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GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF EDUCATION
LANSING

MICHAEL P. FLANAGAN
STATE SUPERINTENDENT

June 3, 2015

MEMORANDUM

TO: House and Senate K-12 Appropriations Subcommittees
FROM: Mike Flanagan, State Superintendent 
SUBJECT: Quarterly Report to the Legislature on Deficit Districts

OVERVIEW

Pursuant to language in Section 102 of the State School Aid Act (MCL 388.1702), the Michigan Department of Education (MDE) is required to report annually to the Legislature on school districts incurring year-end deficits and the districts' progress in reducing those deficits. In this third quarterly report for FY 2014-2015, an analysis of the projected FY 2014-2015 financial data has been completed for those school districts that ended FY 2013-2014 with a deficit. The analysis is conducted using data collected from Deficit Elimination Plans (DEPs) and required monthly budget control reports. It should be noted that since 1976, MDE has provided the Legislature with an annual report on local school districts in financial deficit.

Note: This report was prepared with data as of May 14, 2015.

Section 102(2) of the State School Aid Act (PA 94 of 1979, as amended) states:

"(2) Not later than March 1 of each year, the department shall prepare a report of deficits incurred or projected by districts and intermediate districts in the immediately preceding fiscal year and the progress made in reducing those deficits and submit the report to the standing committees of the legislature responsible for K-12 education legislation, the appropriations subcommittees of the legislature responsible for K-12 education appropriations, the house and senate fiscal agencies, the state treasurer, and the state budget director. The department also shall submit quarterly interim reports

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concerning the progress made by districts and intermediate districts in reducing those deficits. On a quarterly basis, the superintendent of public instruction shall publicly present those reports to the appropriations subcommittees of the legislature responsible for K-12 education appropriations."

The following narrative provides relevant information regarding process, requirements, and selected district information; the attached analysis provides deficit district specific information.

MICHIGAN DEPARTMENT OF EDUCATION (MDE) PROCESS

Under Governor Snyder's Good Government initiative, MDE has included a financial metric on our Scorecard related to DEPs as follows: "Percent of DEPs reviewed within 30 days of receipt from districts." MDE is continuing to achieve 100% on this metric.

In addition, the law requires that deficit districts submit a DEP to MDE. MDE has a formal process in place to ensure that school districts develop and implement DEPs to eliminate their general fund deficits. Long-standing MDE procedures ensure that districts are treated fairly throughout the deficit elimination process. MDE's website (http://www.michigan.gov/mde/0,4615,7-140-6530_6605-106599--,00.html) includes definitions, contact information, a flow chart to ensure accurate completion of required forms, and district requirements related to districts in deficit. MDE provides considerable technical assistance to districts during the DEP development and submission process. When necessary, the process may include requiring district representatives (i.e. administrators, local board of education members, and union representatives) to attend a meeting(s) in Lansing to discuss requirements in the law (see following section), status of the district's financial situation, possible modifications to the district's DEP, and answer questions. The desired outcome of such a meeting is for all of the district's key representatives to leave with a mutual understanding related to what is in the law and what is required of deficit districts. The MDE team stresses that because Michigan is a locally controlled state, district officials must make the difficult decisions that will eliminate the deficit. MDE also includes Department of Treasury (Treasury) staff in these meetings to discuss how processes within Treasury regarding the State Aid Note Borrowing Program and the Emergency Loan Program relate to and affect a district's deficit status. It is imperative that district representatives understand that borrowing through Treasury for cash flow purposes does not negate the need to reduce expenditures in order to eliminate the deficit. As we continue to work with these critical districts, it became apparent that the districts also need to have a conversation with Office of Retirement Systems if there is an issue with MPERS payments and with the Department of Licensing and Regulatory Affairs should the district have reimbursement issues related to Unemployment Insurance. Both agencies are invited to these meetings as necessary.

Public school academies (charter schools) are treated the same as traditional districts when faced with a deficit situation. They receive technical assistance and must submit a DEP to MDE and have it approved.

Since my last report to you on March 5, 2015, MDE staff has met in Lansing with the following deficit districts:

Saginaw City School District – 5/1/2015

- The district is close to selling one of its vacant buildings and will be amending their 2014-15 budget, adopting a 2015-16 budget, and revising their DEP accordingly.

Garden City School District – 5/4/2015

- The district gave the MDE an update on their progress with their approved DEP. Concessions have been reached with all labor groups with the exception of teachers. The district-teacher negotiations have gone to fact finding. As is the case with all deficit districts, the district will be amending their 2014-15 budget, adopting a 2015-16 budget, and revising their DEP accordingly.

REQUIREMENTS IN LAW

DISTRICT REQUIREMENTS

Michigan is a locally controlled state; Sec. 102(1) of the State School Aid Act [MCL 388.1702(1)] states:

"A district or intermediate district receiving money under this act shall not adopt or operate under a deficit budget, and shall not incur an operating deficit in a fund during a school fiscal year. A district having an existing deficit or which incurs a deficit shall not be allotted or paid a further sum under this act until the district submits to the department for approval a budget for the current fiscal year and a plan to eliminate the deficit not later than the end of the second fiscal year after the deficit was incurred or the budget projecting a deficit was adopted. Withheld state aid payments shall be released after the department approves the deficit reduction plan and ensures that the budget for the current school fiscal year is balanced. After the department approves a district's or intermediate district's deficit reduction plan, the district or intermediate district shall post the deficit elimination plan on the district's or intermediate district's website."

The Uniform Budgeting and Accounting Act places the burden for eliminating a district's deficit on the local board of education.

- MCL 141.436(7) – Except as otherwise permitted by Section 102 of the State School Aid Act, 1979 PA 94, MCL 388.1702, or by other law, the legislative body shall not adopt a general appropriations act or an amendment to that act which causes estimated total expenditures, including an accrued deficit, to exceed total estimated revenues, including an available surplus and the

proceeds from bonds or other obligations issued under the Fiscal Stabilization Act, 1981 PA 80, MCL 141.1001 to 141.1011, or the balance of the principal of these bonds or other obligations.

- MCL 141.437(2) – If, during a fiscal year, it appears to the chief administrative officer or to the legislative body that the actual and probable revenues from taxes and other sources in a fund are less than the estimated revenues, including an available surplus upon which appropriations from the fund were based and the proceeds from bonds or other obligations issued under the Fiscal Stabilization Act, 1981 PA 80, MCL 141.1001 to 141.1011, or the balance of the principal of these bonds or other obligations, the chief administrative officer or fiscal officer shall present to the legislative body recommendations which, if adopted, would prevent expenditures from exceeding available revenues for that current fiscal year. The recommendations shall include proposals for reducing appropriations from the fund for budgetary centers in a manner that would cause the total of appropriations to not be greater than the total of revised estimated revenues of the fund, or proposals for measures necessary to provide revenues sufficient to meet expenditures of the fund, or both. The recommendations shall recognize the requirements of state law and the provisions of collective bargaining agreements.
- MCL 141.438(3) – Except as otherwise provided in Section 19, an administrative officer of the local unit shall not incur expenditures against an appropriation account in excess of the amount appropriated by the legislative body. The chief administrative officer, an administrative officer, or an employee of the local unit shall not apply or divert money of the local unit for purposes inconsistent with those specified in the appropriations of the legislative body.

MICHIGAN DEPARTMENT OF EDUCATION REQUIREMENTS

Penalties in law that are to be imposed on deficit districts: (1) withholding state school aid [MCL 388.1702(1)] (see statutory language above); and (2) reporting a violation to the Attorney General who will review the report and determine whether or not to act [MCL 388.1761] (see statutory language below).

To date, as State Superintendent, I have periodically authorized state aid to be withheld from a limited number of deficit districts that have failed to submit timely, required information.

MCL 388.1761 – “A school official or member of a board or other person who neglects or refuses to do or perform an act required by this act or who violates or knowingly permits or consents to the violation of this act is guilty of a misdemeanor, punishable by imprisonment for not more than 90 days, or a fine of not more than \$1,500, or both.” There has been no instance where, as State Superintendent, I have asked the Attorney General’s involvement regarding deficit districts.

DEFICIT ELIMINATION PLANS NOT REQUESTED

Four districts'/academies' deficit fund balances at the end of the 2013-14 fiscal year were caused by timing issues with how grant related revenues and expenditures were recognized. Because reimbursements for expenditures recorded in 2013-14 were not received within 60 days of the last day of the fiscal year, the corresponding revenue had to be recorded in 2014-15. Since the deficit was directly related to this generally accepted accounting principle, and the districts' budgets show positive fund balances at the end of 2014-15, the Department did not request DEPs for the following districts and academies:

- Lakeside Charter School
- Akron Fairgrove Schools
- Blanche Kelso Bruce Academy
- Education Achievement Authority of Michigan

The Department remains concerned with the financial health of these districts and academies, knowing a simple timing issue could cause a deficit situation. We urged the districts and academies to review their current budgets and implement any necessary changes that will lead to stronger and more stable fund balances.

ADDITIONAL SELECTED DISTRICT INFORMATION

DETROIT PUBLIC SCHOOLS

On April 30, 2015, Governor Snyder announced a plan for Detroit Public Schools (DPS). The plan includes a new district, the City of Detroit Education District, which will operate the schools. The current Detroit Public Schools would continue under the direction of the emergency manager. The purpose of the existing DPS would be to pay off the district's current debt. The old district will use an existing local millage to pay off the debt. The state would then pay 100% of the per pupil foundation funds of the new district.

The new district would be managed by a school board of seven Detroit residents. They will initially be appointed by the mayor and governor and will be replaced by elected members over the next six years.

Despite their efforts, it is unlikely that the district will be able to eliminate the deficit without some intervention. Over the last ten years, the district's enrollment has decreased by 102,000, or 68%. Over that same period, the district has reduced total expenditures by \$900 million, or 56%.

As a result of refinancing their debt in 2005 and again in 2012, the district has annual debt service expenditures of \$56 million which represents 8% of their total expenditures and approximately \$1,200 per student. This is a significant reason as to why DPS is unable to generate an annual surplus. Furthermore, there is concern that, due to current cash needs, the district may need to refinance a portion of their debt again which would add to the \$56 million in annual debt service.

BENTON HARBOR AREA SCHOOLS

The district has adopted a resolution choosing the consent agreement option pursuant to Section 8 of 2012, PA436, the Local Financial Stability and Choice Act. On September 23, 2014, the district' school board approved the consent agreement developed by the Department of Treasury and the district superintendent, pursuant to state statute. Treasury and the Department are working with the district to approve their Financial and Operating Plan submitted pursuant to the consent agreement.

FINANCIAL INDEPENDENCE TEAM LEGISLATION

Legislation to develop policy and procedures to address districts and PSAs that trigger "early warning" indicators of financial stress did not pass during the last legislative session. Similar bills were introduced this session (HBs 4325-4330) and currently await consideration in the Senate Committee on Education. The Department is awaiting the outcome of the bills.

DEFICIT DISTRICT DATA

Attachments A and B provide the financial analysis for FY 2014-15.

Additional questions about this report should be directed to Dan Hanrahan, Office of State Aid and School Finance, at HanrahanD@michigan.gov or (517) 373-3350.

Attachments

**DEFICIT DISTRICT QUARTERLY REPORT
TO THE HOUSE AND SENATE K-12 APPROPRIATIONS SUBCOMMITTEES

FINANCIAL ANALYSIS OF MICHIGAN DEFICIT SCHOOL DISTRICTS
PROJECTED 2014-2015**

An analysis of the projected fiscal year 2014-2015 (FY2015) financial data has been completed for those districts that ended fiscal year 2014 (FY2014) with a deficit. The analysis is conducted using data collected from Deficit Elimination Plans (DEPs) and required monthly budget control reports.

Fifty-eight (58) districts and public school academies ended FY2014 in a deficit position. Two were public school academies which closed at the end of FY2014. Attachment B lists the remaining 56 districts and public school academies that ended FY2014 in a deficit position. Fifty-two (52) districts and public school academies ended FY2013 in a deficit position.

Of the 56 operating districts that ended FY2014 in deficit (including the four listed on page 5), Eighteen (18) are projecting to successfully eliminate their deficit by June 30, 2015 (Attachment B, Category 1). Twenty-eight (28) are projecting to reduce their deficit in FY2015 (Attachment B, Category 2). Eight (8) are projecting to increase their deficit in FY2015 (Attachment B, Category 3). Two (2) districts that ended FY2014 in deficit were converted to public school academy systems in FY2013. The predecessor local districts' deficits are being eliminated through the capture of school operating taxes (Attachment B, Category 5).

One (1) district that began FY2015 with a positive fund balance is projecting to end the year with a deficit fund balance (Attachment B, Category 4). That number may change as the year progresses and the districts submit their annual financial data due on October 15, 2015.

Attachment B also includes fund balance information for June 30, 2013 and June 30, 2014.

NOTE: The 2014-15 data in this report are projections from the districts and are subject to change as the fiscal year progresses.

ISD/School Name	June 2013 Fund Balance	June 2014 Fund Balance	Projected June 2015 Fund Balance	Projected 2015 GF Revenues	% Deficit is of Revenues
CATEGORY 1					
Districts that project to eliminate their deficit at June 30, 2015					
Copper Country ISD					
Hancock Public Schools	(\$514,291)	(\$5,856)	\$183,492	\$7,015,731	2.62%
Eaton RESA					
Life Tech Academy	NA	(\$58,751)	\$211,422	\$801,004	26.39%
Gratiot-Isabella RESD					
Ashley Community Schools	(\$225,307)	(\$90,081)	\$171,537	\$2,678,122	6.41%
Kalamazoo RESA					
Lakeside Charter School	NA	(\$233,952)	\$111,389	\$1,411,341	7.89%
Livingston ESA					
Brighton Area Schools	(\$8,500,481)	(\$4,322,572)	\$1,317,749	\$60,549,832	2.18%
Macomb ISD					
East Detroit Public Schools	(\$5,002,724)	(\$1,294,923)	\$197,374	\$35,531,041	0.56%
New Haven Community Schools	(\$236,549)	(\$167,869)	\$101,895	\$12,475,045	0.82%
Newaygo County RESA					
White Cloud School District	(\$580,276)	(\$113,644)	\$420,409	\$9,002,340	4.67%
Traverse Bay Area ISD					
Grand Traverse Academy	\$960,009	(\$365,129)	\$179,877	\$9,447,110	1.90%
Tuscola ISD					
Akron Fairgrove Schools	\$235,003	(\$39,679)	\$142,463	\$2,951,371	4.83%
Wayne RESA					
Hamtramck Public Schools	(\$3,443,659)	(\$1,079,978)	\$1,363,637	\$32,373,017	4.21%
Taylor School District	(\$8,834,147)	(\$3,871,072)	\$104,438	\$67,342,144	0.16%
Ecorse Public School District	(\$1,809,903)	(\$661,837)	\$343,666	\$9,853,647	3.49%
Branch Line School	NA	(\$22,024)	\$30,965	\$730,357	4.24%
Madison-Carver Academy	(\$402,226)	(\$261,020)	\$979	\$3,882,400	0.03%
Southwest Detroit Lighthouse Charter Academy	NA	(\$145,344)	\$15,213	\$3,313,936	0.46%
Blanche Kelso Bruce Academy	\$326,628	(\$502,085)	\$110,252	\$8,428,848	1.31%
EAA					
Education Achievement Authority of Michigan	\$6,781,147	(\$472,258)	\$148,423	\$97,801,500	0.15%
CATEGORY 2					
Districts that began FY2015 in deficit and project to end the year with a reduced deficit.					
Alpena-Montmorency-Alcona ESD					
Alpena Public Schools	(\$863,359)	(\$1,574,627)	(\$623,770)	\$35,784,856	-1.74%
Bay-Arenac ISD					
Essexville-Hampton Public Schools	\$266,067	(\$63,027)	(\$53,747)	\$14,706,611	-0.37%
Berrien RESA					
Benton Harbor Area Schools	(\$15,517,748)	(\$15,145,607)	(\$14,275,715)	\$37,586,888	-37.98%
Calhoun ISD					
Battle Creek Montessori Academy	NA	(\$251,219)	(\$197,145)	\$1,491,231	-13.22%

ISD/School Name	June 2013 Fund Balance	June 2014 Fund Balance	Projected June 2015 Fund Balance	Projected 2015 GF Revenues	% Deficit is of Revenues
CATEGORY 2, continued					
Districts that began FY2015 in deficit and project to end the year with a reduced deficit.					
Cheboygen-Otsego-Presque Isle ESD					
Mackinaw City Public Schools	(\$345,160)	(\$515,500)	(\$515,499)	\$2,274,634	-22.66%
Vanderbilt Area School District	(\$221,573)	(\$195,214)	(\$88,503)	\$1,434,350	-6.17%
Genesee ISD					
Flint Community Schools	(\$10,403,722)	(\$21,964,181)	(\$17,603,104)	\$92,994,737	-18.93%
Beecher Community School District	(\$701,015)	(\$988,531)	(\$847,106)	\$14,149,394	-5.99%
Hillsdale ISD					
Camden Frontier Schools	\$184,226	(\$55,243)	(\$40,131)	\$4,632,361	-0.87%
North Adams-Jerome Public Schools	\$30,421	(\$108,857)	(\$51,271)	\$3,105,618	-1.65%
Livingston ESA					
Pinckney Community Schools	(\$1,847,424)	(\$1,915,772)	(\$1,820,453)	\$31,069,651	-5.86%
Macomb ISD					
Clintondale Community Schools	(\$3,405,650)	(\$2,161,441)	(\$837,531)	\$28,084,348	-2.98%
Mt. Clemens Community Schools	(\$3,586,719)	(\$2,442,338)	(\$2,054,056)	\$13,531,882	-15.18%
Macomb Montessori Academy	NA	(\$213,139)	(\$201,929)	\$1,818,813	-11.10%
Muskegon Area ISD					
Muskegon Heights Public School Academy	(\$553,763)	(\$665,605)	(\$653,916)	\$9,929,912	-6.59%
Muskegon Montessori Academy for Environmental Cha	NA	(\$307,246)	(\$165,848)	\$1,140,929	-14.54%
Oakland Schools					
Pontiac School District	(\$51,677,552)	(\$39,077,646)	(\$35,400,748)	\$87,877,188	-40.28%
Saginaw ISD					
Saginaw City School District	(\$6,157,077)	(\$4,163,177)	(\$332,603)	\$77,516,223	-0.43%
Bridgeport Spaulding Community School District	(\$3,221,274)	(\$2,924,401)	(\$1,549,276)	\$16,565,603	-9.35%
Shiawassee RESD					
Perry Public Schools	(\$1,689,022)	(\$1,578,822)	(\$522,983)	\$11,994,663	-4.36%
Traverse Bay Area ISD					
Suttons Bay Public Schools	\$131,076	(\$351,517)	(\$216,306)	\$7,304,788	-2.96%
Van Buren ISD					
Bangor Public Schools	(\$373,350)	(\$452,425)	(\$333,898)	\$12,239,422	-2.73%
Washtenaw ISD					
Lincoln Consolidated Schools	(\$679,918)	(\$1,372,785)	(\$922,322)	\$43,968,880	-2.10%
Wayne RESA					
Detroit Public Schools	(\$93,881,926)	(\$169,460,308)	(\$166,359,414)	\$707,808,185	-23.50%
Dearborn Heights School District #7	(\$1,769,214)	(\$1,641,961)	(\$47,859)	\$23,869,575	-0.20%
Westwood Community School District	(\$6,311,270)	(\$4,977,195)	(\$3,965,474)	\$24,267,251	-16.34%
Southgate Community Schools	(\$4,906,716)	(\$3,982,984)	(\$1,536,130)	\$41,735,653	-3.68%
Highland Park Public School Academy	(\$620,248)	(\$409,544)	(\$328,192)	\$5,654,620	-5.80%
CATEGORY 3					
Districts that began FY2015 in deficit and project to end the year with a greater deficit.					
Calhoun ISD					
Albion Public Schools	(\$149,003)	(\$714,425)	(\$1,116,714)	\$7,115,928	-15.69%

ISD/School Name	June 2013 Fund Balance	June 2014 Fund Balance	Projected June 2015 Fund Balance	Projected 2015 GF Revenues	% Deficit is of Revenues
CATEGORY 3, continued					
Districts that began FY2015 in deficit and project to end the year with a greater deficit.					
Cheboygen-Otsego-Presque Isle ESD					
Cheboygan Area Schools	\$976,845	(\$232,119)	(\$1,112,070)	\$17,226,327	-6.46%
Dickinson-Iron ISD					
Iron Mountain Public Schools	\$247,143	(\$224,664)	(\$583,402)	\$7,410,666	-7.87%
Macomb ISD					
South Lake Schools	\$689,515	(\$229,386)	(\$1,786,430)	\$20,700,533	-8.63%
Warren Consolidated Schools	\$6,224,809	(\$2,167,334)	(\$4,083,531)	\$165,545,000	-2.47%
Oakland Schools					
School District of the City of Hazel Park	(\$3,919,402)	(\$6,191,945)	(\$11,837,118)	\$41,082,158	-28.81%
Wayne RESA					
Garden City School District	\$1,235,399	(\$606,713)	(\$3,920,595)	\$48,431,769	-8.10%
Detroit Public Safety Academy	NA	(\$537,993)	(\$782,191)	\$1,469,145	-53.24%
CATEGORY 4					
Districts that began FY2015 with a positive fund balance but project to end the year in deficit.					
Wayne RESA					
Gibraltar School District	\$3,306,430	\$1,365,711	(\$1,388,416)	\$32,609,269	-4.26%
CATEGORY 5					
Districts whose deficits are being eliminated through the capture of school operating taxes through Department of Treasury					
Muskegon Area ISD					
Muskegon Heights School District	(\$1,117,702)	(\$1,089,576)	(\$868,007)	\$1,506,677	-57.61%
Wayne RESA					
Highland Park City Schools	(\$7,638,145)	TBD	TBD	TBD	
SUMMARY:					
No. of Districts	Cat.	Description			
18	1	Districts that project to eliminate their deficit at June 30, 2015			
28	2	Districts that began FY2015 in deficit and project to end the year with a reduced deficit.			
8	3	Districts that began FY2015 in deficit and project to end the year with a greater deficit.			
1	4	Districts that began FY2015 with a positive fund balance but project to end the year in deficit.			
2	5	Districts whose deficits are being eliminated through the capture of school operating taxes through Department of Treasury			
*NOTES:					
A	DEP not requested due to timing issues related to generally accepted accounting principles.				
B	District has an emergency loan from Treasury.				
C	Financial emergency declared under PA436.				
D	A note in the district's audited financial statements indicates that the district may owe Genesee ISD up to \$8.6 million that is not recognized in the deficit.				
E	District exists as authorizer of an academy.				