REPORT OF THE EXECUTIVE OFFICER
State Allocation Board Meeting, June 22, 2005

STATE RELOCATABLE CLASSROOM PROGRAM

PURPOSE OF REPORT

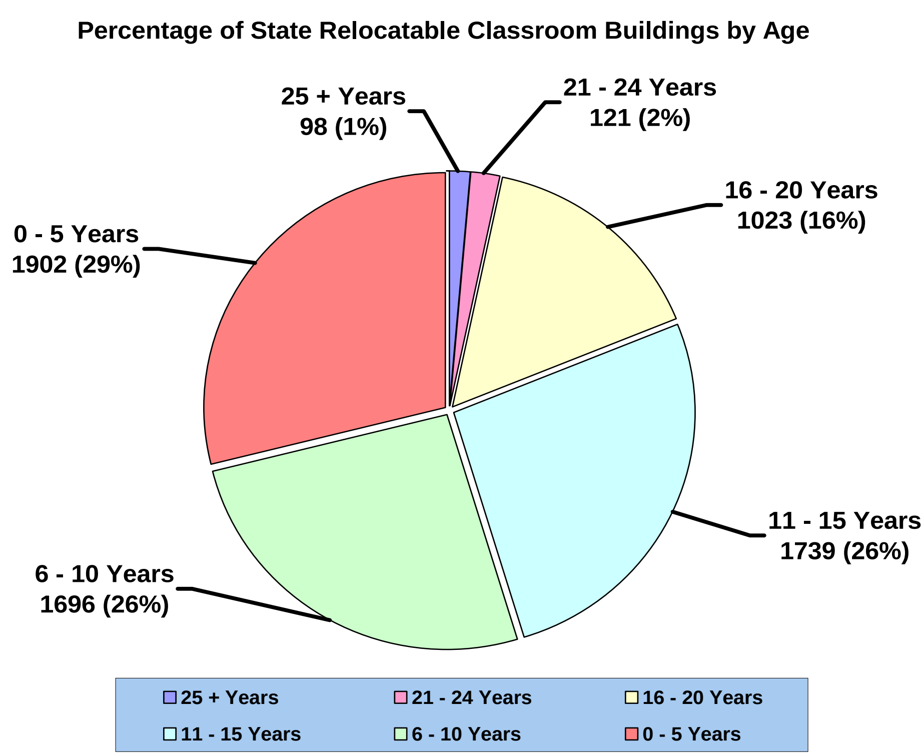
The purpose of this report is to provide the State Allocation Board (Board) with:

1. An overview of the State Relocatable Classroom Program (Program).
2. The general condition of the State Relocatable Classroom (Relocatable) assets.
3. Options for the implementation of an Asset Management Plan (Plan) (Rehabilitation/Disposal).
4. An option for the immediate disposal of all Relocatables 20 years of age and older.
5. A proposal to increase the annual lease payments of a Relocatable.

OVERVIEW

At the Program's inception in 1978, the inventory consisted of less than 100 relocatables designed to assist school districts in times of emergency situations. In fact, the Program was originally entitled the "Emergency Portable Program". Over the years, the Program has evolved into a long-term leasing program which accommodates district student housing needs far beyond the emergency nature of its initial inception. Today, the Board owns 6,579 Relocatables that are leased to school districts. The majority of these classrooms are leased at a rate of $4,000 per year. There are some school districts within the Program that qualify for financial hardship and subsequently lease their Relocatable at a reduced rate. Thus the average annual lease rate is $3,648 per Relocatable, which generates lease payment revenue of approximately $24 million annually. Since 1991, the Board has not increased the lease payments for the Relocatables.

Of the 6,579 Relocatables owned by the Board, the majority of classrooms (5,337) are 15 years of age or less. There are 249 Relocatables that are at least 20 years of age that represent the most potential cost and liability for the State. As this report will show, the cost to maintain a Relocatable substantially increases as it ages.



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OVERVIEW (cont.)

Under the Lease-Purchase Program, the State passed three bond measures between 1990 and 1996 that generated $62 million for the specific purpose of purchasing relocatable classrooms and covering Program operating costs such as transporting Relocatables from one school district to another school district, reimbursing school districts for the cost to set up the Relocatable, and the administrative costs associated with managing the Program.

Over the last ten years, seven times the annual State budget control language has directed the lease payment revenue generated from the Program to be directed to the State's General Fund. During the three years the Program was able to retain these funds, the Board purchased additional Relocatables and was able to sustain the program. However, the last time the Program was able to retain the lease payment revenue was in Fiscal Year 2001-02. Since that time, funds have significantly diminished and are inadequate to sustain the Program and address the growing issues associated with an aging fleet.

These issues have precipitated the need to develop an Asset Management Plan and examine the feasibility of increasing the lease payments on the Relocatables.

AUTHORITY

Education Code (EC) Section 17089 permits the Board to lease a Relocatable to school districts for not less than one dollar per year, and no more than $4,000 per year. The Program currently leases Relocatables to school districts for an annual fee of $4,000. However, the Board has the authority to annually increase the lease payment on Relocatables according to the adjustment for inflation set forth in the statewide cost index for classroom construction as determined by the Board at its January meeting, pursuant to EC Section 17089(a).

EC Section 17089(b) authorizes the Board to require each lessee to undertake all necessary maintenance, repairs, renewal and replacement to ensure that a project is at all times kept in good repair, working order, and condition. All costs incurred for this purpose shall be borne by the lessee.

EC Section 17089(c) states that for the purposes of this section, "good repair" has the same meaning as specified in subdivision (d) of Section 17002.

EC Section 17002(d) states that "good repair" means the facility is maintained in a manner that assures that it is clean, safe, and functional as determined pursuant to an interim evaluation instrument developed by the Office of Public School Construction (OPSC). The instrument shall not require capital enhancements beyond the standards to which the facility was designed and constructed.

EC Section 17094 permits the Board to dispose of a relocatable classroom to the public or private entity in any manner that it deems to be in the best interest of the State, if the Board deems there is no longer a need for the relocatable classroom.

2004 Budget Act - Section 24.30 permits the Controller, upon order of the Director of Finance, to transfer rental income received in the 2004-05 fiscal year, pursuant to Section 17089 of the EC, from the State School Building Aid Fund to the State's General Fund.

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AUTHORITY (cont.)

2005 Budget Act – Section 24.30 (PENDING) permits the Controller, upon order of the Director of Finance, to transfer rental income received in the 2005-06 fiscal year pursuant to Section 17089 of the EC, in an amount as determined by the Department of Finance, from the State School Building Aid Fund to the State's General Fund. Further, the OPSC is authorized to expend revenues in the State School Building Aid Fund per EC Section 17088(f) in an amount as specified by the Department of Finance.

EC Section 17089.2 permits school districts or county superintendent of schools to purchase any relocatable classroom that was leased from the Board prior to December 1, 1991, for an amount equal to the purchase price paid by the Board, including costs for site preparation, furniture and equipment, toilet facilities and transportation of classrooms, less the amount of any lease payment already paid to the Board by the district or county superintendent of schools for that classroom. Payment for purchases made pursuant to this section shall be in equal annual installments for an agreed upon term not to exceed nine years.

State Allocation Board Policy states that the purchase cost to the district shall be called the "net purchase cost" and equal to the purchase price paid by the Board, less rental payments by that district for the relocatable classroom. In no case shall the purchase cost to the district be less than $4,000.

GENERAL CONDITION OF THE FLEET

In order to determine the general condition of the fleet, Staff conducted an inventory survey that requested information from participating school districts regarding the general condition of the Relocatables currently being leased. Staff inquired about the interior, exterior and mechanical conditions of the Relocatables. Of the 304 school districts currently participating in the Program, Staff received 192 responses (63 percent). Of those school districts that responded to the survey, 73 percent of the respondents rated their Relocatables either in good or excellent condition, which represents the majority of classrooms less than 15 years of age. Staff analyzed the remaining 27 percent of the respondents that rated their Relocatables in either fair or poor condition and found that those classrooms were older than 15 years of age. In addition, it has been determined that these classrooms have been transferred from one school district to another a number of times throughout the years, which has contributed to the overall deterioration of the classroom.

Currently, school districts are required to keep the Relocatables in a well maintained condition and bear the costs for the maintenance. Costs vary from each school district, depending on the adoption of a routine maintenance schedule, the age of the classroom, the frequency of moves, location and environment. In recent years, more and more school districts have expressed concern to the OPSC about the rising costs to repair the more expensive building components, such as HVAC systems, roofs, exterior siding, etc. that have exceeded their useful life expectancy. In fact, the repairs necessary to keep a Relocatable in good working order have gone beyond general maintenance needs and have become capital improvement needs. Thus, school districts are asking the State for assistance to replace the major building components and they do not feel that it is their responsibility to pay for these components.

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ASSET MANAGEMENT PLAN

To present a comprehensive report to the Board, Staff met with other State agencies and members from the relocatable manufacturing industry and collected information regarding the major costs and factors that should be considered when developing a Plan. Those factors include useful life expectancy data, major building component rehabilitation costs, relocatable classroom replacement value, and disposal costs.

Useful Life Expectancy

Useful life expectancy is defined as the probable life span of a particular object. For the purposes of this report, Staff will be using the useful life expectancy data provided by members of the relocatable manufacturing industry and individual component manufacturers. It was necessary for Staff to determine the useful life expectancy of each component in order to determine the cost to maintain a Relocatable. The first thing to keep in mind in evaluating useful life expectancy data is the fact that the useful life expectancy of a component is dependent on the level of care and maintenance provided over the years and the location and environment of the Relocatable. As an example, the useful life expectancy for components of a classroom that is located on the coast will vary from components located in a desert region due to the climate conditions.

The useful life expectancy data used for this report takes into consideration that components have received regular maintenance on a routine basis. The majority of components within a Relocatable have a useful life expectancy that range between ten and twenty years of age. In other words, when a component has reached its useful life expectancy, that component is likely to have deteriorated and require replacement. As classrooms continue to age, it is expected that certain components will have reached their useful life expectancy more than once and again require replacement, which will result in additional costs.

Major Building Component Rehabilitation Costs

The rehabilitation costs proposed in this section address the major building components that have exceeded their useful life expectancy and considers that school districts have applied the proper maintenance and repair to the classrooms as prescribed in EC Section 17089 (b). In a typical landlord/lessee relationship, the landlord bears the responsibility to repair or replace the major components. As an example, the replacement of carpet is typically not the responsibility of the lessee unless the damage to the carpet is beyond normal “wear and tear” and determined to be caused by the negligence of the lessee. Anything beyond the cost to keep the facility in a well maintained condition is the responsibility of the landlord. As landlord of the State’s assets, it may be more appropriate that the rehabilitation cost for the major components be borne by the State.

Staff examined the key components that make up a relocatable classroom. These components include such things as; Exterior Siding, Trim and Skirting; Roof; Door and Windows; HVAC; Ramp; Wallboard and Related Items; Ceiling and Electrical Fixtures; and, Flooring. Using cost estimating data from Lee Saylor Base Cost Estimate (2005 edition) and R.S. Means Cost Estimate (2005 edition), and useful life expectancy data from the relocatable manufacturing industry, Staff calculated the estimated cost to rehabilitate a Relocatable over a period of time (See Chart A). In finalizing the cost estimates, Staff made further adjustments to account for additional rehabilitation work that may be necessary to adjacent areas, such as dry rot or damage caused by a leaking roof.

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ASSET MANAGEMENT PLAN (cont.)

Major Building Component Rehabilitation Costs (cont.)

CUMULATIVE COST TO REHABILITATE A SINGLE RELOCATABLE

CHART A		AGE OF RELOCATABLE			
		10 Years	15 Years	20 Years	25 Years
	Cost to Rehabilitate	$17,214	$26,791	$52,229	$67,481

As mentioned earlier, the majority of Relocatable components have a useful life expectancy that range between 10 and 20 years. As the classrooms continue to age, certain rehabilitation costs are duplicated, thus resulting in additional overall costs in subsequent years. For example, if the State were to rehabilitate a Relocatable over a period of 20 years, the State would incur costs for carpet twice over a period of 20 years, since the useful life expectancy for carpet is 10 years.

Relocatable Classroom Replacement Value

Using the latest building specifications, which were used for the Board's 2002 Relocatable building contract, members from the relocatable manufacturing industry estimated that the cost to purchase the same relocatable classroom today would increase approximately ten percent from the 2002 purchase price. Thus, the estimated replacement value of a Relocatable would be $28,000 or more depending on available material costs. Factoring in additional costs for transportation and set-up, the cost to the State to replace a Relocatable could be $40,000 or more.

Under the School Facility Program (SFP), school districts can establish modernization eligibility when their relocatable classroom has reached 20 years of age. However, it is not cost effective to use modernization funds to rehabilitate an older relocatable when the costs to replace a relocatable classroom are comparable. In fact, by using their modernization funds to purchase a new relocatable, the new facility would meet the requirements under Title 24 and address some of the issues related to air quality and noise pollution. School districts typically exercise the option to replace district owned relocatable classrooms when faced with the decision of how to use their modernization funding. The Board may want to consider implementing a similar cost effective practice.

Currently, the Board owns 249 Relocatables that are over 20 years of age. Recognizing that the cost to replace a Relocatable is virtually the same cost to rehabilitate one, it may be prudent for the Board to develop a plan that includes the disposal of Relocatables that incorporates a cost benefit analysis.

Relocatable Classroom Disposal

After evaluating the rehabilitation costs and useful life expectancy data, it was necessary for Staff to research the cost to dispose of a Relocatable. The average cost to dispose of a Relocatable could range from $6,000 to $7,000 per classroom.

As an alternative to incurring the additional expense to dispose of a Relocatable, the Board can sell the classrooms to school districts, other public agencies, or private entities. EC Section 17094 permits the Board to dispose of any relocatable classroom, in any manner that it deems to be in the best interest of the State, if the Board deems there is no longer a need for a relocatable classroom. Additionally, EC Section 17089.2 permits

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ASSET MANAGEMENT PLAN (cont.)

Relocatable Classroom Disposal (cont.)

the Board to sell a Relocatable that was leased from the Board prior to December 1, 1991, for an amount equal to the purchase price paid by the Board, including the cost of site preparation, furniture and equipment, toilet facilities and transportation of classrooms, less any lease payments received for that classroom. The purchase price would include costs associated with improvements made to the Relocatable. The revenue generated from the sale of Relocatables could be used to cover the cost to dispose of some classrooms, as it is anticipated that not every school district, public agency or private entity will purchase all of the Relocatables.

Currently, there are 61 school districts, representing 1,357 Relocatables that have continually leased their classroom since December 1, 1991 and have not elected to purchase the State's relocatable classroom. The OPSC is aware of school districts that have not elected to purchase the State's relocatable classroom due to the high costs associated with adjusting their SFP baseline eligibility. A typical elementary grade level classroom loaded at 25 pupils will generate a base allowance of $169,225 in new construction funding. Districts will not risk the loss of future new construction funding.

Staff determined that the best return on investment for a Relocatable requires the State to dispose of the classrooms at 15 years of age. An analysis of the rehabilitation costs compared to the lease payment revenue generated produces a 57 percent return on investment when Relocatables are disposed of at 15 years of age. Should the State dispose of Relocatables at 20 years of age, the return on investment only yields a 26 percent return on investment.

Based on the information mentioned previously, Staff has developed three options for the Plan, which do not contemplate the purchase of any new Relocatables.

OPTION #1 – REHABILITATION PROGRAM

One of the objectives for implementing a Plan is to allow for more effective planning in relation to the maintenance and repair of a Relocatable. As previously mentioned, the Program requires a school district to maintain the Relocatable throughout the duration of the lease, pursuant to EC Section 17089 (b) and (c). However, as these classrooms continue to age, the OPSC has received complaints from school districts that the repairs necessary to keep a Relocatable in good working order have gone beyond general maintenance needs and have become capital improvement needs.

Using property management principles, the landlord is responsible for the repair or replacement of the major components that contribute to the functionality of a facility. The State is responsible for the major component costs of the Relocatable, unless it is determined that the school district was negligent in providing the proper care and maintenance resulting in the replacement of a component before that component has reached its useful life expectancy. Requiring a school district to replace building components that have outlived their usefulness is inconsistent with normal property management principals and might be unfair to school districts. Therefore, Staff has developed a proactive program that is designed to extend the useful life of a Relocatable while preserving the State's assets.

In order to adopt a Rehabilitation program, it would be necessary to develop a grant program that would provide funds, generated from the lease revenue, to reimburse school districts for rehabilitation costs for key

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ASSET MANAGEMENT PLAN (cont.)

OPTION #1 – REHABILITATION PROGRAM (cont.)

components when those components have reached their useful life. These components would be placed on a schedule and Staff would coordinate with school districts to ensure the key components are rehabilitated. Staff would accomplish this through an education program that would instruct school districts on the proper care and maintenance.

The figures in Chart B represent the cost to rehabilitate three proposed groups of Relocatables. The data illustrates the estimated rehabilitation costs for the major building components if the Board does not elect to adopt a disposal plan, adopt a disposal plan at 20 years and 15 years of age, which account for a graduated schedule for the disposal of Relocatables. Based on the figures below, it is clear that the rehabilitation costs and associated general liabilities to the State are far less if the Board adopts a disposal plan when the classrooms reach 15 years of age, than if the State were not to adopt a disposal plan.

CUMULATIVE COST TO REHABILITATE THE FLEET OVER A PERIOD OF 20 YEARS

CHART B		YEAR 2005	YEAR 2015	YEAR 2020	YEAR 2025	Total
	No Disposal Plan (6,579 classrooms)	$76,183,776	$114,566,706	$177,573,789	$231,679,485	$600,003,756
	Disposal at 20 Years (6,330 classrooms)	$65,920,545	$58,302,072	$38,894,031	$0	$163,116,648
	Disposal at 15 Years (4,869 classrooms)	$26,486,694	$25,093,574	$0	$0	$51,580,268

In determining the overall costs to the State, it is necessary to also factor in the operating costs for the Program. The costs associated with operating this Program do not include the purchase of new Relocatables and include transportation costs to move a Relocatable from one school district to another, administrative costs to manage the Program, and reimbursable allowances for costs associated with setting up the Relocatable. The chart below illustrates the financial shortfall when calculating the rehabilitation costs and the operating costs and comparing those costs to the lease payment revenue generated.

NET PROFIT / LOSS FOR THE PROGRAM OVER A PERIOD OF 20 YEARS

CHART C		COST TO REHABILITATE RELOCATABLES	COST TO OPERATE THE PROGRAM*	REVENUE GENERATED ***	PROFIT / LOSS
	No Disposal Plan (6,579 classrooms)	$600,003,756	$419,890,135	$480,003,840	$(539,890,051)
	Disposal at 20 Years (6,330 classrooms)	$163,116,648	$269,845,305	$221,338,752	$(211,623,201)
	Disposal at 15 Years** (4,869 classrooms)	$51,580,268	$104,373,832	$119,650,752	$(36,303,348)

* The cost to operate the program represents only those costs for transportation, reimbursable allowances, and administrative costs and excludes the initial purchase costs. This Option does not anticipate the purchase of new Relocatables.

**The costs represented under "Disposal at 15 Years" are calculated over a period of 15 years and are not carried forward over 20 years.

*** Revenue generated is based on an average lease payment rate of $3,648 annually.

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ASSET MANAGEMENT PLAN (cont.)

OPTION #1 – REHABILITATION PROGRAM (cont.)

Chart E illustrates the lease payment rate necessary to sustain the Program under Option #1, while adjusting for a graduated schedule for the disposal of the Relocatables. If the Board elects to retain the Relocatables and not adopt a disposal plan, the State may increase its exposure for rehabilitation costs and general liabilities as a result of using Relocatables that have exceeded their useful life expectancy.

The SFP regulations require an adjustment to a school district's baseline eligibility when facilities are added to the inventory. Staff is proposing that school districts that wish to purchase a Relocatable not be required to adjust their SFP baseline eligibility. The purpose of this proposal is to reduce the State's liability due to an aging fleet and provide an incentive to those school districts currently participating in the Program. Further, the existing Relocatables are not comparable to newer relocatable classrooms and the existing Relocatables can not continue to meet the long-term needs for the school districts. To ensure that school districts can purchase a Relocatable without an adjustment to their baseline eligibility, legislative and/or regulatory remedies would need to be enacted to ensure this proposal.

To summarize Option #1:

- Proposes a Rehabilitation Program that provides school districts with the funds to rehabilitate the eight key components of a Relocatable.
- Outlines three disposal plans; no disposal, disposal at 20 years and 15 years of age.
- Requires a lease payment increase to cover the operating and rehabilitation costs identified in this proposal.
- Permits school districts to purchase a Relocatable without impacting their baseline eligibility.

OPTION #2 – PROGRAM PHASE-OUT WITHOUT REHABILITATION

This option requires the State to develop policy and procedures that allows for the phasing out of the Program by disposing of classrooms when they have met a predetermined age. Under this proposal, school districts will still be required to maintain the condition of the classroom. However, when a Relocatable reaches a predetermined age, the Board would have the option to dispose of the classroom.

In determining the appropriate age in which to dispose of a Relocatable under this option, Staff analyzed the useful life expectancy data and determined that 15 years of age would adequately limit the amount of future liability the State would incur, if the State were to retain the classroom beyond 15 years of age. Staff anticipates that under this option, all relocatable classrooms will be completely phased out by the year 2018 or sooner.

Staff determined that the best return on investment for a Relocatable requires the State to dispose of the classrooms at 15 years of age. An analysis of the rehabilitation costs compared to the lease payment revenue generated produces a 57 percent return on investment when Relocatables are disposed of at 15 years of age. Should the State dispose of Relocatables at 20 years of age, the return on investment only yields a 26 percent return on investment.

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ASSET MANAGEMENT PLAN (cont.)

OPTION #2 – PROGRAM PHASE-OUT (cont.)

TOTAL COST TO OPERATE THE PROGRAM VERSUS THE LEASE PAYMENT REVENUE

CHART D		COST TO OPERATE THE PROGRAM*	REVENUE GENERATED***	PROFIT / LOSS
	No Disposal Plan (6,579 classrooms)	$419,890,135	$480,003,840	$60,113,705
	Disposal at 20 Years (6,330 classrooms)	$269,845,305	$221,338,752	$(48,506,563)
	Disposal at 15 Years** (4,869 classrooms)	$104,373,832	$119,650,752	$15,276,920

* The cost to operate the program represents only those costs for transportation, reimbursable allowances, and administrative costs and excludes the initial purchase costs. This Option does not anticipate the purchase of new Relocatables.

**The costs represented under "Disposal at 15 Years" are calculated over a period of 15 years and are not carried forward over 20 years.

*** Revenue generated is based on an average lease payment rate of $3,648 annually.

Chart E illustrates the lease payment rate necessary to sustain the Program under Option #2, while adjusting for a graduated schedule for the disposal of the Relocatables. If the Board elects to retain the Relocatables and not adopt a disposal plan, the State may increase its exposure to general liabilities as a result of using Relocatables that have exceeded their useful life expectancy.

Currently, regulations require an adjustment to a school district's SFP baseline eligibility when facilities are added to the inventory. Staff is proposing that school districts that wish to purchase a Relocatable will not be required to adjust their SFP baseline eligibility. To ensure that school districts can purchase a Relocatable without an adjustment to their SFP baseline eligibility, legislative and/or regulatory remedies would need to be enacted to ensure this proposal.

To summarize Option #2:

- Requires school districts to continue providing for the general maintenance of the Relocatable.
- Outlines three disposal plans; no disposal, disposal at 20 years and 15 years of age.
- Requires a lease payment increase to cover the operating costs for this proposal.
- Permits school districts to purchase a Relocatable without impacting their SFP baseline eligibility.

OPTION #3 - IMMEDIATE SALE OF THE PROGRAM FLEET

This option requires the State to develop policy and procedures that allows for the immediate sale of all Relocatables owned by the Board. Under this proposal, the Board would authorize the sale of 6,579 Relocatables to school districts, other public agencies or interested private entities up to an amount equal to the purchase price paid by the Board, including all purchase costs absorbed by the State, pursuant to EC Section 17089.2.

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ASSET MANAGEMENT PLAN (cont.)

OPTION #3 - IMMEDIATE SALE OF THE PROGRAM FLEET (cont.)

This proposal is supported by two main factors that have developed in recent years. First, the relocatable manufacturing industry has grown and provides school districts with options beyond the State's Program at competitive prices throughout the State. Secondarily, the funds necessary to adequately manage the Program have substantially diminished. It may be prudent for the Board to sell the Relocatables to avoid any future general liabilities and recover costs previously expended on the Program. The funds generated from the immediate sale could be directed to augment various programs administered by the Board, or reduce the debt service on the bonds. Staff would need to come back to present various disposal options of the fleet under this Option.

Currently, regulations require an adjustment to a school district's SFP baseline eligibility when facilities are added to the inventory. However, Staff is proposing that school districts that elect to purchase a Relocatable would be permitted to do so and the school district's SFP baseline eligibility would not be adjusted to reflect an increase in classroom capacity. To ensure that school districts can purchase a Relocatable without an adjustment to their SFP baseline eligibility, legislative and/or regulatory remedies would need to be enacted.

To summarize Option #3;

- Disposes of Relocatables immediately and offer Relocatables at fair market value, pursuant to EC Section 17089.2.
- Permits school districts to purchase a Relocatable without impacting their SFP baseline eligibility.

LEASE PAYMENT INCREASE PROPOSAL

The Board, in the past, has designated funds through various bond measures to fund the Program. These bonds generated $62 million that permitted the OPSC to purchase new relocatable classrooms, cover transportation costs and administrative costs associated with managing the Program. The funds generated from the bond measures have diminished. Without retention of the Program's revenue, it will be necessary for the Board to increase its lease payment rates as shown below in Chart E in order to implement Option #1 or #2. However, pursuant to EC Section 17089, the SAB is limited to an increase in the annual lease payment to a maximum of $6,364 for Fiscal Year 2005-06 based on the annual adjustments for inflation set forth in the statewide cost index for classroom construction since 1991.

VARIOUS LEASE PAYMENT RATE INCREASE OPTIONS

CHART E		OPTION #1 (Rehabilitation)	OPTION #2 (Phase-Out)
	Disposal at 20 Years	$9,500	$8,175
	Disposal at 15 Years	$9,450	$8,720

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STAFF COMMENTS

It may no longer be cost beneficial for the State to remain in this business, because there is now a private portable classroom manufacturing and leasing industry operating throughout California that is able to support the demand for relocatable classrooms at a comparable price. For example, private industry is charging approximately $6,500 per classroom annually, which includes furniture and equipment, transportation, set-up and maintenance costs. The original intent of the Program, to provide housing in emergency situations, remains meritorious. However, this purpose has long since been superseded by the Program's evolution into a long-term lease program. If the Board elects to phase-out of the Program, the Board may address emergencies, such as natural disasters, through the SFP.

Given the comparable lease rates available through private industry, the costs of a comprehensive rehabilitation program exceed the benefits because the State would, in the next ten years, be faced with the additional costs of replacing major building components. The private industry leases include a maintenance/rehabilitation program. The portables provided through the private industry would better meet the current requirements under Title 24 and address some of the issues related to air quality and noise pollution that are associated with the State's older Relocatables.

The Board's existing policy regarding purchasing portable classrooms appears to be appropriate for establishing the fair market value that school districts will be required to pay for Relocatables. Under current statute, school districts are required to pay the initial purchase price of the building, delivery and installation costs, utility connection costs, furniture and equipment costs, architect fees, inspection and Division of the State Architect fees, less lease payment revenues collected for each Relocatable. The Board's policy has been that the purchase cost to the district shall not be less than $4,000.

The State's Annual Budget control language has authorized the transfer of the lease payment revenue generated by the Program to the State's General Fund. The last time the Program was able to retain the lease payment revenue was in Fiscal Year 2001-02. The Program currently lacks sufficient funding to cover the cost of moves requested by school districts and storage of excess Relocatable inventory. The demand for the State's relocatable classrooms has diminished due to the availability of new construction General Obligation Bonds and the expansion of the private portable classroom manufacturing/leasing industry.

Current lease payment revenues are insufficient to cover the costs associated with operating the Program and rehabilitating the aging relocatable fleet. The State's Relocatables have been leased at a rate of $4,000 per year since 1991. To support a rehabilitation program (Option #1) without retention of the Program's revenue, the lease payment rates would be $9,500 with a disposal plan for all buildings at 20 years of age and $9,450 with a disposal plan for all buildings at 15 years of age. To support a phase-out program (Option #2) without retention of the Program's revenue, the lease payment rates required would be $8,175 with a disposal plan for all buildings at 20 years of age and $8,720 with a disposal plan for all buildings at 15 years of age. However, pursuant to EC Section 17089, the SAB is limited to an increase in the annual lease payment to a maximum of $6,364 for Fiscal Year 2005-06 based on the annual adjustments for inflation set forth in the statewide cost index for classroom construction since 1991. To minimize the financial burden on the school districts, Staff is proposing that the Board increase its lease payment rate by $1,000 beginning with the 2005-06 Fiscal Year, with the balance of the increase occurring in the following fiscal year. Based on the districts with the highest number of State Relocatables, the highest increase to any one school district would be $206,000.

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STAFF COMMENTS (cont.)

Provided that all lease payment revenues are strictly dedicated to supporting the Program operation costs, there is no change required to the current lease payment to support a phase-out program, without a rehabilitation program, and a disposal plan for all buildings at 15 years of age. However, a phased approach for the State to withdraw from the long-term leasing of relocatable classroom business needs to be developed that minimizes the fiscal impact on school districts. As mentioned previously, Staff is proposing to change existing regulations to allow school districts to purchase all Relocatables over 15 years of age without a charge to their SFP baseline eligibility. This proposal offers several benefits to both parties. The State will be able to maximize its return on the investment in Relocatables and minimize its exposure in terms of rehabilitation costs, disposal costs, and general liability issues associated with using Relocatables that have exceeded their useful life expectancy. School districts, on the other hand, will receive the benefits of purchasing classrooms and an exemption from the SFP baseline eligibility adjustment that would have otherwise been charged.

RECOMMENDATIONS

1. Approve Option #2 with a disposal plan at 15 years and instruct the OPSC to implement the Phase-Out Program.

2. Direct Staff to present regulations at a future Board for the implementation of Option #2, as specified.

3. Approve the immediate disposal of all relocatable classrooms older than 20 year of age.

4. Require that all lease payment revenues be made available to support the Program.

5. If the Board does not approve Recommendation No. 4, increase the lease payment rate for the Program from $4,000 to $5,000 beginning with the 2005-06 Fiscal Year. Approve the balance of the lease payment rate increase for the 2006-07 Fiscal Year.

6. Authorize the encumbrance of approximately $5 million for relocation expenses, set up costs and other related expenses.

BOARD ACTION

In considering this Item, the State Allocation Board on June 22, 2005 postponed this Item until the July SAB meeting. The Board requested Staff to prepare a report to include:

1. Research the transfer of the current year’s Relocatable proceeds to the General Fund, including review of the tape from the Budget and Fiscal Review Subcommittee No. 1 on Education.

2. History of the authorization for transferring Relocatable funds to the General Fund.

3. A resolution declaring the Board’s desire to retain Relocatable proceeds for the Program’s needs.

4. Input from interested parties regarding the options proposed by Staff including the non-dischargeability of Relocatable buildings to ensure equity.

5. Information about the maintenance work performed by school districts in order to ensure Relocatables are maintained in good repair.