Focus on Education

Privatization Watch

Celebrating 33 Years of Privatization and Government Reform

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Letter from the Editor

Despite decades of increasing government investment in public education in the United States, we continue to lag further and further behind our international peers in what seems to be a steady slide into decrepitude. Yet the successes and innovations coming out of the school reform movement—such as student-based budgeting and charter schools—are playing an increasingly vital role in American education.

The articles within explore the current state of school reform in the United States. The feature article offers a summary of Reason's comprehensive new study on student-based budgeting, *Weighted Student Formula 2009*. The weighted student formula is a policy tool and financing mechanism being used by New York City, Hawaii, Oakland and roughly a dozen other communities nationwide to drive school improvement and create more efficient, transparent and equitable school funding.

This issue also offers an update on the evolving world of school choice, examines the growing interest in non-instructional school services outsourcing, and profiles charter schools' increasing market share. In addition, this issue features an interview with Foundation for Economic Education Chairman Wayne Olson on the U.S. financial system, monetary policy and government regulation.

If there's one silver lining of our current economic recession and widespread government fiscal woes, it's the pressure to do more with less in education. With no money left to blindly throw at the problem, communities are reforming the system itself to better serve the increasingly varied needs of families and students. The data show these reforms are accelerating academic progress, piloting the way for fundamental reform in the way schools do business.

The successes of the school reform movement are playing an increasingly vital role in American education.

Privatization Briefs

Charter Schools Continue to Increase Market Share

President Obama championed charter schools in a major education speech in March 2009, praising their innovation and urging states to lift caps on their growth. Charter schools continue to be the largest example of privatization reforms in public education. These schools operate through a contract with a government authorizer. According to the Center for Education Reform, in the 2008–09 school year, over 4,700 charter schools served more than 1.4 million children across the nation.

The National Alliance for Public Charter Schools reports that in the 2007–08 school year, 12 communities had at least 20 percent of their public school students enrolled in public charter schools, double the number of communities from the 2005–06 school year. Also, 64 communities now have at least 10 percent of public school students in charter schools.

U.S. Military Expanding Housing Privatization Programs

The U.S. military's housing privatization efforts have enjoyed great success over the years, and they continue to expand. In testimony before the Senate Armed Services Committee's Subcommittee on Readiness and Management Support in June 2009, Wayne Arny, Deputy Under Secretary of Defense for Installations and Environment, proclaimed that privatization and other initiatives have dramatically improved military housing over the past decade. "A decade ago, we were maintaining over 300,000 family housing units, two-thirds of which were deemed inadequate by the military departments who owned them," Arny said. "The private sector responded by delivering modern, affordable housing."

The cost savings realized through the military housing privatization program have been significant. The program has allowed the services to leverage housing dollars by 10 to 1, with $2.5 billion in federal funds generating $25 billion in housing development at privatized installations. In addition, contracts require the private-sector partners to cover maintenance and replacement for 50 years, allowing the government to avoid those expenses altogether.

The success of the military housing privatization program prompted the Army to examine other potential areas for privatization, and in June 2009 it announced a new initiative to privatize on-post lodging. Through the Residential Communities Initiative, the Army is moving to privatize on-post lodging for soldiers in a temporary-duty or permanent-change-of-

The private sector responded by delivering modern, affordable housing.

station status who need lodging in Army installations. Beginning August 15, 2009, 10 installations will be participating in the Privatization of Army Lodging program: Fort Rucker, Alabama; Fort Leavenworth, Kansas; Fort Riley, Kansas; Fort Polk, Louisiana; Fort Sill, Oklahoma; Fort Hood, Texas; Fort Sam Houston, Texas; Yuma Proving Ground, Arizona; Fort Myer, Virginia; and Fort Shafter/Tripler Army Medical Center, Hawaii.

According to the privatization plan, Actus Lend Lease will take over responsibility for correcting commercial building code noncompliance issues and renovating the mechanical, electrical and plumbing systems in the 3,200 rooms at the 10 installations. Lodging operations will be handled by InterContinental Hotels Group (IHG). The Actus/IHG team will convert five hotels comprising 933 rooms to Holiday Inn Express facilities over the next two years at no cost to the Army. Enhanced guest services and facilities at the converted hotels will include complimentary breakfasts, free high-speed Internet access, fitness and business centers, courtesy shuttle vehicles, free guest laundry service, pet-friendly rooms and 24-hour honor-system convenience stores. Moreover, more than 80 percent of the current 600-plus Army lodging employees who have applied for positions with IHG will receive offers of employment.

Arizona Plans to Monetize Assets to Close Budget Gap

Arizona Gov. Jan Brewer and legislative leaders struck a deal in August to partially close a $3.4 billion budget gap for fiscal year 2010. A key component of the deal is the revival of recently vetoed proposals to monetize state assets to generate up to $735 million in upfront payments to apply to deficit reduction. In all, 32 properties—including the House and Senate buildings, State Hospital, Phoenix and Tucson head-

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Weighted Student Formula Yearbook 2009

By Lisa Snell

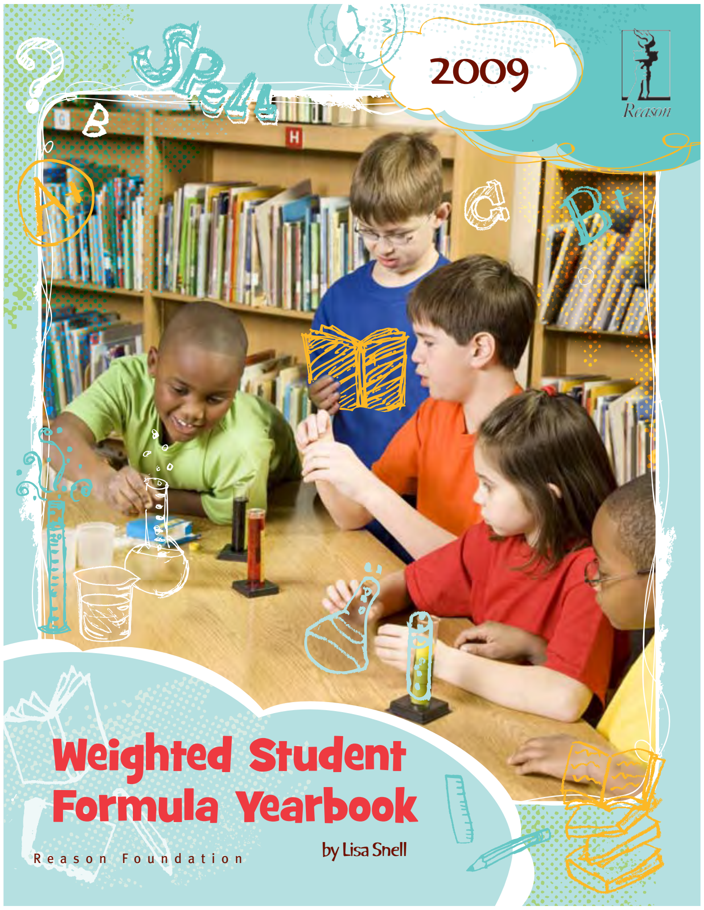
Below is a short synopsis of Reason Foundation's detailed publication, *Weighted Student Formula Yearbook 2009*.

In the United States, weighted student formula initiatives exist in at least 14 school districts and Hawaii. The weighted student formula is a policy tool and financing mechanism that can be implemented within existing district education budgets to create more efficient, transparent and equitable funding. Weighted student formula is a decentralized, student-driven rather than program-driven budgeting process. It goes by several names, including "results-based budgeting," "student-based budgeting," "backpacking," and "fair student funding." In every case the meaning is the same: dollars rather than staffing positions follow students into schools. In many cases, these resources are weighted based on the individual needs of the student, with more funding allocated to students with more expensive educational needs.

Weighted student funding proposes a system of school funding based on five key principles:

1. Funding should follow the child, on a per-student basis, to the public school he or she attends.
2. Per-student funding should vary according to the child's need and other relevant circumstances.
3. Funding should arrive at the school as real dollars—not as teaching positions, ratios or staffing norms—that can be spent flexibly, with accountability systems focused more on results and less on inputs, programs or activities.
4. Principles for allocating money to schools should apply to all levels of funding, including federal, state and local dollars.
5. Funding systems should be as simple as possible and made transparent to administrators, teachers, parents and citizens.

But weighted student funding is only one aspect of a full school empowerment program that gives principals the authority they need to improve school performance and gives schools incentives for academic excellence. Today, in most school districts, individual schools are held accountable for results, but principals have negligible autonomy because decisions about budgeting, expenditures, curriculum and hiring are largely made by district, state and other officials outside individual schools. Integral to meaningful accountability, then, is empowering principals to act as leaders of their schools over these matters.



Furthermore, most school districts have a captive customer base, as parents are forced to send their children to schools dictated by where they live. Empowering parents to pick the public schools they believe best meet their children's unique needs would not only better serve families but would give schools great incentive to demonstrate academic success.

Thus the weighted student formula includes public school choice and principal autonomy. Every school in a district becomes a school of choice, and the funding system gives individuals, particularly school administrators, the autonomy to make local decisions. This autonomy is granted based on the contractual obligation that principals will meet state and district standards for student performance. The weighted student formula is a system-wide reform that allows parents the right of exit to the best performing schools and gives every school the incentive and the authority to change practices to attract and retain families from their communities.

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Good and Bad News for School Choice in 2009

By Lisa Snell

In light of the tough economy and tight state budgets across the United States, school choice continues to be an important policy tool to reduce state education budgets and offer parents more high quality options. Numerous fiscal studies have shown consistently that school voucher and school tax credit programs save money both for state budgets and for local public school districts, even after the fixed costs of public schools (costs that do not go away when students leave a school) are taken into account. A 2005 analysis by the Friedman Foundation for Educational Choice found that America's school choice programs have saved a net total of $22 million for state budgets and $422 million for local school districts. More specifically, for fiscal year 2009 alone, the state of Wisconsin saved $37 million as a result of the Milwaukee school choice program. Similarly, Florida's statewide voucher program for low-income students saved taxpayers $38.9 million in the 2007–08 school year, according to a study released by Florida's Office of Program Policy Analysis and Government Accountability.

In the 2008–09 school year, the Alliance for School Choice reports that more than 171,000 children are benefiting from 18 school voucher and tax credit programs in 10 states. Tax-credit school choice programs give individuals and corporations credits against their taxes for donations they make to scholarship organizations that pay the tuition for low-income children to attend private schools. Student enrollment in school choice programs grew 8 percent over the 2007–08 school year, and has grown 89 percent since the 2003–04 school year. In 2009, the five states with the largest school choice programs are Pennsylvania (43,764 students), Florida (41,843 students), Arizona (29,539 students), Wisconsin (19,538 students) and Ohio (16,411 students).

In 2009, Arizona, Florida and Iowa lawmakers passed legislation to increase investments in tax credit programs and expand access and enrollment. In addition, Indiana lawmakers enacted a new tax credit program to offer students scholarships to private schools.

Not all the news has been positive for school choice programs in 2009, however. The 2009 Omnibus Appropriations Act, a $410 billion spending bill signed by President Barack Obama in March 2009, will cancel the D.C. Opportunity

Children of voucher recipients are 19 months ahead of their public school peers in reading.

Scholarship Program unless it is reauthorized by Congress and authorized by the District of Columbia City Council.

The program, created in 2004, currently provides scholarships worth up to $7,500 to more than 1,700 low-income children, serving families with average incomes of $22,300 per year. Since its inception, the program has given scholarships to more than 3,000 students. The program's per-pupil costs are one-third the cost of educating a child in the traditional D.C. public school system.

Language added to the omnibus bill by Sen. Dick Durbin (D–IL) withholds future funding from the program unless it receives the required approvals. The program received $14 million for the 2008–09 academic year. The federal Department of Education sat on a positive performance review of the program while Congress was dismantling it. After the program was canceled, the Department released the third-year evaluation of it, which was completed in November 2008.

That evaluation shows statistically significant academic gains for the entire voucher-receiving population. Children attending private schools with the aid of the scholarships are reading nearly a half grade ahead of their public school peers who did not receive vouchers. Children in the first cohort of voucher recipients are now 19 months ahead of their public school peers in reading.

President Obama has proposed funding the current 1,700 voucher recipients until they graduate from high school. But the program will not be expanded, and the president will not let new students into it. For the program to survive, new legislation will be needed to reauthorize it. That seems politically unlikely to happen, given the voting record of the legislature on the omnibus spending bill that ended the program.

Lisa Snell is Director of Education at Reason Foundation.

Privatization Helps School Districts to Cut Costs, Focus on Education

By Lisa Snell and Leonard Gilroy

States and municipalities are not alone in facing tremendous fiscal pressures these days. School districts nationwide are being forced to cut costs to respond to the challenges of budget shortfalls and declining tax revenues. More and more often, they are turning to privatization of non-instructional school services to help "right-size" district budgets and maintain a focus on the core mission of educating children.

The school board in Roanoke, Virginia voted in 2009 to contract with a Pennsylvania-based bus company to provide transportation services. The board estimates this will save the school district approximately $250,000 annually. In addition, the company will buy the district's fleet of roughly 150 buses and will acquire 15 new buses every year to replace the aging stock over time. The district's current drivers who meet minimum standards will be offered positions with the company.

A *Roanoke Times* article noted that one school board member said, "a private transportation system would make it possible for school officials to focus more on instruction without the distractions of running a bus system."

Several other school districts are moving to privatize services in 2009 as well. In Columbus, Ohio, the district is planning to contract for a portion of its food operations with a private company that is committed to making the food service department more profitable. The schools' food-service department has been losing money at an annual rate of about $3 million, and officials have long discussed privatizing some of the operations. The company, Sodexo, a Maryland-based food management corporation, plans to raise lunch prices, shrink staffing through attrition, and use its national purchasing power to reduce the district's losses. In Leominster, Massachusetts, the School Committee voted on May 19, 2009, to select a private sector food management firm to take over the school lunch program after the program reported a $400,000 loss. And the Board of Education in Troy, Michigan voted unanimously in 2009 to privatize transportation services and contracted with First Student, Inc. The decision will save the district an estimated $2.5 million over the next three years.

Privatization of non-instructional support services—such as transportation, food, and janitorial and maintenance services—is a common management tool that school boards nationwide use to save money on non-instructional services in order to direct more resources into the classroom.

A 2008 survey of Michigan's 552 public school districts by the Mackinac Center for Public Policy found that 42 percent of the districts were contracting out for food, janitorial, and/or busing services. The research also identified one Michigan district which estimates a three-year savings of $14.7 million to $21.5 million from privatizing all three services, creating a savings of $557 to $814 per pupil each year. A 2007 Mackinac survey found that 78 percent of school districts contracting out services reported cost savings from privatization, and nearly 90 percent reported that they were satisfied with their privatization experience. Similarly, a 2008 survey by the Illinois Policy Institute found that 56 percent of school districts in that state contracted for one or more of the aforementioned services, with 43 percent contracting for transportation services (though recent changes in Illinois state law now threaten to reverse the trend toward privatization).

School districts seeking to cut costs and streamline have other options as well. A 2005 study by Reason Foundation and Deloitte Research estimated that U.S. public school districts could save an estimated $9 billion—the equivalent of funding for 900 new schools, or more than 150,000 new teachers—by combining just a quarter of their non-instructional service costs with other school districts. The study also notes that, in many places, at least 40 percent of every dollar spent on education never makes it into the classroom and is instead spent on business operations such as transportation, food services, information technology, building maintenance, administration,

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The Financial Crisis and the Government's Response: Interview with FEE Chairman Wayne Olson

By Anthony Randazzo

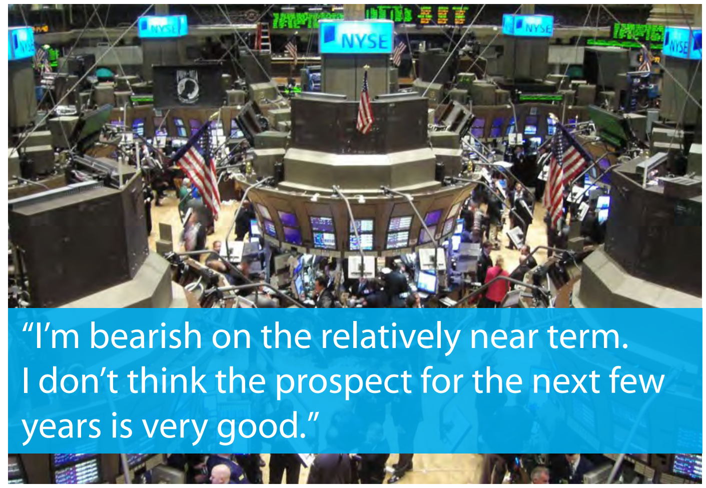
Reason's Anthony Randazzo recently sat down with Wayne Olson, Chairman of the Foundation for Economic Education (FEE), one of the oldest free-market organizations in the United States, to discuss the U.S. financial system, monetary policy, and government regulation. Mr. Olson spent most of his career as a banker focused on fixed-income products with the international financial services institution Credit Suisse. Drawing from his extensive experience, he discussed the financial crisis, Wall Street's culture of risk taking, financial services regulation, the housing market and inflation concerns. The following is an excerpt of that interview. The complete version of the interview is available at http://reason.org/news/show/the-future-of-the-financial-sy-1.

Anthony Randazzo, Reason: Thank you for taking the time to speak to me today, Mr. Olson. With my first question, I'd like to get a perspective on where you're coming from. Our leaders' decisions are profoundly influenced by their perspective of what caused the housing bubble and who is responsible for the financial crisis. What is the framework that you use to approach events in our tumultuous economy?

Wayne Olson: The folks in Washington have defined the causes of the crisis to exclude themselves. But they are the prime motivators for what happened and what's going on. In terms of framework, I've never seen a plainer example of the textbook Austrian business cycle theory than what we've just gone through. Monetary excess causes distortion in investment decisions, and it causes over-investment in long-lived capital goods, as well as excessive consumption because of artificially low interest rates and high liquidity. As a result, the asset prices become grossly inflated and unsustainable.

Randazzo: Is it the nature of Wall Street's drive for gain that drove many people to invest in unwise ways?

Olson: To be fooled by distorted market signals, yes, but I will add that regulatory policies have significantly exacerbated that agency problem and the willingness of institutions to take on risk. When you create this concept that certain things are too big to fail, you increase the optionality of working at a place like that, meaning that upside potential exceeds downside risk.



"I'm bearish on the relatively near term. I don't think the prospect for the next few years is very good."

Randazzo: Do you think it is fair to say that regulators can't keep up with financial product innovation?

Olson: Senator Chuck Schumer from New York once said that if somebody had been properly positioned as a regulator of Bear Stearns, then they would have had all the facts, and they would have been able to see ahead of time, to say "Look, you're taking too much risk here, you've got to scale back," and would've had the authority to make that happen. But let's look at the implications that are involved there.

There's too much information! This is the classic fallacy of central control. The fact of the matter is that the people at Bear Stearns had all of the information, and they couldn't figure it out, right? It's a hellish task to absorb it all and figure out all that information and you're never sure you've got it right. So in Senator Schumer's scenario you've got an omniscient person that's smarter, with a greater ability to absorb information and analyze it than the folks at Bear Stearns. And you have a wise person, a person of discernment, who would've known that the risk was too high. But the guys who do that for the regulatory agencies are no different from the guys working in the credit department at Bear Stearns. The guys who work at the FDIC are the same guys. They went to Wharton, they studied finance, they built models, they worked in banks, they are the same guys. How are these people going to be omniscient? They're going to absorb the information and analyze it better and make wiser decisions? Because they're motivated to carry out the public trust? That wouldn't make them any smarter, and besides, they're motivated to keep their careers going.

Randazzo: The Obama administration's regulatory proposal suggests that it is important to fix the financial services sector's regulation quickly so that the American people will have confidence in the financial structure. Do you believe

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COMMENTARY

Cash-Strapped States Face Challenges, But Also Opportunities

By Leonard C. Gilroy

"Let's not go and get carried away and just look at California as the only state that cannot manage its budget."

– California Gov. Arnold Schwarzenegger to *The New York Times*, July 2, 2009

On July 1, 2009, 46 states began fiscal year 2010, but ongoing fiscal woes and the widespread rollout of economy-dampening tax and fee hikes promise to make this one of the more challenging budget years in some time for cash-strapped states.

According to recent data from the Center for Budget and Policy Priorities, FY 2010 state budget deficits will top $166 billion across 48 states, and cumulative deficits through FY 2011 may top $350 billion. Further, as Stateline.org and *The New York Times* report, FY 2010 is already off to an inauspicious start:

- Legislatures and governors in Arizona, Connecticut, Illinois, Pennsylvania, North Carolina and Ohio failed to agree on FY 2010 budgets as the fiscal year began on July 1. Two months into FY 2010, Pennsylvania policymakers still had not passed a budget, and worse, Arizona's budget was already $1 billion in the red the day it was passed.
- California remains the poster child of fiscal woe. California policymakers approved a budget that included $12 billion in tax increases in February to plug a $42 billion budget deficit, but declining revenues and the failure of revenue-shifting and additional tax measures on a May special election ballot forced legislators to go back to the drawing board to patch a $26.3 billion hole in July. The state issued thousands of IOUs totaling several billion dollars to vendors, contractors, municipalities, financial aid recipients and income tax refund recipients.
- Even in states with approved budgets, budget cuts and tax and fee increases bring heightened economic risk and uncertainty. For example, Nevada will reap an estimated $1 billion in new tax revenues this fiscal year, but will lose by removing those dollars from more productive sectors of the economy that would have had more bang for the buck in terms of growth and job creation. Twenty-five states have already raised taxes this year, according to the Center on Budget and Policy Priorities.

While the state budget budget crisis highlights a systemic failure in fiscal management, it also breeds the opportunity for budget makeovers.

In many ways, while we did see some modest state belt-tightening in FY 2009—and a lot of interest in privatization, streamlining government, and developing fiscally sustainable budget tools and processes—the influx of federal stimulus dollars papered over budget problems in many states and helped policymakers avoid making necessary and politically unpopular reform decisions. According to the Center on Budget and Policy Priorities, stimulus funds have been used to close roughly 40 percent of state budget shortfalls thus far.

Despite routine claims of "decimating vital programs" and "cutting needed spending to the bone" across the states—a predictable rhetorical response on the part of opponents of spending reductions—draconian cuts hardly occurred in most states. Anecdotal evidence suggests that spending cuts rarely exceeded 15 percent for agencies, programs or categorical spending in most places.

But the stimulus gravy train is going to run out, and policymakers will face the inevitability of substantial reductions in the size, scope and price of government in earnest this fiscal year to close well in excess of $150 billion in budget deficits.

That is why, for example, the Arizona House of Representatives' decision in July to let politics destroy a bill that would have created the strongest privatization and government efficiency board in the nation is so disheartening and puzzling. (It obviously wasn't a statement on privatization, as there are several discrete privatization and asset sale/lease proposals embedded in the budget.) Conversely, the looming intensification of the budget crunch also explains why the Louisiana legislature's passage of a bill codifying Gov. Bobby Jindal's Commission on Streamlining Government into statute is such a prescient and sensible action. The commission was created earlier this year to identify ways to privatize government activities, streamline state agencies, and consolidate or eliminate government functions and offices.

These ongoing budget crises serve to highlight a systemic failure in fiscal management by state governments across the country. But at the same time, crisis breeds the opportunity for state budget makeovers. To that end, there are three important steps states should be taking.

First, states need to follow the lead of Washington State, Iowa and others and begin shifting to an outcome-based budgeting system in which policymakers and the public collaboratively rank budget priorities and fund the most important things first. The state government then goes down the list, most important items first, "buying down" with available revenues until they run out of money. This ensures that vital services are being funded before less critical ones, and services not deemed to be of highest importance are reduced or eliminated.

Second, states need to embrace privatization, a proven policy management tool around the world. For example, former Florida Gov. Jeb Bush's administration privatized over 130 services and activities, saving taxpayers in excess of $550 million over eight years. States could even steal a page from Indianapolis, Phoenix, Charlotte and other local governments that have cut costs and improved the quality of services by allowing public employees to bid against private contractors to provide a variety of services, bringing competitive pressures and incentives to bear on the public sector to drive down costs.

Finally, states should inventory and sell underutilized real estate and lease infrastructure assets to private operators, investing the proceeds from these transactions to pay down long-term pension obligations and support long-term budget relief. Chicago has raised over $3 billion this way since 2005, and many other state and local governments are looking to do the same right now.

Solutions like these need to become part of the fiscal solution for states immediately, because most experts predict that state governments will continue to experience fiscal challenges through at least 2011. As far as fiscal year 2010 goes, the only thing standing between a "Year of Fiscal Responsibility" and a "Year of Budget Trauma" is the political will to take the necessary steps to reduce the cost and scope of government.

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BRIEFS

quarters of the Arizona Department of Public Safety, state fairgrounds, and several prisons—are being considered for a sale and leaseback arrangement.

The proposed sale-leasebacks would involve the state repaying financiers through annual lease payments, with ownership of the buildings reverting back to the state at the end of a 20-year lease term. During those 20 years, the state would continue to operate, maintain and use those buildings just as they do today. According to a July 29, 2009 *Arizona Republic* report:

> *The complex financial transaction would allow government services to continue without interruption while giving the state a fast infusion of as much as $735 million, according to Capitol projections. . . . Under the most recent legislative proposal, the state would seek a series of lease arrangements spanning as much as 20 years. Deals that would generate the targeted $735 million in revenue would mean state lease payments totaling $60 million to $70 million a year, according to budget analysts.*

Details of the bidding processes for targeted properties are currently in development.

Los Angeles to Contract Out Operations of Up to 250 Schools

In August 2009 Los Angeles parents successfully convinced the school board to pass a resolution that would allow up to 250 out of 800 district schools to become "schools of choice" run by charter schools and other outside operators. In a 6-1 vote that followed a nearly four-hour debate, board members approved a resolution that will allow outside groups—such as charter school operators, community organizations, as well as in-house talent—to compete to operate 50 new schools set to open in the city over the next four years. The new policy will also invite groups to take on the management task of turning around schools that are chronic underperformers. Under the policy, existing schools become eligible for takeover when they reach their third year in "Program Improvement." A school receives this label after persistently failing a federal standard, called Adequate Yearly Progress, that measures whether a school has the required percentage of proficient students. Based on 2009 test scores there are 252 Los Angeles Unified School District campuses eligible for takeover.

For example, one of the first schools identified for the competitive bidding process because of low academic performance is Garfield High School. The school was made famous by the 1988 film "Stand and Deliver" which chronicles the unlikely success of Jamie Escalante, a teacher who built a rigorous calculus program with disadvantaged students during the 1980s. Garfield has fallen from the "Stand and Deliver" grace. The district chose the initial schools eligible for takeover based on schools that had zero or negative academic improvement in 2009, had high dropout rates (Garfield's is more than 50 percent), and had grade-level proficiency rates lower than 21 percent. Last year, only 5 percent of Garfield students tested as proficient in any math class. Garfield's Academic Performance Index score (which is based on student test scores) fell from 597 in 2008 to 594 in 2009.The state's benchmark is 800. At Garfield High the district will now have the chance to "remake" the high school and choose an education provider with a better academic record. In Los Angeles families will have more access to higher-quality schools than when the district was the monopoly provider of education services.

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OLSON

that consumer confidence is an important aspect of recovery?

Olson: There are several elements of confidence. The most important element of confidence in recovery is the confidence of entrepreneurs and providers of capital. Confidence can't be manufactured. The confidence born of rational, prudent decision-making is the kind of confidence we need. The notion that reshuffling the regulatory framework is going to restore confidence in the financial services sector and is going to make me buy stock in Citigroup is ludicrous. The regulatory framework around financial institutions has grown up over almost one hundred years. There were a lot of smart people that put in years and years of thought and analysis into a certain design. The notion that re-jiggering the thing in the space of three months is going to restore confidence is insane. What it will do, what the behavior of these regulators has done, is impair confidence in the rule of law. And how about confidence in the dollar? That would be a good thing. I don't hear anybody talking about that.

Randazzo: Let's talk about that, confidence in the dollar. There is a lot of debate within the Federal Reserve about how to handle inflation concerns. What do you think the Fed's best reaction is in this case?

Olson: There's not a whole lot the Fed can credibly do or say, because I don't see how the deficit is going to get funded other than by monetizing it. They're saying the right things now about not monetizing the deficit. Yet, the quantity of new debt that needs to be issued by the treasury to finance its operations over the next few years is astronomical. And who's going to buy all of these treasury bonds? To the extent that foreign nations don't, the bonds are going to absorb more of the savings in the United States, and interest rates will naturally rise, because corporations will have to compete with the government for credit. Or the Fed's going to step in and monetize the deficit, and you're going to have a massive increase in money supply.

Randazzo: What kind of problems, moral hazard or otherwise, does the quasi-nationalization of General Motors create?

Olson: There's a bunch of problems with it. Moral hazard is just one of them. The assets that are owned by General Motors, if the natural course of events had gone forward in accordance with the way the law used to be, would have gone into reorganization under Chapter 11 in the federal courts without government money or interference. And these assets would have been sold and redeployed, put in the hands of somebody that could have used them more productively. A bunch of the folks that are on the payroll at GM would have been taken off the payroll at General Motors and redeployed to more productive use. There would be a labor pool available for other employers at reduced labor costs. We're obviously not trying to let prices find their proper level, we're trying to continue to inflate the price of labor and the price of physical assets. You've got to find the right use for that labor and the right use for those capital goods. The bailout of General Motors is doing exactly the opposite.

Randazzo: So with all the turmoil in the economy, but couched in a perspective that we are better off than sixty years ago, are you optimistic or pessimistic about the future of America and the future of the American economy?

Olson: I'm bearish on the relatively near term. I don't know if I'm bearish on equities, but I do believe that there will be inflation commensurate with the seventies. Stagflation had the unemployment rate and inflation rate approaching double digits for a number of years. Bond yields went crazy. People made more money in commodities and real estate than they did in productive assets. Equities sort of drifted most years. They didn't really keep up with inflation, but to the extent that equities are based in hard assets, the inflation we will have soon can inflate the price of equities to some extent as well. In terms of productivity of the economy and value of the dollar and leadership of the world and that sort of thing, I don't think the prospect for the next few years is very good.

Wayne Olson is Chairman of the Foundation for Economic Education. Anthony Randazzo is a policy analyst at Reason Foundation.

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PRIVATIZATION

and other bureaucratic support functions.

The good news for school districts is that these services are widely provided in the private sector—usually at lower cost—with less risk. For instance, Roanoke's school board stands to realize significant long-term operational savings by ridding itself of service-delivery and maintenance obligations of its buses. The district will no longer be responsible for the costs of owning and maintaining those 150 vehicles, taking a major risk off its hands. In fact, policymakers routinely cite this sort of risk transfer as a key benefit of privatization; contracting out offers a powerful method of shifting important long-term capital and operations/maintenance risks to the private sector. And when the contract is up for renewal in five years, the Roanoke board can rebid it to ensure it gets the most cost-effective service provider.

As with any privatization initiative, the key will be developing a strong, performance-based contract that holds the company accountable for meeting enforceable standards that policymakers set. The school board will need to establish a process for monitoring the contractor's performance and ensuring that it delivers.

With a bleak fiscal forecast on the horizon for state and local governments, school districts across the country will need to make strategic management decisions along the lines of Roanoke's if they are going to provide quality education for less money. Budgets may rise and fall, but districts' core missions—preparing students to compete in an increasingly competitive global economy—remain the same. As Roanoke and other districts demonstrate, privatization is one tool school administrators can use to free up dollars from bureaucratic overhead and drive them into the classroom where they belong.

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STUDENT

Under the weighted student formula model, schools are allocated funds based on the number of students that enroll at each school, with extra money for students who need services such as special education, ELL instruction, GATE instruction or help catching up to grade level. Each principal controls how the school's resources are allocated for salaries, materials, staff development and other areas that have traditionally been decided at the district level. Accountability measures ensure that each school meets performance levels. With its emphasis on local control of school funding, most teachers' unions have been reasonably supportive of the weighted student formula model because it devolves autonomy to each school and places responsibility in the hands of each school's principal.

In each district, local context has flavored the innovation in different ways. As with most education policy, school districts vary on the extent to which they have implemented school empowerment, with some attaching funding to individual students and some merely decentralizing authority to the local principals.

1. In 2008, Baltimore City Public Schools began operating under a decentralized weighted student formula plan called "fair student funding." The plan shifted resources and discretion over those resources from the schools' central office to its 202 schools and programs. Under the plan, schools get more resources and have more control over them, so that decisions about students can be made by school leaders rather than at the central office. This shift in resources reconfigured the central office administration into a leaner, more focused entity charged with providing basic administrative support to the schools. In 2008, Baltimore City Public Schools faced a $76.9 million budget shortfall. The fair student funding plan identified $165 million in cuts from the central office to cover the funding shortfall and redistributed approximately $88 million in central office funds to the schools. Schools have dramatic new flexibility over this money. They can redesign their programs according to their students' needs and identify the staffing positions they require within their budget without staffing positions being dictated by the central office. The money follows the students into schools based on the students' individual characteristics. Under this weighted student formula, principals have discretion over at least $5,000 per student as a base funding level, up from about $90 in the 2007–08 school year. Schools also receive $2,200 for each student who is struggling academically and each student qualifying as gifted, plus $900 for every low-income student in high school. On average, schools will receive more than $9,000 per student, with some of that money designated for specific purposes. Unlike most districts that only weight poverty based on the number of children who qualify for the free-lunch program, Baltimore also weights academic achievement.
2. In Los Angeles Unified School District, the innovative partnership called the Belmont Zone of Choice was initiated by teachers and community members. The plan calls for a network of pilot schools with autonomy in five significant areas: staffing, budget, curriculum and assessment, governance, and scheduling. In 2007, the first two pilot schools opened: Civitas School of Leadership and the Los Angeles High School for the Arts. In 2008, three more pilot schools opened: the School of Visual Arts and Humanities, the Academic Leadership Community, and the Los Angeles Teacher Preparation Academy. A total of 10 pilot schools is expected in Los Angeles by 2012. The pilot schools represent a fundamentally different approach to transforming urban public education, providing schools with maximum control over their resources in exchange for increased accountability, all within the economies of scale of an urban school district. Pilot schools are exempt from district policies and mandates. Teachers who work in pilot schools are exempt from teacher union contract work rules, while still receiving union salary, benefits and accrual of seniority within the district. Teachers voluntarily choose to work at pilot schools; when hired, they sign an elect-to-work agreement that stipulates the work conditions in the school for the coming school year. This agreement is revisited and revised annually.

Weighted student formula is a decentralized, student-driven budgeting process.

3. The Boston School District has 21 pilot schools as a result of a partnership launched in 1994 by Mayor Thomas M. Menino, the Boston School Committee, Boston District Superintendent, and the Boston Teachers Union (BTU). The pilot schools were explicitly created to be models of educational innovation and to serve as research and development sites for effective urban public schools. In 2009–10, Boston public schools will open seven new pilot schools, including one run by the BTU. Studies from the Center for Collaborative Education have found Boston pilot schools outperforming district averages on every student-engagement and performance indicator. Boston's pilot elementary, middle and high schools have higher attendance and lower transfer, suspension and dropout rates than the district average. On the Massachusetts Comprehensive Assessment System tests, pilot schools surpass the district averages at every grade level in English and math.
4. In the Chicago Public Schools, Renaissance 2010 (Ren2010) is an initiative to launch 100 new schools in the city's most underserved communities by 2010. Ren2010 was unveiled in June 2004 by Mayor Richard M. Daley, then-schools Chief Executive Officer Arne Duncan, and Chicago business and philanthropic leaders. Its goal is to transform Chicago's public education system and provide all families, regardless of their socioeconomic standing, with options for a high-quality public education. Under Ren2010, new public schools have been started by universities, corporations, foundations, philanthropic citizens, private schools and teachers. The approach is the opposite of the traditional one-size-fits-all view of education. Ren2010 schools are independent, giving school leaders the flexibility to respond to students' education needs. In exchange for this autonomy, they are held to a high degree of accountability. By 2010, Chicago will have 107 Renaissance schools (including new schools and pre-existing charter schools) serving 53,679 students at capacity, representing 13 percent of the Chicago public school enrollment. The first cohort of Renaissance schools from 2005, including charter and non-charter schools, showed larger annual gains on the state test than the average gains for other district schools. The Renaissance schools gained 6.5 percent in 2006–07, compared with 2.3 percent gains for the rest of the Chicago public schools.
5. The Cincinnati Public Schools District was a pioneer in the use of a weighted student formula called "student-based budgeting," which took effect there in the 1999–00 school year. Unlike the previous, centrally controlled allocation system, which resulted in wide swings in funding levels from school to school, dollars now follow the student. A key premise of student-based budgeting is that all students with the same level of need receive the same level of funding within school categories, so a school's budget is tied to its enrollment in each student category. Also, schools determine how their allotted money is spent. In Cincinnati, about 60 percent of the school district's operational budget is spent at the school level. Through the student-based budgeting portion of the school-level budget, principals control close to 80 percent of school resources. Cincinnati continues to be one of the leaders among Ohio's urban school districts in performance. The district is tops among these urban systems in the number of state-level report card indicators earned (nine, versus the next highest urban school system, Columbus, with six), and is second only to Akron in its Performance Index Score, which is based on the state's standardized tests for student achievement.
6. In 2007, then-Superintendent Michael Bennet moved the Denver Public Schools to a weighted student formula they call "student-based budgeting." Schools have flexibility in deciding how they want to prioritize their dollars on key staffing decisions about teachers, intervention services, social workers and librarians. In 2008–09, the school system's operating budget was $712 million; $338 million of that went to the student-based budgeting system, $325 million was controlled centrally and used for direct support services to students, and $49 million was the central office budget. Therefore, principals controlled about 47 percent of the district's operating budget. Denver principals also have more discretion over hiring staff than most urban districts in the United States. The teachers do not change jobs based on seniority, and Denver has an open-market teacher-hiring process in which principals can interview multiple candidates and decide which teachers will fit best with their schools. The district has also used school closure as an accountability mechanism. In 2007, the school board approved closing eight schools that were under-enrolled and lower-performing. The board projected that moving students from these schools to higher-performing schools would save $3.5 million annually. That money is being used to improve the education of students who will be affected by the school closures, deliver additional resources to underperforming schools, and make money available for new schools and new programs.

7. In 2008, Hartford, Connecticut implemented an all-choice system of schools and weighted student funding. Students are equitably funded according to their needs, and this money follows the students to their school of choice. In 2006–07, less than one-half of the school system's money was spent in schools and classrooms. In the system's 2009–10 budget, 70 percent of resources have been allocated to schools and classrooms to support instruction. The district achieved this increase with a 20 percent reduction of central office expenses, including the elimination of 40 district-level positions.
8. In 2007, Joel I. Klein, chancellor of New York City's public schools, announced that the schools would receive their highest ever funding for the 2007–08 school year, and that the administration's new weighted student funding program would bring greater equity and transparency to New York City's public school budgets. Beginning with that school year, the principals and their teams at all 1,500 public schools were given broader control over resources, choosing their staffs and creating programming for their students. Under the new system, schools have increased dollars because the new formula allocates funds based on student need. Before 2007, principals controlled just 6 percent of their schools' budgets. In the 2008–09 school year, each principal controlled about 85 percent of his or her budget. Principals also have greater control over staffing because of a historic agreement the New York City Department of Education negotiated with the United Federation of Teachers. In exchange for an immediate 15 percent increase in teacher salaries, the new contract gives principals the power to make final decisions regarding hiring for all vacancies. There is no more "bumping" by senior teachers, and no more involuntary placements of teachers in any school. This means that, for the first time, principals can choose the teams they think are best for their students.
9. The Oakland Unified School District in 2004 adopted weighted student funding called "results-based budgeting," a process based on a per-student formula that accounts for all expenses associated with school operations. Budgets are allocated to and managed by the schools, increasing equity, transparency, accountability, and site-based decision-making in the budgeting process. In most school districts, schools are charged for average teacher salaries rather than actual teacher salaries. This means a more popular school with more experienced teachers is often subsidized by less popular schools with less senior staff members. In Oakland, schools are charged actual salaries rather than the district average. This increases equity because schools that have more junior teachers with lower salaries will have more resources based on the same number of students to invest in extra staff, teacher development, or additional support mechanisms to help their students achieve. Even though Oakland Unified was forced to make significant budget cuts because of declining enrollment and California's budget crisis, the majority of reductions were made at the central office, and the district worked to protect the unrestricted funding that goes to schools, so that more than 87 percent of the unrestricted budget would go to schools in 2009–10. The school district has posted the largest four-year Academic Performance Index (API) gain among large urban school districts in California.

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Annual Privatization Report 2009, August 2009, Edited by Leonard C. Gilroy, reason.org/apr2009

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Upcoming Conferences

The Performance Institute, Auditing and Evaluating Program Performance, October 26-29, 2009, Arlington, VA

National Council for Public-Private Partnerships 2009 Annual Meeting and Awards Banquet, November 18-20, 2009, Sheraton Phoenix Downtown, Phoenix, AZ

American Legislative Exchange Council, 2009 States & Nation Policy Summit, December 2-4, 2009, Grand Hyatt Washington, Washington, D.C.

Reason Weekend 2010, April 15-18, 2010, New Orleans, LA

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