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GOVERNOR

STATE OF MICHIGAN  
DEPARTMENT OF EDUCATION  
LANSING

MICHAEL P. FLANAGAN  
STATE SUPERINTENDENT

February 27, 2015

**MEMORANDUM**

**TO:** House and Senate K-12 Appropriations Subcommittees  
**FROM:** Mike Flanagan, State Superintendent  
**SUBJECT:** Annual 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 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. This annual report due March 1 can appropriately serve as the required second quarterly report for FY 2014-2015 to be presented March 5, 2015, given the proximity of this annual deadline to the quarterly presentation.

**Note: This report was prepared with data as of February 20, 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*

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*the state budget director. The department also shall submit quarterly interim reports 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](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 December 19, 2014, MDE staff has met in Lansing with the following deficit districts:

**Albion Public Schools – 1/16/2015**

- After their December DEP submission was not approvable, we asked for a meeting. The Department requested a revised DEP be submitted by February 16, 2015. A revised DEP was submitted by the deadline and is currently being reviewed by the Department.

**Hazel Park Public Schools – 2/5/2015**

- During the preparation of their annual audit, it was discovered that the district's deficit increased by \$2.3 million from June 30, 2013 to June 30, 2014. The district had projected that the deficit would decrease in 2013-14. During the meeting with the Department, the district reported that their new auditing firm required the district to correct prior accounting errors. The district must submit a revised DEP by March 16, 2015.

The Department is currently scheduling a meeting with Saginaw Public Schools board and other officials to discuss their deficit situation.

**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. Since my December report to you, because Hazel Park City Schools had not complied with the law in submitting their audit and Financial Information Database, I withheld their state aid beginning with the December 20, 2014 payment. When the required information was received, all payments were released to the district.

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**

The district submitted a revised DEP on December 17, 2014. On January 13, 2015, Darnell Earley was appointed Emergency Manager of Detroit Public Schools, replacing Jack Martin. Mr. Earley had been the Emergency Manager for the City of Flint. We continue to have dialogue with the Emergency Manager and the Chief Financial Officer of the district.

#### **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.

### **FLINT COMMUNITY SCHOOLS**

On December 26, 2014, I approved the district's request to extend their DEP through 2020-2021. This approval was largely based on the continued support provided by the Mott Foundation and the substantial contributions made by all district employees. As I remain very concerned about the district's serious financial state, the Department continues to have weekly contact with the district.

### **SCHOOL DISTRICT OF THE CITY OF SAGINAW**

The district's current DEP includes closing one of their high schools. On February 18, 2015, the board tabled a vote on the interim superintendent's recommendation to close Saginaw High School. The district has a purchase agreement to sell the former Buena Vista High School to Pansophic Learning. The board also voted to demolish the Phoenix Science & Technology Center, but has subsequently rescinded that decision and placed the building back on the market. The district has made a counter-offer to the interested parties. While the sale of either of these buildings could possibly eliminate the deficit this year, it is important to remember that these are one-time events and have no impact on future budgets. The board must continue to make the tough decisions in order to right-size the district and maintain a balanced budget.

### **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 the last legislation session. The Governor's Executive Recommendation for 2015-16 includes similar language. The Department is awaiting the outcome of the proposals.

### **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](mailto:HanrahanD@michigan.gov) or (517) 373-3350.

Attachments

**DEFICIT DISTRICT ANNUAL 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 public school academies 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), Nineteen (19) are projecting to successfully eliminate their deficit by June 30, 2015 (Attachment B, Category 1). Twenty-seven (27) 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).

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

At this time, we are not aware of any districts that began FY2015 with a positive fund balance and are 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.

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
<b>CATEGORY 1</b>					
Districts that project to eliminate their deficit at June 30, 2015					
<b>Copper Country ISD</b>					
Hancock Public Schools	(\$514,291)	(\$5,856)	\$152,663	\$6,604,254	2.31%
<b>Eaton RESA</b>					
Life Tech Academy	NA	(\$58,751)	\$246,205	\$800,736	30.75%
<b>Gratiot-Isabella RESD</b>					
Ashley Community Schools	(\$225,307)	(\$90,081)	\$48,721	\$2,520,364	1.93%
<b>Hillsdale ISD</b>					
Camden Frontier Schools	\$184,226	(\$55,243)	\$6,184	\$4,147,758	0.15%
<b>Kalamazoo RESA</b>					
Lakeside Charter School	NA	(\$233,952)	TBD A	TBD	
<b>Livingston ESA</b>					
Brighton Area Schools	(\$8,500,481)	(\$4,322,572)	\$1,317,749	\$60,549,832	2.18%
<b>Macomb ISD</b>					
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%
<b>Newaygo County RESA</b>					
White Cloud School District	(\$580,276)	(\$113,644)	\$420,409	\$9,002,340	4.67%
<b>Traverse Bay Area ISD</b>					
Grand Traverse Academy	\$960,009	(\$365,129)	\$179,877	\$9,447,110	1.90%
<b>Tuscola ISD</b>					
Akron Fairgrove Schools	\$235,003	(\$39,679)	\$162,856 A	\$2,912,091	5.59%
<b>Wayne RESA</b>					
Dearborn Heights School District #7	(\$1,769,214)	(\$1,641,961)	\$6,559	\$23,316,101	0.03%
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	\$9,583,647	3.59%
Branch Line School	NA	(\$22,024)	\$30,965	\$730,357	4.24%
Madison-Carver Academy	(\$402,226)	(\$261,020)	\$5,179	\$3,877,900	0.13%
Blanche Kelso Bruce Academy	\$326,628	(\$502,085)	\$110,252 A	\$8,428,848	1.31%
<b>EAA</b>					
Education Achievement Authority of Michigan	\$6,781,147	(\$472,258)	\$643,036 A	\$85,991,531	0.75%
<b>CATEGORY 2</b>					
Districts that began FY2015 in deficit and project to end the year with a reduced deficit.					
<b>Alpena-Montmorency-Alcona ESD</b>					
Alpena Public Schools	(\$863,359)	(\$1,574,627)	(\$623,770)	\$35,784,856	-1.74%
<b>Bay-Arenac ISD</b>					
Essexville-Hampton Public Schools	\$266,067	(\$63,027)	(\$26,673)	\$14,706,611	-0.18%
<b>Berrien RESA</b>					
Benton Harbor Area Schools	(\$15,517,748)	(\$15,145,607)	(\$14,275,715) B, C	\$37,586,888	-37.98%
<b>Calhoun ISD</b>					
Battle Creek Montessori Academy	NA	(\$251,219)	(\$154,482)	\$1,762,838	-8.76%

ISD/School Name	June 2013 Fund Balance	June 2014 Fund Balance	Projected June 2015 Fund Balance	Projected 2015 GF Revenues	% Deficit is of Revenues
<b>CATEGORY 2, continued</b>					
Districts that began FY2015 in deficit and project to end the year with a reduced deficit.					
<b>Cheboygen-Otsego-Presque Isle ESD</b>					
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%
<b>Genesee ISD</b>					
Flint Community Schools	(\$10,403,722)	(\$21,964,181)	(\$17,422,905) D	\$93,312,149	-18.67%
Beecher Community School District	(\$701,015)	(\$988,531)	(\$878,190)	\$14,118,771	-6.22%
<b>Hillsdale ISD</b>					
North Adams-Jerome Public Schools	\$30,421	(\$108,857)	(\$51,271)	\$3,105,618	-1.65%
<b>Livingston ESA</b>					
Pinckney Community Schools	(\$1,847,424)	(\$1,915,772)	(\$1,820,453)	\$31,069,651	-5.86%
<b>Macomb ISD</b>					
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)	(\$1,546,953)	\$13,725,306	-11.27%
Macomb Montessori Academy	NA	(\$213,139)	(\$188,662)	\$1,929,438	-9.78%
<b>Muskegon Area ISD</b>					
Muskegon Heights Public School Academy	(\$553,763)	(\$665,605)	(\$397,556)	\$9,838,915	-4.04%
Muskegon Montessori Academy for Environmental Cha	NA	(\$307,246)	(\$182,686)	\$1,181,745	-15.46%
<b>Oakland Schools</b>					
Pontiac School District	(\$51,677,552)	(\$39,077,646)	(\$29,008,898) C	\$79,866,100	-36.32%
<b>Saginaw ISD</b>					
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)	(\$1,615,359)	\$16,444,337	-9.82%
<b>Shiawassee RESD</b>					
Perry Public Schools	(\$1,689,022)	(\$1,578,822)	(\$522,983)	\$11,994,663	-4.36%
<b>Traverse Bay Area ISD</b>					
Suttons Bay Public Schools	\$131,076	(\$351,517)	(\$219,713)	\$7,217,882	-3.04%
<b>Van Buren ISD</b>					
Bangor Public Schools	(\$373,350)	(\$452,425)	(\$333,898)	\$12,239,422	-2.73%
<b>Washtenaw ISD</b>					
Lincoln Consolidated Schools	(\$679,918)	(\$1,372,785)	(\$922,322)	\$43,968,880	-2.10%
<b>Wayne RESA</b>					
Detroit Public Schools	(\$93,881,926)	(\$169,460,308)	(\$164,501,498)	\$691,586,866	-23.79%
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)	(\$1,195,799)	\$40,875,563	-2.93%
Highland Park Public School Academy	(\$620,248)	(\$409,544)	(\$401,723)	\$5,682,339	-7.07%
Southwest Detroit Lighthouse Charter Academy	NA	(\$145,344)	(\$130,132)	\$3,313,936	-3.93%
<b>CATEGORY 3</b>					
Districts that began FY2015 in deficit and project to end the year with a greater deficit.					
<b>Calhoun ISD</b>					
Albion Public Schools	(\$149,003)	(\$714,425)	(\$891,525)	\$7,108,299	-12.54%
<b>Cheboygen-Otsego-Presque Isle ESD</b>					
Cheboygan Area Schools	\$976,845	(\$232,119)	(\$1,112,070)	\$17,226,327	-6.46%

ISD/School Name	June 2013 Fund Balance	June 2014 Fund Balance	Projected June 2015 Fund Balance	Projected 2015 GF Revenues	% Deficit is of Revenues
<b>CATEGORY 3, continued</b>					
Districts that began FY2015 in deficit and project to end the year with a greater deficit.					
<b>Dickinson-Iron ISD</b>					
Iron Mountain Public Schools	\$247,143	(\$224,664)	(\$564,316)	\$7,323,574	-7.71%
<b>Macomb ISD</b>					
South Lake Schools	\$689,515	(\$229,386)	(\$1,214,821)	\$21,167,142	-5.74%
Warren Consolidated Schools	\$6,224,809	(\$2,167,334)	(\$2,450,229)	\$165,021,196	-1.48%
<b>Oakland Schools</b>					
School District of the City of Hazel Park	(\$3,919,402)	(\$6,191,945)	TBD	TBD	
<b>Wayne RESA</b>					
Garden City School District	\$1,235,399	(\$606,713)	(\$1,716,317)	\$46,030,745	-3.73%
Detroit Public Safety Academy	NA	(\$537,993)	(\$786,362)	\$1,428,413	-55.05%
<b>CATEGORY 4</b>					
Districts that began FY2015 with a positive fund balance but project to end the year in deficit.					
We are not aware of any districts that began FY2015 with a positive fund balance and are projecting to end the year with a deficit fund balance					
<b>CATEGORY 5</b>					
Districts whose deficits are being eliminated through the capture of school operating taxes through Department of Treasury					
<b>Muskegon Area ISD</b>					
Muskegon Heights School District	(\$1,117,702)	(\$1,089,576)	(\$868,007)	\$1,506,677	-57.61%
<b>Wayne RESA</b>					
Highland Park City Schools	(\$7,638,145)	TBD	TBD	TBD	
<b>SUMMARY:</b>					
<b>No. of Districts</b>	<b>Cat.</b>	<b>Description</b>			
19	1	Districts that project to eliminate their deficit at June 30, 2015			
27	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.			
0	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			
<b>*NOTES:</b>					
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 2 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.				