REPORT OF THE EXECUTIVE OFFICER
State Allocation Board Meeting, March 28, 2007

ADEQUACY OF NEW CONSTRUCTION GRANTS

PURPOSE OF REPORT

To provide a status on the review of the adequacy of the new construction grant to build new schools under the School Facility Program (SFP).

BACKGROUND

The State Allocation Board (SAB) requested Staff to form an ad hoc committee on grant adequacy (Committee) to determine if the SFP new construction grants are adequate to build schools in California. Specifically, the Board requested that the Committee address mainly two issues: the equitability of the SFP new construction base grant amount to the equivalent allowances provided under the Lease-Purchase Program (LPP) when the State converted programs in 1998; and, if the grants are sufficient to build a complete new school today. The Committee concluded that the new construction base grant was deficient at the time of conversion from the LPP to the SFP. One of the theories for the deficiency, at least in part, was that allowances for general site development were not included. As a result, regulations to provide an additional grant for general site development were approved by the SAB at the August 2006 meeting and were subsequently approved by the Office of Administrative Law. Districts can now receive this additional grant to complete their projects.

The Committee has been unable to determine if the grants are sufficient to cover the actual costs to complete new school projects today. The Committee previously requested data, in the form of a survey, from school districts on completed projects. Very few districts replied. When conducting a preliminary analysis of the information that was received, Staff discovered that a majority of the surveys were incomplete or the information requested was misunderstood resulting in an incomplete analysis. Some districts stated they did not want to complete the survey as they considered projects constructed two to three years ago too old for an analysis on the current climate of school construction. In addition, some districts expressed concern about how the data would be portrayed once it was collected.

Because of the lack of responses, there was no definitive grant adequacy data available during the bond discussions last year. Nonetheless, Assembly Bill (AB) 127, Chapter 35, Statutes of 2006 (Perata/Nunez) provided an increase to the new construction base grant of seven percent for elementary and middle school projects and four percent for high school projects beginning July 1, 2006. AB 127 also provides that, beginning January 1, 2008, the Board has the authority to annually increase the per pupil base grant amount by up to six percent, or reduce the per pupil base grant, by an amount determined based on an analysis of the current costs to build a school.

SUMMARY

The issue of the adequacy of the new construction grant is very complex. First, the Office of Public School Construction (OPSC) is reliant on data provided by others. In order to determine the adequacy of the grants today, it is imperative that a definition of what is a complete and adequate school is created and construction data is provided by the school districts so that a comparison of the two can be conducted to provide a defensible analysis and recommendation to the SAB. The OPSC has requested the Superintendent of Public Instruction to define a “complete school” and assist with identifying schools that were recently constructed that meet this definition. The California Department of Education indicated they had already begun this task. The OPSC will then request the cost data on those schools.

Secondly and more important, even in the event the adequacy of the grants is determined, the ability of school districts to construct complete schools may still not be mitigated. There are significant outside factors that may contribute to the ongoing inadequacy of the grants. This report summarizes those issues.

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DISCUSSION

Determining the Adequacy of the New Construction Grant

There are currently two main challenges that hinder the Staff and the Committee's ability to determine the adequacy of the per pupil grants to build schools. First, although it is understood that the new construction grants were intended to provide half of the funds necessary to construct adequate facilities for a complete new school, there is currently no officially accepted definition of a "complete school". Absent a definition of a "complete school", there is nothing against which the Committee can definitively measure the appropriateness of the State's share of the funding being provided to cover the facilities being constructed. Second, the only cost information that the OPSC has available are the project plans approved by the Division of the State Architect and the amount of State funds apportioned and released for each project, as approved by the SAB. There is no complete, empirical project cost data such as bid documents, construction contracts, total project cost documentation, or square footage data regarding facilities actually constructed that has been made available to the OPSC (with the exception of data provided by a district for an upcoming appeal).

In order to continue the analysis on the grant adequacy issue, Staff believes that a "complete" school must be defined. The Board has requested the assistance of the Superintendent of Public Instruction in determining what constitutes a complete school. Once a complete school is defined, Staff believes that districts should be required to submit data on the projects that meet the criteria of a complete school. The results can be used to determine the adequacy of the new construction grants today by comparing the actual costs to build those projects to the amount of the grant received (both State and district share). Staff further believes that collecting project data from districts will also ensure that the OPSC is in compliance with the Governor's Executive Order on bond accountability. The Executive Order requires that the bond funds approved by the voters are spent efficiently, effectively, and in the best interest of the State while requiring that there are sufficient performance outcome measures in place. Staff will need to rely on districts for their cooperation in providing the data to accomplish this.

Consideration of the Entire Funding Model

It is important to note that, when completing the analysis to determine the adequacy of the grants today, the entire funding model must be taken into consideration. The new construction base grant alone cannot be used to determine the adequacy of the grants, as several adjustments have been made to the total funding model in the last several years. Some of these changes include the calculation of the additional grant for urban/security and geographic location, the source for the yearly Construction Cost Index adjustment, the increase to the new construction base grant provided for in AB 127 beginning July 1, 2006, and the addition of the general site development grant. In addition, any changes to the base grant amount will also provide an increase to the excessive cost hardship grants, such as urban/security, geographic location, small size project, and new school project. It is also important to note that the grants provided should be paying only for the essential facilities of an adequate school, while any enhancements should be borne by the district unless those funds should otherwise be used to offset any financial hardship assistance from the State.

Maintaining the Adequacy of the New Construction Grant

The OPSC, with input from the Committee, must also determine the methodology to be used to determine the adjustment of the per-pupil base grant on an annual basis beginning January 1, 2008, as required in law. It appears the best methodology will be determined by the change in construction costs (on price per square foot basis) from one year to the next based on data collected for each year. The data to conduct the analysis will be collected on a "Project Information Worksheet" that must be submitted with a request for construction funds to be released and with the reporting of project expenditures.

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DISCUSSION (cont.)

Grant Adequacy Concerns

Staff and the Committee continue to meet to endeavor to determine whether the grants are adequate today. However, Staff is concerned that there is a misconception that increasing the State share of the new construction grant is a solution to the school districts difficulties in constructing school facilities. Any amount provided as an increase to the new construction grant may only contribute to future increases in school construction costs in California because there are too many other variables in the equation.

For instance, once the new grants provided by the State are known, the new grants will likely serve as the minimum floor of the cost to construct schools while the profit margins may continue to increase. In addition, an inundation of public work projects at one time has an effect on the bid climate, and with contractors that have the bonding capacity to do public work projects being limited, leads to a limited number of bids on a project (supply and demand). Further, the Public Contract Code "listing law" enables subcontractors to know how many opposing bidders are submitting bids to the general contractor on a project which can lead to inflated bids.

The issue of a district's local control of a project must also be factored in when determining whether the adequacy of the grants can be solved in a "one-size-fits-all" manner. Districts have local control over the choice and type of facilities constructed and the materials being used. While the grants may be sufficient to build a standard school, they are not adequate to support the construction of core facilities sized to accommodate future growth, a state-of-the-art performing arts facility, or an aquatic center. In addition, the way construction contracts are written can adversely impact the number of interested contractors. For example, if a contract is so overly prescriptive to be litigation proof, the result is a daunting document that may deter otherwise qualified contractors. Or, if the district's specifications identify only one or two products that can be used for a project and there is only one source or manufacturer for the product, this can limit the contractors that can competitively bid on the project, thereby increasing the bids. It is important to note that while these circumstances are and should remain local control issues, they are beyond the purview of the SAB and factor into the adequacy of the grant.

Other factors that adversely impact the adequacy of the grants are the high worker's compensation costs that are passed on to owners; changes in the building code requirements; inspection requirements; and, county/city imposed offsite improvements, etc.

Possible solutions to these concerns may include the need to address the Public Contract Code, bonding requirements, local construction contract requirements, worker's compensation costs, etc. via legislation or other means. Staff believes alternative funding methodologies may also be warranted and should be examined in determining the annual adjustment to the new construction grant, such as a grant provided on a dollar per square foot basis, based on the type of facility constructed, with a full and final apportionment provision (where no additional funding will be provided for increased project costs).

RECOMMENDATION

Accept this report.

BOARD ACTION

In considering this Item, the Board accepted the report. The California Department of Education indicated that they could supply to staff within 30 days many projects that have met Title 5 and are complete schools, and would subsequently provide a definition of a complete school. It was emphasized that the definition of a complete school is necessary as soon as possible in order to have a basis of comparison for the construction project and cost data collected and in ample time to meet the statutory timeline of January 2008.