

INTER-OFFICE CORRESPONDENCE
Los Angeles Unified School District

INFORMATIVE

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FROM: Randy Ross
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SUBJECT: **Cutback Budgeting in LAUSD: Lessons from the early 1990s**

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Executive Summary

The susceptibility of LAUSD (and other school districts) to the teeter-tottering of California's fiscal base has been made excruciatingly apparent by the state's approximately \$15 billion (and possibly rising) shortfall. Given LAUSD's reliance on the state for about 90 percent of its funding, the state's problem translates into an equally horrific problem for the District.

Current estimates are that the District will have to address a \$460 million shortfall in anticipated revenue for the 2008-09 school year,¹ which amounts to about 6.5 percent of the District's General Fund budget for the current school year.²

In current dollars, this may be the largest fiscal challenge the District has ever faced. However, in relative terms, a review of historical documents reveals that in the early 1990s, the District had to address a 13 percent shortfall (twice the percentage facing LAUSD today).³

Accordingly, we reviewed LAUSD's cutback-budgeting experience from the early 1990s to tease out lessons and ideas that may help the Board in its efforts to balance LAUSD's budget in this and, perhaps, the coming years.

¹ Note that the \$460 million estimate includes about \$10 million for the Child Development Fund.

² Using Original, Approved, and Projected General Fund budgeted revenues and expenditures from LAUSD's 2007-08 2nd Interim report as alternative denominators, the estimated percent ranges from a low of 6.3 to a high of 6.8.

³ The 1990s problem was precipitated by the then Board's decision to make a major expenditure commitment (a three-year compensation package for employees, including salary increases of 8 percent per year) followed by an unexpected downturn in the economy. The District's current fiscal problem may also be explained by these two factors, however this time around the primary culprit is the economy rather than the Board's budget decisions.

Key findings from our preliminary analysis include:

1. The Board's priorities for addressing budget shortfalls during the early 1990s seemed to be:
 - a) Seek income from other sources;
 - b) Seek efficiencies in District operations;
 - c) Reduce central office functions that are non-mandated or deemed least essential;
 - d) In the event school functions had to be reduced, focus first on functions outside the classroom; and
 - e) Reduce employee compensation.
2. Many of the actions taken in some years were one-time fixes (e.g., restrict carryovers, borrow money, delay purchase of textbooks), which in effect meant that the problem would be carried over to future years.
3. Union-negotiable items accounted for a significant share of budget cuts.
4. Collectively, budget cuts had a multi-tiered effect on employee compensation (for example, furlough days plus reduced salary plus fewer vacation days).
5. The cutback-budgeting process was dynamic; actions were taken throughout the year as new information unfolded.
6. Key uncertainties perennially stressed the budget process.

Overall, our analysis suggests that the Board's decisions in the early 1990s were guided by a host of reasonable priorities in the face of regulatory constraints and enormous fiscal uncertainty. The District's current budget crisis bears great similarity to the early 1990s, and therefore the District's experience from that period should help to inform how the Board responds to the current situation.

Cutback Budgeting in LAUSD in the Early 1990s

We have organized this paper into two major sections. The first section reviews actions taken by the Board and District to address the budget shortfall in the early 1990s. The second major section synthesizes lessons that may help to inform the Board's effort to address the District extant fiscal woes.

Table 1 provides an overview of the budget challenge that confronted LAUSD during the early 1990s. The first shortfall of \$43 million occurred during the 1989-90 school year. This problem was small compared to the deficits that hit the District in subsequent years. In 1990-91, the budget shortfall rose to about \$372 million or about 12 percent of General Fund Budgeted Revenue (GFBR). Rather than abating, the shortfall actually hit the \$400 million mark in both 1991-92 and 1992-93, amounting to nearly 13 percent of GFBR for those years. Despite balancing the budget in these two years, the District would face another shortfall in 1993-94 amounting to about \$150 million.

**Table 1:
LAUSD Budget Shortfall as a
Percent of General Fund - Budgeted Revenue (\$millions)**

School Year	General Fund - Budgeted Revenue	Budget Shortfall	Shortfall as % of Budgeted Expenditures
1989-90	\$ 2,871.6	\$ 43.0	1.5%
1990-91	\$ 3,017.6	\$ 372.3	12.3%
1991-92	\$ 3,150.0	\$ 404.2	12.8%
1992-93	\$ 3,181.8	\$ 400.0	12.6%
1993-94	\$ 3,324.5	\$ 149.9	4.5%

SOURCES: LAUSD Comprehensive Annual Financial Report, FY Ended June 30, 1994; LAUSD 1993-94 Adjusted Final Budget, August 23, 1993.

This sustained budget shortfall was new territory for LAUSD. To grapple with this challenge, the District employed a variety of participatory deliberative strategies. For one, for 1990-91 and 1991-92 the District formed a Districtwide advisory committee to provide suggestions on options for balancing the budget. While the Board, staff, and the Advisory Committee operated under the premise that reductions should be kept away from schools' instructional programs, the sheer magnitude of the problem rendered inevitable some reductions in instructional outlay.

In an effort to reveal the underlying budget priorities of the District during the early 1990s, below we review available data for the three most challenging years from that period: 1990-91, 1991-92, and 1992-93. In each of these years, the budget shortfall approached or exceeded \$400 million.

1990-91

The budget challenge that clouded the 1990-91 school year heralded a coming fiscal drought for LAUSD. Acknowledging its precarious fiscal condition, the District mobilized a District Advisory Committee to provide a preliminary list of proposed adjustments. This committee included representatives from school staffs, central office administration, as well as employee unions and the 10th and 31st District PTAs. The Committee operated under the guideline that budget cuts or adjustments should have the least impact on instruction.

In January 1990 the Superintendent presented to the Board a list of adjustments totaling \$200 million. Data compiled from LAUSD historical budget documents show that these proposed adjustments were distributed across several areas (see Table 2). About 22 percent of the anticipated shortfall would be addressed by raising additional revenue (including borrowing). About 8 percent of the shortfall would materialize through reductions in outlay on facilities, maintenance, and campus environment. Next, 19 percent of the \$200 million would be obtained by cutting central office functions. These three areas accounted for about half the need. To address the remaining \$100 million of

the anticipated shortfall, the proposal included hefty reductions in instruction (23 percent) and instructional support (16 percent). To cover the balance of the need, the proposal included a placeholder pending the identification of additional proposed adjustments amounting to 12 percent of the \$200 million shortfall.

Between January and the publication of the Final Budget (August 1990), the Board convened several meetings in April, May, and June of 1990. In the end, major shifts were made in the locus of budget adjustments. Consistent with the Committee’s key guideline, the Board opted to considerably lower the cuts in instruction and instructional support (from a combined 39 percent to 18 percent of the budget adjustments). In lieu, much greater emphasis was placed on revenue/borrowing (increased from 22 percent to 37 percent) and central office reductions (increased from 19 percent to 28 percent).

Table 2: Proposed Adjustments in LAUSD 1990-91 Budget

Description	Proposed \$ Adjustment, January 1990	Final Budget Adjustment, August 20, 1990
Potential Revenue/Borrowing ⁴	22%	37%
Administration - Central Offices/Regions	19%	28%
Facilities Including Capital Outlay, Maintenance and Campus Environment	8%	17%
Instructional Support Programs	16%	9%
Instructional Programs	23%	9%
Additional Items to be Identified	12%	0%
Other	0%	0%
TOTAL (\$millions)	\$ 200.0	\$ 210.7⁵

Note: For detail, contact R. Ross at randy.ross@lausd.net.

Note that over \$100 million of the proposed budget adjustments in Table 1 were one-time. This meant that, absent increased revenue from the state in subsequent years, resolution of a major portion of the problem would be postponed until the next year(s).

1991-92

Indeed, 1991-92 was among the worst budget years LAUSD has ever experienced, with the original estimated shortfall of \$341 million for the year exceeding 10 percent of the budget. About \$200 million of this shortfall was attributable to ongoing shortfalls from the prior year that had been stalled with one-time fixes. The remaining problem of approximately \$140 million was new (e.g., combination of revenue shortfall and expenditure increases).

⁴ See Appendix for breakdown of borrowing, new revenue, and transfers included in 1990-91 adjustments.

⁵ Information in budgets for subsequent years suggests that the District ultimately reduced its 1990-91 budget by about \$370 million (see Table 1).

While the District projected that it would need to identify \$341 million in adjustments and/or revenue, “in accordance with Board Members’ direction and to provide greater flexibility,” the initial list of items totaled \$638 million, which substantially exceeded the anticipated need (see Table 3).

Notably, the \$638 million list placed greater emphasis on instruction and instructional support than the actions from the prior year. This was necessary partly because revenue/borrowing options had been exhausted in the prior year, and sizeable reductions had been made in central/region office spending. To that end, the listed cuts included items such as the following that had the effect of reducing the size of LAUSD’s teacher force: (1) increase class size; (2) re-norm secondary schools at mid-year; and (3) eliminate preparation period for secondary teachers.

Table 3: Proposed Adjustments in LAUSD 1991-92 Budget

Description	Proposed \$ Adjustment, May 1991	Final Budget Adjustment, September 3, 1991
Potential Revenue/Borrowing	0%	0%
Administration - Central Offices/Regions	2%	17%
Facilities Including Capital Outlay, Maintenance and Campus Environment	3%	4%
Instructional Support Programs	21%	12%
Instructional Programs	24%	30%
Additional Items to be Identified	0%	0%
Other (primarily employee compensation)	50%	37%
TOTAL (\$millions)	\$ 638.0	\$ 275.8

Note: For detail, contact R. Ross at randy.ross@lausd.net.

As with the prior year, budget documentation included a preliminary list of proposed adjustments (including items suggested by presenters at several public hearings) and a listing of the final adjustments in the Final Budget. However, judging by the dates on the documentation, the process occurred later. In 1990-91 the initial proposed adjustments were presented in January, while the initial proposal for 1991-92 was offered in May. It is conceivable that the May date was set deliberately to insure the process took into full account the May revision of the Governor’s Budget.

The bulk of the initial proposals for balancing the budget were for reductions in instruction (24 percent), instructional support (21 percent), and other (50 percent). The “other” category primarily included across-the-board reductions in employee compensation (chiefly pay). Reductions in central/region office operations amounted to only two percent of the proposed adjustments.

Between May and the Final Budget in September the Board selected about \$275 million of budget-balancing actions from the \$638 million smorgasbord. Consistent with the Board's priorities, this process resulted in shifts in the locus of reductions: (1) the central office share went from 2 percent to 17 percent; (2) instructional support's share dropped from 21 percent to 12 percent; (3) instruction's share actually rose from 24 percent to 30 percent; and (4) Other (compensation) was lowered from 50 percent to 37 percent.

Note that the \$275 million fell short of the projected total shortfall of \$341 million. Also engendering cause for concern, the proposed budget fixes included \$122 million of items that had to be negotiated with employee unions and \$120 million one-time items. Moreover, there remained uncertainty in California's fiscal health. Indeed, subsequent LAUSD budgets indicate that the total budget shortfall for the 1991-92 school year rose to about \$400 million.

1992-93

The Chief Business and Financial Officer's Message in the 1992-93 Revised Adjusted Final Budget aptly depicts the fiscal reality confronting LAUSD that year:

The District's 1992-93 Budget was developed in a time of unprecedented financial turmoil for LAUSD. Following three years in which budget reductions and redirections of \$43.0 million (1989-90), \$372.3 million (1990-91) and \$404.2 million (1991-92) were necessary, the District began 1992-93 budget development activities facing the likelihood of further reductions, due to a variety of factors, most important of which were: (a) the ongoing nationwide recession, which negatively impacted state tax revenues; (b) the use of onetime resources to balance prior year budgets; and (c) decreases in non-tax-based revenues, such as the California State Lottery and interest income.

To address the anticipated \$400 million General Fund shortfall for 1992-93, on June 11, 18, and 22, 1992, the Board took a series of votes. The votes included a reduction of \$271 million in negotiable employee compensation, which amounted to about four-fifths of the budget adjustments (see Table 4). In September of the school year, the Board adopted further budget adjustments in order to mitigate the impact of the salary reductions stipulated in the final budget.

**Table 4:
Proposed Adjustments in LAUSD 1992-93 Budget**

Description	Proposed \$ Adjustment, June 1992
Potential Revenue/Borrowing	0%
Administration - Central Offices/Regions	5%
Facilities Including Capital Outlay, Maintenance and Campus Environment	4%
Instructional Support Programs	3%
Instructional Programs	8%
Additional Items to be Identified	0%
Other (primarily employee compensation)	79%
TOTAL (\$millions)	\$ 399.8

Note: For detail, contact R. Ross at randy.ross@lausd.net. The Revised Adjusted Final Budget for 1992-93, published November 25, 1992, did not list the final steps the Board took to balance the budget.

The 1992-93 Final Budget reflected a reduction in salaries averaging 8.7 percent for all District employees. In the interest of equity, the Board decided that employees earning lower salaries would incur smaller percentage reductions in pay.

The 1992-93 school year did not mark the end of the District's budget woes. The 1993-94 school year was stained with a budget shortfall of about \$150 million. Two major factors that helped to explain the problem were the continuing recession plus the use of one-time resources to help balance prior-year budgets. However, the Board's decision to begin increasing salaries suggested that better fiscal days (years) were ahead.

Lessons from the 1990s

Our analysis of the District's experience with the budget challenge of the early 1990s identified several key points that may be applicable to the District's current situation:

- The Board's budget decisions were guided by multiple priorities
- The Board opted for many one-time fixes that pushed the problem into the future
- Union-negotiable items accounted for a large share of budget adjustments
- Budget cuts had a multi-tiered impact on employee compensation
- The cutback-budgeting process was dynamic

- Key fiscal uncertainties perennially placed stress on the budget process

Each of these points is discussed below.

The Board's budget decisions reflected multiple priorities

While the Board's ostensible primary guideline for addressing the budget shortfall was to keep cuts as far away from the classroom as possible, the Board's budget choices over time suggested a more detailed ordering of budget priorities:

1. Enhance revenue (i.e., local taxes, encourage state and feds to continue funding key programs, borrow money, transfer resources to the General Fund from other funds)
2. Improve efficiency of operations (reduce nonpersonnel expenses without reducing level and quality of service)
3. Reduce central office expenditures not needed to carry out contractual and/or legal compliance functions.
4. Reduce school nonclassroom costs (e.g., custodial support, school police)
5. Reduce classroom costs (e.g., increase class size)
6. Reduce employee compensation in an equitable manner

The Board opted for many one-time fixes

Budget shortfalls plagued the District for five consecutive years beginning 1989-90 partly because many of the actions taken by the Board were one-time fixes, which in effect meant that the underlying budget problem would have to be addressed in subsequent years. How a Board perceives the relative merits of various options for balancing the budget during hard times depends in part on how Board members view the District's fiscal prospects in the coming years. When will the economy get better? Will new money materialize next year? The more promising the near future appears, the greater the likelihood that the Board will employ strategies that buy time (i.e., one-time fixes) and thereby minimize the loss of jobs.

Negotiable items accounted for a large share of budget cuts

Given the size the budget crisis the District faced in the early 1990s, inevitably union negotiable items (such as salaries) would have to be put on the table. Generally, because of the time urgency, such items were placed on the reduction list before they were negotiated. The risk is that some of these items might be contested by one or more unions. For example, to balance the 1992-93 budget, the Board's actions included nearly \$180 million in salary reductions. However, UTLA sought and obtained a temporary restraining order, which placed in jeopardy the District's ability to maintain a balanced budget. Because the temporary restraining order was ultimately lifted, the District's budget met state requirements. Had the restraining order not been lifted, one scenario is that bankruptcy proceedings might have been initiated.

Budget cuts had a multi-tiered impact on employee compensation

Given that most of the District's resources are invested in employee compensation, major shortfalls such as that confronting the District in the early 1990s inevitably entail major reduction in employee compensation. While difficult to track amidst the budget balancing act, many employees' compensation was affected in multiple ways, as suggested by the excerpt below from LAUSD's 1993-94 Final Budget:

The Board is aware that a variety of the steps taken to solve the projected \$400 million General Fund shortfall will have multiple effects on some employees' compensation and benefits. As examples, the 1992-93 budget continues to reflect a 2- or 5-day furlough for all employees, which provides for a salary decrease of from 0.9% to 2.1%, depending on assignment basis. When this is added to such factors as a percentage decrease to actual salary rates, a reduction of 4 vacation days continuing from 1991-92 for non-overtime-earning employees, the continuing impact of the "wait" year on all "8-8-and-wait" employees, and the loss of the inflationary adjustment for health and welfare benefits in 1992-93, it is clear that many employees will suffer not just one reduction in the coming fiscal year, but a multitude of reductions that will significantly affect their standard of living. Employees "bumped" into lower paid positions that are then reduced in rate will suffer a particularly difficult multiple impact.

The cutback-budgeting process was dynamic

In the 1990s, as early as January, the Superintendent began recommending strategies for addressing the shortfall for the next year. Ongoing Board deliberation resulted in many changes between the first list and the Final Budget. Moreover, substantive and substantial changes often took place after the adoption of the Final Budget.

The dynamics of the cutback budgeting process owes to the sheer complexity of the process: (1) insufficient timely information is available to the Board for making optimal decisions; (2) new information is constantly under development and revision whose availability will enable the Board to improve the alignment of its actions with its priorities. For example, in planning for the 1992-93 school year, the Superintendent presented preliminary estimates to the Board on April 20, 1992 that indicated a shortfall of \$348 million. A subsequent estimate projected a General Fund shortfall of about \$400 million, a 14 percent increase in the size of the problem.

Key uncertainties perennially stressed the budget process

Given the District's dependence on the state for resources, when California's coffers are fattened with tax dollars, the District also benefits. Likewise, when the state's coffers are barren, the District too suffers a dry spell. Historically, the state's fiscal condition has been cyclical – swinging up and down, hitting highs and lows. Unfortunately, these

movements and their fiscal impact are difficult to predict accurately into the future. Thus, in a typical budget year, a significant ending balance buttresses the reserve for economic uncertainties to create a sturdy budgetary “safety valve” to ease the pressure of random fluctuations in District revenue as well as unanticipated jumps in expenditure. Absent this safety valve, the budget becomes subject to the sometimes unpredictable whims of the economy, as was the case for several years beginning 1990-91.

Concluding Remarks

Our analysis of how LAUSD handled the sustained budget crisis that confronted us in the early 1990s suggests that the Board’s decisions were guided by a host of reasonable priorities and legal constraints (e.g., compliance requirements) in the face of enormous fiscal uncertainty. The current budget crisis confronting the District bears great similarity to the early 1990s, and therefore the District’s experience from that period should help to inform how the Board responds to the current situation.

While the similarities between then and now are great, some aspects of the budget landscape have changed. During the early 1990s, for example, the District developed the budget for one year; now the District is legally required to develop a balanced budget for three consecutive years. Today, the District’s gargantuan building program entails much heavier borrowing than was the case in the early 1990s; so now we need to consider more intently how strategies to balance the budget may impact the interest rates at which we borrow money. Other issues that affect the comparability of the 1990s with today include, for example, liability for retiree lifetime health benefits and restrictions under No Child Left Behind.

Overall, however, the similarities between the time periods seem to overwhelm the differences. Now as then, the budget adjustment process entails the setting of priorities and taking action based on those priorities, ever mindful of legal constraints as well as substantial uncertainty regarding future income.

Appendix

Table 2A:
Proposed Adjustments in LAUSD's 1990-91 Budget
Detail of "Potential Revenue/Borrowing"

Type	Description of Proposed Budget Adjustment	Proposed \$ Adjustment, January 1990	Final Budget Adjustment, August 20, 1990
Borrow	Borrow resources from GF Revolving Construction Funds for one year	\$ 9,000,000	\$ 9,000,000
	Borrow Special Reserve Fund Construction Resources that have not been obligated by contract (GF only)	\$ 16,840,000	\$ 16,840,000
	Borrow Special Reserve Fund Monies for Projects which can be frozen for one year.		\$ 4,877,000
	Issue COPs for Construction and Alterations and Improvements and Replacement of Police Vehicles		\$ 5,492,000
Borrow Total		\$ 25,840,000	\$ 36,209,000
New Revenue	State Reimbursement for Heat Reduction Claims	\$ 17,700,000	\$ 17,700,000
	Increase Civic Center fees		\$ 500,000
New Revenue Total		\$ 17,700,000	\$ 18,200,000
Transfers	Transfer of Fire Loss activities to the General Fund		\$ 12,707,232
	Reduce Budget of Workers' Compensation Fund		\$ 10,000,000
Transfers Total			\$ 22,707,232
Grand Total		\$ 43,540,000	\$ 77,116,232

Selected References

LAUSD Budget (Budget Services and Financial Planning Division)

- *1989-90 Final Budget*, Volume 1, August 28, 1989
- *1990-91 Final Budget*, August 20, 1990
- *1991-92 Final Budget*, September 3, 1991
- *1992-93 Revised Adjusted Final Budget*, November 25, 1992
- *1993-94 Adjusted Final Budget*, August 23, 1993

Recommendations for Budget Reductions (Budget Services and Financial Planning Division)

- *Recommendations for Budget Reductions 1990-91*, presented by L. M. Britton, Superintendent of Schools, January 1990.
- *Recommendations for Budget Reductions 1991-92*, presented by W. R. Anton, Superintendent of Schools, May 1991.
- *Superintendent's Recommendations for Budget Reductions*, 1992-93 School Year, Revised June 11, 1992

Comprehensive Annual Financial Reports (CAFR)

- *CAFR FY Ended June 30, 1989* (includes letter from Superintendent Leonard Britton and CBFO Robert Booker dated December 4, 1989)
- *CAFR FY Ended June 30, 1990* (includes letter from Superintendent William Anton and CBFO Robert Booker dated December 3, 1990)
- *CAFR FY Ended June 30, 1991* (includes letter from Superintendent William Anton and CBFO Robert Booker dated December 9, 1991)
- *CAFR FY Ended June 30, 1992* (includes letter from Superintendent Sydney A. Thompson and CBFO Robert Booker dated December 7, 1992)
- *CAFR FY Ending June 30, 1993* (includes letter from Superintendent Sydney A. Thompson and Controller Olonzo Woodfin, III dated December 6, 1993)
- *CAFR FY Ending June 30, 1994* (includes letter from Supt. Sydney A. Thompson, CFO Henry Jones and Controller Olonzo Woodfin, III dated December 8, 1994)