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May 27, 2021

VIA E-MAIL

Dear Mr. Soldani,

On May 13, 2021, the financial consultants for the City of Malibu (“City”) met with Shin Green, the financial consultant for the Santa Monica-Malibu Unified School District (“SM-MUSD”) regarding the City’s Petition for Unification (“Petition”) and its accompanying financial proposal. Present for the City was La Tanya Kirk-Carter from Kirk Carter & Associates, Terry Ryland from the Ryland School Business Consulting, and Cathy Dominico from Capital Public Finance Group.

When we spoke on May 5, 2021, in preparation for this meeting, we agreed the financial consultants would meet without any other parties present and that we would have a written deliverable that would document what was accomplished in the meeting. Although the City’s consultant team thought the meeting time would be spent reviewing both financial proposals, the group in fact focused mostly on the City’s proposal. Attached is the City’s deliverable from that meeting, including a review of where the parties agree and disagree, from the perspective of the City’s consultants team.

As documented in the attached memo, it has become even more obvious to the City that there are some basic differences in how the parties view school funding fundamentals. Therefore, the City renews its request for the parties to participate in a binding arbitration that would lead to a negotiated agreement on how the school district should separate. The City hopes binding arbitration—*as opposed to any further non-binding negotiation*—would accomplish a few things. First, the City believes a third-party arbiter could help establish basic guidelines for what is possible and practical in a revenue sharing agreement between the parties. Second, the City believes that both parties need to have a vested interest in what happens during the arbitration in order for there to be a reasonable return on the investment that would be required to prepare and participate in any future negotiations. Finally, since SM-MUSD’s proposal has not changed since it was originally presented in 2018, the City believes it unwise to make any new offers unless and until SM-MUSD is willing to also engage in compromise.

To this end, the City offers the following three names as potential arbiters for any upcoming negotiation.

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1. Nick Schweizer, Deputy Director, Sacramento County Office of Education
2. Joel Montero, Former Executive Director, Fiscal Crisis and Management Assistance Team (FCMAT)
3. Terena Mares, Deputy Director, Marin County Office of Education

The City has not contacted any of the three listed, but does ask SM-MUSD to either consider one of these or, likewise, offer three names for the City's consideration. In the alternative, the City is also open to picking an arbiter from one of the traditional dispute resolution services, such as JAMS or Judicate West.

The City looks forward to SM-MUSD's response after careful and sincere consideration of its offer to continue negotiations. Until that time, the City will continue proceed with its Petition before the Los Angeles County Office of Education's County Committee on School District Organization.

cc: Steve McClary, Interim City Manager, City of Malibu
Ben Drati, Superintendent, Santa Monica-Malibu Unified School District

Sincerely,



Christine N. Wood
for BEST BEST & KRIEGER LLP

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MEMORANDUM

TO: SCHOOL SEPARATION AD HOC COMMITTEE
Councilmember Karen Farrer
Councilmember Mikke Pierson

FROM: SCHOOL SEPARATION FINANCE CONSULTING TEAM
Terri Ryland, Ryland School Business Consulting
LaTanya Kirk-Carter, KirkCarter & Associates
Cathy Dominico, Capitol PFG

SUBJECT: OVERVIEW OF CONSULTANT TEAM MEETING WITH SANTA MONICA-MALIBU
UNIFIED SCHOOL DISTRICT'S CONSULTANT, SHIN GREEN

DATE: MAY 21, 2021

Councilmembers Farrer and Pierson,

On May 13, 2021, the three finance experts on the City's school separation consulting team met with Santa Monica-Malibu Unified School District's (SM-MUSD) financial consultant for school separation, Shin Green, at the request of the SM-MUSD. The purpose of the meeting was for Mr. Green to better understand the financial component of the City's most recent proposal to SM-MUSD.

Mr. Green's *interpretation* of the City's proposal resulted in a financial contribution from the future Malibu Unified School District (Malibu USD) that was quite significant and appeared to be unaffordable to Malibu USD. As such, SM-MUSD questioned their understanding of the proposal since it resulted in such an unfavorable situation for Malibu USD and felt that a meeting could provide some clarity. The consultant meeting did not address SM-MUSD's financial proposal in significant detail. A general comment related to SM-MUSD's proposal confirmed that the District's proposal has not changed over the course of three years of negotiations.

Meeting participants included Mr. Green as well as Terri Ryland, LaTanya Kirk-Carter and Cathy Dominico, of the City's consulting team. Several financial concerns were discussed during the almost two and a half hour consultant meeting. This memorandum will provide an overview of the discussion and identify areas of agreement and disagreement on the issues discussed during the meeting.

Discussion of City's Financial Model

The City's consulting team described our approach to developing the financial model for school separation. The City's model is intended to demonstrate a *methodology* for allocating all school district revenue sources to the future Malibu USD and Santa Monica Unified School District (Santa Monica USD). Comparatively, the SM-MUSD model of the City's proposal is based on District *projections* of future revenue and the allocation of such revenues.

The City's team walked-through the analysis that was the basis for the City's proposal, using the spreadsheets developed by Ms. Ryland. The description of the analysis demonstrated how the Local Control Funding Formula (LCFF) was completed and applied to each district, the estimated property taxes, and the backfill from Malibu USD that may be required to make the State whole in the event that Santa Monica USD is no longer basic aid after separation. Next, Ms. Ryland showed how the Other Local funding sources were allocated between Malibu USD and Santa Monica USD based on where such revenues were generated, resulting in almost all of the funding being allocated to Santa Monica USD, thus increasing their per pupil funding with approximately 15% less students to serve. This analysis resulted in a higher per pupil funding amount for Santa Monica USD than they currently receive, as such no additional transfer from Malibu USD to Santa Monica USD was needed. However, the team explained that in the event that one or more of the Other Local funding sources declined on a per pupil basis, for example sales tax revenues, then Malibu USD would provide additional funding to Santa Monica USD to bring them back up to current per pupil funding levels. The team further discussed a reasonable cost of living adjustment on the funding sources, so they were not stagnant over the 10-year period that Malibu proposed to keep Santa Monica USD funding at least as high as they are currently.

Mr. Green then described how he had completed his calculations interpreting the City's proposal. His analysis converted existing SM-MUSD revenues to a per pupil funding figure. The sum of State aid, property taxes, redevelopment funding and other LCFF sources were totaled to determine the total LCFF sources of funds. Then, Other State, Federal and Local Funding sources were added in to calculate the per pupil funding of the combined district. These revenues sources were projected over time while student enrollment declined over time, resulting in increasing per pupil funding amounts. A secondary model was created to calculate the revenue sources on a per pupil basis for Santa Monica USD post-separation. In Mr. Green's model, projected property taxes per pupil decreased by approximately \$3,000 per pupil for Santa Monica USD post-separation due to the projected loss of property tax revenues from Malibu. This resulted in a commensurate per pupil transfer from Malibu USD to Santa Monica USD.

The City's team identified two main concerns with this approach to the analysis. First of all, it is necessary to calculate each district's LCFF entitlement, which will change each year, then calculate the combination of State aid and property taxes needed to reach the LCFF amount. This equates to the amount that Malibu USD would need to transfer in property taxes to keep the State whole. The separate LCFF calculation was not completed by Mr. Green. He lowered the property tax amount but forgot to include the offsetting State Aid increase that would hold the LCFF entitlement fairly constant. The group agreed that both Supplemental Property taxes and Educational Revenue Augmentation Fund (ERAF) funding should both be included as property tax funding sources for a non-basic aid school district. Second of all, the manner in which property taxes were allocated to the two districts in Mr. Green's analysis was different from how the City team was proposing to allocate property taxes.

Areas of Agreement

The consultants representing both agencies agreed that there were different approaches to calculating the amount that Malibu USD would transfer to Santa Monica USD based on the terms of the City's proposal. Additionally, the consultants agreed that how the City proposed to allocate property taxes to the future school districts was not how the School District's consultant had allocated the property taxes in his interpretation of the City's proposal. Finally, the consultants agreed that both Supplemental Taxes and ERAF should be included in Santa Monica USD's property tax revenues to the extent that the District was not basic aid.

Areas of Disagreement

The consulting teams were not aligned with how to calculate LCFF funding entitlement for the future school districts, and how the Malibu USD transfer to Santa Monica USD would be determined. Additionally, the consultants did not come to any agreement related to how property taxes could be allocated between the two districts. A further discussion of the disagreement related to property taxes is described in more detail below.

Property Tax Allocation

Both the City's consulting team and SM-MUSD's consultant agreed that the allocation of property taxes was a source of significant disagreement between the two parties and that each party was calculating the property tax funding differently. Even in SM-MUSD's consultant's interpretation of the City's proposal, property taxes were being calculated in a different way than what was actually proposed by the City.

The City proposed to allocate property taxes to each school district based on the geographic location of where the property taxes were generated. The property taxes generated in the Tax Rate Areas (TRAs) that would be served by Malibu USD would be allocated to Malibu USD and the property taxes generated in the TRAs that would be served by Santa Monica USD would be allocated to Santa Monica USD. Any transfers from Malibu USD to Santa Monica USD required to make the State whole would be handled through a property tax sharing agreement or another type of agreement to be worked out with guidance from the County and the California Department of Education. Other transfers to maintain Santa Monica's per student funding level would be funding from any legally available funding source of Malibu USD, not necessarily property taxes.

SM-MUSD's consultant did not believe that property taxes could simply be allocated geographically. Mr. Green's interpretation of the City's proposal used an allocation based on the percentage of assessed value in each future district, which resulted in a different property tax amount for each district than what the City had included in its analysis. Mr. Green's property tax amount used to project future per pupil funding was based on an estimate of future property tax revenue if the school districts remained together. Further, Mr. Green did not think that the County Auditor would be able to retroactively calculate how much in property taxes came from each TRA, even though he acknowledged that the share of tax revenue within each TRA likely did not change much since Proposition 13 was approved in 1978. Additionally, Mr. Green expressed concern that the original property tax allocation from the late 1970's, when Proposition 13 and all related trailer bills went into effect, was based on the District's budget at the time. He did not believe there would be a way to fairly allocate those late-1970s revenues between the two districts.

The City's consulting team clarified our understanding of his concerns and referred Mr. Green to a manual used by county property tax managers throughout the State that demonstrated the calculation for allocating property taxes by TRA. The City team also referred Mr. Green to Revenue and Taxation Code Section 99 which specifically calls for the county auditor to calculate property taxes by geography for a jurisdictional change.

Areas of Agreement

The consultants agreed that the way in which Mr. Green had allocated property taxes in his interpretation of the City's proposal was not what was intended by the City. There was also agreement that coordination would be needed with both the County and California

Department of Education related to how property tax transfers would be handled in order to offset additional State Aid if Santa Monica USD was not basic aid after reorganization.

Areas of Disagreement

Mr. Green did not agree that property taxes could be calculated and then allocated on a geographic basis. He further believed that such an allocation would be a financial detriment to Santa Monica USD due to the pre-Proposition 13 share of property taxes in each community. The City's consulting team disagrees with the fact that property taxes cannot be calculated and allocated geographically and does not think that Mr. Green's concerns related to the pre-Proposition 13 allocation is material, especially since the Revenue Limit was already in effect at that time and the District's budget was likely funded from both property taxes and State aid, just as it was until 2018 when SM-MUSD first became basic aid.

Redevelopment Funding

A brief discussion occurred during the meeting regarding redevelopment funding. The City's consulting team asked a clarifying question related to SM-MUSD's application of redevelopment funding. There is a redevelopment project area in the Santa Monica portion of SM-MUSD. Both consulting teams agree that with reorganization, redevelopment funding would be allocated to Santa Monica USD. However, the City's team had understood from a previous presentation that SM-MUSD believed that redevelopment funding would simply go away when the debts and obligations of the former redevelopment agency were repaid, resulting in a loss of funding for Santa Monica USD.

Mr. Green clarified his understanding of redevelopment funding, explaining that currently SM-MUSD receives some funding from the local redevelopment agency. After the redevelopment funding goes away, the property taxes the District receives will actually increase since funds will no longer be diverted to the debts and obligations of the former redevelopment agency. The future Santa Monica USD would no longer receive redevelopment pass-through payments nor residual property tax funding, but general property tax revenues would increase.

The group did not specifically review how redevelopment dollars were accounted for in Mr. Green's analysis of the City's proposal. The City's consultants included a portion of the redevelopment pass-through payments and the redevelopment residual funding as part of property taxes for Santa Monica USD. The other portion of redevelopment pass-through payments are accounted for as part of Other Local funding.

Areas of Agreement

The consultants generally agreed on how redevelopment funding worked and that it would be allocated to Santa Monica USD after separation.

Serrano v. Priest

During the meeting, the City consulting team asked Mr. Green to clarify comments that District staff and leadership have made publicly related to Serrano v. Priest, a court case from 1968 that preceded the creation of the school district Revenue Limit funding model which equalized per student funding throughout the State. Specifically, the SM-MUSD Superintendent stated that the City's proposed school separation would go against Serrano-Priest by shifting property taxes from school districts like Inglewood and Compton to a new Malibu School District.

Mr. Green explained SM-MUSD's position that this separation could set a precedent for wealthy communities, or a specific high property tax value segment of a community, to separate from their school district in order to form a wealthy school district with high property tax revenues and low student enrollment. This would then harm the remaining school district populations in less wealthy areas.

The City's consulting team was adamant that this is not the case in this situation and that creating a school district with high property tax revenues and low student enrollment is absolutely not the driving factor behind the desire to separate. Both the City's school separation team and the Malibu community have clearly demonstrated the desire to separate is due to the lack of local control over school district decisions, the lack of attention by school district leadership in several areas as well as the separate and distinct community identity of Malibu as compared to Santa Monica. Further, the City's team adamantly stated that there would be no revenue loss to any other school district in the County due to this school district reorganization. There is only one other basic aid school district in Los Angeles County, all other school districts are funded up to their LCFF funding amount by a combination of property taxes and State aid. ***If*** there was a loss of property tax funding, which there would not be from this reorganization, those districts would simply receive additional State aid to offset any property tax loss.

Areas of Agreement

Both the City and School District's consultants agreed that this argument was based on a hypothetical scenario, not the specific basis for the City's actual petition to separate from SM-MUSD.

Areas of Disagreement

It is not clear whether Mr. Green supported the City's consultants assertions that this reorganization was not in violation of Serrano v. Priest. The City's consultants requested that Mr. Green show the math for the Serrano Priest assertion, if in fact something like that could happen.

Program Cuts Resulting from School Separation

Also during the meeting, the City's consulting team asked Mr. Green to clarify public comments and a newspaper ad that identified \$19 million of program cuts that Santa Monica USD would be forced to make as a result of school district separation. Mr. Green was not able to show where the \$19 million figure was derived. At first, he directed the City's team to the SM-MUSD fiscal recovery plan. Then, he explained that the cuts may not be just program cuts, but general cuts that the District will need to make if separation occurs.

The City's consulting team argued that cuts identified in the fiscal recovery plan have nothing to do with reorganization and concurred that general administrative cuts would occur, but the District would be educating 15% less students, so cuts should be expected. Those administrative positions would be available at the new Malibu USD, so that the people in those positions would just be relocated to the new district, not terminated.

Further, the City's team pressed Mr. Green on the \$19 million figure because it was not clear how that figure was calculated given the fact that SM-MUSD was only \$4 million into basic aid for 2020-21. In other words, SM-MUSD only received about \$4 million more than its minimum LCFF funding amount for 2020-21. That equates to under \$400 per student. Applying the \$400 per student to the estimated 8,800 students in Santa Monica USD, equates to

approximately \$3.5 million. Therefore, **at most**, the District would only lose \$3.5 million after separation and that did not account for the fact that Malibu's proposal specifically includes a provision to transfer funding to Santa Monica USD to make up for this type of funding loss. This figure is nowhere near the \$19 million figure that has been publicly communicated by SM-MUSD. The City's consulting team further verified the amount of excess property taxes by showing the California Department of Education's *LCFF Summary Data, FY 2020-21 P-1 Principal Apportionment* schedule to document for Mr. Green the official source of the City's information.

Areas of Agreement

The consultants from both the City and SM-MUSD agreed that the excess tax figure of just under \$4 million was accurate for 2020-21.

Areas of Disagreement

The origin of the \$19 million in program cuts was not identified. The City's consulting team does not agree that there would be a decline in funding at all on a per student basis, so program cuts should not be necessary except for existing cuts due to a structural budget deficit. Additionally, the City's team does not agree with the characterization of the cuts. Administrative cuts from one district that is losing a percentage of its student population are expected in any separation and those should not be called program cuts. Those positions are not eliminated, however, as they will be moved to the new district.

Summary

The discussion between the City's consulting team and Mr. Green provided our team with a better understanding of how SM-MUSD interpreted the City's proposal and where such discrepancies occurred. It also provided the team with an understanding of the areas of agreement and disagreement on the financial analysis. Many of the areas of disagreement do not have an obvious middle ground or solution. Based on the areas of disagreement, assistance from an independent third party may be needed in order to develop a reasonable financial solution to meet the common goal of school separation.

Please let us know if you have any questions or would like additional information on any of this information.

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