF funding as anticipated in the Governor’s budget. The upper dotted line represents this same balance plus $140 million non-recurring funds.

Figure 2. L.A. Unified Year-End Reserve Balance 2015-2018



Note. Data for the Year-End Reserve Balance were drawn from the following reports: For FYs 2016 and 2017, figures were retrieved from their respective LAUSD Unaudited Actual reports. Data for FYs 2018, 2019, and 2020 were drawn from the 2017-2018 LAUSD 1st Interim Financial Report. Other figures were generated by adding amounts derived by the IAU's calculations of full LCFF funding and the LAUSD share of one-time (1x) state surplus funding to existing LAUSD projections.

Thus, adding to the reserve would maintain the balance in the budget for a year longer, which could be a good decision if the District expected revenues to rise within two years or if the District planned cost reductions phased in over two years, because it would diminish the extent to which the District would be forced to balance the budget through more dramatic measures such as increased class-sizes, closed programs, or other dramatic stabilization measures. However, it might not be the optimal use of such funds if there are opportunities to use the funds in more strategic ways.

STRATEGY 3: SPEND ON GOALS

The third strategy entails making a strategic decision to spend the money on specific goods or activities that provide some value to the District, *i.e.* contribute to specific goals.

Spending can be recurring or non-recurring. Recurring program spending includes hiring new long-term staff or entering into long-term contracts. However, government finance authorities (including Los Angeles County Office of Education and L.A. Unified staff) do not recommend spending non-recurring money this way simply because, after the initial expenditure that comes from such revenue, permanent sources of money must be found to continue the program or contract. Determining the appropriate one-time expense with the greatest leverage for accomplishing the mission of the District is the challenge.

The governor's budget envisions non-recurring expenditures to include *content standards implementation, technology, professional development, induction programs, deferred* *maintenance, and employee benefits*. Examples of the goods and services that L.A Unified might purchase legitimately as non-recurring expenditures are:

- Instructional materials, textbooks
- Limited-term professional development
- Contract staff, such as coaches, consultants
- Promotional or administrative materials for schools and school facilities
- One-time start-up costs of programs intended to be self-sustaining

Criteria for Evaluating Options for Spending Non-Recurring Funds

If the decision is made to spend the non-recurring discretionary funds, rather than pay down debt or save, the next step is to assess spending options. The following three criteria are useful for evaluation:

1. Risks/Rewards
2. Tradeoffs/Priorities
3. Principles/Goals/Mission/Policies/Regulations

First, any expense the District chooses to incur with special non-recurring funds carries **risks and uncertainties as well as potential rewards**, which must be considered together and balanced. Sometimes, risks of failure and squandered resources are high, but the benefits of success would make the risk worthwhile. On the other hand, an option with high potential rewards is less attractive if it is less feasible considering District capabilities and possible resistance to change.

Second, whether explicit or not, **all spending options come with tradeoffs**. At L.A. Unified, resources are scarce and the District will need to assess its priorities and make decisions accordingly. If it decides, for example, to pay staff bonuses, it is deciding that other expenditures are lower priorities. Whether it is obvious or not, these tradeoffs are found in every budget.

Third, spending plans also can be evaluated in terms of how and whether they align with stated **principles, goals or the overall mission of the District.** Also, the District may have instituted certain policies or be required to follow federal, state or country regulations. If spending plans do achieve goals as stated in the strategic plan, Local Control Accountability Plan, Instructional Technology Task Force, L.A. Unified Advisory Task Force or Independent Financial Review Panel recommendations, or follow regulations, then the importance of the goal or need to adhere to regulations compared to other goals should be considered: How *critical* is any given activity to the mission of the District? How should any one expenditure be prioritized over another?

Another consideration is whether a potential expenditure might be made using other, already existing funds such as bond proceeds. Expenses paid from other revenue streams include:

- Facilities
- Information technology assets and projects
- Career Technical Education

Since these activities are funded through other sources, spending the funds received through mandated cost reimbursements on these activities runs the risk of being duplicative. On the other hand, if these programs need supplementary funding for non-recurring activities, use of the new money may be warranted.

Finally, the Board can consider prior uses of non-recurring funds. The District has frequently received non-recurring allocations from the state. Discretionary funds categorized as mandated cost reimbursements appeared in four of the last five budgets and ranged from $15 million in FY 2013 to $137 million in FY 2017. Another consideration is that mandated cost reimbursement was not reflected in the FY 2018 budget because funds were not made available for the current year. However, funds allocated in last year's California state budget are slated to be disbursed in May 2019. Thus, they can be included in the 2018-2019 budget and will likely contribute to the beginning balance in the 2019-2020 budget (see Board report from June 20, 2017).

Examples of Spending

This section includes a number of examples of uses for discretionary non-recurring revenue from the state. **The purpose is not to recommend a particular use, but to model how the Board can evaluate potential uses** in terms of the criteria discussed above. Other strategic initiatives or expenditures not mentioned here could be evaluated in a similar way.

NGSS science curriculum roll-out

The State Board of Education will adopt new science materials for use with NGSS science curricula in November 2018. Non-recurring funds could be assigned to purchase new science materials, relieving pressure on the Books and Supplies resource in the General Fund.

- Risks/Rewards: Minimal uptake of resources.
- Tradeoffs/Priorities: NGSS materials are already budgeted; using the non-recurring funds to pay for them means being able to use the previously budgeted funds for something else.
- Alignment with Policies/Goals: State policy adopted in 2013-14 includes high quality science instruction. District goals include proficiency for all and 100% graduation.

Social studies curriculum roll-out

Social studies is the last primary content area to change in response to Common Core State Standards. But in July 2016, the State Board of Education adopted a new History–Social Science Framework for kindergarten through grade 12. The revised framework includes new content emphases. Course descriptions for the four major high school courses and the various suggested electives have been completely rewritten. A new emphasis on literacy development includes explicit linkages to the *California Common Core State Standards for English Language Arts and Literacy in History/Social Studies, Science, and Technical Subjects;* the *English Language Arts/English Language Development Framework;* and the *California English Language Development Standards.* This collaborative emphasis between language arts and history/social science instruction has potential for improving English Language Arts proficiency and could possibly benefit from a one-time expenditure on new instructional materials and teacher professional development. Primarily middle and high school student outcomes stand to improve with an effective use of the new framework.

- Risks/Rewards: Effective rollout of new curricula requires change management as well as adequate funding. The improvement over status quo is potentially large, but may take several years to be realized; successful implementation is uncertain.
- Tradeoffs/Priorities: Though NGSS materials are already budgeted, social studies is relatively neglected as an instructional priority. Spending on this area means not spending on other instructional or management priorities.
- Alignment with Policies/Goals: State policy adopted in 2016 includes high quality social studies instruction. District goals include proficiency for all and 100% graduation.

Digital content

The Division of Instruction is actively exploring the implementation of digital content in conjunction with the District's Learning Management System (LMS), called Schoology. Non-recurring funds might be useful to fund pilot programs that explore ways to bring down instructional materials, reproduction and textbook costs.

- Risks/Rewards: Impractical or unpopular digital content might not effectively supplant textbooks. There might be hidden costs; it might require expensive hardware or not be truly cost-effective.
- Tradeoffs/Priorities: Funds might be used on more traditional and reliable instructional materials with lower risks but achieve lower efficiencies.
- Alignment with Policies/Goals: There are potential cost savings. Proficiency for all and 100% graduation are objectives in the strategic plan and LCAP.

IT professional development

Although certain information technology exenditures are funded from bond proceeds, professional development is not. The ITI Task Force Recommendation 5 calls for more professional learning related to the use of Schoology and other learning technologies. Parent access to PASSport and District dashboards is not evenly distributed across schools and Board districts. Funds could be used to promote use of these tools among teachers or to provide training and outreach to reach more parents. Some factors to consider in spending discretionary funds on IT professional development are:

- Risks/Rewards: PD can be essential to ensure that investments in systems are not squandered by misuse or lack of use of the systems. However, PD can be ineffective, may meet resistance from users, or could create demand for ongoing support that is not sustainable.
- Tradeoffs/Priorities: Spending on this area means not spending on other instructional or management priorities.
- Alignment with Policies/Goals: ITI Task Force Recommendation #5 is to deliver professional learning. Better use of instructional technology can enhance parent, community and student engagement and promote proficiency for all objectives in the strategic plan, as well as goals #2 (proficiency) & #4 (parent engagement) in the LCAP.

External evaluation

Currently the District is conducting a large number of innovative programs and instructional models such as dual language immersion, the UCLA Community School, Pilot Schools, after school programs, credit recovery programs, foster youth support services and programs, and attendence initiatives. However, the quality of implementation and the cost-effectiveness of many of these programs are not well established. In order to facilitate bringing successful programs to scale, high-quality, objective—and preferably independent—program monitoring and evalution is needed.

- Risks/Rewards: Evaluations can vary in quality and are often not taken seriously as formative. On the other hand, $140 million could buy a lot of high-quality evaluation.
- Tradeoffs/Priorities: This would mean not using the funds for durable goods that directly benefit instruction. The return is uncertain.
- Alignment with Policies/Goals: Properly done, evaluation supports high caliber principals, teachers, schools, and programs. It promotes excellence and high expectations for objectives in the strategic plan and LCAP.

STRATEGY 4: INVEST

Any spending can be evaluated in terms of its potential return, whether defined as financial return or accomplishment of mission and goals. But given the imbalance between the District's current and projected revenue, which is leveling off, and its expenditures, which are growing, it is particularly worthwhile to **consider spending that can increase future revenue**. Spending that produces financial returns includes purchasing assets that can be leased, licensed or sold at a profit. It also includes spending on programs or activities that increase enrollment or attendance, which is linked to District revenue. Using the money to fund one-time startup costs for an activity that will generate its own source of revenue is another example of an investment. In any case, the goal would be to use non-recurring money to initiate a self-sustaining process.

Examples of Investing

Increase attendance or enrollment

Increasing the number of students who attend class is the most direct way to spend windfall funds to enhance revenue since any increase in ADA would raise income. Programs to increase the students who attend District schools can be focused on attendance, traditional K-12 enrollment, or non-traditional enrollment.

Programs to increase attendance have been recommended by the L.A. Unified Advisory Task Force. The District-wide awareness effort to educate parents, students, and the community about the importance of attending school that is currently underway could be extended or enhanced if it is determined that it positively influences the attendance rate. The Advisory Task Force estimated that at least $20 million more annually could be generated from the state if the proportion of chronically absent students could be reduced from about 14% to below 11%.

Further analysis is needed to identify the attendance-focused interventions that work, to understand how much revenue they can generate, and to assess whether their cost justifies their benefit. In this analysis, it is important to consider that **improving attendance is good not just for bringing more money to the District and schools; it benefits students directly and profoundly.** Thus, expenditures that help the District meet its goals may be justified, but evaluation of attendance programs to determine the most effective approaches is still important.

Outreach to communities, including efforts to enhance how schools present themselves to their neighborhoods, has the potential to attract new students to certain schools. Funding to schools for outreach efforts could be accomplished via a competitive grant program to make efficient use of scarce resources. The District's Education Technology Grant Program is an example of how such a program could work.

One non-traditional enrollment-increasing strategy is to **increase enrollment in the District's transitional kindergarten (TK) program**. Given that L.A. Unified's early childhood education (ECE) programs enroll fewer students than are enrolled in kindergarten, a potential market exists for raising enrollment in TK. Further, TK programs are a way to connect with families and engage children in schooling early in life, with likely dividends in later years, both in student outcomes and in continuing enrollment in District schools. Students who are enrolled in the TK program draw funds from the state based on ADA, though students who are in the expanded transitional kindergarten (ETK) do not generate the same level of funding. Further analysis is needed to understand exactly how much additional state revenue would be generated from increasing TK enrollment and how much it would cost the District. In addition, it would be important to conduct a market analysis to determine how many more four-year-olds are available and interested in attending a TK program in Los Angeles.

Employee health and wellness initiatives

Another way to think about investment is to invest in employee health and wellness programs to bring down health care costs. These programs are generally of two types: *lifestyle management* and *disease management*. Research shows that lifestyle management programs have a limited ability to lower health care costs, but the ones that work reduce unhealthy behaviors, which, along with health risks, are directly related to elevated health care costs. These unhealthy behaviors and health risks include inadequate physical activity, smoking, obesity, diabetes, and high blood pressure. Each of these risks is associated with $700 to $2,000 in additional annual health care costs per employee.

Though lifestyle management-type wellness programs can reduce healthcare costs in a group of employees, a more effective way of bringing down costs is to implement a disease management program to reduce actual healthcare claims and thereby lower insurance premiums. This type of program is designed to prevent at-risk employees from becoming ill and help chronically ill employees stabilize their conditions.

Generally speaking, a disease management program at L.A. Unified would entail reviewing demographic characteristics and health care use and expenditures to identify individuals with a specific chronic disease, such as asthma, diabetes, congestive heart failure, coronary heart disease, end-stage renal disease, depression, high-risk pregnancy, hypertension, or arthritis. Next, L.A. Unified would coordinate with healthcare providers to provide program enrollees access to multidisciplinary teams of providers, including physicians, nurses, pharmacists, dieticians, respiratory therapists, and psychologists, to educate and help individuals manage their conditions. Disease management programs are based on the concept that individuals who are better educated about how to manage and control their condition receive better care. Counseling, home visits, 24-hour call centers, and appointment reminder systems have been used to support individuals who are managing their chronic conditions.

A recent Rand study, *Do Workplace Wellness Programs Save Employers Money?,* found that disease management programs at Fortune 100 companies were able to deliver $136 in savings per member, per month, and a 30% reduction in hospital admissions.[4]

The mandated cost reimbursement funds would not be available to fund such a wellness program on an ongoing basis, but they could be used as start-up funds to initiate a program that would bring returns to the District over time and more than pay for itself.

[4] Retrieved from https://www.rand.org/content/dam/rand/pubs/research_briefs/RB9700/RB9744/RAND_RB9744.pdf

Start up costs associated with the use of underutilized property assets to generate revenue

In March 2017, the Facilities Division made a presentation to the Board regarding the use of underutilized property to address District goals. A number of ways were identified to monetize assets, but the approach that Facilities recommended was partnering with private firms to develop property for commercial, residential or mixed use. Revenue generated through such projects over the long term could be substantial, and used to support District educational programs. However, the initial pursuit of these projects requires startup capital, which may be an appropriate use for non-recurring discretionary funds.

A major effort to advocate for legislative and policy changes that support the District's financial stability

The District carries out an ongoing program of political advocacy with a budget that is constrained by all the other ongoing priorities of the District. However, this is an area with potentially large positive returns relative to the cost. Winning support for higher direct funding of K-12 education is only a start; there are other areas in which the goal might be to reduce the costs faced by the District, with health care costs being the largest and most critical area of concern. Political action is also needed to secure more equitable funding for special education, and perhaps to adjust some of the terms of cost-sharing and facilities-sharing between charter schools and districts to ensure that both are adequately funded for the children they serve. Devoting a large, non-recurring discretionary inflow of funds to political advocacy for a short period of time could make the difference in winning the support of key legislators on critical issues.

STRATEGY 5: INVEST TO TRANSFORM

The first three strategies above assume that the non-recurring funds are to be spent or allocated during a single year. The fourth strategy describes a few ways to invest the money, not in financial instruments such as stocks and bonds, but as start-up capital for programs intended to generate self-sustaining revenue gains in the long run. This section describes a fifth strategy combining elements of several of the others. It involves three steps, one of which is optional.

A. Invest the funds for a financial return and schedule withdrawals from that investment over a pre-planned number of years.

This investment approach is similar in concept to an annuity. The goal would not be to preserve the invested principal in perpetuity, although that is an option. Rather, the goal would be to schedule the withdrawals over a long enough period, e.g., 10 or 20 years, to support a major initiative without relying on other funds from the District. The details of the investment would have to be structured according to California law as well as County and District fiscal policy, but under certain conditions might be counted as part of the District's operating reserves.

B. Solicit matching funds from donors.

This is optional, but if pursued it could leverage the power of the funds to accomplish much more than the District could do with its own funds alone. One good way to attract contributions would be to create and market a quasi-separate entity that would have brand name recognition while also reassuring donors that their gifts would go to a specific initiative. One example of such an entity is the Partnership for Los Angeles Schools (PLAS). Other possibilities might be networks of schools similar to Pilot Schools or affiliated charter schools. Strategy 5 could involve funding an existing entity to expand its scope to more schools, or it could be created and branded from the start as a new initiative. This decision would require careful consideration of opportunities and tradeoffs, as well as discussions with potential partners.

C. Create (or expand) a focused initiative with the potential to transform a meaningful subset of the District such as a number of carefully selected high-need schools.

Board Members sometimes talk of creating a "Marshall Plan" or "surge" to tackle the difficulties of turning around schools with long histories of low achievement. An infusion of discretionary funds could be the way to carry out such an effort, but only under certain conditions. The funds must be large enough to support a substantial agenda for change at the school level, but they must also be sustained over enough years to ensure that the change takes root in the school instead of failing for lack of continued support. With an initial amount of $140 million and careful financial management, the invest-to-transform strategy would make it possible to guarantee ongoing support for an initiative for a pre-identified number of years.

Table 3, below, shows several combinations of funding per school and project duration that could be supported with these funds. For example, the table shows that with a *conservative* average rate of return of 3.9%, and with a 1% allowance for program management and evaluation, this strategy could support an investment of **$329,758 average per school per year for 50 schools for 10 years**, with the actual amount per school varying with the number of students. This is an amount that, if well-used, could support an enduring transformation of the school. Clearly, the appropriate amount per school would depend on its size and grade span as well as other local conditions. A per-pupil allocation might make sense in many cases, and a per-pupil amount can easily be calculated from the given information. For example, over 10 years, an allocation of $650 per student per year would allow inclusion of over 26,000 students per year in the program.

In contrast, the least focused option would involve investing the funds for a perpetual return instead of drawing down the principal, and spreading the funds out to all schools in the District. This would provide a cash infusion averaging $7,083 per school or $10.75 per student per year, which would buy a few useful resources but would not be enough to support a transformational difference in student outcomes.

Table 3. Funds available per year from various investment strategies

Term	District total	Less program mgt & eval	Number of schools *(dollars per school per year)* 25	50	75	178	740
All at once	140,000,000	(5,600,000)	5,376,000	2,688,000	1,792,000	755,056	181,622
5 years	31,359,504	(1,254,380)	1,204,205	602,102	401,402	169,130	40,683
10 years	17,174,913	(686,997)	659,517	329,758	219,839	92,629	22,281
20 years	10,210,433	(408,417)	392,081	196,040	130,694	55,068	13,246
30 years	7,998,200	(319,928)	307,131	153,565	102,377	43,136	10,376
Perpetually endowed	5,460,000	(218,400)	209,664	104,832	69,888	29,447	7,083

Note. Projection by the IAU. Assumptions are that the initial fund is $140 million, the average rate of return is 3.90%, and that program management and evaluation would cost 4% of the total used per year.

The numbers in this table are based on conservative assumptions. Any matching funds contributed to the District as a result of these strategies would directly increase the number of years, the number of students and schools, and/or the amount funded per student or school. The state might choose to award substantially more funding to the District, much of which might be available to sustain ongoing programs, but some of which might fit the irregularly occurring criteria emphasized here.

Note that the same algorithms would work with many different assumptions about the beginning amount, the financial rate of return, the number and size of the schools, and the number of years. For instance, this amount could fund **a broader initiative focused on the District's 178 middle schools to dramatically improve instruction and student supports for 10 years for an average of $92,629 per school per year**.

In deciding how many schools and how many years to include in the initative, it is important to **keep the effort focused enough to make a real difference where it is implemented, yet not flood schools with resources they have no way to use effectively and efficiently** starting from their status quo. The example of 50 schools receiving an average of $329,758 per year over 10 years might be about the right balance. This is a question that should be answered in the planning stages after careful analysis, and then adhered to over time so that year-to-year expectations of support are met.

Discretionary funds are ideal for such a transformational initiative because their uses are not constrained by the rules of categorical or restricted funding sources such as Title I. The Title I guidelines can provide a starting point for more creative thinking about how to use the funds at the school level. The initiative could and should include innovative practices that traditional sources of funding might not support. Thus, this strategy represents a valuable opportunity to try something new. There should be some degree of autonomy for schools to be engaged in planning the initiative and thus contributing to decisions about spending. The District would also be free to select schools based on its own criteria and specific commitments made by schools to participate.

As mentioned above, PLAS, Pilot Schools, affiliated charter schools, or examples from other districts might serve as models for planning a transformational initiative, although careful evaluations of their implementation and outcomes would be necessary before choosing a model. Since its formation in 2007, PLAS has refined its model of school support to focus on building school capacity to create and sustain long-term change. Its approach has five critical components: a) work with the District to achieve change in low-performing schools and gain insight into changes the District can make to better support such schools, b) use funds to supplement existing district supports and resources and address gaps when needed, at the overall annual cost of about $650 per pupil, c) focus on school leaders, teachers, and engaged parents and community partners to ensure that each group is working effectively to improve student achievement, d) make schools and classrooms restorative communities to create a school culture and environment conducive to academic achievement, and e) model the actions needed district-wide to illuminate barriers to success and illustrate what is possible in other schools. A focused initiative funded by the invest-to-transform strategy might use some of these principles of school support and change whether or not modeled directly on PLAS.

CONCLUSION

This informative has provided an overview of uses for discretionary irregularly occurring funds expected from the state legislature for FY 2019. These uses are categorized as paying off debt, saving, spending on educational goals, and investing in revenue enhancing initiatives, with a fifth strategy we call invest-to-transform. These strategies are outlined below, in Table 4. Good arguments can be made for each of these options. The Board or the Superintendent may also develop different ideas or suggestions, which can be evaluated using the framework discussed in this report.

Table 4. Strategies and examples for the use of irregularly occurring funds

Strategy	Examples
Strategy 1: Pay down debt	One-time OPEB or Supplemental Pension Fund payment
Strategy 2: Save	Reinforce operating reserves
Strategy 3: Spend	IT professional development NGSS science curriculum rollout Social studies curriculum rollout Digital textbooks External evaluation
Strategy 4: Invest	Increase attendance or enrollment Employee health and wellness Developing underutilized property
Strategy 5: Invest-to-transform	Invest for financial return, then spend over time on an innovative school improvement initiative in selected high-need schools

To decide between paying down debt, saving, spending, and investing, the Board should consider the amount of money expected, and ask whether it can have a meaningful impact relative to the size of the problem. For example, $140 million could have a relatively small effect on the OPEB liability or add one year of cushion to the operating reserve for the General Fund. On the other hand, perhaps $140 million is the perfect amount to completely fund the rollout of a new secondary social studies curriculum or evaluate a dozen District educational programs. Perhaps the funds can effectively catalyze change by kick-starting school-based community outreach programs or transform instruction by increasing teacher uptake of technology.

These funds might also be the right size to make investments in projects with financial returns, such as joint occupancy developments that generate new revenues, disease-management programs that produce costs savings, or an intensive program of legislative and policy advocacy that could both increase revenues and reduce costs. Such uses of special funds would be high-leverage because their effects could be potentially multiplied many times over. Using these funds on start-up costs of programs is justified if the net returns are expected to be positive, and especially if the programs are designed to be self-sustaining once established.

Finally, using the invest-to-transform strategy, these funds could provide over $300,000 per year per school to 50 schools or $650 per year per student to 26,000 students for 10 years (or some other equivalent combination) to fund a strategic initiative to transform long-term struggling schools.

Overall, the most important consideration for deciding how to allocate this money may be whether the choice is strategic or opportunistic: Does the proposed use of funds advance the goals and priorities of the District in an enduring, transformative way that might not be feasible without such funds?