

ARIZONA STATE SENATE
RESEARCH STAFF



TO: JOINT LEGISLATIVE AUDIT COMMITTEE
Senator Robert Blendu, Cochair
Representative John Nelson, Cochair

DAWN NAZARY
LEGISLATIVE RESEARCH ANALYST
EDUCATION K-12 COMMITTEE
Telephone: (602) 926-3171
Facsimile: (602) 926-3833

DATE: November 1, 2007

SUBJECT: Sunset Review of the School Facilities Board

Attached is the final report of the sunset review of the School Facilities Board, which was conducted by the Senate Education K-12 and House of Representatives Education (K-12) Committee of Reference.

Pursuant to Title 41, Chapter 27, Arizona Revised Statutes, the Committee of Reference, after conducting a sunset review on September 26, 2007, recommends that the School Facilities Board be continued for two years.

This report has been distributed to the following individuals and agencies:

Governor of the State of Arizona
The Honorable Janet Napolitano

President of the Senate
Senator Tim Bee

Speaker of the House of Representatives
Representative Jim Weiers

Senate Members
Senator Karen Johnson, Cochair
Senator Ron Gould
Senator Linda Gray
Senator Leah Landrum Taylor
Senator Victor Soltero

House Members
Representative Andrew Tobin, Cochair
Representative Doug Clark
Representative Sam Crump
Representative David Lujan
Representative Jackie Thrasher

School Facilities Board
Arizona State Library, Archives & Public Records

Senate Republican Staff
Senate Democratic Staff
Senate Research Staff

House Majority Staff
House Democratic Staff
House Majority Research Staff

DN/jas

**Senate Education K-12 and
House Education (K-12) Committee of Reference
Committee of Reference Report**

Background

Pursuant to § 41-2953, Arizona Revised Statutes, the Joint Legislative Audit Committee (JLAC) assigned the sunset review of the School Facilities Board to the Arizona Auditor General.

In 1994, Arizona's system of school capital finance was declared unconstitutional by a Court decision in *Roosevelt v. Bishop* because of a failure to conform to the state Constitution's "general and uniform" clause. The Court opined that the system, which allowed school districts to rely heavily on secondary property, which is driven by the property wealth, created an unequalized system and funding disparities between school districts. On July 9, 1998, during a special session, legislation was passed reforming the way traditional K-12 public schools (not including charter schools) are constructed in Arizona. This legislation called Students Fair and Immediate Resources for Students Today, commonly known as Students FIRST, established the School Facilities Board (SFB) to administer the Building Renewal, the Deficiencies Correction and the New School Facilities program to provide capital funding for K-12 schools.

Pursuant to A.R.S. § 15-2001, the ten-member board consists of nine gubernatorial appointments who serve four-year terms and the Superintendent of Public Instruction or a designee. The nine appointed members include a school district governing board representative, a taxpayer representative, a school construction representative, a public school facilities manager, an architect, an engineer, a classroom teacher, a demographer and a private business representative. The Superintendent of Public Instruction or the Superintendent's designee serves as an advisory nonvoting member.

Budget

According to the Joint Legislative Budget Committee's (JLBC) FY 2007-2008 Appropriations Report, the SFB's FY 2007-2008 appropriated staff consists of 20.0 full-time equivalent positions and appropriated state General Fund budget level is set at \$532,695,100, as detailed as follows:

• Administration	\$ 1,944,400
• New Construction	\$370,000,000
• Debt Service	\$ 71,967,200
• Building Renewal	\$ 86,283,500
• Energy Pilot Program	\$ 2,500,000

Committee Sunset Review Procedures

The Committee of Reference held one public meeting on Wednesday, September 26, 2007, to review the audit report prepared by the Auditor General and the additional four sunset factors prepared by the SFB, as required by A.R.S. § 41-2954, subsection E, and to receive public testimony. The Committee of Reference received testimony from the Executive Director of the SFB.

Committee of Reference Recommendations

The Committee of Reference recommends that the School Facilities Board be continued for two years.

Sunset Report Requirements Pursuant to A.R.S. § 41-2954

I. Identify the problem or the needs that the agency is intended to address.

In July 1994, the Arizona State Supreme Court held in *Roosevelt v. Bishop* that the state's statutory scheme for financing public education violated the Arizona Constitution. Article XI, § 1 of the Arizona Constitution requires that the Legislature enact laws that provide for the establishment and maintenance of a general and uniform public education.

On July 9, 1998, the four-year struggle to create a new capital finance system ended when the Legislature passed and Governor Hull approved S.B. 1101 (Laws 1998, 5th Special Session, Ch. 1), commonly known as Students FIRST. Students FIRST responds directly to guidance provided by the Supreme Court which recognized that the state's constitutional obligation is limited to funding a public school system to a prescribed level of adequacy. "The concepts of statewide equalization and local option to go above and beyond the standards are irreconcilable unless the legislature establishes standards for adequate capital facilities." Students FIRST responds to the constitutional requirement by setting adequacy standards for school buildings and by creating the SFB.

Once adequacy standards were established, the Legislature had to ensure that districts have sufficient funding to meet the standards. The financing system had to provide funds to: 1) bring existing facilities up to an adequate standard; 2) construct new and adequate facilities for growing districts; and 3) maintain all capital facilities at the adequacy level. To accomplish this, Students FIRST established a Deficiencies Correction Fund, New School Facilities Fund and Building Renewal Fund.

II. State to the extent practicable, in quantitative and qualitative terms, the objectives of the agency and its anticipated accomplishments.

In 1998, the SFB was given the responsibility of implementing the Students FIRST law. This was viewed by some as a near impossible task, as the program incorporated deficiencies correction, preventive/major maintenance and new school construction, for all public schools in the State of Arizona. Students FIRST has not been without shortcomings, as it is a program that has never been done elsewhere. In a way, the SFB built the first airplane while flying it, as the SFB had to create the model while implementing the program. Given that challenge, there is a lot of which to be proud.

Deficiency Corrections

In the deficiencies correction project, the SFB first established the minimum school facility guidelines, and then assessed all 1,300 of the state's public schools (over 8,000 buildings) to identify building systems and equipment that were deficient.

By June 30, 2006, there were 9,002 deficiency projects corrected throughout the state at a cost of \$1.3 billion. The majority of these involved roofing, HVAC, electrical, fire alarms and replacement

space. All of the projects have made significant strides in improving our state's school facilities. The program has had an especially great impact on the rural districts and the low wealth urban districts that were unable to afford the costs associated with school repair on their own. In addition, the deficiency program timing was ideal from a cost standpoint, as deficiency corrections work employed thousands of our state citizens during a time when Arizona was in an economic downturn. Competition and pricing also benefited significantly from the downturn, allowing the state to receive maximum value for the dollars spent.

New School Facilities

As of June 7, 2007, the SFB has awarded 328 new school projects with a total value of approximately \$2.78 billion. Of the 328 projects, 235 have been completed, 29 are under construction and 64 are board approved with some in design.

As of FY 2006-2007, the SFB has purchased 2,006 acres of land valued at \$155.2 million and has received 1,765 acres in donations and paid a 20 percent donation factor of \$38.1 million but the appraised value of the donated land was approximately \$190.4 million, saving the state \$152.3 million in land acquisition costs.

Without Students' FIRST, Arizona would not have been able to produce the educational infrastructure mandated by the growing population. The varying levels of property wealth and district bonding limitations of the old system set artificial limits on the amount of infrastructure that the system could provide.

Building Renewal

The SFB distributes building renewal based on the district's successful completion of building renewal plans and prior year expenditures reports. The building renewal appropriated supports 110.6 million square feet, 10,336 buildings and 1,425 schools that have a replacement value of \$11.8 billion. Each year the state adds about 3 million square feet to the school inventory. There is no dedicated funding for preventative maintenance but districts are allowed to spend up to 8 percent of their building renewal dollars on preventative maintenance. Districts maintain preventative maintenance plans and currently complete approximately 40 percent of recommended preventative maintenance.

Last year the SFB developed a web-enabled building renewal planning application that was upgraded this year to include prior year building renewal expenditures and renovations reporting. The automation will allow the SFB to provide better management data to decision makers about the type of building renewal projects (e.g. HVAC or plumbing), identify how districts are managing their plans by comparing prior year plans with expenditures, identify the amount of funds sitting in district ending balances that are being saved for future projects, etc.

III. Identify any other agencies having similar, conflicting or duplicative objectives, and an explanation of the manner in which the agency avoids duplication or conflict with other such agencies.

There are no other agencies that have conflicting or duplicative objectives but the Arizona Department of Administration (ADOA) General Services Division has some similar processes.

Building and Planning Services

Building inspections – Provide inspections of all buildings in the ADOA building system and state-funded projects under construction.

Building renewal – Review annual building renewal project requests. Allocate annual appropriation to agencies for specific projects and allocate funds for emergency requests throughout the year.

Capital Improvement – Prepare annual ADOA Building System Capital Improvement Plan, review agency capital requests and submit recommendations to the Governor's Office of Strategic Planning and Budgeting and the Joint Legislative Budget Committee.

Construction Review – Review and approve all state-funded construction documents, including contracts, plans, specifications and payment applications.

Construction Services

Provides a full service project management team to coordinate things like the planning, designing, construction and environmental services for public funded projects (e.g., Department of Health Services State Laboratory, Southern Arizona Veteran's Memorial Cemetery Administration Building, Arizona State Prison Complex – Lewis).

IV. Assess the consequences of eliminating the agency or of consolidating it with another agency.

Given the nature of the Supreme Court decision, the functions of the agency would need to be carried out either by the agency in its current form or be consolidated with another agency to carry out the existing mission. The elimination of the agency or its functions would take the state back to where it was prior to the Supreme Court decision with disparities in school facilities given the vast differences in property wealth across the state and the impacts on local taxpayers.

Attachments:

1. Committee Agenda Notice
2. Committee of Reference Meeting Minutes
3. Auditor General Presentation Handouts
4. Chairman's Letter requesting additional sunset factors
5. SFB Response (additional sunset factors)

**COMMITTEE OF
REFERENCE
AGENDA NOTICE**

REVISED

REVISED

REVISED

Interim agendas can be obtained via the Internet at <http://www.azleg.state.az.us/InterimCommittees.asp>

ARIZONA STATE LEGISLATURE
INTERIM MEETING NOTICE
OPEN TO THE PUBLIC

**SENATE K-12 EDUCATION COMMITTEE AND HOUSE K-12 EDUCATION COMMITTEE
COMMITTEE OF REFERENCE**

Date: Wednesday, September 26, 2007

Time: 9 A.M.

Place: SHR 1

AGENDA

1. Call to Order
2. School District Performance Audits of Amphitheater Unified School District, Bisbee Unified School District and Alpine Elementary School District
 - a. Presentation by Auditor General
 - b. Response by the School District
 - c. Public Testimony
 - d. Recommendations by the Committee of Reference
3. School Facilities Board Sunset Audit
 - a. Presentation by Auditor General
 - b. Response by the School Facilities Board
 - c. Public Testimony
 - d. Recommendations by the Committee of Reference
- 4. School District Performance Audits of Litchfield Elementary School District, Avondale Elementary School District, Deer Valley Unified School District and Union Elementary School District
 - a. Presentation by Auditor General
 - b. Response by the School District
 - c. Public Testimony
 - d. Recommendations by the Committee of Reference
5. Adjourn

Members:

Senator Karen Johnson, Co-Chair
Senator Ron Gould
Senator Linda Gray
Senator Leah Landrum Taylor
Senator Victor Soltero

Representative Andrew Tobin, Co-Chair
Representative Doug Clark
Representative Sam Crump
Representative David Lujan
Representative Jackie Thrasher

8/29/07

9/6/07

jt
sp

Persons with a disability may request a reasonable accommodation such as a sign language interpreter, by contacting the Senate Secretary's Office: (602)926-4231 (voice). Requests should be made as early as possible to allow time to arrange the accommodation.

**COMMITTEE OF
REFERENCE
MEETING MINUTES**

ARIZONA STATE LEGISLATURE

SENATE K-12 EDUCATION COMMITTEE AND HOUSE K-12 EDUCATION COMMITTEE COMMITTEE OF REFERENCE

Minutes of the Meeting
Wednesday, September 26, 2007
9:00 a.m., Senate Hearing Room 1

Members Present:

Senator Karen Johnson, Co-Chair
Senator Ron Gould
Senator Linda Gray
Senator Victor Soltero

Representative Andrew Tobin, Co-Chair
Representative Doug Clark
Representative Sam Crump
Representative David Lujan
Representative Jackie Thrasher

Members Excused:

Senator Leah Landrum Taylor

Staff:

Dawn Nazary, Senate Education Committee Analyst
Brian Lockery, House of Representatives Education Committee Analyst
Ingrid Garvey, House of Representatives Education Committee Assistant Analyst

Co-Chairman Tobin called the meeting to order at 9:03 a.m. and attendance was taken.

PRESENTATIONS

The Auditor General's Office on School District Performance Audits

Sharron Walker, Director, Division of School Audits, Auditor General's office,
distributed the following handouts:

- Amphitheater Unified School District Performance Audit (Attachment A)
- Bisbee Unified School District Performance Audit (Attachment B)
- Alpine Elementary School District Performance Audit (Attachment C)
- Litchfield Elementary School District Performance Audit (Attachment D)
- Avondale Elementary School District Performance Audit (Attachment E)
- Deer Valley Unified School District Performance Audit (Attachment F)
- Union Elementary School District Performance Audit (Attachment G)
- Copy of PowerPoint presentation K-12 Education Committee of Reference
September 26, 2007 School District Performance Audits (Attachment H)

Ms. Walker gave a brief overview of the audit process. In November 2000, voters approved Proposition 301, which increases state sales tax by 6/10ths of 1% for 20 years to fund educational programs. The school districts can only use this money for specified uses and the proposition requires the Auditor General's Office to monitor the dollars spent in the classroom and conduct performance audits on randomly selected school districts. Also, in the 2006 Legislative Session House Bill 2064 added various audits of the state's English Language Learner (ELL) Program. She explained that the most recent fiscal year data is compared to the National average, the State average and a pool of similar school districts. The performance audits focus primarily on four operational areas: plant operations, administration, food service, transportation. Ms. Walker distributed a handout "Implementation Status of DSA Reports" (Attachment I) and stated that there is a statutory requirement to follow up on the school districts implementation of the audit recommendations.

Ann Orrico, Manager, Division of School Audits, Auditor General's Office, explained the findings and recommendations of the Amphitheater Unified School District audit as shown in the PowerPoint presentation Attachment H.

Vicki Balentine, Superintendent, Amphitheater Unified School District, explained the progress, as outlined in the handout "Amphitheater Public Schools" (Attachment J), that the district is making on the recommendations from the performance audit.

Senator Linda Gray questioned literacy levels of ELL students graduating from the Amphitheater Schools.

Ms. Balentine explained that not all ELL students and Special Ed students reach Adequate Yearly Progress (AYP) (National Assessment of Education).

Representative Thrasher asked for more information about the intergovernmental agreement with Pima County.

Ms. Balentine explained that the intergovernmental agreement is in reference to security and will save approximately \$20,000. The staffing levels will continue to be monitored but not at the sacrifice of school safety. She stated that parts of the district are in high crime areas and rural areas.

Scott Little, Chief Financial Officer, Amphitheater Unified School District, further explained the agreement with the Pima County Sheriffs Office. He also explained that a portion of plant costs is due to the age of many of the buildings in the District.

Senator Soltero stated that student's and parents' sense of safety concerning schools has a large impact on how that student succeeds in that school.

Senator Gray asked how many state supplied resource/probation officers the District has.

Ms. Balentine stated that there is a grant through Oro Valley for two resource officers that are shared between two high schools. She said the City of Tucson has reallocated their resource officer staff this year to focus at the elementary and middle school levels only. She stated that the District has had to hire off-duty police officers to provide that service.

Ross Ehrick, Manager, Division of School Audits, Auditor General's Office, explained the findings and recommendations of the Bisbee Unified School District audit as shown in the PowerPoint presentation Attachment H.

Paul McDonald, Superintendent, Bisbee Unified School District, explained what progress has been made in implementing the Auditor General's recommendations. He explained that the taxpayers in this district are willing to support the district as long as no schools are closed. An override is expected this year. He explained that schools sharing administration have shown to lower performance levels in both schools. The community is firm that all four facilities stay open due to the fact that the school facilities are the only facilities in the area.

Senator Gray questioned the teachers being paid less in this school district and how the district is able to keep teachers. She also asked about enrollment fluctuations.

Mr. McDonald stated that it must be the weather and that the district has been able to keep all positions filled with teachers from all across the country without the salary coming into question. He explained that the enrollment stays in the area of 1,000 students.

Senator Soltero asked what percent of teachers have been employed a while and what percent are new.

Mr. McDonald stated that approximately 75% of the teachers grew up in the area and came back. He said that about 25% are transplants. He stated that specialists are not on staff and are paid under support staff which adds to administrative costs.

Representative Tobin asked about storage of Bisbee museum antiques.

Mr. McDonald stated that the storage of various town items was just allowed and that the Auditor General's recommendations authorized all of the items be evicted. He stated that some of the storage space is now being rented out to various groups for activities or storage.

Representative Crump questioned meals per student dollars being higher than comparable districts.

Mr. McDonald stated that since the audit, the district is better able to accurately calculate cost per student. He also stated that suppliers charge a fuel surcharge for the distance to deliver to the district.

Representative Tobin asked if distance learning technology has been considered. Mr. McDonald stated that nothing in that field has been considered to this point.

Ann Orrico, Manager, Division of School Audits, Auditor General's Office, explained the findings and recommendations of the Alpine Elementary School District audit as shown in the PowerPoint presentation Attachment H.

Representative Tobin questioned reimbursing parents for two round trips to take their children to school.

Ms. Orrico stated that monthly payments were approximately \$200 to \$300 per month per student for transportation. She stated that comparable districts do not pay parents to transport their children.

Senator Gray questioned the district filing any 1099 forms for the payments to parents.

Ms. Orrico stated that question was not asked in the audit.

Michael Cox, Administrator, Alpine Elementary School District, distributed a letter to Michelle Corse (Attachment K) which shows that Alpine School District was following a formula received from Arizona Department of Education (ADE). The Auditor General's Office and ADE are conferring to decide on the correct formula and Alpine School District will follow the formula it is instructed to use. Mr. Cox distributed a handout "Alpine Elementary School District 6-Month Follow-Up Report To Performance Audit Report Issued October 2006" (Attachment L) and explained what progress has been made in implementing the Auditor General's recommendations.

Senator Johnson questioned how parent transportation is organized and reimbursed. She asked why Alpine Elementary School District reimburses transportation costs when other schools do not.

Mr. Cox stated that some parents carpool and now only those who would qualify for free and reduced lunches are being reimbursed. Alpine Elementary School District was told that it is legal.

Senator Gray stated, in 2005 the Alpine Elementary District was given \$355,000 in transportation money, but spent less than \$64,000. She asked where the rest of the money was spent. She asked if the \$125,000 that was charged over was paid back.

Linda Fite, Office Manager, Alpine Elementary School District, explained that the monies were spent on the new building, grounds, furniture, and equipment.

Senator Gray questioned how transportation monies could be used to build a facility.

Ms. Fite explained that during budgeting when you find your revenue control limit you can spread it between M&O and Outlay.

Senator Gray stated that she feels there is a flaw in the law in which it is said "may provide transportation". She said she sees this as a scheme to be able to get additional revenue to put in other areas. She asked if reimbursement to parents for transportation is considered income for those parents and if the district filed 1099 forms. She also asked what the highest amount was paid to a parent to drive their children to and from school.

Ms. Fite stated that no the District did not file any 1099 forms. She said that the largest payment she believes was approximately \$5,000 for the year.

Senator Gould asked if the children bring their lunch to school.

Mr. Cox stated that was correct.

Senator Gray questioned whether the \$125,000 in excess revenue the Alpine Elementary District received was paid back.

Ms. Fite stated that the District did not pay that money back because they were working under the guidance of ADE and did not see the money as excess. Ms. Fite stated that the District is willing to do whatever is necessary to come into compliance.

Representative Tobin asked if the Auditor General had any comments about Senator Gray's concerns.

Ms. Orrico stated that ADE instructed Alpine School District to report transportation costs in the way they did and has not asked for reimbursement. She stated that the Auditor General's Office and ADE are working together to clarify the situation. Ms. Orrico explained that the transportation excess monies can be spread to other areas. She said that because ADE has not agreed with the Auditor General's Office on proper reporting they have not asked for the money to be returned.

Senator Gray asked what the Governing Board has decided to do on the subject.

Mr. Cox stated that the Governing Board has decided to continue as it has been doing.

Senator Gray questioned what the excess money would be spent on in the future.

Ms. Fite stated that since the audit, the number of reimbursements paid out has decreased and that the money is now being put back into the classroom. She explained that the number of teachers has also been increased to a ratio of one teacher to nine students.

Representative Clark made a statement about being proud and wanting to commend the product coming out of the Alpine Elementary District, however, the District needs to follow the letter of the rules and not the spirit of the rules. He stated that the system needs to be above reproach.

Co-Chairman Tobin recessed the Committee at 10:51 a.m. for a short break.

Co-Chairman Tobin reconvened the Committee at 10:57 a.m.

The Auditor General's Performance Audit of the School Facilities Board

Shan Hays, Performance Audit Manager, Auditor General's Office, explained some background, the findings and recommendations of the School Facilities Board audit as shown in a copy of the power point presentation "School Facilities Board Performance Audit August 2007" (Attachment M).

Representative Lujan questioned the recommendation for the Legislature to change the building renewal formula to make the funding more predictable.

Ms. Hays explained that the Legislature has not funded according to the formula except for one year. The districts have suggested it would be easier if there was a way to insure how much money would be received.

John Arnold, Executive Director, School Facilities Board (SFB), explained that one of the most important things done by the Board is to raise awareness of facilities. He explained that the formula for inflation is retroactive, which means it works for facilities being built now but not appropriate for facility grants for future projects.

Senator Johnson questioned the stabilization of inflation costs.

Mr. Arnold said that yes costs have stabilized for the metro area, but in rural areas a premium is still being paid due to travel costs. He explained that districts were losing up to 30% of their buying power between the date the project was awarded and the date they started construction. He said that the Board established the Minimum Existing Standard and then recognized the need to cap certain areas of construction.

Representative Tobin questioned the Board's statutory authority to alter the formula.

Mr. Arnold said that the statute is not entirely clear on this issue. The statute dictates that the School Facilities Board establish a standard. The Board has discussed this issue with the Attorney General's Office, the Joint Legislative Budget Committee and the Auditor General's Office. The Attorney General's informal decision is that it is within the Board's statutory authority.

Senator Gray questioned how many gyms a school can have.

Mr. Arnold stated that the districts can outlay their money however they see fit. The Board said that it will only fund one gym floor, if they build more than one gym they need to get the funding locally.

Representative Lujan stated that for the first four years he was the Assistant Attorney General for the School Facilities Board. He said that he agrees the Board is responsible to provide any extra monies needed to build a school to the minimum standard.

Mr. Arnold stated that the School Facilities Board clarified minimum guidelines. He said that programs have been put in to effect to improve oversight and reporting. He stated that in some places statutes are vague enough that interpretations will have to be made and agreed upon.

Senator Gray questioned an audit regarding doors, where the SFB is criticizing the district but the SFB would have had to approve the building. She asked if the industry standards for energy saving were guidelines or standards that must be met.

Mr. Arnold stated that state law requires that school districts meet the current IECC (International Energy Conservation Code) standards and that the SFB enforces those standards on all schools. He said the statute gives the districts full design authority.

Senator Gray questioned the audit done on the Union School District that lists the doors opening directly outside is an energy wasting design.

Mr. Arnold stated that there has been much discussion about the subject, but that design is allowed under the state law.

Senator Johnson questioned building a school with a capacity of 100 when only 40 children attend that school.

Mr. Arnold stated that particular school building was approved to replace a building that had exceeded its usefulness. He stated that the school has asked for more space because they think they are going to grow.

Senator Soltero questioned using two doors then a space and two doors like in restaurants.

Mr. Arnold stated that the design is a local decision but that most do not do that because it costs space.

Senator Johnson questioned a final decision on the Auditor General's finding playground equipment, landscaping, public address systems and such being inappropriate expenditures.

Mr. Arnold stated that the statute says that the SFB will review the findings and report to the Department of Education, but the SFB does not yet have a system to review the issues. He takes full responsibility for not getting that set up. He said the Auditor General's Office is helping to set up standards for this purpose.

Representative Tobin questioned controls not being applied, relying too much on outside consultants and the state ownership of a database.

Mr. Arnold stated that the SFB has 15 employees and is the 9th largest expender in the state, spending almost \$500 million a year. He said that they do not have dedicated technology staff. He said that the Auditor General has a concern that any information or technology would not be owned by the State. He explained that this would be corrected when the new contract comes due. He said that the SFB needs to formalize and improve their controls.

Senator Johnson questioned Mr. Arnold's opinion on prototype schools and the opportunity to save money with them.

Mr. Arnold stated that he is a supporter of using prototype schools, but again that authority rests with the school districts. He said that he does not think they will completely eliminate design fees.

Senator Gould stated that as a contractor a standard floor plan would save money and increase the bidding process.

RECOMMENDATIONS BY THE COMMITTEE OF REFERENCE

Senator Johnson moved that the Senate K-12 Education and the House K-12 Education Committee of Reference recommend that the School Facilities Board be continued for three years until June 30, 2011.

Senator Gould made a substitute motion that the Senate K-12 Education and the House K-12 Education Committee of Reference recommend that the School Facilities Board be continued for two years until June 30, 2010.

Senator Gray asked if the Auditor General would do another audit in two years.

Debbie Davenport, Auditor General, stated that it is the Joint Legislative Audit Committee who determines whether the Auditor General's Office or a Committee of Reference would hear the next sunset.

Senator Soltero stated that he supports continuing the Board for three or more years.

Senator Gould stated that the logic behind his substitute motion is that the Legislators all serve two-year terms. He said that due to the amount of money, it deserves the Legislature's attention and continuous review.

Representative Tobin requested Dawn Nazary to restate the substitute motion. The motion PASSED by roll call vote of 5-4-1 (Attachment 1).

Co-Chairman Tobin recessed the meeting for one-half an hour at 12:05 p.m.

Co-Chairman Tobin reconvened the meeting at 12:44 p.m.

The Auditor General's Office on School District Performance Audits

Ann Orrico, Manager, Division of School Audits, Auditor General's Office, distributed a copy of her PowerPoint presentation "Education Committee of Reference September 26, 2007 School District Performance Audits" (Attachment N) and explained the findings and recommendations of the Union Elementary School District audit.

Representative Tobin questioned increases in administration costs despite previous overspending.

Ms. Orrico stated that salary and benefit costs were going to be increasing in fiscal year 2007 due to pay increases for administrators.

Representative Clark questioned if they are contracts that are already in place or new contracts that have been written.

Ms. Orrico stated that the pay increases are contracts put in place at the end of fiscal year 2006.

Peter Davis, Receiver for Union Elementary School District, stated that as a receiver he has to file a 120 day report on the financial situation and a plan for restructuring the district. He said that he just took over in June and the report is not yet finished, but should be out in approximately three weeks.

Bill Christensen, Superintendent, Tolleson Elementary School District, explained that through an inter-governmental agreement (IGA) he has been retained as a Superintendent for Union Elementary School District as well as providing business services, transportation and various other services. He said that with the audit they are better able to quickly address the main problems. He stated that progress is being made but there is still a great deal of work to be done. He stated that for transportation they have consolidated bus routes to reduce cost. He said that the administrative costs have been reduced by three administrators that have resigned. He stated that plant operations and maintenance has been addressed, in that there is no longer overtime and the employees are now fiscal year employees instead of 12-month.

Representative Tobin asked how a receivership works.

Mr. Davis explained that there are no preset models for a receivership, but it is a work in progress involving many agencies. He explained that while the 120 day report is being put together action is being taken to eliminate costs. He said that the receiver takes control of the Governing Board and gets advice from neighboring districts.

Representative Tobin questioned the district failing academically and asked what goals are being set to get the school on track academically.

Mr. Christensen explained that an improvement plan has been designed. He explained that each school in the district operated very independently of each other. They had different texts, different evaluations, different curriculums and different models. The curriculums were blended together, a staff development calendar was put in place and teacher committees were brought together to concentrate on making academic improvement. He stated that the academic side is of more concern than the financial side.

Representative Tobin asked where the parents are in this situation.

Mr. Christensen explained that they are split down the middle. Many are very supportive, but a lot of parents are not supportive due to lack of information regarding the situation.

Representative Tobin asked Mr. Christensen for his opinion on how the state should track superintendents. He asked what can be done to Superintendents that put districts in poor financial and academic positions.

Mr. Christensen stressed that early intervention is necessary.

Senator Gray questioned what should be done to superintendents that create these situations.

Mr. Christensen said he would support removing the superintendents and possibly sanctions to prevent them from doing this again.

Mr. Davis said one option that has been reviewed are breaches of fiduciary duty by Governing Board members, Superintendents, and other fiduciaries of the districts and holding them accountable. He said he had looked into the receiver bringing a lawsuit or otherwise against those individuals for their gross negligence and for their breaches of the confidences of the taxpayers of that district.

Senator Gray questioned the custodian that was paid over \$44,000 being a relative of either a Board member or administrator.

Mr. Davis stated that situation is currently being investigated along with several others. He said that across the board every position in the district is grossly over paid. Many of the administrators gave themselves massive raises after a year that they over spent the

budget by \$1 million and during a year that they were overspending the budget by \$1.2 million which was approximately 20% of their budget.

Senator Gray asked if this fraud is at the level that charges could be brought against individuals at the school district.

Mr. Davis stated that he has contacted the Attorney General about some of the things that have been found. He said the intent is to submit his report to the Attorney General so that further investigation can be done.

Senator Gray asked about unification with another school district.

Mr. Christensen stated that there are many areas with problems with unification or consolidation. One problem is tax rates and the financial impact on the people of the district. He stated that consolidation is basically what is happening currently.

Senator Johnson questioned if there is enough evidence at this point to bring charges.

Mr. Davis stated that is the job of the Attorney General's office. He said that the receivership is involved civilly with this but not criminally. He said the school does not have the resources to perform a criminal investigation.

Mr. Christensen stressed the sustainability of the school in the future.

Representative Crump questioned special needs transportation being so high and the ethics and reliability in the program.

Mr. Davis stated that is the top problem discussed with the Attorney General's office.

Mr. Christensen stated that student transportation is an area of great alarm. He stated that the contract was terminated in July. He said that there was no oversight of the transportation program. That all transportation employees were put through training and health screenings and a few employees were eliminated through that process. Now the district is down to a core group of employees that are fully compliant with standards.

Representative Crump asked staff to provide the general standards for a school bus.

Mike Quinlan, Manager, Division of School Audits, Auditor General's Office, explained the findings and recommendations of the Avondale Elementary School District audit as shown in the PowerPoint presentation Attachment N.

Dr. Catherine Stafford, Superintendent, Avondale Elementary School District, explained that they had a wonderful audit. She stated that half of the recommendations from the Auditor General's office have been implemented and the other half are being implemented currently.

Ross Ehrick, Manager, Division of School Audits, Auditor General's Office, explained the findings and recommendations of the Deer Valley Unified School District audit as shown in the PowerPoint presentation Attachment N.

Representative Crump questioned monies the Auditor said were supplanted, but the District said they were not.

Mr. Ehrick stated that the records are incomplete so a definitive answer is unavailable. He said the Auditor General's office has talked to the district about putting money back into the 301 fund.

Jim Migliorino, Executive Director of Fiscal Services, Deer Valley Unified School District, explained that four of the 12 recommendations from the audit have been implemented, seven are in the process of being implemented and the district disagrees with the Auditor General's recommendation about the supplanted money.

Representative Tobin questioned the issue of supplanting money.

Mr. Migliorino stated that part of the problem is the ability to account for the funds. He said that they added teachers from the class reduction funds.

Mr. Ehrick stated that the district budgeted for eight additional staff, but they added 22 staff.

Mr. Migliorino stated that the district grew enough throughout the year so additional teachers were needed.

Senator Gray questioned the satellite transportation facility.

Mr. Migliorino stated that the issue is being studied and savings calculated.

Mike Quinlan, Manager, Division of School Audits, Auditor General's Office, explained the findings, recommendations and follow-up of the Litchfield Elementary School District audit as shown in the PowerPoint presentation Attachment N.

Senator Gray questioned the administrator who received \$50,000 bonus money.

Mr. Quinlan stated that the district has now worked the bonuses into contracts and have set up goals to earn the bonuses.

Dr. Julianne Lein, Superintendent, Litchfield Elementary School District, stated that the district concurs with the audit findings and has implemented all of the recommendations.

There being no further business, the meeting was adjourned at 1:52 p.m.

Respectfully submitted,

Shelley Ponce

Shelley Ponce
Committee Secretary

(Tapes and attachments on file in the Secretary of the Senate's Office/Resource Center, Room 115.)

SENATE K-12 EDUCATION COMMITTEE AND HOUSE K-12 EDUCATION COMMITTEE COMMITTEE OF REFERENCE

ARIZONA STATE LEGISLATURE
FORTY-EIGHTH LEGISLATURE – ROLL CALL VOTE

Recommendation: Substitute motion: The Senate K-12 Education and the House K-12 Education Committee of Reference recommend that the School Facilities Board be continued for two years until June 30, 2010

MEMBER	AYE	NO	NOT VOTING	OTHER
Senator Ron Gould	X			
Senator Linda Gray		X		
Senator Leah Landrum Taylor			X	
Senator Victor Soltero		X		
Representative Doug Clark	X			
Representative Sam Crump	X			
Representative David Lujan		X		
Representative Jackie Thrasher		X		
Representative Andrew Tobin, Co-Chair	X			
Senator Karen Johnson, Co-Chair	X			

Committee Secretary Shelley Ponce Date 9/26/07
Attachment 1

**AUDITOR GENERAL
PRESENTATION
HANDOUT**

School Facilities Board

Performance Audit

August 2007

Shan Hays
September 26, 2007



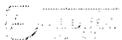
Overview

- Background
- 5 Findings
 - New school construction impacts on General Fund
 - Building renewal formula
 - Improvements:
 - building renewal oversight
 - controls over payments
 - database controls



Background

- Students FIRST Act established Board
- Board duties:
 - Set minimum adequacy guidelines for school facilities
 - Guidelines cover 9 statutory areas
 - Administer 4 funds



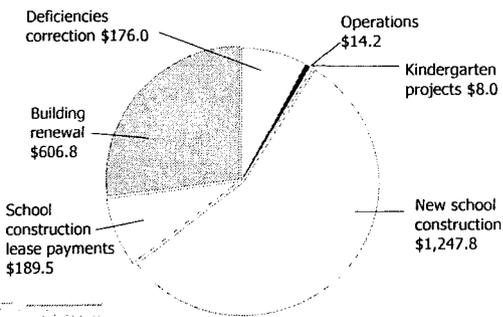
Board duties: four funds

- Deficiency Corrections
- New School Facilities
- Building Renewal
- Emergency Deficiencies Correction



General Fund appropriations

Fiscal years 1999-2007 (millions)



Other revenues FY99-06

- Bond revenues \$1.1 billion
 - Used for deficiencies correction
 - No new bonds issued since 2001
- Lease-to-own agreements \$900 million
 - Used for new school construction



Finding 1

Future new school construction costs will place increasing demands on General Fund



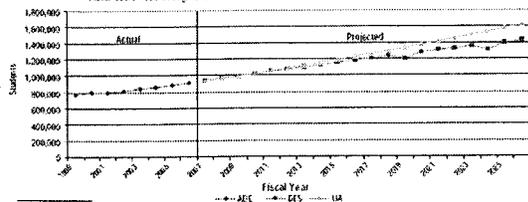
General Fund pays for new schools

- Current funding mechanism relies on appropriations
- Prior years' fund balances nearly gone
- Lease-to-own stopped



Projected enrollment growth

Figure 3. Actual and Projected Student Growth
Fiscal Years 1999 through 2026



Projected construction costs

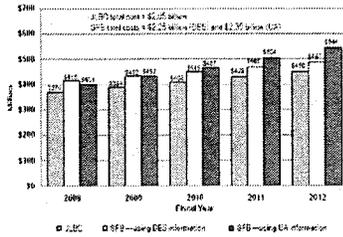
Total 2008 to 2012:

JLBC
\$2.05 billion

SFB (DES pop)
\$2.25 billion

SFB (UA pop)
\$2.35 billion

Figure 4: Comparison of JLBC and SFB Projected Costs for New School Construction Fiscal Years 2009 through 2012



Interpretations affect amounts

- ARS §15-2041 has formula
 - Projected enrollment
 - Square feet per student by grade level
 - Cost per square foot
 - Annual adjustment for market conditions



Interpretations affect amounts

- Additional awards available if needed
- Board interpretations guide staff:
 - Ex: limit number of buildings to lower costs
 - Ex: design elements
 - Adds \$7 per square foot
 - 2006 total \$131 to \$160 per square foot



Recommendation

SFB should seek a formal Attorney General opinion and comply with the opinion once it is received.



Finding 2

Building renewal formula may need modification



Building renewal funding

- ARS §15-2031 contains funding formula
 - square feet
 - building age
 - new construction costs



Actual funding has varied

1999	Funding based on Students FIRST
2000	10% increase
2001	Full formula funding
2002 and 2003	Partial formula funding
2004	No funding
2005, 2006, 2007	Full funding of a revised, lower formula

Actual total:
\$606.8 million

Formula total:
\$1.14 billion



Change attempts vetoed

- Bills in 2003-2006 vetoed
- Litigation prompted vetoes
- State was awaiting final court order
 - 8/31/07 update: court has placed on inactive calendar until 3/3/08



Task Force considering changes

- Legislative Task Force
- Possible changes:
 - Building life limit
 - Portable buildings treatment
 - Replacement value calculation
 - Square feet



Recommendation

- The Legislature should consider modifying the school district building renewal funding formula to make funding more predictable.



Finding 3

SFB should improve oversight of districts' use of building renewal monies



Building renewal monies restricted

Allowed purposes

- Building renovations and major repairs
- Upgrades to maintain or extend a building's useful life
- Infrastructure costs
- Portable or modular building placement or relocation



Staff provide some oversight

- Districts submit 2 reports
- District plans reviewed
- Review of spending has increased



Staff & auditors found problems

- Inappropriate building renewal expenditures
 - Playground structure replacement
 - Public address system
 - Landscaping
- No action on inappropriate expenditures



Recommendations

- Develop process for spending review
- Review spending annually (staff or contract)
- Give districts a chance to challenge
- Report inappropriate expenditures



Findings 4 and 5

**Improve controls over payments
and database**



Controls important

- State's 9th largest appropriation
 - \$426 million paid out in FY 2006
- Purpose of controls:
 - Ensure payments appropriate
 - Account for payments properly
 - Protect data used for tracking projects and managing payments



Controls can be improved

- Some good practices in place
- Payment controls not always applied
- Recommendations:
 - policies and procedures
 - initiate close-out when most of award has been spent



Controls can be improved

- Database lacks documentation, overall control framework
 - Over-reliance on consultant Policies and procedures
- Recommendation:
 - Strengthen database controls
 - Modify database consulting contract



Legislative Questions



Legislative questions

- Surveyed districts regarding school designs
 - 38 responses
 - 15 use prototype designs
 - 16 go beyond required energy efficiency
- Examined accuracy of information
 - Reasonable accuracy and methods
 - Hired demographer to improve projections



Sunset factor recommendation

- Consider eliminating annual audit of bond receipts and debt service
 - Repeal ARS §§15-2092 and 15-2063



Performance Audit School Facilities Board

August 2007

Shan Hays
September 26, 2007



**CHAIRMAN'S LETTER
ON ADDITIONAL
SUNSET FACTORS**

**KAREN JOHNSON
DISTRICT 18**

STATE SENATOR
FORTYEIGHTH LEGISLATURE

1700 WEST WASHINGTON
PHOENIX, ARIZONA 85007-2890

PHONE (602) 926-3160

TOLL FREE 1-800-352-8404

FAX (602) 926-3429

E-MAIL kjohnson@azleg.state.az.us



Arizona State Senate

COMMITTEES:

EDUCATION CHAIRMAN

APPROPRIATIONS

JUDICIARY

NATURAL RESOURCES

July 10, 2006

Mr. Frank Davidson, Chairman
School Facilities Board
1700 West Washington Suite 230
Phoenix, AZ 85007

Dear Mr. Davidson:

The sunset review process prescribed in Title 41, Chapter 27, Arizona Revised Statutes, provides a system for the Legislature to evaluate the need to continue the existence of state agencies. During the sunset review process, an agency is reviewed by a legislative committee of reference. On completion of the sunset review, the committee of reference recommends to continue, revise, consolidate or terminate the agency.

The Joint Legislative Audit Committee (JLAC) has assigned the sunset review of the School Facilities Board to the committee of reference comprised of members of the Senate Education K-12 Committee and the House of Representatives Education Committee. JLAC has directed the Auditor General to conduct a performance audit of the School Facilities Board.

Pursuant to A.R.S. § 41-2954, the committee of reference is required to consider certain sunset factors in deciding whether to recommend continuance, modification or termination of an agency. In addition to the 12 sunset factors that are addressed in the Auditor General performance audit, please provide your agency's response to the required factors as listed below:

1. Identify the problem or the needs that the agency is intended to address.
2. State, to the extent practicable, in quantitative and qualitative terms, the objectives of the agency and its anticipated accomplishments.
3. Identify any other agencies having similar, conflicting or duplicate objectives, and an explanation of the manner in which the agency avoids duplication or conflict with other such agencies.
4. Assess the consequences of eliminating the agency or of consolidating it with another agency.

Mr. Frank Davidson
July 10, 2007

Page 2

In addition to responding to the four factors listed above, please provide the committee of reference with copies of your most recent annual report. Your response should be received by September 1, 2007, so we may proceed with the sunset review and schedule the required public hearing. Please submit the requested information to:

Dawn Nazary
Arizona State Senate
1700 West Washington
Phoenix, AZ 85007

Thank you for your time and cooperation. If you have any questions, please feel free to contact me at 602-926-3160 or Dawn Nazary at 602-926-3171.

Best regards,



Senator Karen S. Johnson

KSJ/kw
Attachment

cc: Representative Andy Tobin
John Arnold, Executive Director, School Facilities Board
Mr. Brian Lockery, House of Representatives Majority Research Analyst
Mr. Javan Mesnard, Senate Majority Policy Advisor
Ms. Nikki Amberg, Senate Minority Policy Advisor
Ms. Karla Phillips, House of Representatives Majority Policy Advisor
Mr. Chris Kotterman, House of Representatives Minority Policy Advisor

**SFB RESPONSE
(ADDITIONAL
SUNSET
FACTORS)**

ARIZONA STATE SENATE
RESEARCH STAFF



DAWN NAZARY
LEGISLATIVE RESEARCH ANALYST
SENATE EDUCATION K-12 COMMITTEE
Telephone: (602) 926-3171
Facsimile: (602) 926-3833

TO: MEMBERS OF THE SENATE EDUCATION
K-12 AND HOUSE EDUCATION (K-12)
COMMITTEE OF REFERENCE

DATE: August 28, 2007

SUBJECT: School Facilities Board Response to Statutory Sunset Review Questions

Attached is the School Facilities Board response to the four statutory questions required as part of the Committee of Reference review. The School Facilities Board will be in attendance at the September 26, 2007 Committee of Reference meeting to answer any questions related to the sunset audit conducted by the Auditor General and the attached response.

Please feel free to contact me if you need any further assistance.

cc: Brian Lockery



STATE OF ARIZONA
SCHOOL FACILITIES BOARD

Governor of Arizona
Janet Napolitano

Executive Director
John Arnold

August 13, 2007

Dawn Nazary
Arizona State Senate
1700 West Washington
Phoenix, AZ 85007

Dear Ms. Nazary,

We look forward to working with you and the committee of reference during the sunset review process. In addition to the 12 sunset factors that are addressed in the Auditor General's performance audit, please accept our response to the additional four questions delineated in Senator Johnson's July 10, 2006 letter addressed to our Board chairman Mr. Frank Davidson.

1. Identify the problem or the needs that the agency is intended to address.

In July 1994, the Arizona State Supreme Court held in *Roosevelt v. Bishop* that the state's statutory scheme for financing public education violated the Arizona Constitution. Article XI, section 1 of the Arizona Constitution requires that the legislature enact laws that provide for the establishment and maintenance of a general and uniform public education.

On July 9, 1998 the four-year struggle to create a new capital finance system ended when the legislature passed and Governor Hull approved SB 1101 (Laws 1998, 5th Special Session, Ch. 1) commonly known as Students FIRST. Students FIRST responds directly to guidance provided by the Supreme Court which recognized that the state's constitutional obligation is limited to funding a public school system to a prescribed level of adequacy. "The concepts of statewide equalization and local option to go above and beyond the standards are irreconcilable unless the legislature establishes standards for adequate capital facilities." Students FIRST responds to the constitutional requirement by setting adequacy standards for school buildings and by creating the School Facilities Board.

Once adequacy standards were established, the legislature had to ensure that districts have sufficient funding to meet the standards. The financing system had to provide funds to 1) bring existing facilities up to an adequate standard; 2) construct new and adequate facilities for growing districts; 3) and maintain all capital facilities at the adequacy level. To accomplish this, Students FIRST established a Deficiencies Correction Fund, New School Facilities Fund, and Building Renewal Fund.

2. State to the extent practicable, in quantitative and qualitative terms, the objectives of the agency and its anticipated accomplishments.

In 1998, the School Facilities Board was given the responsibility of implementing the Students FIRST law. This was viewed by some as a near impossible task, as the program incorporated deficiencies correction, preventive/major maintenance and new school construction, for all public schools in the state of Arizona. Students FIRST has not been without shortcomings, as it is a program that has never been done elsewhere. In a way, the School Facilities Board built the first airplane while flying it, as the SFB had to create the model while implementing the program. Given that challenge, there is a lot of which to be proud.

Deficiency Corrections

In the deficiencies correction project, the SFB first established the minimum school facility guidelines, and then assessed all 1,300 of the state's public schools (over 8,000 buildings) to identify building systems and equipment that were deficient.

By June 30, 2006, there were 9,002 deficiency projects corrected throughout the state at a cost of \$1.3 billion. The majority of these involved roofing, HVAC, electrical, fire alarms, and replacement space. All of the projects have made significant strides in improving our state's school facilities. The program has had an especially great impact on the rural districts and the low wealth urban districts that were unable to afford the costs associated with school repair on their own. In addition, the deficiency program timing was ideal from a cost standpoint, as deficiency corrections work employed thousands of our state citizens during a time when Arizona was in an economic downturn. Competition and pricing also benefited significantly from the downturn, allowing the state to receive maximum value for the dollars spent.

New School Facilities

As of June 7, 2007 the School Facilities Board has awarded 328 new school projects with a total value of approximately \$2.78 billion. Of the 328 projects, 235 have been completed, 29 are under construction, and 64 are board approved with some in design.

As of FY 2007, the School Facilities Board has purchased 2,006 acres of land valued at \$155.2 million and has received 1,765 acres in donations and paid a 20% donation factor of \$38.1 million but the appraised value of the donated land was approximately \$190.4 million, saving the state \$152.3 million in land acquisition costs.

Without Students' FIRST, Arizona would not have been able to produce the educational infrastructure mandated by the growing population. The varying levels of property wealth and district bonding limitations of the old system set artificial limits on the amount of infrastructure that system could provide.

Building Renewal

The School Facilities Board distributes building renewal based on the district's successful completion of building renewal plans and prior year expenditures reports. The building renewal appropriated supports 110.6 million square feet, 10,336 buildings, and 1,425 schools that have a replacement value of \$11.8 billion. Each year the state adds about 3 million square feet to the school inventory. There is no dedicated funding for preventative maintenance but districts are allowed to spend up to 8% of their building renewal dollars on preventative maintenance. Districts maintain preventative maintenance plans and currently complete approximately 40% of recommended preventative maintenance.

Last year the School Facilities Board developed a web-enabled building renewal planning application that was upgraded this year to include prior year building renewal expenditures and renovations reporting. The automation will allow the School Facilities Board to provide better management data to decision makers about the type of building renewal projects (e.g. HVAC or plumbing), identify how districts are managing their plans by comparing prior year plans with expenditures, identify the amount of funds sitting in district ending balances that are being saved for future projects, etc.

3. Identify any other agencies having similar, conflicting or duplicative objectives, and an explanation of the manner in which the agency avoids duplication or conflict with other such agencies.

There are no other agencies that have conflicting or duplicative objectives but the Department of Administration (ADOA) General Services Division has some similar processes.

Building and Planning Services

Building inspections - provide inspections of all buildings in the ADOA building system and state-funded projects under construction.

Building renewal - review annual building renewal project requests. Allocate annual appropriation to agencies for specific projects and allocate funds for emergency requests throughout the year.

Capital Improvement - Prepare annual ADOA Building System Capital Improvement Plan, review agency capital requests, and submit recommendations to the Governor's Office of Strategic Planning and Budgeting and the Joint Legislative Budget Committee.

Construction Review—review and approve all state-funded construction documents including contracts, plans, specifications and payment applications.

Construction Services

Provides a full service project management team to coordinate things like the planning, designing, construction and environmental services for public funded projects (e.g.,

Department of Health Services State Laboratory, Southern Arizona Veteran's Memorial Cemetery Administration Building, Arizona State Prison Complex - Lewis).

4. Assess the consequences of eliminating the agency or of consolidating it with another agency.

Given the nature of the Supreme Court decision, the functions of the agency would need to be carried out either by the agency in its current form or be consolidated with another agency to carry out the existing mission. The elimination of the agency or its functions would take the state back to where it was prior to the Supreme Court decision with disparities in school facilities given the vast differences in property wealth across the state and the impacts on local taxpayers.

Please feel free to contact me if you have any questions.

Sincerely,

A handwritten signature in black ink, appearing to read 'John Arnold', with a stylized flourish at the end.

John Arnold
Executive Director