

THE COST OF CHARTER SCHOOLS: LOS ANGELES UNIFIED SCHOOL DISTRICT

A Fiscal Impact Policy Brief

OVERVIEW

MGT of America’s recently released report examines the fiscal impact of independent charter schools on LAUSD. The results show that the unmitigated growth of charter schools currently results in over half a billion dollars in lost revenue and added costs. That figure is expected to only increase in future years.

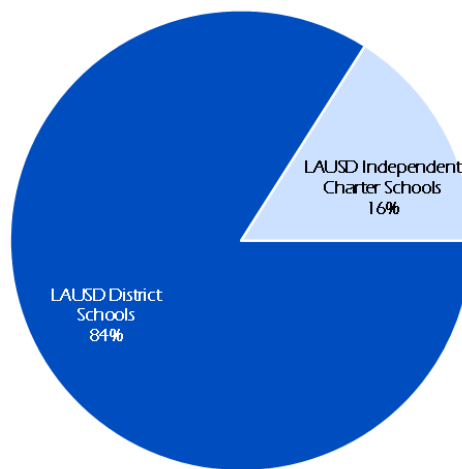
This means there are, and will be, fewer resources available to maintain and improve high-quality community schools in every neighborhood. This will have a particular impact on the highest-needs students, who tend to be served by LAUSD more so than independent charters.

This fiscal crisis exacerbates the pre-existing problem of inadequate funding of California schools, with the state’s per pupil funding consistently hovering in the bottom 25% nationwide. Both issues must be addressed in order for all students to have access to a high-quality education.

Taken together, the findings in the report paint a picture of a system that prioritizes the growth opportunities for charter school operators over the educational opportunities for all students.

Two hundred and twenty-one independent charter schools currently operate within LAUSD’s boundaries. These schools currently enroll about 101,000 students. Meanwhile, more than 540,000 students attend schools run by LAUSD, representing 84 percent of all students. MGT of America’s recently released report *Fiscal Impact of Charter Schools on LAUSD* shows that the fiscal impact of charter schools on LAUSD is unsustainable if left unchecked, and will contribute to the eventual bankruptcy of LAUSD. The unmitigated growth of charter schools will diminish the educational opportunities for the overwhelming majority of students through factors outside of their control.

Figure 1: Enrolled LAUSD Students



As the number of independent charter schools continues to grow, it becomes increasingly important for LAUSD to quantify, forecast, and manage the costs associated with independent charter school expansion.

MGT’s findings point to key changes in policy and practice that can be deployed to create a more financially sustainable system that benefits all students. LAUSD, the State of California, and the Federal Government have a variety of tools at their disposal to expand educational

opportunities for students and to ameliorate the financial impacts that have the potential to destabilize the entire Los Angeles public school landscape.

These tools include but are not limited to: changing fiscal management practices to create an accurate accounting of independent charter school oversight costs; collecting all fees and reimbursements due to the district from co-located charter schools; fully funding all instructional mandates; identifying immediate opportunities at the state level to improve district programs to better serve the needs of Los Angeles’ students; and publically analyzing the educational and economic impacts of each charter school authorization.

This brief takes a selection of the findings from the MGT report and proposes equitable solutions to mitigate some of the impacts of those findings. Although not all of the findings from the report are addressed herein, the findings taken as a whole paint a picture of a system that prioritizes the growth opportunities for charter school operators over the educational opportunities for all students. All discussions of sustainable school finance take place within the larger context of the need to ensure not just fully equitable distribution of existing dollars, but fully adequate funding from both state and federal sources.

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WORKING TOGETHER TO BUILD:

High-quality community schools in every neighborhood. Standards regarding equity, access, and transparency for all publicly-funded schools. A system that provides an excellent education for all students, especially for those students overcoming the structural inequities of racism and poverty. These are the priorities that guide the work of both UTLA and In The Public Interest.

None of these priorities can be achieved within the confines of an unstable public school system. LAUSD oversees over 200 independent charter schools, more than any other school district in the country. Because UTLA represents educators at both LAUSD and charter schools, we know that high-quality schools exist in both environments. We recognize that the best student outcomes occur when educators have a voice to advocate for learning and working conditions.

Buoyed by inequitable state laws and financial loopholes, the number of charter schools appears set to grow rapidly through market share initiatives planned by billionaire investors, including real estate mogul Eli Broad and the Walton heirs of Wal-Mart. In this environment, it becomes even more critical to methodically investigate the fiscal and educational impacts of unmitigated charter growth.

LAUSD lost more than half a billion dollars to charter schools in 2014-15

By far, the most significant financial impact identified in the report is the declining enrollment lost to independent charter schools*. When students leave district schools for charter schools*, the district immediately loses the revenue for that student, but critical educational infrastructure, oversight costs, and a larger portion of higher-needs students stay with the district. The negative impact on LAUSD has serious ramifications for all students in the district, including charter and LAUSD students.

Based on an analysis of LAUSD's 2014-15 Comprehensive Annual Financial Report, MGT has shown that charter expansion has cost the district more than \$508 million in funding. According to MGT, every student who leaves the district for a charter results in a net loss of \$4,957 in state funding. One of the ways this harms the district is through

the variety of fixed costs which the district cannot adjust immediately in response to the enrollment decline. For example, district facilities are built to meet the needs of the enrolled student population. Utility costs for these facilities will not shrink in response to enrollment decline, so the district must continue to bear these fixed costs.

Unmitigated charter school growth limits educational opportunities for the more than 540,000 students who continue to attend schools run by the district, and as this sum grows, it further imperils the financial stability of LAUSD as an institution. This also means that charter schools will be put at risk since these schools rely on subsidies, facilities, and staff support from LAUSD to continue operating.

* Throughout the rest of this brief, "charter schools" will be used exclusively and interchangeably to mean "independent charter schools", as affiliated charter schools are "schools of the district" and are treated as such for budgeting purposes.

Independent charter school oversight costs LAUSD nearly \$15.4 million per year

The Charter Schools Act of 1992 established an unfunded mandate at the state level for each chartering authority to conduct ongoing oversight for all charter schools it has authorized. To cover these costs, the act allows chartering authorities to assess a fee equal to one percent of a charter's revenue, not including private money donated to the charter school. While all independent charters in LAUSD are paying

these fees, they do not come close to covering the full costs of charter oversight cost incurred by LAUSD.

At first glance, many of the costs associated with charter oversight may seem relatively small. However, taken together they are indicative of an unsustainable system that allows independent charter school oversight costs to steadily

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encroach onto the district’s general funds. In addition, MGT’s analysis, while thorough, was subject to scope and time limitations, and thus may not have captured all direct and indirect costs associated with charter oversight.

LAUSD must either redirect money that could otherwise be spent on educational opportunities for district students; or fail to fulfill its oversight obligation, leaving charter school students vulnerable to financial fraud, waste, and abuse.

According to MGT, the district is spending an additional \$15.4 million each year on independent charter school oversight costs that are not covered by oversight fees. This means that LAUSD must either redirect \$15.4 million that could be spent on educational opportunities for district students; or fail to fulfill its oversight obligation,

leaving charter school students vulnerable to financial fraud, waste, and abuse.

\$2.9 million in direct oversight cost overrun in 2015-2016

The oversight shortfall begins with the Charter Schools Division (CSD), which is responsible for monitoring the district’s independent charter schools. While LAUSD expects to collect \$8.8 million in oversight fees, the total expenses for CSD alone are expected to top \$11.7 million in 2015-2016. Compliance with Charter Schools Act oversight mandates will cost the district nearly \$3 million over the statutorily allowable revenue in the 2015-2016 school year alone. This means the district will transfer an additional \$3 million of other monies into charter school oversight, funds that could have been channeled into expanding educational opportunities at district schools. The CSD also occupies space within the district’s Beaudry office, costing the district an estimated \$92,000 per year in utilities and custodial upkeep. This is another annual cost that is not covered by the one percent oversight fee.

\$13.8 million in indirect oversight costs spread across other district divisions

Part of the unfunded mandate to provide oversight to independent charters requires LAUSD to understand each charter school’s unique internal administrative systems and practices. In addition to CSD, other divisions within LAUSD such as the Office of the Inspector General (OIG) and the Special Education Division (SPED), provide services to charter schools that are unaccounted for in CSD’s budget. For example, the OIG recently requested an additional

budget allocation of \$570,228 for additional staff that would be solely dedicated to support charter school oversight.

Charter oversight is not confined to these three divisions. According to MGT, each charter school requires district staff to support these schools by performing work beyond their core duties. This means that these staff, who ostensibly are devoted to district functions, are less able to respond to the needs of schools directly run by the district. For example, MGT estimates show that significant legal and contract compliance staff time is required to review and comment on each charter school application, renewal or “material revision.” Time and opportunity costs compound as the number of charter schools increase. MGT has calculated the value of this staff time at approximately \$13.8 million per year.

\$2 million due to uncollected co-location fees from charters operating rent free in district schools in one year alone

Under Proposition 39, LAUSD is entitled to assess either a 3 percent fee on co-located charter schools that have been granted rent-free space within district schools; or they can charge a one percent fee and collect a minimal amount for the charter’s share of facility expenses. MGT has found that LAUSD has opted to collect a one percent fee from the 56 co-located charter schools, which is the lower of the two amounts. Assessing the higher fee allowed by state law would have generated an additional \$2 million in revenue for LAUSD in the 2015-16 school year.

Although it falls outside the scope of the MGT report, UTLA has found that in addition to undercharging co-located charters for oversight fees, the district has not collected reimbursements to which it is entitled. When a charter school petitions to co-locate, the space allotted to them is based on self-reported predicted enrollment. When this enrollment falls significantly short, resulting in an over-allocation of space, the district has the right to collect a reimbursement for this extra space according to a formula set by the CDE and Proposition 39 regulations.

Data from LAUSD were not obtained in time to arrive at an exact total, but according to interviews with district staff, tens of millions of dollars are likely at stake. This is one of the few financial protections for the district within the Proposition 39 regulations and it is essential that the district take this opportunity to work towards a more sustainable financial relationship with independent charter schools.

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A larger portion of LAUSD students have special needs compared to independent charters. Funding formulas disproportionately penalize district schools for serving this high-needs population.

Providing appropriate support and a comprehensive educational program for special education students is both ethically right and legally required. However, the existing systems of funding this moral and legal mandate financially disadvantage the schools that serve those students requiring the most intensive support.

As shown in Figure 2, special needs students are overrepresented at district schools and underrepresented at independent charter schools, on a per capita basis. This is particularly true for those with the most severe disabilities. This enrollment imbalance, combined with insufficient state and federal funding structures, places additional unfunded financial and instructional responsibilities on the district.

At the federal level, the Individuals with Disabilities Education Act (IDEA) is meant to ensure that students with special needs are provided with a free and appropriate public education that is tailored to their individual needs. State level funding formulas are meant to provide school districts with the funding needed to comply with IDEA. Unfortunately, the federal government has never fully funded the mandated educational requirements of IDEA, and in California the Local Control Funding Formula (LCFF) is applied in such a way as to require school districts to use general funds to ensure every student with special needs receives a comprehensive education.

This population disproportionality, combined with the MGT finding that unmitigated charter growth will contribute to financial problems at LAUSD, means that special education students and their parents have particular cause to be alarmed by the report’s findings as the district is providing the bulk of the services to the students most in need.

LAUSD educating more high-need special education students than independent charter schools

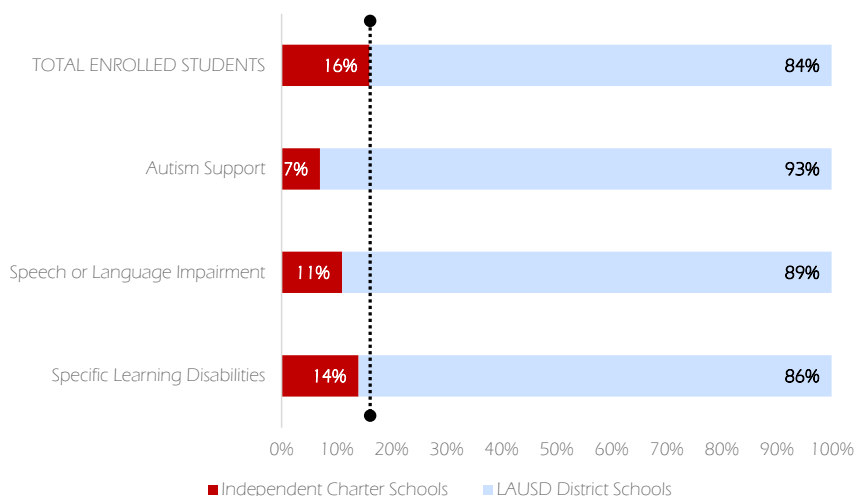
While LAUSD enrollment has declined, the share of special education students has increased from 11.5 percent in 2004-05 to 13.5 percent in 2014-15. In contrast, Special Education students only accounted for 8.1 percent of independent charter students, as of December 2013. More strikingly, of those special education students enrolled at LAUSD schools 30 percent are considered “Moderate to Severe”, double the percentage of the highest-needs special education students attending independent charter schools.

The exact cause of the increase in the share of special education students falls beyond the scope of this brief. However, it must be noted that similar discrepancies between charter schools and district-run schools across the country have led to allegations that some charter schools implicitly limit their student bodies to ensure high scores on standardized tests. A 2013 Reuters special report found, for

example, numerous instances of charter school applications which “[r]equire[d] that applicants document any disabilities or special needs. The U.S. Department of Education considers this practice illegal on the college level but has not addressed the issue for K-12 schools.”

Whatever the reason behind this discrepancy here in Los Angeles, MGT’s analysis shows that overall, charter schools serve a different population of special education (SPED) students. LAUSD has a significantly higher proportion of the highest-need SPED students compared to charter schools. Figure 2 highlights several other categories of students with special needs and compares their enrollment rates to the overall ratio of independent charter school enrollment

Figure 2: Share of Special Needs Students Compared to Share of All Students Enrolled



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to the total number of LAUSD students. Sixteen percent of students within the boundaries of LAUSD attend independent charter schools. However, this ratio does not carry across different categories of high-need SPED students. Just seven percent of students requiring autism support attend independent charter schools.

State laws and funding formulas penalize district schools for serving higher needs students

The State of California does not allocate funding based on the actual need or cost of instruction for SPED students. For example, a student with severe mobility issues would require significant staff support throughout the school day, while a student with a mild speech impediment may require less frequent support. Although the first student’s support services would cost significantly more than the second’s, current funding formulas do not distinguish between the different services each of these students will receive. Therefore, although LAUSD incurs higher SPED student instruction costs relative to its charter schools, it receives the same amount of funding per student ADA regardless of need.

In other words, district schools must stretch fewer dollars to educate greater numbers of high-need special education students because state funding formulas do not account for higher costs associated with educating high-need students,

State funding formulas do not allow LAUSD time to adjust to charter enrollment growth, costing LAUSD an estimated \$55 million per year

State funding to a district or charter school is based on the average daily attendance (ADA) at each district. When a

This practice introduces additional financial pressures and uncertainty at a time when sound, long-term financial planning is of the utmost importance to maintaining support for the programs and services that schools rely on.

student leaves a district, the district loses the state funding that was previously allocated to that student. The State of California provides for a “soft landing” when district enrollment declines. In most cases, district funding is maintained at the prior year’s ADA to allow the district time to adjust its costs to meet the needs of its new enrollment.

In establishing this system, the state has recognized that adjusting costs to reflect enrollment changes is a difficult process and that it can take more than a single year for a district to realize savings due to cost adjustments.

and federal mandates remain unfunded. There are three mechanisms by which the district incurs higher SPED instructional costs than independent charter schools.

First, the District must transfer more dollars from general revenues to supplement the shortfall in funding received specifically for those students, in order to cover the increasingly higher costs of instructing a larger proportion of higher needs special education students.

Second, the district funds 14 full-time SPED staff to support charter schools, but funds those positions largely through district revenue that ostensibly should be used to support in-district SPED services.

Third, because state law allows charter schools to belong to any Special Education Local Plan Area (SELPA) anywhere in the state, the district created a Memorandum of Understanding (MOU) that, in effect, provides a subsidy to the charter schools through a discount to the special education contribution that, in theory, should be contributed to “equitably”. In effect, this SELPA MOU was created as a concession to keep charter schools from going outside the district to a SELPA such as the El Dorado County SELPA, located in Lake Tahoe over 500 miles away, whose fee structure was designed to attract charter schools, undercutting other districts like LAUSD.

However, this “soft landing” approach is not applied uniformly. In other words, if a student leaves LAUSD for the Santa Monica-Malibu Unified School District, the state pays both LAUSD and Santa Monica Unified for the next school year. But when students leave a district for an independent charter school, the state immediately reduces the district’s funding, rather than allowing the district a year to adjust costs to match enrollment figures.

This practice introduces additional financial pressures and uncertainty to the district at a time when sound, long-term financial planning is of the utmost importance to maintaining support for the programs and services that schools rely on. MGT estimates that LAUSD loses more than \$55 million in state funding as a result of this funding practice as independent charter schools have expanded.

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What's next? Common-Sense Solutions at Every Level

The Charter Schools Act of 1992 was signed into law with the intent of enabling charter schools to be more innovative in the way they served students. Although independent charter schools have a separate governance structure and are granted significant exemptions from state laws, the district is still ultimately responsible for protecting the best interests of all students. However, in many ways the district's options are limited, both from the limitations inherent in an Act that focuses primarily on growth opportunities for charter school operators rather than educational opportunities for all students, and from the growing fiscal impacts of unmitigated charter school growth. The financial crisis facing the district, the body that maintains ultimate accountability for students' best interests, should be the defining reason we re-examine the current model of charter school approval, funding, and oversight.

The financial crisis facing the district, the body that maintains ultimate accountability for students' best interests, should be the defining reason we re-examine the current model of charter school approval, funding, and oversight.

UTLA and ITPI have outlined some solutions to the problems identified in the MGT report. There are opportunities at the local, state, and federal level to address the financial and accountability loopholes. These suggestions are not meant to be an exhaustive list of solutions to the problems. In addition, other proposals have been already put forward, such as the Annenberg Charter Accountability Standards, and the Public School Accountability Proposal put forward (but not ultimately implemented by the district) by UTLA in 2014 negotiations with LAUSD. For example, the Annenberg Standards proposed that local decisions to not authorize a charter school should be honored, and not overturned by

another authorizing body. These are just a few examples of other solutions that could also be implemented to address the inequities in our current educational system.

District-led Solutions

All families, whether their children attend district or independent charter schools, want to see their neighborhood schools succeed, because stable neighborhood schools are critical to creating thriving communities and allowing students access to a broad array of educational opportunities. Addressing some of the funding inequities outlined in this brief will be the key to maintaining and growing neighborhood district schools and to providing the oversight and support necessary for independent charter schools. There is a mutual interest, across district and charter stakeholders, for LAUSD to survive and thrive – for the benefit of all students. District-led action is indispensable to this process.

District Action 1: Accurate assessment of current and future oversight costs

If the district wants to create new programs tailor-made to meet the needs of diverse communities, it will be necessary to forecast how much revenue will be available over the next five, 10, or 20 years. Sustainably operating and growing successful school models for district schools, and appropriately fulfilling oversight responsibilities for charter schools, is impossible without understanding all costs associated with independent charter school authorization and oversight. Quantifying and managing these costs is a necessary pre-condition to responsible financial planning. The district should include in the assessment a study of how much staff time outside the charter school division is being used to support independent charter schools, and assign those costs appropriately and transparently to CSD.

District Action 2: Assess all fees and reimbursements owed by independent charter schools for use of rent-free space under Proposition 39

The district must use all tools at its disposal to manage the costs associated with the growth of independent charter schools. This means using the tools outlined by Proposition 39 to recoup the costs associated with charters schools co-located within existing district facilities. According to MGT's estimates, collecting these funds would generate an additional \$2 million each year that could be reinvested into balancing out the stresses placed on co-located district schools. In addition, the district has the opportunity to thoroughly review its policies related to Proposition 39 so that all costs and revenues associated with co-located charters can be responsibly assessed. Within that review, the district must calculate the value of

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the over-allocation reimbursements it has foregone; assess how to retroactively collect those reimbursements, which likely figure in the tens of millions of dollars; and collect those reimbursements going forward.

District Action 3: Continue investing in high-quality district neighborhood schools

Every day, schools throughout the district provide a high-quality, comprehensive education. For example, magnet programs have a waiting list of 44,000 students. LAUSD should ensure the continued growth and replication of these successful programs. The district should also continue to invest in improving educational opportunities at those schools that need additional support.

The fiscal crisis outlined in the MGT report presents a chance for the district to analyze the reasons students and their families are attending independent charters, and to develop outreach and retention strategies. If enrollment declines are to be reversed, then it will be imperative for the district to lift up those schools that are providing Los Angeles students with the well rounded, high-quality education they need to succeed.

State laws and funding formulas must better support the realities of instructional and oversight needs

Adjusting state funding parameters to appropriately fund the instructional needs of every student is another necessary step in creating a stable educational structure for all students. Fixing flawed state laws that limit districts' options across the state will also allow districts to better fulfill their obligation to protect the best interests of students enrolled in both district and charter schools.

State Recommendation 1: Fund Special Education and English Language Learners based on actual costs of instruction

Funding based on actual cost of instruction of SPED students would take into account the fact that district-run schools instruct far more high-need Special Education students than their independent charter counterparts overall.

Funding based on actual cost of instruction of SPED students would take into account the fact that district-run schools instruct far more of the highest-need special education students than their independent charter counterparts overall. Providing the same amount of funding for every special education student ignores the reality that different students require different levels of academic support to access the education they deserve.

The state should also ensure that every independent charter school is prepared to accommodate, instruct, and support all special education students that wish to enroll. The fact that independent charter schools overall do not serve the same profile of special education students as their district-run counterparts is cause for concern and should be thoroughly investigated. That English Language Learner (ELL) funding mirrors the SPED funding loophole that ignores actual cost of instruction creates the same perverse incentive

to underserve the students with the highest needs.

In 2014-15 bargaining, UTLA put forward the proposal that the district require and publish annual reports that identify schools that serve substantially lower percentages of special populations; mandatory reporting of student suspensions, expulsions, and dismissals; and investigations in cases where more than a certain percentage of special population students leave during a single year. These prudent ideas should be implemented statewide to protect all students.

State Recommendation 2: Provide districts with across-the-board "soft landing" protection

The state already recognizes the fact that adjusting costs to reflect enrollment realities takes time. Consequently, the State should treat all departing students the same for funding purposes. District students should not be penalized by state funding formulas that do not allow districts the appropriate time to adjust costs to meet new enrollment figures. The district should

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also create a system to quantify movement from district schools to charter schools so that loss of funding can be anticipated and accounted for in the budgeting process.

State Recommendation 3: Inform the community of the economic and educational impact of each proposed new charter school

As the stakeholders that will be affected by the educational ramifications of changes to the system; and as the taxpayers that fund both district and charter schools, the community should be made aware of the potential positive and negative effects of any proposed new school. Much as environmental impact statements are already required under US environmental law for certain actions that significantly affect “the quality of the human environment”, economic and educational impact statements should be required for actions that significant affect the quality of the educational environment. These economic and educational impact statements should be used to encourage communication, cooperation, and informed decision-making between all the stakeholders affected by educational decisions, including parents, students, teachers, district officials, and charter school operators.

Federal Solutions

Many school districts around the country are also grappling with the educational and economic impacts, both positive and negative, of charter schools. Although state charter laws and regulations vary, we have identified an immediate need to fully fund educational mandates in IDEA.

Another issue facing government agencies and school districts nationwide is the future issue of funding retirement benefits, a problem that is not unique to LAUSD. In Los Angeles, the future issue of retiree benefits is being tackled by the Health Benefits Committee and the district. However, the MGT report identifies a fiscal crisis right in front of us that affects revenue and expenses today. It is fiscally prudent to manage both issues, but we can immediately address the current problem of the half billion dollar fiscal impact from charter schools through common-sense solutions identified in this policy brief.

Federal Recommendation 1: Fully fund educational mandates in IDEA

Pushing for full federal funding of the IDEA is a critical component to providing districts with dedicated, dependable sources of funding that will be used to ensure every student with special needs receives appropriate supportive services to ensure they receive a comprehensive education tailored to their needs. The district should work with state and federal legislators from the Los Angeles area to advocate for full IDEA funding. This change alone would allow the district to redirect over \$700 million of general fund dollars towards increasing educational opportunities across the district.

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Strong leadership at the local and state level is needed so that immediate action is taken to create a sustainable educational system. An equitable system that addresses the financial and accountability loopholes will create the framework for district and charter schools to work together to provide an excellent education for all students.

MGT has calculated the total fiscal impact of unmitigated charter school growth at more than half a billion dollars in decreased revenue and increased costs in the 2014-15 school year alone. If current trends continue, this half billion dollar price tag should be seen as a floor, rather than a ceiling, especially since there are likely unaccounted impacts that fell outside the scope of MGT's report.

A key component of this annual cost is LAUSD's ongoing responsibility to provide oversight and support for every independent charter school in the district. Every time an independent charter school opens, district revenues shrink and mandated costs increase, creating an unsustainable financial structure that places every student in the district, and at existing charter schools, at risk. A system where decreased revenue is accompanied by increased costs, and that punishes schools that serve the highest needs students, is not sustainable.

Fundamentally, this system forces LAUSD to constantly choose: redirect money that could otherwise be spent on educational opportunities for district students; or fail to fulfill its oversight and support obligations, leaving charter school students underserved and vulnerable to financial fraud, waste, and abuse.

Failing to address the substantial costs identified in the MGT report will ultimately lead to financial insolvency and the need for state takeover of the largest school district in California. This would create instability for students at both district-run neighborhood schools and at independent charter schools. It is imperative that decision-makers at all levels of responsibility understand the consequences of inaction and take immediate, pro-active steps to ensure district insolvency does not threaten the educational opportunities of every Los Angeles student.