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BEFORE THE SENATE COMMITTEE ON DEFICIT REDUCTION

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Good morning. I am Eden Martin, and I serve as President of The Commercial Club of Chicago and of its Civic Committee. The Commercial Club consists of 500 members from the business, professional, foundation and not-for-profit communities in the greater Chicago area. The Civic Committee includes 90 CEO's or senior officers of the major corporations, banks and professional firms and research universities in the area. The Civic Committee's mission is to help make Chicago a better place to live and work. Our number one priority over the years has been to help improve our educational system, particularly the schools that serve inner-city children in Chicago.

The purpose of these hearings is to consider the State's budget. Today, the focus is on expenditures for education – principally K-12 schools. This year – Fiscal 2009 – the State of Illinois has appropriated some \$7.4 billion in own-source revenues for elementary and secondary education (as well as another \$2.2 billion for higher education).

As you know, on Monday, March 2, 2009, the Civic Committee published an updated report on the state of the State's finances. It showed that: (a) Illinois is now facing a huge gap – over \$8 billion per year – between revenues and costs, in its annual operations; (b) the State's accumulated debts and unfunded obligations now amount to \$116 billion or more, depending on how some of these are calculated; and (c) Illinois is nearing a “tipping point” where the obligations will become so large that it will be virtually impossible to sustain operations in the future without enormous tax increases or service reductions, or both, that could drive businesses and investment out of the State.

It is essential that the State undertake serious reforms to its pensions and retiree health care arrangements, and to make major cuts and put in place programmatic efficiencies – amounting to billions of dollars annually.

K-12 education is a huge area of expenditure. My message today is that our K-12 educational system is very inefficient in Chicago. This is because CPS is a monopoly, and monopolies are inherently less efficient than enterprises in competitive markets – where customers have choices, and where, by exercising those choices, they can put pressure on service

providers to do a better job. (I do not address here any question of relative inefficiency in downstate or suburban schools.)

When monopoly markets are converted to competitive markets, they typically produce goods and/or services that are either higher quality than before, or at lower cost, or both. You can expect that if the CPS monopoly were made competitive – if all or most students in Chicago were given the choice of a charter or contract school – the competition thus created would make *all* schools (both CPS and the new “choice” schools) both higher-quality and lower cost.

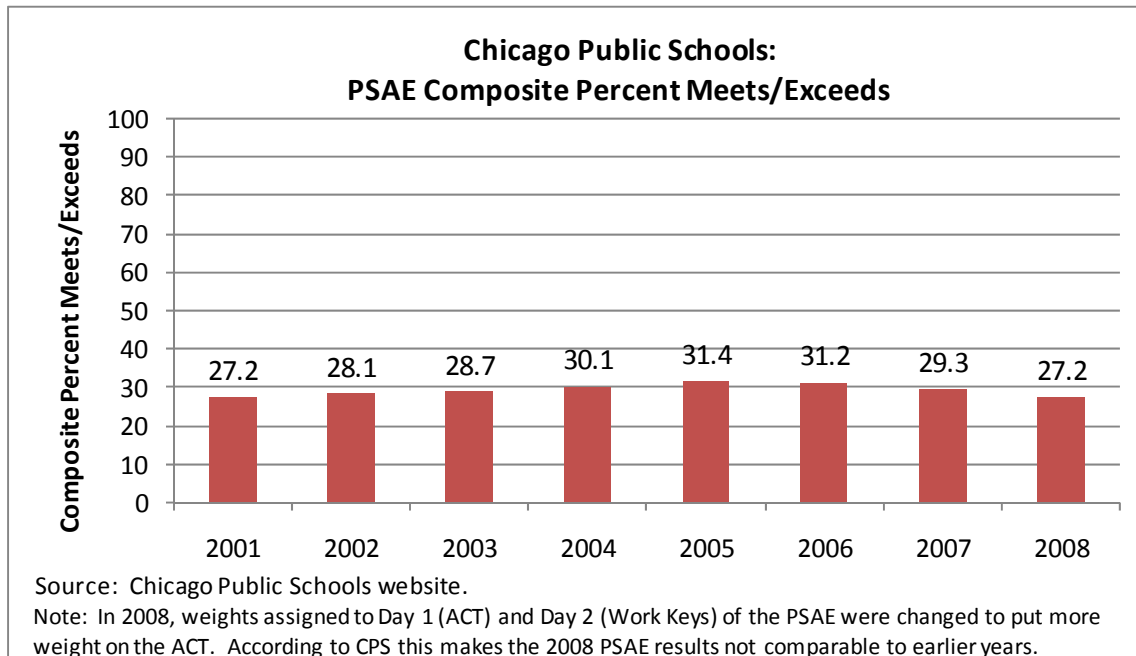
CPS today spends on average a little over \$11,000 per pupil – about the same as DuPage County schools. The problem is not that this is too much. It is rather that the public gets so little for its money. The main reason we have advocated more charter schools is to create competition, which in turn will produce greater pressure and focus for improved quality.

It is worth noting that Chicago’s charter schools operate with per-pupil funding from CPS that is much lower than the moneys available to the “regular” CPS schools. Estimates of how much lower range from \$3,000 to \$4,000 per pupil. The way to cure this inequity, however, is not to bring the other CPS schools down to the level of charter funding, but to bring the charters up to the CPS average.

The 2008 ISAT and PSAE scores are the most recent scores available for Illinois and Chicago – school-by-school. The last such tests students take are those for the 11<sup>th</sup> grade; so they are the best basis for assessing the performance of students throughout their entire K-12 school experience.

High school (11<sup>th</sup> grade) student performance trends as reflected in the 11<sup>th</sup> grade PSAE test results are essentially flat over the past 8 years —showing little or no improvement. (This 11<sup>th</sup> grade test is the last such exam given in the high schools, and by the spring of 11<sup>th</sup> grade, many students have already dropped out of school. A recent study by CPS’s Office of High Schools and High School Programs reported that the 2006 CPS dropout rate was 44%). The PSAE composite in 2001 showed that only 27.2 percent of CPS students in 11<sup>th</sup> grade were “meeting” or “exceeding” State academic standards. These scores rose slightly during the first few years of the new decade, but then fell in 2006, 2007 and 2008 – and now stand at 27.2 percent, the same as 2001.

Thus, over 70 percent of Chicago’s 11<sup>th</sup> graders (no similar tests are given in the 12<sup>th</sup> grade) continue to fail to meet State standards in math, reading and science on a composite basis. The chart below shows the trend of the composite PSAE scores for Chicago from 2001 to 2008.



While these results are disappointing at the aggregate level, they are even more disturbing when one examines the performance of individual high schools. Looking at the overall percentage of Chicago students who meet or exceed standards on the PSAE masks the huge difference in student performance between “selective enrollment” high schools and average neighborhood high schools.

Of the 99 reporting CPS high schools in 2008, only eight “selective enrollment” high schools exceeded the 62.5% benchmark (established under NCLB) for the percentage of students meeting or exceeding State standards in at least one subject in 2008. The remaining 91 Chicago high schools (some of which are also “selective enrollment”) did not reach this benchmark; more than half of these schools have less than 20% of their students meeting State standards on the PSAE, and many have fewer than 10% of their students meeting State standards (see attached Appendix A).

The “meeting” standards test is not rigorous. A better measure of readiness to succeed in college is whether students “exceed” State standards. By that measure, only a tiny fraction of the students in Chicago’s inner-city schools are educationally prepared for college – or for the demands of a job in our modern technological society, or for the demands of citizenship.

Because so few inner-city high school graduates are prepared for college, few earn a bachelor’s degree. A study of the Consortium on Chicago School Research, released in April

2006, reports that of every 100 freshmen entering a Chicago public high school, only about six will earn a bachelor's degree by the time they are in their mid-20s. For African-American and Hispanic male freshmen, only about three out of every 100 will earn a bachelor's degree by the age of 25.

The consequences of the failures of big city school systems such as Chicago's are profound beyond statistics or description, and they fall predominantly on children from poor minority families.

The main reason why the Chicago schools fail (like those in many other big cities) is that the schools are monopolies. Like monopolies in the private sector, their customers do not have choices. Unlike school families in suburban environments which can relocate to communities with better schools, the poorer residents of inner-city Chicago do not have such options. Monopoly providers in both the private and public sectors know that their customers are trapped – that there are no consequences to the service providers if they fail. In such circumstances, the normal incentives that exist in competitive environments to work hard and improve do not exist; and the management techniques and cultures of high expectations that reflect those incentives are non-existent.

I believe that the way to achieve transformational change in Chicago's public schools is not by managing the monopoly better, or feeding it more resources, but by ending it. More choice and competition would surely lead to an incentive structure and "culture" aimed at achieving educational results. Boswell quoted Samuel Johnson to the effect that nothing so concentrates the mind as the prospect of a hanging. Similarly, nothing so focuses the minds of executives, managers and employees in competitive industries as the prospect of losing an important customer. Where customers can be lost – where they can move to a different supplier – the focus of attention is on serving them better. But when customers are trapped, the focus shifts to those who work for the enterprise, and to how that enterprise can be managed in their interests rather than the customers.

The immediate pay-off from more charter schools stems from the fact that such schools operate with greater flexibility and innovation, outside the strictures of the CPS bureaucracy and the restrictive provisions of the labor agreement with the CTU. (Even though they receive lower per pupil funding than regular CPS schools, charters generally perform better on State assessments, a topic we will address later.) But the longer-term and far more powerful pay-off will come from creating competitive markets – which will in turn shift the focus away from serving the interests of the bureaucrats and teachers, and toward educating children.

Competition is a concept of economics and human motivation. It is also a concept of freedom. The economic proposition is well understood. Where many suppliers produce goods or services and sell them in a market where there are many other sellers, buyers can choose.

They will choose based on quality and price. If one supplier produces widgets or legal briefs of poorer quality or greater price, buyers will choose another supplier. Because suppliers know this, they work hard to assure high quality and low price. This focus on results is unrelenting. If a particular producer cannot do as well on either the quality or price front, it will soon go out of business.

The pressures are all in the direction of constant improvement – better quality, greater productivity in production, lower cost and price. Markets which are competitive thus tend to satisfy more human wants than markets which are uncompetitive.

Competition creates pressures on managers and workers to do as well as possible; and there is discomfort and sometimes unpleasantness associated with the pressures. But the societal tradeoff is that the managers and workers who experience the pressure are also consumers, who enjoy the benefit of goods and services that are of higher quality and lower cost than would be the case in the absence of those pressures.

The net effect is that in competitive markets, human enterprises experience a pervasive array of incentives to achieve good results – better widgets and services produced at lower cost. Everyone who has worked in firms operating in competitive markets has experienced these incentives. Although there is more to life than money, economic motivations are important to most people, who therefore strive for promotions and excellent work reviews – and for the resulting economic rewards.

By contrast, in noncompetitive environments, these pressures and incentives either do not exist or exist to a far weaker degree. In monopoly markets, customers and clients do not have the same array of choices. If customers are dissatisfied with the quality of the widgets or the price of services, they have little or no alternative source of supply. In such cases, the suppliers can afford to relax. There is no need to be compulsive about quality or cost, or strategic direction, or the performance of employees. Quality degrades and costs increase. Prices tend to escalate – not only because costs are higher, but also because the monopoly firms have what economists call “market power,” the ability to charge prices in excess of marginal costs.

Urban education in Chicago – the provision of school service from kindergarten through 12<sup>th</sup> grade – is a monopoly. Virtually all Chicago schools that provide free public education from K-12 are run by CPS. To be sure, there are private schools – both church and secular. But these schools charge tuition. There may be scholarships, but it is rare for students to be able to attend these schools at no cost. Only a small fraction – less than 10% -- of school families have access to a charter school or contract school – schools funded publicly but managed by independent operators.

The Catholic schools in Chicago today offer far fewer alternatives than in the past, and the choice is not free. The Archdiocese has closed some 240 schools, and enrollment is now down from 366,000 in 1964 to about 100,000 at the end of 2005. Moreover, tuition in these schools has increased dramatically – up to \$3,000 for elementary schools, and \$6,700 for high schools. Even with these tuition revenues, the Archdiocese must rely on fundraising to cover over 30% of its costs of operating its schools.

For most of the families who live in Chicago's inner-city – those who are poor and minority – the option of sending their children to a private school at no cost is nonexistent; and the possibility of doing so on a tuition-paying basis is usually more theoretical than real.

Wealthy and middle-class families have the ability to move to the suburbs so their children can attend good suburban schools. Large numbers of them have in fact done so. Indeed, the low quality of Chicago's public schools has almost certainly played a part in pushing large chunks of Chicago's middle-income population out of the city and into the suburbs – a phenomenon which has further exacerbated income disparities between the suburbs and the city.

But for those who live in Chicago's inner-city communities, this ability to move to another school district is virtually non-existent. Residents generally lack the financial resources to move to the suburbs. And though they may move from one area of Chicago to another, the schools in all these areas are almost all managed and maintained by the same monopolist – CPS. Those schools receive approximately the same amount of money per student, and operate subject to the same CPS structure of policies and controls. Not insignificantly, they also operate pursuant to the terms of the same 300-plus page union agreement between CPS and the CTU.

For all these reasons, if one were to set out to design a monopoly system in which the customers/clients had few or no options and in which the elasticity of demand is near zero, that system would have the characteristics of the Chicago public school system.

It is therefore not surprising that one finds within CPS a total absence of the network of pressures and incentives that induce workers in competitive firms to perform well and efficiently. The absence of these pressures and incentives helps explain many of the characteristics of CPS' operations.

CPS has a chaotic system, or non-system, of recruiting and hiring new teachers. It does not have in place effective systems for inducting new teachers, or evaluating teachers. There is little or no purpose to evaluations. Most teachers in the probationary period are promoted to tenured positions. Once teachers are tenured, there is no practical way to get rid of them. Moreover, evaluations are irrelevant to compensation because the track-and-lane system built into the union contract deprives management of the ability to make salaries dependent on the quality of teacher performance. There are no bonuses.

CPS' central office does not manage particular schools; and there is little or no incentive on those who do manage the schools – the local principals – to go through the hassles that are involved in proceeding administratively against incompetent teachers.

No human service enterprise of 46,000 workers providing services to 415,000 people would be structured this way if it operated in a competitive environment. Or, to put it another way, in a competitive environment no human services entity structured and operating this way would long survive. The competitive alternatives would quickly deprive the monopoly of its customers and its revenue. And the threat of this loss would induce all service providers in the market to transform the way they do business.

I do not doubt that the teaching profession has its share of saints, and that there are many teachers in Chicago who do what they do primarily because of their enjoyment of the work and the satisfaction they derive from seeing that work reflected in the achievements of their students. Similar satisfactions may be enjoyed by other “professions” as well.

But it simply does not follow that these teachers – or any other category of “professionals” -- should somehow be insulated from competitive pressures and incentives.

It is frequently said that America has the best system of higher education in the world. If that is true, why is it true? Is it because we are inherently better at educating 19 year olds than 17 and 18 year olds? Or is it because there is something structurally different about the environments in which the educational services are provided?

Universities may not all be models of efficiency. But they operate in highly competitive environments – for students, for faculty, for money. The people who run our universities know that most students and their families have choices. The students with the best academic records and prospects for continued success have the best choices. So colleges and universities compete vigorously to attract them. This competition covers most if not all aspects of the services offered, as well as the collateral aspects of college life.

In Chicago's K-12 school system, these economic incentives are completely lacking. It cannot be an accident that the students who attend our excellent colleges and universities have a broad array of choices – and that those who attend schools within the CPS K-12 system do not.

To sum up: the Chicago Public Schools do not deliver efficient educational services to the school families of Chicago. The principal reason lies in the monopoly nature of the enterprise. Ending the monopoly would bring both an improvement in the quality of services and a reduction in the costs of those services.

The Civic Committee welcomes any reasonable reform that will bring cost savings to State and local government. But in the case of CPS, our primary concern is with quality – not

cost. We believe that bringing competitive options to the school families of Chicago would, over time, improve the performance of the schools and the learning of their students. If competition enables the schools to save money, particularly in their non-educational and central office operations, so much the better.

The best way to bring competition and educational choice to Chicago is to lift the cap on charter schools. Charter schools are typically more innovative and operate with greater flexibility. They have greater ability to exercise quality control over their teachers, and to get rid of failing teachers. They can also vary the pay of successful and unsuccessful teachers. They are not bound by the operating rigidities of the existing CTU labor agreement. The number of charter schools for Chicago is now capped by law at 30. We are at that cap. Chicago now has over 10,000 school families and students in lines to get into the existing charter schools. The charter campuses offer choices to only a small fraction of the Chicago school population – perhaps in the range of 7-8%.

The recent record of the charter schools – though far from perfect – is better than that of the traditional public schools in the same neighborhoods. The charter schools often experience “start-up” problems just like traditional schools; but the longer they are in business, in general the better their relative performance.

A chart attached as Appendix B contains the most recent Chicago charter school performance data comparing the meets/exceeds percentages on 2008 State assessments of charter schools and their nearest neighborhood schools.

Fourteen out of nineteen charter elementary/middle schools for which this data is available outperformed the nearest neighborhood school on the 2008 ISAT. On average, charter schools outperformed neighborhood schools by about seven percentage points.

All six of the charter high schools for which this data is available outperformed the nearest neighborhood school on the 2008 PSAT. On average, charter schools outperformed neighborhood schools by about nine percentage points.

Too many data points and statistics tend to cause the mind to shut down. But consider this. In Chicago’s 19 “magnet” and “selective enrollment” high schools, applying the ACT “college readiness” benchmark to 11<sup>th</sup> graders who took the ACT test in the spring of 2008, about 45% of the students were deemed “ready” for college math – meaning they would have a decent chance to get a B or a C in a college freshman-level class. About 30% were “ready” in science. But in Chicago’s other 69 neighborhood high schools – those which serve about three-quarters of the students in Chicago – *only about 6.4%* were “ready” for college math. And *only about 2.3%* were “ready” for college science. And this is after the drop-out process was already well advanced. The failure is massive.



Charter schools would give the students in those 69 inner-city neighborhoods an alternative – a better choice. The dynamics of choice and competition would, over time, make all schools better.

The citizens of Chicago and Illinois – and the school families of Chicago – are not getting their money's worth. Fundamental reform is urgently needed – but not just because of economics. It is needed because of fairness. The cap on charter schools in Chicago should be lifted.

## Appendix B

### Charters vs. Nearest Neighborhood Schools: Comparison of 2008 Meets/Exceeds Percentages on State Assessments

Charter School	Charter 2008 Composite M/E	Nearest Neighborhood School	Neighborhood School Composite M/E	HS or Elem/Middle	Difference Between Charter and Neighborhood School
ACT Middle School	64.1%	Hefferan Elementary	84.3%	Elem/Middle	-20.2%
Alain Locke	81.0%	Calhoun North Elementary	72.6%	Elem/Middle	8.4%
ASPIRA Haugan Middle School	60.8%	Volta Elementary	75.8%	Elem/Middle	-15.0%
Betty Shabazz	81.9%	Avalon Park Elem	47.0%	Elem/Middle	34.9%
Bronzeville Lighthouse	51.5%	Attucks ES	49.8%	Elem/Middle	1.7%
Catalyst Howland	47.6%	Johnson Elementary	40.0%	Elem/Middle	7.6%
Chicago Math and Science	78.9%	Field Elementary	63.4%	Elem/Middle	15.5%
Chicago Virtual	69.0%	Brown W. Elementary	57.5%	Elem/Middle	11.5%
Choir Academy	72.1%	Abbott Elementary	58.4%	Elem/Middle	13.7%
Erie Elementary	74.2%	Lafayette Elementary	64.1%	Elem/Middle	10.1%
Galapagos Elementary	63.5%	Cameron Elementary	55.0%	Elem/Middle	8.5%
KIPP Ascend	73.3%	Sumner Elementary	72.4%	Elem/Middle	0.9%
LEARN Charter	80.3%	Lawndale Elementary	49.8%	Elem/Middle	30.5%
Legacy Charter	57.1%	Mason S Elementary	55.1%	Elem/Middle	2.0%
Namaste	89.0%	Greene, N Elementary	76.9%	Elem/Middle	12.1%
Passages Elementary	79.8%	Peirce Elementary	84.3%	Elem/Middle	-4.5%
Perspectives S Loop K-8	73.2%	Haines Elementary	87.0%	Elem/Middle	-13.8%
Providence Englewood	70.4%	Bass Elementary	44.1%	Elem/Middle	26.3%
Young Womens Leadership K-8	59.5%	Drake Elementary	60.4%	Elem/Middle	-0.9%
<b>AVERAGE - ELEM/MIDDLE</b>					<b>6.8%</b>
Ace Tech High School	12.7%	Phillips HS	3.7%	HS	9.0%
ACT Charter High School	9.8%	Marshall HS	3.9%	HS	5.9%
ASPIRA Ramirez	25.4%	Senn HS	15.6%	HS	9.8%
North Lawndale College Prep	14.5%	Manley HS	6.7%	HS	7.8%
Perspectives S Loop 9-12	17.8%	Phillips High School	3.7%	HS	14.1%
Young Womens Leadership 9-12	16.0%	Dunbar HS	6.6%	HS	9.4%
<b>AVERAGE - HIGH SCHOOL</b>					<b>9.3%</b>

Source: CPS Office of New Schools (January 6, 2009)