

**Malibu Unification Negotiations Committee  
Meeting Minutes  
Tuesday, January 24, 2017**

**SMMUSD District Offices,  
Board Training Room (next door to Board Conference Room)  
1651 16th St., Santa Monica, CA 90404**

I. Call to Order / Roll Call

*The Committee called the meeting to order at 7:00 p.m. with all members present:*

*Tom Larmore*

*Laura Rosenthal*

*Paul Silvern*

*Manel Sweetmore*

*Debbie Mulvaney*

II. Approval of January 16, 2017 Meeting Minutes

*Mr. Silvern offered a technical edit to the draft minutes. By consensus, the Committee approved the corrected minutes of January 16, 2017.*

III. Discussion of Resignation of Malibu Team Member (Makan Delrahim)

*The Committee agreed that the Report to the Board should explain that Mr. Delrahim served as a Malibu Team member between May 2016 and mid-January 2017, and that his resignation was due to an employment change. The Committee also agreed that, for the record, Mr. Delrahim should be asked to submit a formal resignation letter to the Malibu City Manager.*

*The Committee's consensus was that it was impractical at this point in the negotiations process for the Malibu City Manager (Reva Feldman) to appoint a new member. Ms. Rosenthal reported that she had consulted with Ms. Feldman on this issue, and that she is in accord with not appointing a replacement Committee member at this time.*

IV. Follow-up Items from Previous Meeting

A. Status report/discussion on SSC's review of revenue neutrality formula and related spreadsheet of projections

- *Mr. Sweetmore reported that he has scheduled a teleconference with SSC for the purpose of walking SSC through the mechanics of the spreadsheet.*
- *Mr. Larmore and Mr. Silvern shared SSC's recommended options regarding how the Formula should calculate the revenue per ADA for a theoretical SMMUSD. By consensus, the Committee agreed that all calculations in the Formula should be based on data from the audited financial statements for SMUSD and MUSD.*

- *In addition, the Committee agreed that the Report should recommend that SMUSD and MUSD ask their respective auditors to include the needed data (i.e. a division of revenue in the Unrestricted General Fund vs. Restricted General Fund) as a supplemental schedule in the audited financials.*

B. Discussion of upcoming planning session regarding rollout of the Committee's report to the Board

*In preparation for the planning session, Mr. Silvern and Ms. Rosenthal solicited the Committee's views on the rollout of the Report to the Board. Issues discussed included the Committee's interest in:*

- *An opportunity to brief Board members, either individually or in pairs, on the Report before the Committee's public presentation; these meetings will need to be structured to remain compliant with Brown Act requirements.*
- *Figuring out a schedule that explicitly addresses the City of Malibu role, as outlined in the Board's Action Item, to review and act on the Report.*
- *Ensuring that stakeholder groups (e.g., District employee unions, AMPS, PTA Council) have a timely opportunity to become familiar with the Report and ask questions to clarify their understanding of the Agreement. Related to this, briefings/presentations about the Report for community members should be scheduled in both Santa Monica and Malibu.*

V. Continuation of Worksession and Editing on Memorandum Report and Term Sheets

*The Committee considered and recommended multiple edits to the latest versions of the Memorandum Report and Term Sheets. By consensus, the Committee decided that:*

- *The Report should add the Committee's glossary of acronyms, terms, and phrases as Appendix E. The current glossary will need to be updated to include more recently added definitions.*
- *The Executive Summary embedded in the Memorandum Report should be no longer than two pages. It does not need to be written as a "stand-alone" document. Once the Report is completed, the Committee may need to work on preparing some sort of stand-alone summary that could be used at community briefings after the Report has been submitted to the Board.*
- *The Committee's recommendation for the Board to consider supporting processing the unification matter entirely through special State legislation (rather than the petition procedure outlined in the State Education Code, or some combination of special State legislation and the Education Code procedure) should be further articulated in the Report and its placement should be moved up to appear earlier both in the Memorandum and Term Sheets.*

- *Before submitting the Report to the Board, the Term Sheets should be reviewed by Jan Maez, SMMUSD Chief Financial Officer, and John Lemmo, Procopio as domain experts. The Committee clarified that the purpose of these pre-release reviews is to obtain feedback on the feasibility, legality, and enforceability of the Agreement. The Committee agreed to aim for getting the Term Sheets in “good enough shape” to give to Ms. Maez and Mr. Lemmo next week.*
- *Also, before submitting the Report to the Board, a final draft of the full Report and its appendices should be shared with several members of the community (one from Santa Monica and one from Malibu) to obtain feedback on the readability of the Report. Ms. Mulvaney agreed to line up someone from Santa Monica, and Ms. Rosenthal agreed to line up someone from Malibu.*

*Specific assignments that resulted from the editing session were:*

- *Mr. Sweetmore will draft the sections in the Memorandum Report and Term Sheets regarding the cost of living adjustment and the annual cycle of Formula calculations.*
- *Mr. Larmore will work with Ms. Orlansky to articulate the assignment for Procopio’s pre-release review.*
- *Ms. Rosenthal agreed to work on reducing the Executive Summary to two pages.*
- *Ms. Orlansky will prepare revised drafts of the Memorandum Report and Term Sheet that responds to the comments voiced by Committee members. The draft will be circulated again for feedback from all Committee members.*
- *All Committee members will continue to work on identifying sections in the different documents being prepared for delivery to the Board that need additional editing for purposes of clarifying both the intent and implementation of the Agreement.*

VI. Upcoming meetings

- *Tuesday, January 31, 2017, 7-9 p.m., at Malibu City Hall*
- *Tuesday, February 7, 2017, 7-9 p.m. at District Offices in Santa Monica (Hold)*

VII. Adjournment

*The Committee meeting adjourned at 9:25 p.m.*

## MEMORANDUM REPORT

To: Members of the Board of Education  
Santa Monica-Malibu Unified School District

From: The Malibu Unification Negotiations Committee

Date: XXXXXXXX, 2017

Subject: Negotiated Terms of Agreement on the Financial Implications of Reorganizing  
SMMUSD into Two Separate Unified School Districts

This memorandum ("Report") is the Malibu Unification Negotiations Committee's ("Committee") report back to the Santa Monica-Malibu Unified School District (SMMUSD or "District") Board of Education ("Board"). As directed by the Board, this Report documents the items negotiated and the unanimously approved terms of agreement ("Agreement") reached for each item by the two negotiating teams appointed by the Board and City of Malibu City Manager. The signatures of all Committee members (page X) denote that both negotiating teams approve this Report and its attachments.

The District's approved General Fund budget for 2016-2017 is \$171.2 million, of which the Board approved \$150.5 million for expenditures with a projected fund balance of \$20.7 million. The District currently serves 11,003 Kindergarten through 12<sup>th</sup> grade students in the two non-contiguous coastal communities of Santa Monica and Malibu. Approximately 84 percent of the District's students attend 12 schools located in the City of Santa Monica, and 16 percent attend five schools located in Malibu. Appendix A contains a map of SMMUSD that shows the locations of its schools by community; the map also depicts how the Malibu portion of SMMUSD includes the City of Malibu and certain unincorporated area north of the Malibu city limits.

In December 2015, the Board established the Committee to address the financial implications of a potential reorganization of the current SMMUSD into two separate K-12 school districts, a Santa Monica Unified School District (SMUSD) and a Malibu Unified School District (MUSD). The Board provided a list of financial issues for the Committee to address and articulated objectives for the negotiations. A priority assignment for the Committee was to negotiate terms that would enable the reorganization to occur without a negative impact on the financial condition of the stand-alone Santa Monica Unified School District (SMUSD). The Committee's report to the Board is organized as follows:

Part I:	Executive Summary
Part II:	Background
Part III:	Overview of the Committee's Process
Part IV:	Summary of the Negotiated Agreement
Part V:	Acknowledgements

Part VI (page X) contains the Committee members' signatures, certifying that they each have read, understood, and agreed to the terms of agreement, as set forth in this Report and its Appendices.

This Report includes four Appendices:

- Appendix A: Map of SMMUSD that depicts the boundaries of the District and shows the location of current schools.
- Appendix B: A categorized listing of electronic links to all the resources used by the Committee as the basis of discussion and decision-making, including the Committee's agendas, minutes, consultant reports and other documents.
- Appendix C: Term Sheets that contain details of the Committee's negotiated Agreement for each of five topic areas.
- Appendix D: An illustrative projection of calculations and payments for the proposed Revenue Neutrality formula as summarized in the Report and presented in more detail in the Term Sheet for Topic #1: Operating Budget Impact. The projection is based on the best information available at the time of this writing.

## Part I: Executive Summary

In December 2015, the SMMUSD Board of Education (Board) established the Malibu Unification Negotiations Committee (“Committee”) to negotiate an agreement on the financial implications of a potential reorganization of the current District into two separate school districts: the Santa Monica Unified School District (SMUSD) and Malibu Unified School District (MUSD).

The Board assigned the Committee financial issues to address and articulated objectives for the negotiations. A priority assignment for the Committee was to negotiate terms that would eliminate any significant adverse financial effects of reorganization on SMUSD as a stand-alone district. The Board’s Financial Oversight Committee and District finance staff had raised concerns about this potential financial result in a report to the Board during the fall of 2015.

The Committee consisted of three members appointed by the Board to represent the interests of a potential separate SMUSD (the “Santa Monica Team”), and three members appointed by the Malibu City Manager to represent the interests of a potential separate MUSD (the “Malibu Team”). The Board directed the Committee to appoint an impartial facilitator, and instructed both teams to “work cooperatively with one another and with their counterparts, to develop and agree upon terms that promote the aspirations of the Board.”

**The Committee’s Process.** Between March 2016 and January 2017, the Committee held more than 30 meetings. In its early meetings, the Committee selected a facilitator, adopted Ground Rules, and selected outside legal and school finance consultants. The Committee also adopted guiding principles for its negotiations, which stated that all terms of an agreement:

- Must be financially viable for both SMUSD and MUSD.
- Must ensure a degree of predictability for both SMUSD and MUSD, to enable each school district to be able to plan ahead with a reasonable degree of resource certainty.
- Must avoid establishing potential negative incentives for either SMUSD or MUSD, e.g., create a disincentive to pursue increased revenue or otherwise improve education.
- Must be clear and understandable, legal, and enforceable.

Where it proved useful to the negotiation process, the Committee developed supplemental guiding principles specific to the issues on the table. The Committee adopted a Plan of Work that was organized around the Board’s objectives for the negotiations, and the Committee employed a set of “Term Sheets” to track the Committee’s agreements.

**Overview of the Negotiated Agreement.** The Committee reached a consensus package of principles, terms, conditions, and procedures that address the Board’s objectives. Together, these constitute the Committee’s Agreement. The next two pages summarize the Committee’s Agreement, organized by the five key issues addressed during the negotiations.

**Issue #1: Operating Budget Impact of Reorganization.** The Board's objective on this issue was to eliminate any significant adverse financial effects of reorganization on SMUSD as a stand-alone district. The Committee adopted the term "Revenue Neutrality" to describe this Board objective, and reached agreement on a Revenue Neutrality Formula that:

- Specifies how to calculate the financial effect of reorganization on SMUSD;
- Establishes a method for implementing a fair schedule of payments from MUSD to SMUSD that, in the aggregate, results in Revenue Neutrality; and
- Calculates the payment owed in any single year in a way that takes Malibu's ability to pay into account, while also maintaining predictable and stable budget growth for both districts in an amount at least equal to a cost of living adjustment.

Other key provisions related to the Revenue Neutrality Formula are that calculations will be performed by an expert third-party jointly selected by SMUSD and MUSD, based on actual financial data (i.e., not on projections), and performed beginning with the first year following separation through fiscal year 2029-2030. The Agreement provides for amending the length of the Revenue Neutrality arrangement if the data evidence SMUSD can exist without any significant adverse Financial Effect from reorganization, and specifies what significant external events would trigger a renegotiation of the Formula and payment schedule.

**Issue #2: Division of the District's Assets (cash, land/buildings).** The Board's objective on this issue was to allocate the District's assets in a way that is fair to both MUSD and SMUSD and that considers the sources and uses of cash in various funds.

With respect to dividing the District's cash balance at the time of separation, the Agreement outlines a method for each fund. For funds where the source of revenue (in relative terms) has tracked the number of students in Santa Monica and Malibu, the division will be based on the pro rata Average Daily Attendance (ADA) between what will be SMUSD and MUSD. For other funds where the source or use of revenue evidenced a different division would be more equitable, the Committee designed an alternative method.

With respect to land and building, the Agreement provides that all schools will be allocated to the respective district where they are located. The District's other land and buildings (all located in Santa Monica) will be allocated to SMUSD, but with the provision that if SMUSD ever sells the District Headquarters or a revenue-producing property, then the net proceeds will be split between SMUSD and MUSD according to a methodology based on relative ADA.

**Issue #3: Bond-Related Items and Other Liabilities.** The Board's objective on this issue was to allocate bond debt, a mechanism for bond refinancing, and the authority to issue authorized but not-yet-issued bonds in a manner that is fair to both SMUSD and MUSD.

To address the Board's bond-related objectives, the Agreement provides that:

- The District's existing bond debt will be allocated between SMUSD and MUSD based upon the respective assessed values of Santa Monica and Malibu; and each district should be authorized to make decisions regarding refinancing of this debt without need to coordinate with the other.
- The allocation of authorized but not-yet-issued bonds should depend on the status of projects and plans of SMUSD and MUSD at the time of separation, and be made consistent with the guiding principles adopted by the Committee.
- After the date of separation, the decision by either SMUSD or MUSD to issue bonds should be left to the sole discretion of each district.

**Issue #4: Environmental Liability.** The Board's objectives on this issue included establishing a structure under which MUSD assumes responsibility for any remaining remediation of any contamination in Malibu schools and indemnifies SMUSD for any future claims arising from such remediation work.

To address the Board's objectives, the Agreement recognizes that the current ongoing remediation of PCBs (polychlorinated biphenyl), as contemplated in SMMUSD's building replacement and renovation program will not be affected by separation. This remediation program is scheduled to be completed by December 2019.

The Agreement also provides that any source of environmental liability for which no such plan has been developed, whether or not known at the time of separation, will be the responsibility of the school district that owns the property where the liability exists. And further, each district will indemnify the other district against such environmental liability.

**Issue #5: Implementation of the Committee's Recommendations.** While negotiating details of the implementation process were beyond the scope of the Board's objectives, the Committee agreed it was important to offer a recommendation on how to resolve the financial items identified in the report that, due to various reasons, cannot be finalized until the actual time of separation or post-separation.

For this purpose, the Committee recommends the appointment of two groups.

- Appointed by the Board, **Group One** should be tasked to work on the things that need to happen between the time the Board approves moving forward with unification and the time that separation occurs.
- Appointed by the respective Boards of Education of SMUSD and MUSD after separation occurs, **Group Two** should be tasked to work on all remaining issues that must be resolved to ensure a smooth transition to the interactions of the two districts going forward.

**SOMETHING SHORT AND SWEET ABOUT IMPLEMENTATION OPTIONS??**



## Part II: Background

**General.** Over the past five years, the District and Advocates for Malibu Public Schools (AMPS) studied multiple issues related to a potential reorganization of SMMUSD into two separate K-12 districts: a Santa Monica Unified School District (SMUSD) and a Malibu Unified School District (MUSD). Paradoxically, State law refers to this process of reorganization as “unification.”

Among the many questions addressed by these studies, a particular focus of attention has been on how to divide the finances of the current District between two new districts, and the potential that a reorganization could affect the revenue per student in a stand-alone Santa Monica district as compared with the existing District. (See Appendix B-X, SSC’s Review of Prior Reports and Analyses of District Reorganization.)

During 2014 and 2015, the District’s Financial Oversight Committee (FOC) and consultants for AMPS analyzed many of the issues associated with dividing the District’s financial assets and liabilities between two potentially new districts. The FOC and District financial staff also performed a focused review on potential aggregate and per-student revenues in each new district as compared with the current District.

The FOC’s initial projections showed that reorganizing the District would have a negligible impact on the revenue available to a stand-alone SMUSD. However, in the fall of 2015, based on updated financial information, the FOC and District financial staff reported to the Board that a reorganization could, at least for a period of time, materially reduce revenue to SMUSD on a per student basis (as measured by Average Daily Attendance, or ADA) when compared to revenue per ADA without separation.

The reasons for this negative fiscal impact on SMUSD are complex. They include the intricacies of how State funds are provided to local school districts in California, the fact that although a stand-alone SMUSD would keep certain revenues provided by the City of Santa Monica (currently shared with the Malibu schools), it would no longer receive property tax revenue generated in the Malibu community, and SMUSD is likely to achieve “minimum State aid” and “basic aid” status more slowly than would a combined District. (State law allows a school district that achieves “minimum” or “basic” aid status to keep more of its property taxes for funding its schools.)

For further explanation of these issues, including how the State’s Local Control Funding Formula (LCFF) affects the finances of a reorganization, more about the implications of achieving “minimum” and “basic” State aid status, see Appendix B-X for SSC’s presentation on school finance in California.

**The Board's Establishment of the Malibu Unification Negotiations Committee.** On December 17, 2015, the Board unanimously adopted an Action Item (Appendix B-X) to establish the Committee to negotiate the financial implications of a potential reorganization of the current District into SMUSD and MUSD. In creating the Committee, the Board's Action Item stated:

The Board of Education expressed its unanimous desire for the co-existence of the Santa Monica Unified School District and the Malibu Unified School District as two excellent school districts serving their respective communities and providing the best educational opportunities for their respective students as long as it can be accomplished in a manner that does not have a negative impact on the financial condition of the remaining Santa Monica Unified School District. (Board Action Item, 12/17/2015, Recommendation No. A.16)

The Committee consisted of two teams of negotiators. The District's Superintendent would appoint three members to represent the interests of a potential separate SMUSD (the "Santa Monica Team"); and the City Manager of the City of Malibu would appoint three members to represent the interests of a potential separate MUSD (the "Malibu Team").

The Board directed the negotiating teams to appoint an impartial facilitator to assist in the negotiations and instructed both teams to "work cooperatively with one another and with their counterparts, to develop and agree upon terms that promote the aspirations of the Board." The Board set the scope and objectives for the negotiations, established a process to follow after the Committee submits a report, and outlined criteria for determining success. of the negotiations. (See below.)

The Board's Action Item acknowledged that the Committee would likely require access to outside consultants to advise on school budgeting and finance and legal issues. Based on past discussions, the Board Action Item noted an expectation that AMPS would pay for any consultants the Committee hired, and that the appropriate agreements between the District and AMPS to implement this arrangement would be executed before negotiations started. The Board Action Item directed that District and AMPs to evenly split the facilitator's fees.

**The Board's Stated Objectives for the Committee's Negotiations.** The Board's objectives for the negotiations, as stated in the Action Item creating the Committee, included:

- Elimination of any significant adverse financial effects of separation on SMUSD.
- Allocation of cash in the General Fund Account and the Capital Facilities Fund in a manner which is fair to both MUSD and SMUSD considering the sources and uses of cash in the various funds.
- Allocation of bond debt and authority to issue authorized but unissued bonds in a manner which is fair to both MUSD and SMUSD and establishment of any legal mechanisms that might be required to achieve fairness.
- Establishment of a mechanism that would permit refinancing of outstanding bonds in order to reduce property tax assessments.

- Establish a procedure under which agreements on the preceding four items can be revisited on a reasonable schedule.
- Establishment of a structure under which MUSD assumes responsibility for any remaining remediation of any contamination in Malibu schools and indemnifies SMUSD for any future claims arising from such remediation work or failure to undertake appropriate work.
- Dismissal of the pending lawsuit against SMMUSD or an enforceable agreement from the plaintiffs that SMUSD will be dismissed from the lawsuit.
- Receipt by the Board of a legal opinion from a firm selected by the Board with respect to any potential continuing exposure of SMUSD following separation and a conclusion by the Board that any such exposure is reasonable.

It should be kept in mind that the financial issues assigned to the Committee for negotiations address a subset of the statutory criteria for the State Board of Education to apply before approving the reorganization of a school district via the procedure contained in the State Education Code. Appendix B-X contains a chapter from the *California Department of Education's School District Organization Handbook*, (dated September 2016), that explains the legal criteria governing reorganization proposals under this State law. As discussed later in this Report, the petition procedures outlined in the State Education Code are not the sole option for implementing school district reorganization in California.

**What Happens Following Receipt of the Committee's Report.** The Board's Action Item creating the Committee outlined the following steps to follow the submission of a report to the Board, should the Committee collectively determine that negotiations achieved the Board's objectives:

- The signed report will be made available for public inspection.
- Following a two-week period for public review, the Board will discuss the final written report on the negotiations as a Discussion Item during a regular Board Meeting.
- The Board may determine that changes to the negotiated agreement are required, based on comments from the public and its own discussion. If so, the Board will communicate the required changes to the Santa Monica negotiating team and ask them to reopen the negotiations with the goal of incorporating the required changes.
- After the changes are incorporated, the written report will be modified as needed.
- Alternatively, if the Board determines that no changes in the negotiated agreement are required, then the final report will be presented to the Board as a Major Action item at the next regular Board meeting.

**The Board's Conditions for the Determination of Successful Negotiations.** The Board's Action Item creating the Committee articulated four conditions for determining that the negotiations have been completed successfully. In sum:

- The negotiating teams collectively determine that negotiations have achieved the Board's objectives and present the evidence for their determination to the Board.

- Any technical and legal concerns regarding the negotiated agreements have been resolved satisfactorily.
- The Board determines that negotiations have achieved its objectives and formally approves the written report and the agreements therein as a Major Action Item during one of its regular public meetings.
- The Malibu City Council formally approves the written report and agreements therein during one of its regular public meetings.

### Part III: Overview of the Committee's Process

**Committee Members Appointed.** On January 21, 2016, the Board of Education approved the Superintendent's nomination of the three members of the Santa Monica Team and formally acknowledged the three members appointed to the Malibu Team by the Malibu City Manager. The members of the Committee are listed below.

Santa Monica Team	Malibu Team
Tom Larmore	Laura Rosenthal
Debbie Mulvaney	Manel Sweetmore
Paul Silvern	Makan Delrahim*

\* In April 2016, Makan Delrahim replaced Kevin Shenkman, an original Malibu Team member. In January 2017, Mr. Delrahim resigned from the Committee due to an employment change.

Between March 2016 and January 2017, the Committee held more than 30 meetings. All Committee meetings were open to the public and the Committee operated under the rules of the State's Brown Act. The meeting location rotated between the District offices in Santa Monica and Malibu City Hall. Support with taking minutes was provided by the District for meetings held in Santa Monica and by the City of Malibu for meetings held in Malibu. Appendix B-X contains a complete set of the Committee's meeting agendas and minutes.

**Committee's First Order of Business.** The Committee convened several pre-negotiation meetings in March 2016 to select a facilitator, develop the agreement between the District and AMPS regarding the payment of consultant fees, and begin the process of selecting consultants to provide legal support and expertise on school financing in California.

During its initial meetings, the Committee selected Karen Orlansky to serve as its facilitator and adopted Ground Rules that addressed expectations for Committee member conduct that makes for effective groups, meeting logistics, compliance with the Brown Act, public comments at Committee meetings, and the method adopted by the Committee for making decisions by consensus. The Ground Rules also included a written agreement on the role of the facilitator. Appendix B-X contains the adopted Ground Rules.

The Committee selected Procopio (a full-service law firm located in San Diego) to provide legal support, and School Services of California, Inc. (SSC) to provide consultant services related to school budgeting and finance. The retention agreements with the Committee's consultants were formally signed in May 2016.

Early on, the Committee recognized that its discussions and subsequent public reporting would benefit from adopting a glossary that defined key words and phrases as well as acronyms for use during the negotiations. Appendix B-X contains the latest version of the glossary, which was updated throughout the course of the Committee's work.

**Plan of Work.** To guide its work, the Committee adopted a Plan of Work that essentially mirrored the Board's charge to the Committee. The Committee organized its negotiations into four key financial issue areas:

- Operating budget impact of reorganization;
- Division of the District's assets (cash balances, land, buildings);
- Bond-related items and other financial liabilities; and
- Environmental liability.

The Committee added a fifth category for addressing issues related to implementation of its recommendations. Appendix B-X contains a copy of the Committee's Plan of Work.

**Principles Adopted to Guide the Negotiations.** The Committee adopted general principles to serve as guidelines for its negotiations. The Committee agreed that all terms of an agreement related to the financial reorganization of the District into two separate districts:

- Must be financially viable for both SMUSD and MUSD.
- Must ensure a degree of predictability for both SMUSD and MUSD, to enable each school district to be able to plan ahead with a reasonable degree of resource certainty.
- Must avoid establishing potential negative incentives for either SMUSD or MUSD. For example, creating a disincentive to pursue increased revenue or otherwise improve education in their schools.
- Must be clear and understandable, legal, and enforceable.

As the Committee worked its way through each of the four financial issue areas, where it proved useful to the negotiation process, the Committee developed additional guiding principles specific to the issues on the table. Part IV of this Report explains the supplemental issue-specific guiding principles adopted by the Committee.

**Term Sheets.** To track the Committee's tentative agreements along the way, the Committee employed a set of "Term Sheets," one for each of the five topics in its Work Plan. The Term Sheets set forth the principles, terms, conditions and procedures through which agreement was developed, and collectively served as the basis for documenting an eventual agreement. The term sheets were updated after each meeting to reflect the Committee's discussion and decision-making. Appendix C contains the final term sheets that together with this memorandum constitute the unanimously approved Committee's Agreement.

#### **Resource Materials Used by the Committee**

Many resources informed the Committee's fact-finding, deliberations and decision-making. Appendix B to this Report contains a categorized listing of these resources, together with electronic links to access the referenced documents.

## Part IV: Summary of the Committee's Negotiated Terms of Agreement

Based on the Board's direction, the Committee organized its negotiations into four major financial issues: the operating budget impact of reorganization; division of the District's assets; bond-related items and other financial liabilities; and environmental liability. A fifth category was added to address implementation issues. The Board's objectives for each issue area and a summary of the major terms of agreement negotiated by the Committee are summarized below. As referenced above, Appendix C contains the Term Sheets with further details on each of the items negotiated.

### Issue #1: Operating Budget Impact of Reorganization

**Board's Objective:** Eliminate any significant adverse financial effect on a Santa Monica only district (SMUSD) as a result of the unification of Malibu as a separate school district (MUSD).

Definitions Adopted by the Committee for Key Words and Phrases*	
Revenue Neutrality	The Board's objective to eliminate any significant adverse Financial Effect on SMUSD from the unification of Malibu as a separate school district.
Revenue Neutrality Formula (Formula)	The Committee's agreed-upon method for calculations and related payment schedule that, in the aggregate, results in Revenue Neutrality.
Average Daily Attendance (ADA)	The average number of pupils actually attending class. The State requires school district to collect and report ADA data annually.
Financial Effect	The difference in revenue per ADA in a Santa Monica only district vs. what the revenue per ADA would have been if separation had not occurred and SMMUSD continued to exist.
Delta See alternative definition below	The annual measurement of the "Financial Effect" multiplied by SMUSD's ADA. If the Delta is a negative number, then MUSD will owe a payment in that amount to SMUSD. If the Delta is a positive number, then MUSD will receive a credit in that amount toward any future payment owed.
Cumulative Delta	The sum of the Delta for any fiscal year added to any amount of the Delta remaining unpaid from prior years. A positive Cumulative Delta balance represents a credit to MUSD that will be applied against future negative Deltas.

**Alternative definition of Delta offered by one member for Committee to consider:**

The annual measurement of the "Financial Effect" multiplied by SMUSD's ADA. A negative value (i.e., the revenue per ADA for SMUSD is less than that which would have been realized by a hypothetical SMMUSD) creates an obligation on the part of MUSD to make a payment in that amount to SMUSD. A positive value (the revenue per ADA for SMUSD exceeds that which would have been realized by a hypothetical SMMUSD), will result in a credit to MUSD offsetting future payment obligations.

## Major Negotiated Terms and Conditions

The Committee approached negotiations on the operating budget impact of reorganization in multiple steps. The Committee adopted common definitions and guiding principles, studied the fiscal assumptions and projections provided by the Committee's educational consultants - School Services of California, Inc. (SSC), and developed and evaluated options for consistency with the guiding principles.

Through this process, the Committee adopted a Revenue Neutrality Formula which can be used to calculate the Financial Effect of reorganization on SMUSD, and establish a schedule of payments from MUSD to SMUSD that will maintain predictable and stable budget growth for both districts and, in the aggregate, eliminate any significant adverse financial effect of separation on SMUSD.

## Guiding Principles Behind the Revenue Neutrality Formula

The agreed-upon Formula aligns with the general principles adopted by the Committee for all terms of an agreement (see page X). In addition, the Committee developed four supplemental principles specific to the Revenue Neutrality Formula.

- The formula must provide predictable and stable operating budget growth for both SMUSD and MUSD.
- The formula must provide for annual calculations of the Delta beginning with the first year following separation through the fiscal year 2029-2030, subject to termination due to the Delta being below an established threshold for three consecutive years.
- If the Delta in any year would require a payment by MUSD that would cause Malibu's operating budget growth to be less than a specified cost of living adjustment, the unpaid amount will be deferred for payment (plus interest) in future years.
- In the aggregate, the payments from MUSD to SMUSD over time must equate to the Cumulative Delta plus interest, if applicable.

### *The Committee needs to discuss this next paragraph – both content and placement:*

Note: 2029-2030 was chosen as the final year for calculating the Delta because the Committee believed a 12-year period to be a reasonable compromise, and based on projections derived from the analysis prepared by SSC, it is likely that SMUSD will become a "basic aid" district in 2030-2031.

## Key Elements of the Negotiated Formula

- **An expert third party will perform the Revenue Neutrality Formula's annual calculations.** The respective Boards of Education of SMUSD and MUSD will select a neutral third party with expertise in California school finance to perform all calculations related to the Revenue Neutrality formula.



- **Delta calculations will use data from the unaudited and audited financial statements of SMUSD and MUSD, not from projections.** Calculations of per-ADA Unrestricted General Fund revenues for what would have been SMMUSD in the absence of separation will be derived from financial data that are available for the separated districts and the State budget. Student counts will be based on Average Daily Attendance (ADA) data reported to the State, average over a three-year period.
- **The Formula specifies the revenue sources to include in the Delta calculation.** All revenue sources to be counted belong to the Unrestricted General Fund, meaning that the funds are not earmarked for a particular program. A handful of Unrestricted General Fund revenue sources are excluded because they either would make no mathematical difference or could create a disincentive for pursuing increased revenue to support education.
- **The sum of payments to SMUSD from MUSD over time will equate to the Cumulative Delta, while the schedule of annual payments takes Malibu's ability to pay into account.** The Delta will be calculated and tracked each year beginning with the first year following separation (assumed to be 2018-19) through 2029-2030. In the aggregate, MUSD will pay SMUSD an amount equal to the Cumulative Delta, plus interest (if applicable). The actual payment owed in any single year will be calculated to maintain predictable and stable budget growth for both districts in an amount at least equal to a cost of living adjustment.
- **If the data demonstrate SMUSD can exist without any significant adverse Financial Effect from reorganization, then the formula provides for amending the original length of the Revenue Neutrality arrangement.** Beginning three years after separation or 2022-2023 (whichever is later), if there are three consecutive years during which the Delta is less than 0.5 percent of SMUSD's Unrestricted General Revenue Fund, then the Revenue Neutrality arrangement ends except that any outstanding payments due to SMUSD from MUSD will still be paid.
- **Criteria for renegotiating the formula and terms of payment.** It is anticipated that separation of SMMUSD into SMUSD and MUSD should occur by the fiscal year 2018-2019. If, however, implementation is delayed beyond 2021-2022, it is agreed that the formula and terms of payment will be revisited and open for renegotiation based on the same principles adopted for the original negotiation.
- **Recommended action to ensure the enforceability and legality of the formula for Revenue Neutrality.** To ensure the enforceability and legality of the formula and related provisions to accomplish the Board's goal of Revenue Neutrality, the Committee recommends the terms of the negotiated agreement be included in special State legislation and related documents that implement the unification of MUSD as a separate school district.

*Q: Do you want to add more here about the expected content of special State legislation?*

**Projection of the Revenue Neutrality Formula: Delta Calculations and Estimated Payments.**

To illustrate how the Formula would work in practice, Appendix D is a spreadsheet containing a projection of the calculations and payments under the negotiated Revenue Neutrality Formula. A guide for understanding how to interpret the projection accompanies the projection.

*Q: Do you want to start each issue on a new page?*

**Issue #2: Division of the District's Assets**

**Board's objective:** Allocate the cash in SMMUSD's General Fund Accounts and the Capital Facilities Fund in a manner that is fair to both MUSD and SMUSD considering the sources and uses of cash in the various funds.

**Major Negotiated Terms and Conditions**

The Committee approached Issue #2 by separating the assignment into negotiations on the District's cash balances and negotiations on the District's land and buildings. The Committee added three supplemental guiding principles for its Issue #2 negotiations:

- The allocation of cash assets will be decided by fund, and will be guided by a method representing a fair and equitable division of the ending fund balances between SMUSD and MUSD that takes the sources and uses of funds into consideration.
- The negotiated methods of asset division are intended for a one-time use because the division is expected to occur at the time of separation.
- For items where the necessary data are not available at this time, the fair and equitable division between SMUSD and MUSD will be assigned to a group appointed closer to the time that separation actually occurs.

The Committee studied information about the sources and uses of cash in various funds, and reviewed an inventory of SMMUSD's land and buildings. The committee developed and evaluated options for consistency with the guiding principles and the Board's objectives, and reached a package of consensus terms that align with the Board's objective. The Committee's Agreement on dividing SMMUSD's assets is summarized below.

**Agreed-upon Methods for Dividing the District's Cash Balances**

**The ADA Method.** For funds where the source of revenue (in relative terms) has essentially mirrored the number of students in Santa Monica and Malibu, the Committee agreed that the most fair and equitable division of cash assets should be based on a calculation of the pro rata Average Daily Attendance (ADA) between what will be SMUSD and MUSD. As a point of reference, the current Santa Monica/Malibu ADA ratio is 84%/16%.

To account for changes in student counts between now and the time of separation, the Committee designed a calculation method titled the “ADA Method,” which is the three-year average of the ADA split between what will be SMUSD and MUSD. The three years will be the year that separation occurs and the prior two years.

The Committee agreed that three funds met the criteria for applying the ADA Method: the Unrestricted General Fund, the Restricted General Fund, and the Cafeteria Special Revenue Fund.

**Alternative Methods.** For funds where the source of revenue (in relative terms) has not mirrored the ADA ratio between Santa Monica and Malibu, the Committee designed an alternative method. The Committee developed alternative methods for the division of five funds: Adult Education Fund; Child Development Fund; Deferred Maintenance Fund; Capital Facilities Fund; and Special Reserve for Capital Projects Fund.

The Committee agreed that in the case of the Building Fund and Retiree Benefit Fund, a decision on a fair and equitable allocation of cash assets should be deferred until a time closer to separation when the needed data are available. In the case of the Retiree Benefit Fund, the Committee recognized that there likely will be a need to hire an actuary to evaluate the appropriate and fair split of the funds in this account.

### **Agreements for Dividing SMMUSD’s Land and Buildings**

The Committee considered the allocation of SMMUSD’s land and buildings in three categories: schools; land/buildings used for SMMUSD activities that serve both Malibu and Santa Monica students and/or faculty; and land/buildings that are a source of revenue for SMMUSD. The agreements and related provisions for dividing these assets between SMUSD and MUSD are summarized below.

#### **Schools**

- School buildings will be allocated to the respective district where they are located.
- If MUSD decides not to provide for a continuation high school program in its own facilities, MUSD will be provided assurance that MUSD students will be able to participate in SMUSD’s continuation high school (currently located at Olympic High School in Santa Monica).

#### **Land/buildings used for SMMUSD activities that serve both Malibu and Santa Monica students and/or faculty**

- The Washington West property will be treated as if it were a school, and therefore will be allocated to Santa Monica, where it is located.

- The District Headquarters building will be allocated to SMUSD, and SMUSD will assume sole responsibility for paying the outstanding debt owed on the Certificates of Participation used to fund the purchase of this property. If/when SMUSD sells District Headquarters, then the net proceeds will be split between SMUSD and MUSD according to the ADA Method at the time of separation.

#### **Land/buildings that are a source of revenue for SMMUSD**

- The land/buildings that are a source of revenue are all located in Santa Monica and will be allocated to SMUSD.
- If/when SMUSD sells any of the land/buildings that were a source of revenue for SMMUSD, the net proceeds from the sale will be split between SMUSD and MUSD according to the ADA method at the time of separation.

*New page?*

#### **Issue #3: Bond-Related Items**

**Board's objective:** Allocate bond debt and authority to issue authorized but unissued bonds in a manner that is fair to both SMUSD and MUSD; and establish a mechanism that would permit refinancing of outstanding bonds.

#### **Major Negotiated Terms and Conditions**

The Committee approached Issue #3 by breaking down the assignment into negotiations related to bonds issued by SMMUSD before the date of separation; the allocation of authorized but-not-yet-issued bonds; and bonds that would be issued post-separation. The Committee added three supplemental guiding principles for its Issue #3 negotiations:

- Post-separation, each district (SMUSD and MUSD) should, to the maximum extent possible, be provided sole discretion to make its own decisions regarding refinancing of existing bond debt and the issuance of new bonds.
- Post-separation, any decisions regarding the allocation of authorized but-not-yet-issued bonds should be consistent with decisions and commitments regarding projects and division of bond authority made prior to separation.
- Decisions regarding the allocation of authorized but-not-yet-issued debt should place priority and mutual respect on the needs and preferences expressed by SMUSD and MUSD at the time the allocation decisions are made.

The Committee studied information available in background and other resource materials about the status of Measure BB and Measure ES bond funds, posed legal questions on bond-related issues to Procopio (see Appendix B-X), and spent time discussing and evaluating different methods and approaches. In sum, the Committee reached a consensus Agreement on bond-related issues that align with the Board's objectives and the Committee's guiding principles. The elements of this Agreement are summarized below.

### **Negotiated Agreements on Bonds Issued by SMMUSD Before Separation**

With respect to bonds issued by SMMUSD before separation, the Committee agreed:

- SMMUSD's existing bond debt should be allocated between SMUSD and MUSD based upon the respective assessed values of Santa Monica and Malibu on the most recent assessment rolls as of the date of separation.
- The special State legislation and related district reorganization documents should explicitly address the issue of refinancing any of the existing SMMUSD debt that is allocated between SMUSD and MUSD. Specifically, the law should provide that any decisions regarding refinancing of this debt can be made independently by SMUSD or MUSD, without need to coordinate with the other.

### **Negotiated Agreement on the Allocation of Authorized But-Not-Yet-Issued Bonds.**

The Committee agreed that this issue lends itself to a recommendation for a process because the exact allocation of authorized but-not-yet-issued bonds will depend on the status of projects and plans of SMUSD and MUSD at the time of separation, as well as the amount of bond funds being allocated at the time. The Committee's recommended process is to delegate the allocation of this outstanding bonding authority to "Group 2," which is one of the transition/implementation groups the Committee recommends be appointed closer to the actual time of separation. (For more on Group 2, see page X.)

The Committee agreed that Group 2 should be directed to allocate the authorized but-not-yet-issued bonds between SMUSD and MUSD in a manner consistent with the supplemental guiding principles developed by the Committee for bond-related items.

### **Negotiated Agreements on Bonds Issued Post-Separation.**

The Committee agreed that:

- After the date of separation, the decision by either SMUSD or MUSD to issue bonds should be left to the sole discretion of each district.
- Any debt owed on bonds issued post-separation by either SMUSD or MUSD, is the sole responsibility of the district that issued the bonds.

#### **Issue #4: Environmental Liability**

**Board's Objectives.** The Board's objectives on the issue of environmental liability, as stated in the December 2015 action creating the Committee, were:

- Establish a structure under which MUSD assumes responsibility for any remaining remediation of any contamination in Malibu schools and indemnifies SMUSD for any future claims arising from such remediation work.
- Dismissal of the pending lawsuit against SMMUSD or an enforceable agreement from the plaintiffs that SMUSD will be dismissed from the lawsuit.
- Receipt by the Board of a legal opinion from a firm selected by the Board with respect to any potential continuing exposure of SMUSD following separation and a conclusion by the Board that any such exposure is reasonable.

Note: With respect to the Board's objective regarding dismissal of the lawsuit brought by America Unites for Kids against SMMUSD, the Committee's understanding is that the September 1, 2016 ruling by Judge Anderson on this lawsuit essentially eliminated the Committee's need to address this objective as part of its negotiations. While the court's decision is on appeal, the Committee understands that the issues on appeal are limited to (a) whether attorneys' fees should be awarded to the plaintiff and (b) whether the injunction imposed by the court on certain private parties should be reversed; the court's decision regarding the obligations of SMMUSD to complete remediation work has not been appealed.

#### **Major Negotiated Terms and Conditions**

The Committee approached its Issue #4 negotiations by dividing the assignment into two categories: environmental contamination for which SMMUSD has developed, approved, funded and begun a remediation plan; and environmental contamination for which no such plan has been developed, whether or not known at the time of separation.

The Committee studied information in background and other resource materials that addressed issues of environmental liability specific to a possible reorganization of the District. The Committee posed legal questions to Procopio (See Online Appendix B-X) and spent time discussing and evaluating different methods and approaches to addressing the Board's objectives. The Committee's Agreement on environmental liability issues is summarized below.

**Agreement on environmental liability for which SMMUSD has developed, approved, funded, and begun a remediation plan.** The Committee agreed that the current ongoing remediation of PCBs (polychlorinated biphenyl), as contemplated in SMMUSD's building replacement and renovation program will not be affected by separation. This remediation program will continue to be funded after separation (by the bond program) and is scheduled to be completed by December 19, 2019.

The Committee further agreed that any remediation project that is underway at the time of separation will be subject to further negotiation by Group 2 (See Issue #5, Implementation) to work out the logistics of project management and completion.

***Committee needs to confirm an agreement was made on this next sentence:***

In addition, If SMUSD becomes liable for any personal injury associated with this contamination, MUSD will contribute a portion of the ultimate cost determined by the ADA Method.

**Agreement on environmental liability related to contamination that is either not known about before separation or is known about before separation but for which SMMUSD has not yet developed, approved, or funded a remediation plan.** For this category, the Committee agreed that each district will be liable for its own properties and in charge of developing, approving, funding, and implementing a remediation plan. For schools in Malibu, the Committee agreed that the portion of ES bonds allocated to Malibu could serve as a potential source of funding for this remediation work.

The Committee also agreed that MUSD will indemnify SMUSD for any liability associated with any contamination falling within this category in Malibu property, and SMUSD will indemnify MUSD for any liability associated with any contamination falling within this category in Santa Monica property.

New page?

**Issue #5: Implementation**

As previously discussed by the Board, with respect to the actual implementation of a district reorganization, there are several different avenues available. In sum, these are a petition to the Los Angeles County of Education (LACOE), special State legislation, or some combination of the two. (Online Appendix X and Y contain excerpts from the California Department of Education, District Organization Handbook, dated September 2016.)

Negotiations on the details of the implementation process were beyond the scope of the Board's objectives for the Committee. However, the Committee agreed it was important to offer a recommendation on how to resolve the financial items identified in the report that, due to various reasons, cannot be finalized until either at the actual time of separation or in the time period post-separation.

For this purpose, the Committee recommends the appointment of two groups.

**Group One:** The SMMUSD Board should appoint Group One to work on the things that need to happen between the time the Board approves moving forward with unification and the time that separation occurs.

Candidate tasks for Group One are:

- Monitoring of any special state legislation being drafted at the Board's direction;
- Monitoring negotiations for project management and completion of capital improvement projects in Malibu schools that are underway at the time of separation
- Monitoring negotiations for completing the remediation of environmental contamination in Malibu schools that are underway at the time of separation.

**Group Two:** After separation occurs, the respective Boards of Education of SMUSD and MUSD should appoint Group Two to work on the logistics and any outstanding issues that need to be resolved to ensure a smooth transition to the interactions of the two districts going forward.

Candidate tasks for Group Two are:

- Based on the status of capital projects at the time of separation, making final recommendations about the allocation of "cash" in the Building Fund.
- Based on the status of ES bond authority used at the time of separation, making final recommendations about the allocation of authority to issue authorized but not yet issued bonds.



## **V. Acknowledgements**

The Committee thanks the following individuals and organizations for their time and contributions to the Committee's work.

SMMUSD Board of Education  
City of Malibu  
Advocates for Malibu Public Schools

### District Superintendents

Dr. Ben Drati, SMMUSD Superintendent  
Dr. Chris King, former Interim Superintendent  
Dr. Sylvia Rousseau, former Interim Superintendent  
Dr. Sandra Lyon, former SMMUSD Superintendent

### SMMUSD Staff

Janece Maez, Associate Superintendent Business and Fiscal Services, Chief Financial Officer  
Sarah Wahrenbrock, Assistant to the Superintendent  
Diana Kamibayashi, Senior Office Assistant, Office of the Superintendent  
Maryanne Solomon, Webmaster  
Gail Pinsker, Community and Public Relations Officer  
Kim Nguyen, Senior Administrative Assistant, Fiscal Services

### SMMUSD Consultants/Contractors

Anthony Hsieh, Keygent Advisors LLC  
Alliance of Schools for Cooperative Insurance Programs (ASCIP)  
Theodore Scott Smith, SMMUSD contractor (assisted with taking minutes)

### City of Malibu Staff

Reva Feldman, City Manager  
Christi Hogin, City Attorney  
Mary Linden, Executive Assistant, City Manager's Office  
Kathleen Stecko, Senior Office Assistant, Planning Department

### Procopio

John Lemmo, Partner

### School Services of California, Inc.

Robert Miyashiro, Vice President  
Mike Ricketts, Associate Vice President  
Kelly Saterfield, Governmental Relations Assistant

## VI. Signatures of Agreement

The members of the Malibu Unification Negotiations Committee certify that they have read, understood, and agreed to the terms of agreement, as set forth in this Report and its Appendices.

Tom Larmore \_\_\_\_\_ Date \_\_\_\_\_

Debbie Mulvaney \_\_\_\_\_ Date \_\_\_\_\_

Laura Zahn Rosenthal \_\_\_\_\_ Date \_\_\_\_\_

Paul J. Silvern \_\_\_\_\_ Date \_\_\_\_\_

Manel Sweetmore \_\_\_\_\_ Date \_\_\_\_\_

Makan Delrahim (?) \_\_\_\_\_ Date \_\_\_\_\_

## Appendix C: The Committee's Final Term Sheets

This Appendix contains the Committee's final Term Sheets, which collectively comprise the Committee's Negotiated Agreement (Agreement). The Committee organized the Term Sheets by the five issues in the Committee's Plan of Work. In turn, the Committee's Plan of Work was based on the Board's objectives, as outlined in the December 17, 2015 Board Action that established the Committee.

Issue	Begins on Page
Issue #1, Operating Budget Impact	C-x
Issue #2, Division of SMMUSD Assets	C-x
Issue #3, Bond-related Items and Other Liabilities	C-x
Issue #4, Environmental Liability	C-x
Issue #5, Implementation Steps	C-x

## Term Sheet for Topic #1, Operating Budget Impact

### I. The Board's Objective

As stated in the Board's action creating the Committee, the objective for negotiations related to the operating budget impact was to eliminate any significant adverse financial impact on a Santa Monica only district (SMUSD) as a result of a potential District "unification," or division of the existing SMMUSD ("District") into SMUSD and a Malibu-only district (MUSD).

The Board anticipated the possibility of a significant Financial Effect after receiving a second report on the potential financial implications of unification from the District's Financial Oversight Committee (FOC) and District financial staff in the fall of 2015. Based on updated District financial data, the report concluded there was a distinct possibility that that a reorganization could, at least for a period of time, materially reduce revenue to SMUSD on a per student basis (as measured by Average Daily Attendance, or ADA) when compared to revenue per ADA without separation.

The reasons for this negative fiscal impact on SMUSD are complex. They include the intricacies of how State funds are provided to local school districts in California, the fact that although a stand-alone SMUSD would keep certain revenues provided by the City of Santa Monica (currently shared with the Malibu schools), it would no longer receive property tax revenue generated in the Malibu community, and SMUSD is likely to achieve "minimum State aid" and "basic State aid" status more slowly than would a combined District. (State law allows a school district that achieves "minimum" or "basic" aid status to keep more of its property taxes for funding its schools.)

For further explanation of these issues, including how the State's Local Control Funding Formula (LCFF) affects the finances of a reorganization, more about the implications of achieving "minimum State Aid" and "basic State aid" status, see Appendix B-X for SSC's presentation on school finance in California.

Definitions Adopted for Key Words and Phrases*	
Revenue Neutrality	The Board's objective to eliminate any significant adverse Financial Effect on SMUSD from the unification of Malibu as a separate school district.
Revenue Neutrality Formula (Formula)	The Committee's agreed-upon method for calculations and related payment schedule that, in the aggregate, results in Revenue Neutrality.
Average Daily Attendance (ADA)	The average number of pupils actually attending class. The State requires school district to collect and report annual ADA data.
Financial Effect	The difference in revenue per ADA in a Santa Monica only district vs. what the revenue per ADA would have been if separation had not occurred and SMMUSD continued to exist.
Definitions continued on next page	

Delta <i>See alternative definition below</i>	The annual measurement of the “Financial Effect” multiplied by SMUSD’s ADA. If the Delta is a negative number, then MUSD will owe a payment in that amount to SMUSD. If the Delta is a positive number, then MUSD will receive a credit in that amount toward any future payment owed.
Cumulative Delta	The cumulative sum of an annual Delta added to any amount of the Delta remaining unpaid from prior years. A negative Cumulative Delta balance represents a credit to MUSD that will be applied to future negative Deltas.

\*See Appendix B-X for the Committee’s full glossary of acronyms, words, and phrases.

***Alternative definition of Delta offered by one member for Committee to consider:***

The annual measurement of the “Financial Effect” multiplied by SMUSD’s ADA. A negative value (i.e., the revenue per ADA for SMUSD is less than that which would have been realized by a hypothetical SMMUSD) creates an obligation on the part of MUSD to make a payment in that amount to SMUSD. A positive value (the revenue per ADA for SMUSD exceeds that which would have been realized by a hypothetical SMMUSD), will result in a credit to MUSD offsetting future payment obligations.

## **II. The Committee’s Approach**

The Committee approached its negotiations on the operating budget impact of reorganization in multiple steps. The Committee adopted common definitions and guiding principles, studied the fiscal assumptions and projections provided by the Committee’s educational consultants - School Services of California, Inc. (SSC), and developed and evaluated options for consistency with the guiding principles.

Through this process, the Committee adopted a Revenue Neutrality Formula, which can be used to calculate the Financial Effect of reorganization on SMUSD, and establish a schedule of payments from MUSD to SMUSD that will maintain predictable and stable budget growth for both districts and, in the aggregate, eliminate any significant adverse financial effect of separation on SMUSD.

## **III. Guiding Principles**

The Committee designed the Revenue Neutrality Formula based on the general principles the Committee adopted for all portions of an agreement plus four additional guiding principles developed specifically for the Formula and its related provisions, as noted below.

The general principles applicable to all portions of an agreement are that all terms must: be financially viable for both SMUSD and MUSD; ensure a degree of predictability for both SMUSD and MUSD; enable each district to plan ahead with a reasonable degree of resource certainty; avoid establishing potential negative incentives for either SMUSD or MUSD to pursue increased

revenue or otherwise improve education in their schools; and be clear and understandable, legal, and enforceable. (See Memorandum Report, page X.)

In addition, the formula also aligns with the following four guiding principles developed specifically for achieving Revenue Neutrality:

- The formula must provide predictable and stable operating budget growth for both SMUSD and MUSD.
- The formula must provide for annual calculations of the Delta beginning with the first year following separation through the fiscal year 2029-2030, subject to termination due to the Delta being below an established threshold for three consecutive years.
- If the Delta in any year would require a payment by MUSD that would cause Malibu's operating budget growth to be less than a specified cost of living adjustment, the unpaid amount will be deferred for payment (plus interest) in future years.
- In the aggregate, the payments from MUSD to SMUSD over time must equate to the Cumulative Delta plus interest, if applicable.

***The Committee needs to discuss this next paragraph – both content and placement:***

Note: 2029-2030 was chosen as the final year for calculating the Delta because the Committee believed a 12-year period to be a reasonable compromise, and based on projections derived from the analysis prepared by SSC, it is likely that SMUSD will become a "basic aid" district in 2030-2031.

#### **IV. Details of the Formula and Related Implementation Terms and Conditions**

The balance of this term sheet outlines the details of calculating the Revenue Neutrality Formula, explains how the calculations translate into a schedule of payments (or payment credits) from MUSD to SMUSD, and outlines several additional provisions related to implementing the Formula. It is organized into the following explanatory sections:

- The method for annually calculating the Financial Effect of separation on SMUSD, i.e., the Delta.
- The method for annually calculating the payment to be made by MUSD to SMUSD (or credit to be booked) based on the size of the Delta and Malibu's "ability to pay."
- The mechanics of a three-year Revenue Neutrality tracking process.
- The designation of a third-party to perform the above calculations (to include the timing of calculations and payments).
- Criteria for renegotiating the formula or terms of payment, if required by a significant future change in events.
- Recommended actions to ensure the enforceability and legality of the Revenue Neutrality Formula.

## A. The Method for Annually Calculating the Financial Effect of Separation on SMUSD (i.e., the Delta)

The Delta is an annual calculation of the Financial Effect of District separation on SMUSD. It is defined as the difference in revenue (positive or negative) per ADA in SMUSD vs. what the revenue per ADA would have been if SMMUSD still existed, multiplied by SMUSD's student count, as measured by ADA. If the Delta is negative, meaning that the revenue per ADA in SMUSD for any year is less than what the revenue per ADA would have been in SMMUSD for that year, then it is considered an adverse Financial Effect.

### 1. Sources of Data for the Delta Calculation.

Average Daily Attendance (ADA): The student count used in the agreed-upon Revenue Neutrality Formula will be ADA data, which is the average number of pupils actually attending classes. The State requires school districts to compile and report ADA data annually.

*The Subcommittee needs to discuss this next paragraph, drafted after receipt of SSC's comments on the Formula. One Committee member commented that "It is confusing to say both unaudited actuals and audited financial statements. We need to be clear that the actual delta will be based on audited actuals but that some preliminary calculations may use the unaudited actuals."*

Unaudited Actuals and Audited Financial Statement Data: The calculations in the agreed-upon Revenue Neutrality Formula will use data from a combination of Unaudited Actuals and audited financial statements for SMUSD and MUSD, which are generally available in September and December of each year, respectively. Calculations related to revenue for what would have been SMMUSD will be derived from these financial data.

### 2. Revenue Sources to Include and Exclude in the Calculation of Financial Effect.

The Delta will be calculated each year beginning with the first year following separation, which we have assumed to be 2018-19, through 2029-2030 using the sources of Unrestricted General Fund revenue identified in the following table.

Groupings	Unrestricted General Fund Revenue Sources for Delta Calculations
State revenue	<ul style="list-style-type: none"> <li>All categories of LCFF revenue.</li> </ul> <p>Note: LCFF is the acronym for Local Control Funding Formula, which is the primary source of State funding for K-12 public education in California. In the current fiscal year (2016-2017), LCFF revenue accounts for 62% of SMMUSD's total revenue.</p>
Locally-generated revenue	<ul style="list-style-type: none"> <li>Parcel tax revenue</li> </ul>

	<ul style="list-style-type: none"> <li>• Revenue from leases and rentals</li> <li>• City of Santa Monica contract revenue</li> <li>• City of Malibu contract revenue</li> <li>• Santa Monica Measure Y and Measure GSH revenue</li> </ul>
New sources of local revenue generated post-separation	<ul style="list-style-type: none"> <li>• Revenue from any new revenue sources established and generated post-separation by Santa Monica.*</li> </ul>

\* Other new sources of revenue that Malibu generates post-separation will be incorporated into the assessment of Malibu's "ability to pay" (explained further below), but will not be used in the calculation of the Delta. This is based on the general principle to avoid establishing potential negative incentives for either district to pursue increased revenue or otherwise improve education in their schools. New sources of locally generated Santa Monica revenue are included because the small amount (i.e., ADA share) that will benefit MUSD is not considered a disincentive.

If the State changes the method under which it funds public schools from the current LCFF approach, the parties will meet and confer in order to make reasonable changes if necessary, to the formula, as discussed later in this report. If any of the locally generated sources of revenue in Santa Monica is terminated, it will be removed as an item of revenue in calculating the Delta.

The calculation of the Delta will exclude the following sources of revenue applicable to the Unrestricted General Fund:

- Education Foundation Revenue (currently SMMEF) or any similar parent, PTA, or local business generated revenue. The rationale for excluding revenue from these sources is that these monies are raised by local organizations in each district respectively, and exclusion aligns with the guiding principles not to create any disincentives for local fund raising efforts.
- Lottery Funding Revenue and Mandated Cost Block Grant Revenue (MBG). These two sources of State funds are allocated (as General Fund revenue) to each school district based on the same dollar amount per unit of annual ADA. As a result, the inclusion of revenue from these sources would have no effect on the calculation of the Delta.

**B. The Method for Calculating and Tracking the Payments To Be Made To SMUSD By MUSD Based On the Size of The Delta and MUSD's "Ability To Pay."**

As noted above, the Delta will be calculated each year beginning with the first year following separation, which the Committee assumed to be 2018-19, through 2029-2030.

- If the Delta is a negative value (i.e., the revenue per ADA for SMUSD is less than that which would have been realized by a hypothetical post-separation SMMUSD), then the amount will be counted towards funds owed to SMUSD by MUSD.



- If the Delta is a positive value (i.e., the revenue per ADA for SMUSD exceeds that which would have been realized by a hypothetical post-separation SMMUSD), then the amount will accrue to MUSD as a credit toward any funds owed to SMUSD.

In the aggregate, MUSD will pay SMUSD an amount equal to the Cumulative Delta, plus interest (as applicable). The actual payment owed to SMUSD by MUSD in any single year will be calculated to maintain predictable and stable budget growth for both districts in an amount at least equal to a cost of living adjustment.

The formula incorporates MUSD's "ability to pay" in several ways. Specifically, the formula:

- Takes into account the fact that the MUSD budget will need unrestricted (*alternative word suggested to use here is "additional"*) growth in the early years to ensure the financial viability of the new district, including the ability to fund one-time start-up costs and initiate a reserve fund.
- Provides that the MUSD budget will not experience a net reduction in its budget year over year due solely to a required payment to SMUSD
- Provides that Malibu's annual budget can grow at a rate equal to (*Manel is drafting new language to replace the current reference to the State's Local Control Funding Formula (LCFF) cost-of-living adjustment rate*)

In assessing MUSD's ability to pay, any sources of local MUSD revenue adopted after separation shall be included in determining its revenue for the "ability to pay" calculation but, as explained earlier, will not be included in revenue for calculating the Delta.

The mechanics of how the Revenue Neutrality Formula determines the annual payment amount are outlined below: As noted earlier, 2029-2030 was chosen as the final year for calculating the Delta because the Committee believed a twelve-year period to be a reasonable compromise and based on projections derived from the analysis prepared by SSC, it is likely that SMUSD will become a "basic State aid" district in 2030-2031.

- If, in any year through 2029-2030, the Delta is negative, MUSD will owe a payment in that amount to SMUSD, except to the extent that any credits remain available from prior years to offset the amount of that payment.
- The amount of the payment to be made by MUSD for any year will be the lesser of:
  - The amount of the negative Delta for that year (less any remaining credits) plus any unpaid amounts, plus interest, remaining from prior years; or
  - The amount by which MUSD's Unrestricted General Fund revenues for the year exceed its operating budget for the prior year adjusted by the (*insert new COLA language*)

- Any amount paid by MUSD that is less than the amount of the Delta (less any remaining credits) will be carried forward into the next year with interest at the rate earned by both SMUSD and MUSD on funds deposited with the County of Los Angeles Treasurer's pooled investments account comprised of short-term securities (i.e., currently 0.9XX%).
- Beginning in 2030-2031, no further calculations of the Delta will be made and annual payments will be due by MUSD in an amount equal to the lesser of:
  - Any Cumulative Delta from prior years, plus interest, or
  - The amount by which MUSD's Unrestricted General Fund revenues for the year exceed its operating budget for the prior year adjusted by the *(insert new COLA language)*
- This procedure will continue for each year until all amounts owed by MUSD to SMUSD, including interest, have been paid in full.

To illustrate how the Revenue Neutrality Formula would work in practice, attached to this Term Sheet is a projection of calculations and payments, based on the best information available at this time. A guide for understanding how to interpret the projections accompanies the projection.

### **C. The Mechanics of The Three-Year Revenue Neutrality Tracking Provision**

The formula also includes what the Committee termed the "three-year Revenue Neutrality tracking provision." This element was included in consideration of the lengthy period during which the Delta will be measured, and that during this period there may come a point at which regular relatively small and inconsequential amounts might be owed by MUSD to SMUSD, which the Committee believes would demonstrate that the two districts are operating independently with no significant adverse Financial Effects on SMUSD. The tracking phase and three-year tracking provision will work as outlined below:

- The tracking phase will begin either three years after separation occurs or 2022-23, whichever is later.
- During the tracking phase, if there are three consecutive years during which the Delta is less than 0.5% of SMUSD's Unrestricted General Revenue Fund, then the Revenue Neutrality arrangement ends, except that any outstanding payments due to SMUSD from MUSD must still be paid.
- If there remains a credit at that time arising from previous calculations of the Delta, SMUSD will not be required to make any payment to MUSD.

#### **D. The Designation of A Third-Party To Perform the Above Calculations and Annual Timing of Calculations and Payments**

1. Designation of a Third-Party. Once MUSD becomes a separate school district, the Board of Education of SMUSD and Board of Education of MUSD will jointly designate a neutral third-party with expertise in all matters related to K-12 public school financing in California to perform the annual calculations associated with the Delta and resulting payment schedule. The two districts will share equally in any costs associated in hiring this neutral third party.

*Need to decide on and insert description of how the two districts formally agree to accept the calculations performed by this third-party. [Let's discuss before we write]*

*Insert any additional advice from SSC about reducing the uncertainties related to calculating the revenue for a school district that no longer exists.*

#### **2. Calendar of Calculations and Payments.**

*The description below will be replaced with the draft language Manel is working on, based on the chart he drew two meetings ago.*

As noted above, the calculations in the agreed-upon Revenue Neutrality Formula should use data from the audited financial statements ("audited financials") for SMUSD and MUSD, which are expected to be available in December of each year.

It is expected that the initial annual calculation of the Delta and associated payment (or booking of credit) will proceed as follows:

- 1) The audited financials for the first fiscal year of separation will be available in December of the second fiscal year of separation.
- 2) The formal calculation of the Delta using these audited financials will be performed the following month, that is, in January of the second fiscal year of separation.
- 3) The decision to use audited financials as the source of data means that there will be no payment (or credit) at the beginning of the first or second fiscal year of separation. The payment (or booking of a credit) at the end of the second fiscal year of separation will reconcile the Delta for the first fiscal year of separation.

This pattern of reconciling the Delta for each fiscal year at the end of the next fiscal year will continue for the length of the payment agreement.

**E. Criteria for Renegotiating the Revenue Neutrality Formula or Terms of Payment****1. Before separation occurs.**

Everyone's best efforts will aim for effectuating separation of SMMUSD into SMUSD and MUSD by 2018-2019. If, however, implementation is delayed beyond 2021-2022, then the formula and terms of payment will be revisited and open for renegotiation. The Committee recommends that any renegotiation should be conducted within the context of the basic principles outlined in the Committee's recommendations to the Board.

**2. After separation occurs.**

*The Committee needs to review these next two paragraphs –language drafted by Tom to address renegotiations post-separation:*

It is possible that a force majeure event may occur, such as an earthquake or major fire, that could adversely impact MUSD and its ability to make payments by requiring a divergence of funds for emergency repairs, cleanup, obtaining alternate classroom or administrative facilities, or providing for other needs. If such an event occurs and MUSD concludes that it cannot make all or any portion of a payment that would otherwise be due to SMUSD under the formula, MUSD shall notify SMUSD of the amount that it cannot pay for the applicable year, together with appropriate calculations demonstrating such inability, and its obligation to make a payment will be deferred for up to one year and interest shall accrue on the unpaid amount.

If at any time when the Delta is to be calculated or MUSD is required to make a payment to SMUSD there has been a significant change in any of the key underlying assumptions in the formula or SSC's projections, such as the manner in which the State provides funds for public schools or the manner in which property is taxed, either district may notify the other that it wishes to meet and confer regarding the formula and the terms of payment. If either district gives such a notice, the districts should meet to discuss appropriate changes in the formula applying the basic principles utilized by the Committee and any other principles agreed upon by the districts.

**F. Recommended Action to Ensure the Enforceability and Legality of the Revenue Neutrality Formula**

To ensure the enforceability and legality of the formula and related provisions to accomplish the Board's goal of Revenue Neutrality, the Committee recommends the terms of the negotiated agreement be included in special State legislation and related documents that implement the unification of MUSD as a separate school district.

## **Term Sheet for Issue #2, Division of the District's Assets**

### **The Board's Objective**

As stated in the Board's action creating the Committee, its objective for negotiations related to the division of SMMUSD's assets was to include a method(s) for the allocation of the cash in SMMUSD's General Fund Accounts and the Capital Facilities Fund at the time of separation. The Board stated that "the method will be fair to both SMUSD and MUSD, considering the sources and uses of cash in the various funds."

### **The Committee's Approach**

The Committee approached its negotiations on the division of SMMUSD's assets between SMUSD and MUSD by separating the assignment into two major categories:

- Develop a method(s) for dividing SMMUSD's cash assets (i.e., ending fund balances) at the time of separation; and
- Develop a method(s) for dividing SMMUSD's land and buildings at the time of separation.

The Committee added three guiding principles tailored for the negotiations related to the division of SMMUSD's assets. The Committee studied information available in background and other resource materials about the sources and uses of cash in the various funds, and reviewed an inventory of SMMUSD's land and buildings. The Committee posed questions to District staff to clarify their understanding of the funds and most recent balance sheets. The Committee reviewed the provisions in State law governing the division of assets in school district reorganizations. Finally, the committee developed and evaluated options for consistency with the guiding principles.

In sum, the Committee reached a package of consensus agreements on the issues identified above that aligns with the Board's objectives. The details are explained below.

### **Guiding Principles and Definitions**

The Committee developed the methods for dividing items listed on SMMUSD balance sheet based on the general principles the Committee adopted for all terms of an agreement plus three additional guiding principles developed specifically for this issue.

As a result, the methods for dividing SMMUSD's assets align with the Committee's agreement that all terms must: be financially viable for both SMUSD and MUSD; ensure a degree of predictability for both SMUSD and MUSD; enable each school district to be able to plan ahead with a reasonable degree of resource certainty; avoid establishing potential negative incentives for either SMUSD or MUSD to pursue increased revenue or otherwise improve education in

their schools; and be clear and understandable, legal, and enforceable. (See Memorandum Report, page X.). In addition, the methods for addressing balance sheet items at the time of separation also meet the following three guiding principles:

- The allocation of cash assets will be decided by fund, and will be guided by a method representing a fair and equitable division of the ending fund balances between SMUSD and MUSD that takes the sources and uses of funds into consideration.
- The negotiated methods of asset division are intended for a one-time use because the division is expected to occur at the time of separation.
- For items where the necessary data are not available at this time, the fair and equitable division between SMUSD and MUSD will be assigned to a group appointed closer to the time that separation actually occurs.

#### **A. Negotiated Agreements on How to Divide SMMUSD's Cash Assets**

For each major fund, the Committee negotiated a method for dividing SMMUSD's cash assets at the time of separation between SMUSD and SMUSD. Consistent with the Board's objectives, the Committee considered both the sources and uses of each fund. The Committee's agreed-upon methods are described below in three categories:

- Cash assets to be divided using the "ADA Method;"
- Cash assets to be divided using an alternative method; and
- Cash assets to be divided based on information available closer to the time of separation.

##### **(1) Cash Assets to be Divided Using the "ADA Method"**

For funds where the source of revenue (in relative terms) has essentially mirrored the number of students in Santa Monica and Malibu, the Committee agreed that the most fair and equitable division of cash assets at the time of separation should be based on a calculation of the pro rata Average Daily Attendance (ADA) between what will be SMUSD and MUSD. As a point of reference, the current Santa Monica/Malibu ADA ratio is 84%/16%.

To account for changes in student counts between now and the time of separation, the Committee designed a calculation method titled the "ADA Method:"

**The ADA Method** is the three-year average of the ADA split between what will be SMUSD and MUSD. The three years will be the year that separation occurs and the prior two years.

The funds to be divided using the ADA Method are listed below, along with each fund's 2015-2016 cash balance, and the Committee's comments on why the ADA Method is recommended.

**Name of Fund**                      **Unrestricted General Fund**  
2015-2016 Ending Balance:    \$32,609,848

The bulk of the Unrestricted General Fund money comes from local property taxes and the State. State funding sources include LCFF revenue (the primary source of State financial support for K-12 public education), Lottery Fund Revenue, and Mandated Cost Block Grant Revenue. Local revenue deposited into the Unrestricted General Fund includes: parcel taxes; revenue from leases and rentals; revenue from SMMUSD's contract with the City of Santa Monica; revenue from SMMUSD's contract with the City of Malibu; Santa Monica sales tax revenue from Measure Y and the recently adopted Measure GSH. Funds raised by the Santa Monica-Malibu Education Fund (SMMEF) are also deposited into the Unrestricted General Fund.

*Committee Member Comment: We need to re-evaluate the SMMEF money, as the money raised is for the following year so we need to know when SMMEF gives those funds to the district. If it occurs after July 1, then we're fine here. If it is before July 1, then we need to exclude those funds from this calculation*

While the component parts of the Unrestricted General Fund do not each (by themselves) mirror the Santa Monica/Malibu ADA ratio, the Committee's analysis revealed that the net contributions to the Unrestricted General Fund closely mirror the ADA split. It is for this reason, plus the fact that it greatly simplifies the calculation required, the Committee agreed that a fair and equitable division of the fund balance in the Unrestricted General Fund should be based on the ADA Method.

As a double-check on the fairness of using the ADA Method for this Fund, the Committee recommends that a similar analysis be repeated at the time of separation to ensure the mathematical finding cited above still holds.

**Name of Fund**                      **Restricted General Fund**  
2015-2016 Ending Balance:    \$5,197,573

The source of revenue for the Restricted General Fund are XXX and XXX. Funds deposited in the Restricted General Fund must be used for specific purposes, such as XXX.

The Committee agreed that the fund balance in the Restricted General Fund should be divided between SMUSD and MUSD according to the ADA Method for reasons that parallel the logic of this method for the fund balance in the Unrestricted Revenue Fund. Similarly, the Committee recommends the mathematical analysis of the component parts of the Restricted General Fund be repeated at the time of separation to ensure the fairness of using the ADA Method.

**Name of Fund**                      **Cafeteria Special Revenue Fund**  
2015-2016 Ending Balance:    \$195,976

The Cafeteria Special Revenue Fund is for operation of the food service program. The ADA Method is recommended for allocating the fund balance at the time of separation because food service programs exist in both Santa Monica and Malibu, and students in both jurisdictions have contributed to the fund.

**Committee Member Comment:** *Have we verified if this is based on ADA or based on students on Free and Reduced lunch? if it's the latter, we need to divide based on the number of students who fall into those categories per district.*

## **(2) Cash Assets to be Divided Using an Alternative Method**

For funds where the relative source of revenue (i.e., Santa Monica vs. Malibu) has not mirrored the ADA ratio, or if there is a more equitable way to divide a fund balance, the Committee designed an alternative method. For the five funds listed below, the Committee agreed the fund balance at the time of separation should be divided according to an alternative method. Provided for each fund is a summary description of fund, the projected fund balance from 2015-2016, a description of the agreed-upon allocation method, and any Committee's comments on this method.

**Name of Fund**                      **Adult Education Fund**  
2015-2016 Ending Balance:    \$659,900

The Adult Education Fund is a Special Revenue Fund. The source of revenue for this fund is the State, which pays school districts a set amount per student participating in Adult Education

The agreed-upon allocation method is to divide the fund balance between SMUSD and MUSD based on the ratio (calculated as a three-year average) of students enrolled from each community in Adult Ed. The three years will be the year of separation and the prior two years.

Note: If MUSD decides not to plan on offering its own Adult Education, then the entire fund balance will be transferred to SMUSD.

**Name of Fund**                      **Child Development Fund**  
2015-2016 Ending Balance:    \$234,491

The Child Development Fund is a Special Revenue Fund. The source of revenue for this fund is the State, which pays school districts a set amount per student participating in Child Development programs.



The agreed-upon allocation method is to divide the fund balance between SMUSD and MUSD based on the ratio (calculated as a three-year average) of students enrolled from each community in Child Development program(s). The three years will be the year of separation and the prior two years.

Note: If MUSD decides not to plan on offering its own Child Development program, then the entire fund balance will be transferred to SMUSD.

**Name of Fund**                      **Deferred Maintenance Fund**  
2015-2016 Ending Balance:    \$212,196

The Deferred Maintenance Fund is a Special Revenue Fund. The purpose of this fund is to fund routine maintenance needs across all of SMMUSD's buildings, located in both Santa Monica and Malibu.

The agreed-upon method of allocation is to divide the fund balance between SMUSD and MUSD will be the percent of SMMUSD's total floor area square footage in Santa Monica vs. Malibu buildings at the time of separation.

*Missing info: Source of revenue for this fund*

**Name of Fund**                      **Capital Facilities Fund (developer fees)**  
2015-2016 Ending Balance:    \$1,236,679

The Capital Facilities Fund is the repository of developer fees to SMMUSD. The agreed-upon allocation method will be to divide the fund balance between SMUSD and MUSD based on a three-year average of the percent of total dollar amounts contributed from developments located in Santa Monica vs. Malibu. The three years will be the year of separation and the prior two years.

Note: Development contributions by location are tracked annually, so the allocation method recommended should be relatively simple to implement.

*Missing info: explanation of what these funds are used*

**Name of Fund**                      **Special Reserve for Capital Projects Fund**  
2015-2016 Ending Balance:    \$5,244,209

*(term sheet included the statement "available funds not yet designated? Can someone explain does this means?)*

The Special Reserve for Capital Projects Fund is the repository of the tax increment pass through funding from the former Santa Monica Redevelopment Agency (RDA). This fund pays for the annual debt service on the existing Certificates of Participation (COPs) for the 16<sup>th</sup> Street building (District Headquarters). The annual debt service for principle and interest is \$1.869M.

\$5 million of this fund is reserved to cover shortfalls occurring in Measure BB, and the balance is used to fund other capital projects as they are identified by the District as a priority. There has been no pattern established for using these funds for capital projects based on the project's location in Malibu or Santa Monica

The agreed-upon allocation method is to divide the fund balance at the time of separation between SMUSD and MUSD based on the ratio of total ES funds allocated to bond-funded projects in Malibu schools and bond-funded projects in Santa Monica schools. To be specific, the Santa Monica/Malibu allocation ratio will be 78/22. This is calculated as the allocation to Malibu of (at least) \$77 million out of 350.6 million, which is the amount remaining of \$385 million (the ES total) after subtracting the \$34.4 million allocated for system-wide technology improvements.

### **(3) Cash Assets to be Divided Based on Information Available Closer to the Time of Separation**

The Committee agreed that the decision on a fair and equitable allocation of cash assets in the following two funds should be deferred until a time closer to separation. The reasons for this are somewhat different for each fund, as explained below.

<b>Name of Fund</b>	<b>Building Fund</b>
2015-2016 Ending Balance:	\$92,741,212

The Building Fund will contain the end-of-year cash balance of SMMUSD bond proceeds in the year prior to separation.

This issue lends itself to a recommendation for a process because the exact allocation will depend on the status of projects in Santa Monica and Malibu at the time of separation. The recommended process is to delegate this allocation decision to Group 2, the second transition/implementation group appointed jointly by the respective Boards of SMUSD and MUSD. (See the term sheet on Issue #5: Implementation.)

The guiding principle recommended for Group 2 to follow is to allocate the cash balance consistent with the decisions and commitments regarding projects and division of bond authority made prior to separation, and the status of projects underway at the time of separation, including that Malibu receives \$77 million (at minimum) out of Measure ES's total of \$385 million.

<b>Name of Fund</b>	<b>Retiree Benefit Fund</b>
2015-2016 Ending Balance:	\$5,120,174

The MUNC recommends the details of allocating the fund balance in the Retiree Benefit Fund also be assigned to Group 2.

The most equitable allocation of the cash balance in the Retiree Benefit Fund will need to be based on the most recent actuarial data available at the time of separation, and will be linked to how the liability for providing retiree health benefits is divided between SMUSD and MUSD at the time of separation. The Committee believes that an actuary will need to be engaged to make the determination of a fair and equitable split of this fund.

*Missing: One sentence description of source of funds for the Retiree Benefit Fund*

## **B. Negotiated Agreements on How to Divide SMMUSD's Land and Buildings**

The committee agreed to consider the allocation of SMMUSD's land and buildings in three categories: schools; land/buildings used for SMMUSD activities that serve students and/or faculty in both Malibu and Santa Monica; and land/buildings that are a source of revenue for SMMUSD.

The agreed-upon method and related provisions for dividing these fixed assets between SMUSD and MUSD at the time of separation are described below.

### **Category 1: Schools**

- School buildings will be allocated to the respective district where they are located.
- To the extent MUSD does not provide for a continuation high school program in its own facilities, MUSD will be provided assurance that MUSD students who require enrollment in a continuation high school will be able to participate in SMUSD's continuation high school, which is currently located at Olympic High School in Santa Monica. (Whether this assurance of participation needs to be included in the special state legislation related to unification will be part of Group 1's research and recommendations on the details of implementation.)

### **Category 2: Land/buildings used for SMMUSD activities that serve both students and/or faculty in Malibu and Santa Monica.**

All of the property in this category is located in Santa Monica. The agreed-upon allocation method for each property is as follows:

- The District Headquarters building (located in Santa Monica) will be allocated to SMUSD, and SMUSD will assume sole responsibility for paying the outstanding debt owed on the COPs used to fund the purchase of this property. If the District Headquarters is ever sold, then the net proceeds will be divided between SMUSD and MUSD according to the ADA Method at the time of separation. (See page X for explanation of the ADA Method.)
- The Washington West property will be treated as if it were a school, and therefore will be allocated to Santa Monica as the district where it is located.

**Category 3: Land/buildings that are a source of revenue for SMMUSD**

- The land/buildings that are a source of revenue (which are all located in Santa Monica) will be allocated to SMUSD.
- However, if/when SMUSD sells any of the land/buildings that were a source of revenue for SMMUSD, the proceeds from the sale will be split between SMUSD and MUSD according to the “ADA method” at the time of separation. (See page X for explanation of the ADA method.)

*At least for the moment, I moved the rest of this term sheet that addressed other balance sheet liabilities (except environmental liability) to the end of Issue #3.*

### **Term Sheet for Issue #3, Bond-Related Items**

#### **The Board's Objective**

The Board's stated objectives for the Committee included developing a method(s) that is fair to both SMUSD and MUSD for the: allocation of bond debt; refinancing of bond debt; and allocation of the authority to issue authorized by unissued bonds.

#### **The Committee's Approach**

The Committee divided its negotiations on bond-related into four discrete assignments:

- Develop a method for allocating payments between SMUSD and MUSD on bond debt owed on bonds issued by SMMUSD before the date of separation.
- Develop an approach for the refinancing of the bond debt issued by SMMUSD before separation and allocated to SMUSD or MUSD at the time of separation.
- Develop a method for allocating the amount of authorized but-not-yet-issued bonds between SMUSD and MUSD.
- Develop a method for SMUSD and MUSD to issue bonds post-separation.

The Committee adopted common definitions and added supplemental guiding principles tailored for the negotiations related to bond-related items. The Committee studied information available in background and other resource materials about the status of Measure BB and Measure ES bond funds. The Committee posed a series of legal questions on bond-related issues to Procopio (see Online Appendix B-X), and spent time discussing and evaluating different methods and approaches to addressing the four assignments.

In sum, the Committee then reached a package of consensus agreements on bond-related issues that align with the Board's objectives and the Committee's guiding principles. The details of the Agreement are explained below.

#### **Guiding Principles and Definitions**

The Committee developed its agreements on bond-related items based on the general principles the Committee adopted for all terms of an agreement plus three additional guiding principles developed specifically for this issue area.

As a result, the methods for dividing SMMUSD's assets align with the Committee's agreement that all terms must: be financially viable for both SMUSD and MUSD; ensure a degree of predictability for both SMUSD and MUSD; enable each school district to be able to plan ahead with a reasonable degree of resource certainty; avoid establishing potential negative incentives for either SMUSD or MUSD to pursue increased revenue or otherwise improve education in

their schools; and be clear and understandable, legal, and enforceable. (See Memorandum Report, page X.)

The Committee developed three additional guiding principles for its negotiations on bond-related items:

- Post-separation, each district (SMUSD and MUSD) should, to the maximum extent possible, be provided sole discretion to make its own decisions regarding refinancing of existing bond debt and the issuance of new bonds.
- Post-separation, any decisions regarding the allocation of authorized but-not-yet-issued bonds should be consistent with decisions and commitments regarding projects and division of bond authority made prior to separation.
- Decisions regarding the allocation of authorized but-not-yet-issued debt should place priority and mutual respect on the needs and preferences expressed by SMUSD and MUSD at the time the allocation decisions are made.

Definitions Adopted for Key Words and Phrases*	
ES Funds	Refers to the funds made available to SMMUSD as a result of Measure ES, which was approved by the voters in November 2012. Approval of Measure ES authorized the Board to issue general obligation bonds, in an amount not to exceed \$385,000,000.
BB Funds	Refers to the funds made available to SMMUSD as a result of Measure BB, which was approved by the voters in November 2006. Approval of Measure BB authorized the Board to issue general obligation bonds, in an amount not to exceed \$268,000,000.

\*See Online Appendix B-X for the Committee's full glossary of acronyms, words, and phrases.

#### A. Negotiated Agreement on Bonds Issued by SMMUSD Before Separation

**Committee member suggestion:** *Perhaps some notation that these bonds can only be used for capital improvements and technology.*

With respect to the Measure BB and Measure ES bonds issued by SMMUSD before separation, the Committee reached the following agreements:

- SMMUSD's bond debt should be allocated between SMUSD and MUSD based upon the respective assessed values of Santa Monica and Malibu on the most recent assessment rolls as of the date of separation.
- The special State legislation and related reorganization documents should explicitly address the issue of refinancing any of the existing SMMUSD debt that is allocated between SMUSD and MUSD. Specifically, the law should provide that any decisions regarding refinancing of this debt can be made independently by SMUSD or MUSD, without need to coordinate with the other.

To accomplish the above, Procopio advises that language in the special State legislation needs to specify that each successor district is treated as the issuing district (SMMUSD will not exist anymore) for purposes of Government Code section 53580 and related statutes, and that each is separately responsible for IRS (Internal Revenue Service) tax compliance and continuing disclosures under SEC (Securities and Exchange Commission) regulations.

## **B. Negotiated Agreement on the Allocation of Authorized But-Not-Yet-Issued Bonds**

As of this writing, an additional \$295 million remains in bonding authority under Measure ES that has been authorized but not issued.

The Committee agreed that this issue lends itself to a recommendation for a process because the exact allocation of authorized but-not-yet-issued bonds will depend on the status of projects and plans of SMUSD and MUSD at the time of separation. The Committee's recommended process is to delegate the allocation of this outstanding bonding authority between SMUSD and MUSD to Group 2, the second transition/implementation group appointed jointly by the respective Boards of SMUSD and MUSD. (See the Term Sheet on Issue #5: Implementation.)

The Committee agreed that Group 2 should be directed to allocate the authorized but-not-yet-issued bonds consistent with the following two supplemental guiding principles the Committee adopted for bond-related items:

- Allocate the authority consistent with decisions and commitments regarding projects and division of bond authority made prior to separation, including that Malibu receives \$77 million (at minimum) out of ES's total of \$385 million; and

*Committee member comment: Need to mention here that the bond fund balance needs to be part of this calculation*

- Mutual respect for the needs and preferences of SMUSD and MUSD at the time the allocation decision is made.

## **C. Negotiated Agreement on Bonds Issued Post-Separation**

With respect to the method for SMUSD or MUSD to issue bonds post-separation, the Committee agreed that:

- After the date of separation, the decision by either SMUSD or MUSD to issue bonds should be left to the sole discretion of each district.
- Consistent with the above agreement, any debt owed on bonds issued post-separation by either SMUSD or MUSD is the sole responsibility of the district that issued the bonds.

### **OTHER LIABILITIES HERE?**

*At least for now, I moved this section – that had been part of Issue #2 here.*

The Committee addressed some remaining items listed on SMMUSD's balance sheets that are considered liabilities (and not assets) and that are not covered by Issue #3, Bond-related items or Issue #4, Environmental Liability.

### **Committee Agreements on the Division of Other Balance Sheet Items**

This final section provides the Committee's consensus agreements on three other balance sheet items. All three are liabilities (as opposed to assets), but are not addressed in the Committee's Agreement on either Issue #3, Bond-Related Items or Issue #4, Environmental Liabilities.

### **Certificates of Participation (COPs)**

The Certificates of Participation liability on SMMUSD's balance sheet reflects the debt owed on the financing for the District's Headquarters' building. Consistent with the Committee's recommendation that the Headquarters building is allocated to Santa Monica, SMUSD will assume sole responsibility for paying the outstanding debt owed on the COPs used to fund the purchase of this property.

### **Compensated absences**

The Committee agreed that the liability associated with compensated absences should "move" with the individual teacher or other staff member who has accrued this unused leave. In other words, post-separation, SMUSD should inherit the liability for personnel who are SMUSD employees, and MUSD should inherit the liability for personnel who are MUSD employees.

### **OPEB (Other Postemployment Benefits)**

OPEB is a Government Accounting Standards Board (GASB) term for the outstanding liability for paying benefits (other than pensions) to retired public sector employees.

The Committee agreed that the most equitable allocation of OPEB liability should be based on the most recent actuarial data available at the time of separation, and should be linked to how the funds already set-aside for providing retiree health benefits is divided between SMUSD and MUSD at the time of separation. Because the allocation of this liability depends on decisions that will be made closer to the time of separation, the Committee recommends the details of allocating the OPEB liability between SMUSD and MUSD be assigned to Group 2. (See Issue #5, Implementation.)



### **Term Sheet for Issue #3, Environmental Liability**

#### **The Board's Objectives**

The Board's objectives on the issue of environmental liability, as stated in the December 2015 action creating the Committee, were:

- Establish a structure under which MUSD assumes responsibility for any remaining remediation of any contamination in Malibu schools and indemnifies SMUSD for any future claims arising from such remediation work.
- Dismissal of the pending lawsuit against SMMUSD or an enforceable agreement from the plaintiffs that SMUSD will be dismissed from the lawsuit.
- Receipt by the Board of a legal opinion from a firm selected by the Board with respect to any potential continuing exposure of SMUSD following separation and a conclusion by the Board that any such exposure is reasonable.

Note: With respect to the Board's objective regarding dismissal of the lawsuit brought by America Unites for Kids against SMMUSD, the Committee's understanding is that the September 1, 2016 ruling by Judge Anderson on this lawsuit essentially eliminated the Committee's need to address this objective as part of its negotiations. While the court's decision is on appeal, the Committee understands that the issues on appeal are limited to (a) whether attorneys' fees should be awarded to the plaintiff and (b) whether the injunction imposed by the court on certain private parties should be reversed; the court's decision regarding the obligations of SMMUSD to complete remediation work has not been appealed.

#### **The Committee's Approach**

The Committee approached its Issue #4 negotiations by dividing the assignment into two categories: environmental contamination for which SMMUSD has developed, approved, funded and begun a remediation plan; and environmental contamination for which no such plan has been developed, whether or not known at the time of separation.

The Committee studied information in background and other resource materials that addressed issues of environmental liability specific to a possible reorganization of the District. The Committee posed legal questions to Procopio (See Online Appendix B-X) and spent time discussing and evaluating different methods and approaches to addressing the Board's objectives. The Committee's Agreement on environmental liability issues is summarized below.

The Committee then reached a package of consensus agreements on environmental liability issues that align with the Board's objectives and the Committee's guiding principles. The details are explained below. For the legal advice provide by Procopio to the Committee on bond-related issues, see Appendix B-X.

## Guiding Principles

The Committee developed its agreements on environmental liability issues based on the general principles the Committee adopted for all terms of an agreement. The Committee did not find the need to add any more guiding principles specific to environmental liability issues.

As a result, the Committee's agreements on environmental liability issues align with the Committee's agreement that all terms must: be financially viable for both SMUSD and MUSD; ensure a degree of predictability for both SMUSD and MUSD; enable each school district to be able to plan ahead with a reasonable degree of resource certainty; avoid establishing potential negative incentives for either SMUSD or MUSD to pursue increased revenue or otherwise improve education in their schools; and be clear and understandable, legal, and enforceable.

## Major Negotiated Terms and Conditions

### **1. Agreement on environmental liability for which SMMUSD has developed, approved, funded, and begun a remediation plan.**

The Committee agreed that the current ongoing remediation of PCBs (polychlorinated biphenyl), as contemplated in SMMUSD's building replacement and renovation program will not be affected by separation. This remediation program will continue to be funded after separation (by the bond program) and is scheduled to be completed by December 19, 2019.

The Committee further agreed that any remediation project that is underway at the time of separation will be subject to further negotiation by Group 2 (See Issue #5, Implementation) to work out the logistics of project management and completion.

***Committee needs to confirm an agreement was made on this next sentence:*** In addition, If SMUSD becomes liable for any personal injury associated with this contamination, MUSD will contribute a portion of the ultimate cost determined by the ADA Method.

### **2. Agreement on environmental liability related to contamination that is either not known about before separation or is known about before separation but for which SMMUSD has not yet developed, approved, or funded a remediation plan.**

For this category, the Committee agreed that each district will be liable for its own properties and in charge of developing, approving, funding, and implementing a remediation plan. For schools in Malibu, the Committee agreed that the portion of ES bonds allocated to Malibu could serve as a potential source of funding for this remediation work.

The Committee also agreed that MUSD will indemnify SMUSD for any liability associated with any contamination falling within this category in Malibu property, and SMUSD will indemnify MUSD for any liability associated with any contamination falling within this category in Santa Monica property.

### **Term Sheet for Issue #5, Implementation Steps**

In its action creating the Committee, the Board outlined the process that will occur directly after the Committee submits its report to the Board. (See Memorandum Report, page X.)

As previously discussed by the Board, with respect to the actual implementation of a district reorganization, there are several different avenues available. In sum, these are a petition to the Los Angeles County of Education (LACOE), special State legislation, or some combination of the two. (Online Appendix X and Y contain excerpts from the California Department of Education, District Organization Handbook, dated September 2016.)

Negotiations on the details of the implementation process were beyond the scope of the Board's objectives for the Committee. However, the Committee agreed it was important to offer a recommendation on how to resolve the financial items identified in the report that, due to various reasons, cannot be finalized until either at the actual time of separation or in the time period post-separation.

For this purpose, the Committee recommends the appointment of two groups.

**Group One:** The SMMUSD Board should appoint Group One to work on the things that need to happen between the time the Board approves moving forward with unification and the time that separation occurs.

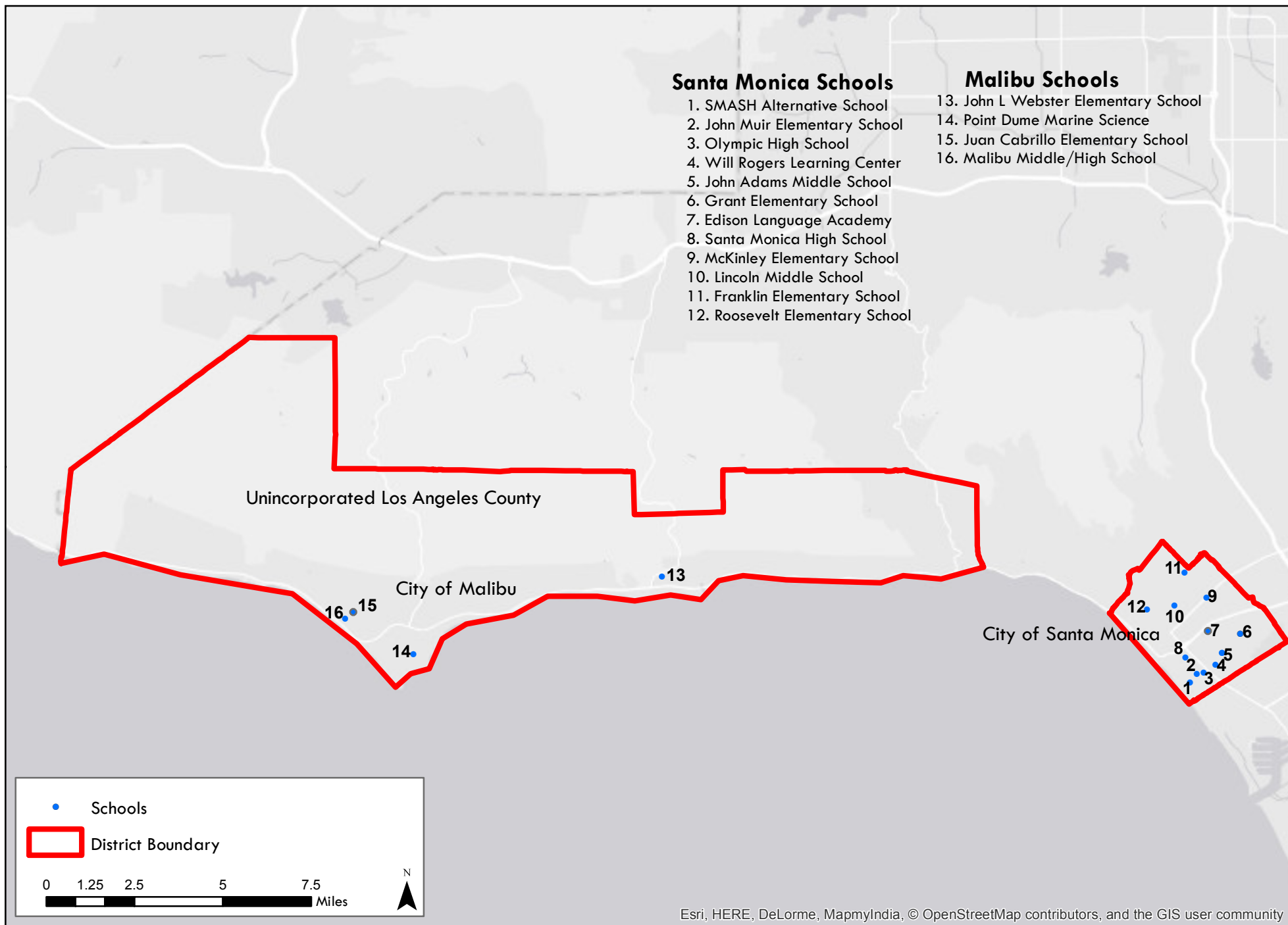
Candidate tasks for Group One are:

- Monitoring of any special state legislation being drafted at the Board's direction;
- Monitoring the negotiations for project management and completion of capital improvement projects in Malibu schools that are underway at the time of separation
- Monitoring the negotiations for completing the remediation of environmental contamination in Malibu schools that are underway at the time of separation.

**Group Two:** After separation occurs, the respective Boards of Education of SMUSD and MUSD should appoint Group Two to work on the logistics and any outstanding issues that need to be resolved to ensure a smooth transition to the interactions of the two districts going forward.

Candidate tasks for Group Two are:

- Based on the status of capital projects at the time of separation, making final recommendations about the allocation of "cash" in the Building Fund.
- Based on the status of ES bond authority used at the time of separation, making final recommendations about the allocation of authority to issue authorized but not yet issued bonds.



# Santa Monica-Malibu Unified School District

Date: 1/19/2017