PROPOSITION 39
IMPACT ON HOMEOWNER PROPERTY TAXES

SEPTEMBER 18, 2000
This report outlines the results of an independent study conducted by Metropolitan West Financial and Strategic Services, LLC to determine the historical impact of the passage of the largest local general obligation school bond initiatives in seven regional California areas on homeowner property tax bills. In addition, the study analyzes the provisions of Proposition 39 on the November 2000 election ballot to determine its approximate impact on the property tax bill for an average California home.

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ABOUT THE AUTHORS

Metropolitan West Financial and Strategic Services (MetWest) Specializes in advising public and private entities on issues related to state and local government budgetary matters, issues relating to capital financing for municipalities, tax policy, regulatory issues, state and local government procurement programs, public-private partnerships, and federal issues relating to state and local governments.

Principals in the firm who contributed to this analysis include:

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Other members of MetWest who contributed to this study:

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The purpose of this study is to determine the historical impact of passage of the largest local general obligation (G.O.) school bond initiatives on the property tax bills of homeowners in California. In addition, this study analyzes the provisions of Proposition 39, the Smaller Classes, Safer Schools and Financial Accountability Act that qualified for the November 2000 general election, to determine its potential impact on a property tax bill for an average California home.

**SUMMARY OF FINDINGS**

- Proposition 39 adds a new category of local general obligation school bonds (local G.O. school bonds) that requires a 55 percent voter approval but imposes limitations and accountability measures not contained in current law;

- Proposition 39 further imposes a strict cap on property tax assessments that can be used to pay for “Prop 39 bonds” approved and sold in a particular election. The effect of this cap is to limit the amount of bonds per initiative that can be authorized and sold.

- Based on our review of the largest local G.O. school bond initiatives passed over the last ten years in small, medium and large school districts, we found the highest approved property tax rate increases for these bonds to range between 0.426 percent and 29.1 percent (See Endnote 11). Over 80 percent of these bonds increased property tax rates by less than 10 percent. Within our sample of the highest approved property tax rate increases, the median was 4.2 percent.

- Using information publicly available from the State Board of Equalization, we calculated the average annual property tax bill for a California homeowner to be approximately $1,692.

- Under the provisions of Proposition 39, the maximum annual property tax increase resulting from a local G.O. school bond election is limited to $60 per $100,000 of assessed value. Based on the average assessed value of a home, a California homeowner could experience a maximum increase in their annual property tax bill of
less than $100 for a G.O. school bond approved in a local election under the provisions of Prop 39. The actual increase on an individual homeowner’s property tax bill will depend on a number of factors including the actual tax rate approved by the county, the assessed value of the home and the size of the bond issue.

- Our analysis further indicates that the portion of the average property tax bill devoted to repayment of local G.O. school bonds approved at an election held under the provisions of Proposition 39 would not exceed approximately 5.6 percent of the annual property tax bill for the average California homeowner.

- We believe the claim that Proposition 39 will result in a “doubling of property taxes” to pay for new school bonds is significantly overstated and historically inaccurate.

FINANCING THE LOCAL SHARE OF SCHOOL CONSTRUCTION COSTS

- A large portion of the local share of construction costs for K-12 school facilities is financed with locally issued general obligation bonds. Under current law, these bonds require two-thirds voter approval and contain a pledge that the county (i.e., the local entity that actually issues bonds for the school district) will impose whatever property tax increases are necessary to pay for the interest and principal on the bonds.

- Once the bonds are approved and sold, the county board of supervisors annually approves the appropriate property tax rate increase for the bonds that is sufficient to pay interest and principal that will come due during the fiscal year.

- Since 1990, over 690 G.O. school bond measures have been placed on local election ballots in approximately 43 percent of the state’s 1,055 school districts. Approximately 53 percent of these ballot measures received the necessary two-thirds voter approval while approximately 47 percent failed to gain the two-thirds vote. Of the approximately 360 approved bond authorizations, we included in our study 61 of the largest bond authorizations approved by voters in seven regional areas around California.

METHODOLOGY USED FOR THIS STUDY

- To gain a statewide perspective on the impact of the largest voter approved school bond initiatives, we grouped the approved bond measures into seven regional areas: Northern California area, Sacramento area, San Francisco Bay area, Central California area, Los Angeles County, San Diego County and Southern California area.
For each of the seven regional areas, we ranked the measures approved by voters from largest to smallest in terms of dollars of bonds authorized. Within that ranking, we selected the five largest bond authorizations for each regional area and reviewed this initial sample to determine whether all, or any portion, of the approved school bonds had actually been sold. For those regions where the bond authorizations had not been fully sold, we expanded our sample to include the five largest bond authorizations for which the bonds had been fully sold.

We then obtained the specific property tax rates used to repay the bonds sold under the bond authorization. To determine the maximum impact to property tax bills, we selected the highest tax rate increase approved in any one year for each bond authorization. The relative property tax increases needed to pay for bonds was determined by comparing the base one-percent property tax rate to the highest tax rate increases from our sample of bond authorizations. For example, if the highest rate approved for a bond was $40 per $100,000 or 0.04 percent of assessed value, the increase would be calculated as 0.04%/1.0% or 4 percent increase. The one-percent base rate was placed in the California Constitution with the passage of Proposition 13 in 1978.

Our focus on the largest regional G.O. school bond initiatives and the highest approved property tax rate increases for these bonds may produce a conservatively high estimate of the impact of these bonds on homeowner property tax bills.

To obtain the maximum permissible increase in a homeowner’s property tax bill as the result of the approval of a local bond initiative under Proposition 39, we calculated the average assessed value for California homes and multiplied that number by the maximum tax rate allowed under Proposition 39 -- $60 per $100,000 of assessed value, or 0.06 percent.

**SAMPLE OF SCHOOL BONDS USED FOR THIS STUDY**

Appendix A contains a complete list of the 61 bond measures included in our study. We considered a bond “fully sold” if 98 percent of the amount of bonds authorized by voters had actually been sold. We excluded from our sample bonds that had been sold but had not yet been assigned a property tax rate by the county.
INVESTMENT IN SCHOOL FACILITIES

With school enrollment at 6 million, California has the largest public school system in the United States. These children attend 8,000 schools around the State in 1,055 school districts. The total investment in these school facilities is over $80 billion. Unfortunately, enrollment growth in many districts outstrips available facilities. In addition, many facilities, in mostly urban districts, are in need of repairs and modernization.

Adequate school facilities are critical to the delivery of a quality education to students. One estimate places the investment needed for school facilities over the next ten years at almost $30 billion. Although a portion of this amount will be paid for by the State, about one-half will be the responsibility of the local school districts. Traditionally, school districts have financed their share with long-term financing such as notes or bonds which are repaid from property tax revenues.

BOND FINANCING FOR SCHOOLS

A large portion of the local share of school construction costs is financed with long-term general obligation bonds. Under current law, each bond authorization ballot measure must be approved by a two-thirds majority vote.

Once the voters approve the bonds, bonds are issued, usually by the county on behalf of the school district, and sold to investors who exclude the interest they earn on the bonds from federal income tax. The entire amount of the bonds authorized may be sold at one time or the bonds may be sold over several years as construction progresses and funds are needed.

Locally issued general obligation bonds for school construction are secured, most often, by a pledge to levy ad valorem (i.e., proportional to value) property taxes in an amount equal to the debt service on the bonds. The county board of supervisors approves a property tax rate each year that, based on the assessed value of property in the tax rate area, appears to be sufficient to pay the interest and principal that will come due on the bonds during the fiscal year. Once bonds are sold it may take several months to approve a tax rate for the bonds. We excluded from our sample several bonds that had been sold but had not yet been assigned a property tax rate by the county.
Other methods are available to finance these costs (e.g., developer fees and Mello-Ross Community Act special taxes), however, none of these alternative methods are impacted by Proposition 39. Since Proposition 39 only applies to local G.O. school bonds, we have focused our study only on that method of financing.

Tax-exempt general obligation (G.O.) bonds represent the most inexpensive way to finance school construction. Because G.O. bonds have a higher credit rating than other types of financing, bondholders accept lower interest rates, bond insurers charge less for bond insurance and investors do not usually require a reserve fund for the bonds. The result is that a larger portion of the bond proceeds can be devoted to building school facilities and a smaller portion is needed for bond issuance costs. In addition, tax-exempt G.O. bonds carry relatively lower interest rates which translates into fewer general fund dollars for debt service.

**PROPERTY TAX BILLS FOR HOMEOWNERS**

Each year homeowners pay a property tax based on the assessed value of their home. With the passage of Proposition 13 in 1978, the basic property tax rate contained in the State Constitution used to calculate the annual property tax bill, is one percent of assessed value. Proposition 13, however, also allows rates higher than one-percent to pay for local bonds approved by two-thirds of the voters.

According to information available from the State Board of Equalization, the average property tax rate in the State is 1.069 percent of assessed value. With the average assessed value of a California home at just over $158,000 and the average rate of 1.069 percent, an average property tax bill for a California homeowner comes to approximately $1,692. (See discussion on Page 7 and Page 9.)

**PROPOSITION 39**

**CALIFORNIA’S INITIATIVE PROCESS**

The California Constitution provides a process by which citizens may place various measures on general election ballots for a vote of the people. An increasing number of these measures, or “voter initiatives,” have been placed on ballots beginning in the late 1970s. Many of these initiatives have had profound financial and programmatic impacts on state and local government.
LOCAL VOTES FOR SCHOOL BONDS

Locally issued G.O. bonds must be approved by a two-thirds majority vote of the local electorate. The election process requires the local school board to adopt a resolution ordering the county superintendent of schools to initiate an election to vote on the authorization of school bonds. If the ballot measure authorizing the bonds is approved, the school board then adopts another resolution requesting the county board of supervisors to issue bonds on behalf of the school district.

The two-thirds super majority vote requirement is a high hurdle for local school bond authorization. Since 1990, over 690 school bond measures have been placed before local voters. Of those measures, approximately 53 percent received the two-thirds voter approval and approximately 47 percent failed to achieve at least a two-thirds vote.

BASIC PROVISIONS OF PROPOSITION 39

Proposition 39, which qualified as an initiative ballot measure for the November 2000 general election, proposes to add a new category of general obligation bond approval for local G.O. school bonds. The new category reduces the supermajority vote requirement to 55 percent from two-thirds. The reduced voter approval threshold for “Prop 39 bonds” comes with new limitations and restrictions. In brief, these limitations and restrictions:

- Allow bond measures to be placed only on ballots for regularly scheduled state and local elections and statewide special elections;
- Require the establishment of citizens’ oversight committees for 55 percent voter approved local G.O. School bonds;
- Limit property tax increases to pay bond debt service to $60 per $100,000 of assessed value for unified school districts;
- Require two annual independent audits to determine the propriety of expenditures.

If a school district is unable or unwilling to comply with these restrictions, the district may still pursue a “traditional” local G.O. school bond, which requires a two-thirds vote, but contains none of the restrictions listed above.
The Study

Purpose of the Study

The purpose of this study is to examine the historical impact of the passage of the largest local G.O. school bond initiatives on the property tax bills of homeowners in the districts where bonds were issued. In addition, in this study we estimate the maximum permissible impact that local school G.O. bonds approved under the provisions of Proposition 39 could have on the property tax bill for the average California home.

Methodology

To conduct our study we examined bond measures placed on local election ballots from January 1, 1990 through July 31, 1999.

This nearly ten-year time period covers a wide-ranging economic cycle, from a severe statewide recession in the early 1990s, through recovery, to strong economic growth. The period also covers a complete cycle of depressed home values, with accompanying rollbacks in assessed values by local property tax assessors, through a recovery in property values. In addition, low inflation throughout the study period provides for reasonable comparison of all bonds issued during the ten-year period. Finally, the ten-year period is a sufficient span of time to encompass changing community and school district leadership and administrations.

We identified over 360 local general obligation bond measures for schools approved by local voters during the time period under study.

To gain a statewide perspective, we grouped the approved bond measures into seven regions:

- Northern California Area (excluding the Sacramento region)
- Sacramento Area
- San Francisco Bay Area
- Central California Area
- Los Angeles County
- San Diego County
- Southern California Area (excluding Los Angeles County and San Diego County)
See Appendix A for a detailed list of counties included in each of the seven regional areas.

For each bond included in our sample, we obtained the property tax rates approved in each fiscal year by the county board of supervisors. To determine the largest impact on property tax bills as a result of the approval of the local school bond, we selected the highest tax rate approved to date for the bonds sold. To gain a perspective on the magnitude of property tax increases adopted to pay for school bonds, we compared these highest tax rates for school bonds to the base one-percent property tax rate limit approved by voters with the passage of Proposition 13 in 1978.

It should be noted that our focus on only the largest school bond initiatives and the highest approved property tax rate increases for school bonds sold may result in a conservatively high estimate of the impact on homeowner property tax bills.

Finally, to determine the maximum impact on the property tax bill for an average California home, we obtained the statewide assessed value for homes from the State Board of Equalization, the state agency charged with overseeing local property tax assessors. From this information, we obtained the average assessed value of a home in California and multiplied that value by the maximum rate allowed under Proposition 39 - $60 per $100,000 of assessed value, or 0.06 percent.

**SCHOOL BOND SAMPLE SELECTED FOR THIS STUDY**

We identified the five largest bond measures -- in terms of dollars of bonds authorized -- adopted by local voters within each of the seven regions. The rationale for selecting the largest bond measures was to obtain a sample that would measure the largest effect on property tax bills.

However, we found that not all the bonds associated with most of the large bond authorizations had been sold. As previously discussed, bonds authorized by voters generally are not sold until several months after the election and many times are sold piecemeal as school construction progresses and funds are needed to pay various contractors. Unless the bonds are fully sold, the total impact of the entire bond authorization cannot be fully measured.

Therefore, to gain a more complete and accurate picture, we expanded our sample to include the largest bond authorizations in the seven regional areas where substantially all of the authorized bonds have been sold. For this sample, we included the five largest bond authorizations in each of the seven regions where at least 98 percent of the bonds authorized had actually been sold. Appendix B contains a complete list of all 61 bond authorizations in our sample.
As discussed above, property tax rates are not assigned by the county until after bonds are actually sold. Therefore, bonds can be sold and outstanding for several months before the first property tax rate is approved by the county. We excluded from our sample, several bonds that were sold but have not yet been assigned a property tax rate by the county.

FINDINGS

IMPACT OF AUTHORIZED AND ISSUED BONDS ON HOMEOWNER PROPERTY TAX BILLS

The highest approved property tax rates for each of the bond authorizations included in our sample gave us a range $4.26 per $100,000 of assessed value to $291.00 per $100,000 of assessed value.

Of the total number of the highest property tax rates in our sample, the median highest rate was $42 per $100,000 of assessed value. We found that only 18 percent of these highest rates fell above $100 per $100,000 of assessed value and, in fact, only one of the highest rates for the 61 bonds in our sample fell above $160 per $100,000 of assessed value.

IMPACT OF PROPOSITION 39 ON A PROPERTY TAX BILL FOR AN AVERAGE CALIFORNIA HOME

In addition to analyzing empirical evidence regarding the impact of local voter-approved school general obligation bond measures on local property tax rates over the past ten years, we also analyzed the likely impact of local general obligation bond measures approved for schools under the provisions of Proposition 39 on property taxes.

To assess the potential increase in property taxes on an “average” California home resulting from an election held pursuant to the provisions of Proposition 39, we calculated the average assessed value of California homes. These calculations are based upon statistical information regarding property taxes, assessed values and the number of homeowner’s exemptions filed that is maintained and published by the California State Board of Equalization (the BOE).
Utilizing information published by the BOE regarding the number of homeowners exemptions filed -- which is a proxy for the total number of owner-occupied residential units in California -- and the assessed value of all properties claiming the homeowner’s exemption for the 1999-2000 tax year, it is possible to derive an average assessed value for owner-occupied homes in California. We performed this calculation using two values for the assessed value of properties receiving the homeowners’ exemption: the gross assessed value, with no adjustment for the value of exemptions; and the assessed value excluding the value of all exemptions.

These calculations yield an average assessed value, for the 1999-2000 tax year, of:

- $165,287, based upon the gross assessed value; and
- $158,305, based upon the assessed value, as adjusted for all exemptions to the gross assessed value, such as the homeowners’ exemption.

The method of calculation is illustrated below:

<table>
<thead>
<tr>
<th>Gross Assessed Value(^{12}) (No Adjustment for Exemptions) ($ in billions)</th>
<th>Number of Homeowners’ Exemptions Filed for 1999-2000 Tax Year(^{13})</th>
<th>Average Assessed Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>$856.948</td>
<td>5,184,593</td>
<td>$165,287</td>
</tr>
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</table>

<table>
<thead>
<tr>
<th>Assessed Value(^{14}) (Excluding All Exemptions) ($ in billions)</th>
<th>Number of Homeowners’ Exemptions Filed for 1999-2000 Tax Year</th>
<th>Average Assessed Value</th>
</tr>
</thead>
<tbody>
<tr>
<td>$820.749</td>
<td>5,184,593</td>
<td>$158,305</td>
</tr>
</tbody>
</table>

Existing provisions of the Education Code, as amended by the recent passage of Assembly Bill 1908 (Lempert) (Chapter 44, Statutes of 2000), which will become effective January 1, 2001, if Proposition 39 is approved, impose strict limitations on:

- The bonds that may be issued as a percent of taxable property within a district. This cap varies depending upon the type of district as follows.
  - school districts -- 1.25 percent of the taxable property within the district\(^{15}\); and
  - unified school districts -- 2.5 percent of the taxable property within the district\(^{16}\); and
- community college districts -- 2.5 percent of the taxable property within the district\textsuperscript{17}.

The tax rate that may be levied to meet the debt service requirement on bonds issued pursuant to a successful school general obligation bond election held under the provisions of Proposition 39. This maximum rate also varies by type of district as follows.

- school districts -- a maximum rate of $30 per $100,000 of taxable property\textsuperscript{18};
- unified districts -- a maximum rate of $60 per $100,000 of taxable property\textsuperscript{19}; and
- community college districts -- a maximum rate of $25 per $100,000 of taxable property\textsuperscript{20}.

Using these maximum tax rates allowed under Proposition 39 and its supporting legislation, we calculated the maximum likely annual impact on the average home in California. To make this calculation, we multiplied the assessed value of an average home by $60 per $100,000 of taxable value, which is the maximum rate permitted under the Education Code with the passage of Proposition 39. This calculation is illustrated below for the average assessed value results based upon both the gross assessed value figures and the assessed value adjusted for exemptions figures.

<table>
<thead>
<tr>
<th>Average Assessed Value</th>
<th>Maximum Rate Per $100,000 of Assessed Value</th>
<th>Likely Annual Impact on Average Home</th>
</tr>
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<tbody>
<tr>
<td>$165,287</td>
<td>X 0.06%</td>
<td>$99.17</td>
</tr>
<tr>
<td>$158,305</td>
<td>X 0.06%</td>
<td>$94.38</td>
</tr>
</tbody>
</table>

Of course, the actual increase to the property tax bill of any particular homeowner’s property tax bill will depend on a number of factors, including the actual tax rate approved by the county, the assessed value of the home and the size of the bond issue.
“PROP 39 SCHOOL BONDS” AND PROPERTY TAX BILLS

According to the latest information available from the State Board of Equalization, the average property tax rate in California is 1.069 percent of assessed value. Using this rate and the average assessed value as calculated above, the total annual property tax bill for the average California home is approximately $1,692 ($158,305 x 1.069%).

As shown above, the maximum permissible impact on the average property tax bill as a result of a successful “Prop 39 school bond initiative” is $94.38. This amount represents approximately 5.6 percent ($94.38/$1,692.00) of the property tax bill for an average home in California for which the homeowner’s exemption has been claimed.

CONCLUSION

Over the next ten years, billions of dollars will be needed to build new schools and repair and modernize older facilities. Without substantial financial means, school districts will, as they have in the past, use tax-exempt general obligation bonds to finance most of their share of these construction costs. Proposition 39 proposes a new category of bonds that contains limitations and accountability requirements, but reduces the required voter approval to 55 percent from two-thirds.

From our study of the largest school bond initiatives approved by voters in school districts around the state and based on our review of the highest property tax rates approved to pay for those bonds, we conclude that property tax bills do not double as the result of the passage of local G.O. school bonds. In fact, only one of the highest property tax rate increases for the 61 bonds in our sample fell above 16 percent, far below the 100 percent increase that would be needed to double a property tax bill.

Finally, our analysis further indicates that the portion of the average property tax bill devoted to repayment of local G.O. school bonds approved at an election held under the provisions of Proposition 39 would not exceed approximately 5.6 percent of the annual property tax bill for the average California homeowner.

2. California Department of Education, Number of Schools by Enrollment Size and by Type, 1999-2000.

3. California’s Coalition for Affordable School Housing, Some Facts About California’s Public School System, www.cashnet.org//.


7. California Constitution, Article XIII A, Section 1 (b).

8. California Education Code, Section 15100 et seq.

9. California’s Coalition for Affordable School Housing.


11. The 1997 G.O. bond for this school district was issued with a waiver which allowed the district to exceed the maximum allowable bonding capacity of 2.5 percent of assessed property in the district. The approved property tax rate peaked at $291 per $100,000 of assessed value in FY1997, then dropped to $198 in FY1998 and $159 in FY1999.


15. California Education Code, Section 15268.

16. California Education Code, Section 15270 (a).

17. California Education Code, Section 15270 (b).

18. California Education Code, Section 15268.

19. California Education Code, Section 15270 (a).

20. California Education Code, Section 15270 (b).