RICK SNYDER
GOVERNOR

STATE OF MICHIGAN
DEPARTMENT OF EDUCATION
LANSING

MICHAEL P. FLANAGAN
STATE SUPERINTENDENT

February 27, 2014

MEMORANDUM

TO: House and Senate K-12 Appropriations Subcommittees

FROM: Mike Flanagan, State Superintendent

SUBJECT: Quarterly Report to the Legislature on Deficit Districts

OVERVIEW

The Michigan Department of Education (MDE) is required in Section 102 of the State School Aid Act to report quarterly to the Legislature on school districts incurring year-end deficits and the districts' progress in reducing those deficits. In this second quarterly report for FY 2013-2014, an analysis of the projected FY 2013-2014 financial data has been completed for those school districts that ended FY 2012-13 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 second quarterly report for FY 2013-2014 can appropriately serve as the required annual report due March 1 given the proximity of this presentation to the annual deadline.

Section 102(2) of the State School Aid Act (Public Act No. 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 Deficit Elimination Plans (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 Deficit Elimination Plan (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. 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 MPSERS payments and with the Department of Licensing and Regulatory Affairs (LARA) should the district have reimbursement issues related to Unemployment Insurance. Both agencies are invited to these meetings as necessary.

Since my last report to you on December 12, 2013, MDE staff has met in Lansing with the following deficit districts:

Flint Community Schools

- December 17, 2013 – Discussion regarding Genesee Area Skills Center and the debt owed to Genesee ISD
- January 15, 2014 – Discussion involved coordination of revised DEP approval and Treasury borrowing

Saginaw City School District

- February 18, 2014 – Discussion included academic program improvements and their link to the DEP, the district's 2015-16 budget, and submission of the required DEP forms by COB on Friday, February 21, 2014 (NOTE: any additional union action documentation was due by 3 p.m. on February 24, 2014)

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. Our experience has found that the charter authorizer will step in and either close the school or take other steps early in the process so a meeting in Lansing has not yet been necessary.

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 the Mackinaw City Public Schools has not complied with the law in submitting their DEP, I have withheld their state aid beginning with the December 20, 2013 payment. When the required information has been received, I will release all payments.

"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." (MCL 388.1761) There has been no instance where, as State Superintendent, I have asked the Attorney General's involvement regarding deficit districts.

ADDITIONAL SELECTED DISTRICT INFORMATION

DETROIT PUBLIC SCHOOLS

Detroit Public Schools administration recently requested additional time to develop a revised Deficit Elimination Plan (DEP). The following reasons for the extension were considered:

- Time to verify the February 12, 2014 pupil count
- Time to finalize current negotiations with unions (including the DFT) due to wage and health care re-openers in their contracts
- Time to make a decision on FY 2015 school closures
- Time to negotiate pending electricity rates with Detroit Public Lighting officials

Because each of these issues has a significant impact on the District's ability to implement a revised DEP and Financial and Operating Plan, MDE granted the district until March 31, 2014 to perform additional comprehensive analysis of the above and to further determine the financial impact each will have on the district's revised DEP and its Finance and Operating Plan (NOTE: The Finance and Operating Plan is due to Treasury as part of the Emergency Manager requirements).

PONTIAC SCHOOL DISTRICT

The Pontiac School District continues to operate under the Consent Agreement authorized under PA 436. The district's Deficit Elimination Plan was approved on January 21, 2014. The Plan does not call for the deficit to be eliminated until 2022-23, making it a 10-year Plan. While I was hesitant to approve such a Plan, a shorter time period did not seem feasible given the severity of the deficit and the district's various needs including capital outlay for needed infrastructure repairs. The district has lost approximately 50% of its pupil count since 2004-05, a major reason why I insisted that an Education Plan be required by the Consent Agreement. This Education Plan was developed in conjunction with MDE staff and is intended, in part, to stem the loss of pupils from the district.

A major concern with the district is its cash flow. Our colleagues at Treasury have worked with the district to secure a $13.8 million Tax Anticipation Note to help the district through its cash crisis. The district's Finance and Operating Plan required by the Consent Agreement is, in part, based on securing an additional $10 million yet this school year through an Emergency Loan administered by Treasury. Staff from both Treasury and MDE are working to ensure that these arrangements are not financing the status quo, rather that they ensure the arrangements are based on the district showing evidence of making the necessary decisions to eliminate the deficit.

FLINT COMMUNITY SCHOOLS

MDE approved Flint Community Schools' seven-year DEP on February 4, 2014. While this is the longest time given to a district not under PA436, there are strict contingencies built into the approval letter that will be closely monitored including the requirement that the district submit an Education Plan that is to be developed with input from MDE staff. The DEP will be revoked if the district does not comply with the contingencies. In addition, the Mott Foundation is providing financial assistance to the district by way of funding both financial and academic consultants. These individuals will be in the district for a period of at least two years. This is very encouraging news and is one of the main reasons I felt that the seven-year DEP could be approved.

In addition, the State Budget Director, State Treasurer, and I approved a partial advance of the district's regular State Aid payment in February 2014 to help the district meet its February payroll obligation.

Finally, the audited financial statement for Flint Community Schools shows a deficit fund balance of $10.4 million. Note 2 in this statement indicates that the district may owe Genesee ISD up to $8.6 million that is not recognized in the deficit. This is a development that our team is monitoring closely and helping the district and ISD to resolve.

SAGINAW CITY SCHOOL DISTRICT

Saginaw City School District was required to submit a DEP by February 10, 2014. The Superintendent of the district proposed closing a high school, a middle school, and an elementary school which met with significant community opposition. In order to get additional input from the community, the district asked for, and was granted, an extension of time to February 18, 2014 to submit the DEP. A successful meeting was held with the district on February 18, 2014 (see Saginaw City School District, page 3); all required MDE forms have been submitted and are under priority review.

A complicating factor with this district has been the inheritance of pupils from the dissolved Buena Vista district and additional costs associated with buildings from the dissolved district that are not needed. Based on a recent letter to the district from Senator Kahn, Senate Bill 608 could potentially award $2.5 million to the district for "reimbursements to receiving school districts for costs associated with the transfer of property from a dissolved school district to a receiving school district". Saginaw's deficit increased due to costs associated with receiving buildings (i.e. maintenance, insurance, utilities, etc.) when Buena Vista was dissolved. This anticipated revenue was included in the district's revised DEP. Should this revenue not be appropriated, the district must revise the DEP to reflect this change.

BENTON HARBOR AREA SCHOOLS

Benton Harbor Area Schools submitted a DEP that was rejected by MDE because it contained assumptions that were not acceptable. On February 12, 2014, the district submitted a revised DEP which projects to eliminate the deficit in 2027-28. Staff is in the process of analyzing the revised DEP and making a determination of next steps.

EXECUTIVE BUDGET RECOMMENDATION

The FY2015 budget includes several efforts to help school districts that are struggling financially. A joint effort between MDE, Treasury, and CEPI will develop an early warning system to identify troubled schools earlier. In addition, the Governor is recommending a Financial Independence Team made up of new staff from both Treasury and MDE. Under this collaborative proposal, MDE would be funded for four additional staff to proactively help financially struggling districts that are not quite yet in deficit but appear headed that way. Two staff would work in our State Aid Unit on financial matters with the districts; two staff would be in our Office of Educational Improvement and Innovation and would work with districts on required Education Plans.

DEFICIT DISTRICT DATA

Attachments A and B provide the financial analysis for FY2013-14.

Additional questions about this report should be directed to Glenda Rader, Office of State Aid and School Finance, at raderg@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 2013-2014

An analysis of the projected fiscal year 2013-2014 (FY2014) financial data has been completed for those districts that ended fiscal year 2013 (FY2013) with a deficit. The analysis is conducted using data collected from Deficit Elimination Plans (DEPs) and required monthly budget control reports.

Fifty (50) districts and public school academies ended FY2013 in a deficit position. One of those districts consolidated with another district effective July 1, 2013. Additionally, two of the districts that ended FY2013 with a deficit dissolved subsequent to June 30, 2013, and one academy was closed by its authorizer. Attachment B lists the remaining 46 districts and public school academies that ended FY2013 in a deficit position. Attachment B also includes fund balance information for June 30, 2011 and June 30, 2012.

Of the 46 operating districts that ended FY2013 in deficit, eight (8) are projecting to successfully eliminate their deficit by June 30, 2014 (Attachment B, Category 1). Twenty-eight (28) are projecting to reduce their deficit in FY2014 (Attachment B, Category 2). Eight (8) districts are projecting to increase their deficit in FY2014 (Attachment B, Category 3). Two (2) districts' deficits are being eliminated through the capture of school operating taxes through Department of Treasury (Attachment B, Category 5).

Four (4) districts that began FY2014 with a positive fund balance are projecting to end the year with a deficit fund balance (Attachment B, Category 4). That number is likely to change as the year progresses and the districts submit their annual financial data due on November 15, 2014.

NOTE: The 2013-14 data in this report are projections from the districts and are subject to change as the fiscal year progresses.

ISD/School Name	June 2012 Fund Balance	June 2013 Fund Balance	Projected June 2014 Fund Balance		Projected 2014 GF Revenues	% Deficit is of Revenues
CATEGORY 1						
Districts that project to eliminate their deficit by June 30, 2014						
Alpena-Montmorency-Alcona ESD						
Atlanta Community Schools	$81,446	($31,842)	$26,686		$2,692,249	0.99%
Gratiot-Isabella RESD						
Ashley Community Schools	($164,856)	($225,307)	$21,857		$2,583,566	0.85%
Macomb ISD						
New Haven Community Schools	($323,332)	($236,549)	$10,190		$12,122,779	0.08%
Menominee ISD						
Menominee Area Public Schools	($129,287)	($53,664)	$116,506		$12,404,258	0.94%
Muskegon Area ISD						
Muskegon Heights Public School Academy	NA	($553,763)	TBD		TBD	
Newaygo County RESA						
White Cloud School District	($693,720)	($580,276)	$201,471		$10,822,870	1.86%
Oakland Schools						
Avondale School District	($1,338,397)	($239,564)	$49,786		$35,643,618	0.14%
Washtenaw ISD						
Ypsilanti Community Schools	($9,014,364)	($7,511,013)	$7,666,395		$69,188,066	11.08%
CATEGORY 2						
Districts that began FY2014 in deficit and project to end the year with a reduced deficit.						
Alpena-Montmorency-Alcona ESD						
Alpena Public Schools	$1,070,904	($863,359)	($697,810)		$34,366,404	-2.03%
Berrien RESA						
Benton Harbor Area Schools	($16,099,422)	($15,517,748)	($14,652,967)	B	$31,825,237	-46.04%
Cheboygen-Otsego-Presque Isle ESD						
Mackinaw City Public Schools	($23,914)	($345,160)	TBD	A	TBD	
Genesee ISD						
Beecher Community School District	$680,450	($701,015)	($180,280)		$14,706,959	-1.23%
Copper Country ISD						
Hancock Public Schools	($743,491)	($514,291)	($199,950)		$6,502,154	-3.08%
Livingston ESA						
Brighton Area Schools	($7,388,781)	($8,500,481)	($2,741,160)		$58,129,153	-4.72%
Macomb ISD						
East Detroit Public Schools	($7,545,877)	($5,002,724)	($3,947,214)		$36,953,975	-10.68%
Clintondale Community Schools	($4,772,258)	($3,405,650)	($1,646,085)		$28,917,204	-5.69%
Mt. Clemens Community Schools	($4,790,635)	($3,586,719)	($2,116,137)		$16,621,965	-12.73%
Oakland Schools						
Pontiac School District	($37,683,487)	($51,677,552)	($44,585,359)		$74,104,036	-60.17%
School District of the City of Hazel Park	($1,527,137)	($3,919,402)	($1,474,630)		$40,152,648	-3.67%

ISD/School Name	June 2012 Fund Balance	June 2013 Fund Balance	Projected June 2014 Fund Balance		Projected 2014 GF Revenues	% Deficit is of Revenues
CATEGORY 2, continued						
Districts that began FY2014 in deficit and project to end the year with a reduced deficit.						
Cheboygen-Otsego-Presque Isle ESD						
Vanderbilt Area School District	($155,449)	($221,573)	($97,412)		$1,462,754	-6.66%
Saginaw ISD						
Saginaw City School District	($5,100,750)	($6,157,077)	($3,496,624)		$84,945,906	-4.12%
Bridgeport Spaulding Community School District	($2,561,221)	($3,221,274)	($2,263,085)		$14,782,441	-15.31%
Shiawassee RESD						
Perry Public Schools	($1,083,873)	($1,689,022)	($1,000,685)		$11,342,787	-8.82%
Wayne RESA						
Detroit Public Schools	($76,345,661)	($93,881,926)	($76,523,348)		$685,398,919	-11.16%
Dearborn Heights School District #7	($657,094)	($1,769,214)	($702,386)		$23,283,981	-3.02%
Hamtramck Public Schools	($3,776,824)	($3,443,659)	($1,984,986)		$31,379,783	-6.33%
Redford Union Schools	($4,114,455)	($1,962,334)	($1,089,534)		$28,814,529	-3.78%
River Rouge School District	($3,427,203)	($1,107,736)	($376,575)		$17,264,458	-2.18%
Romulus Community Schools	$2,393,436	($2,323,910)	($2,120,017)		$33,078,851	-6.41%
Taylor School District	($5,941,851)	($8,834,147)	($4,275,714)		$62,771,248	-6.81%
Westwood Community School District	($6,240,031)	($6,311,270)	($3,000,381)		$26,140,849	-11.48%
Ecorse Public School District	($1,536,593)	($1,809,903)	($785,992)		$9,571,464	-8.21%
Southgate Community Schools	($3,249,656)	($4,906,716)	($2,572,659)		$44,057,750	-5.84%
Madison-Carver Academy	NA	($402,226)	($209,790)		$2,806,137	-7.48%
Highland Park Public School Academy	NA	($620,248)	TBD		TBD	
HEART Academy	($93,780)	($344,498)	($341,833)		$1,606,478	-21.28%
CATEGORY 3						
Districts that began FY2014 in deficit and project to end the year with a greater deficit.						
Calhoun ISD						
Albion Public Schools	$514,594	($149,003)	($285,819)		$9,861,514	-2.90%
Genesee ISD						
Flint Community Schools	($11,497,002)	($10,403,722)	($12,705,124)	C	$101,733,021	-12.49%
Livingston ESA						
Pinckney Community Schools	$865,569	($1,847,424)	($2,301,618)		$30,846,762	-7.46%
Monroe County ISD						
Bedford Public Schools	($626,901)	($189,632)	($716,701)		$39,070,411	-1.83%
Muskegon Area ISD						
Muskegon Public Schools	$1,295,727	($1,169,873)	($1,203,797)		$49,968,529	-2.41%
Oakland Schools						
Oak Park School District	($5,557,347)	($1,617,163)	($1,888,656)		$47,196,771	-4.00%
Van Buren ISD						
Bangor Public Schools	$154,974	($373,350)	($837,807)		$11,449,279	-7.32%
Washtenaw ISD						
Lincoln Consolidated Schools	$745,440	($679,918)	($1,172,091)		$42,874,470	-2.73%

ISD/School Name	June 2012 Fund Balance	June 2013 Fund Balance	Projected June 2014 Fund Balance		Projected 2014 GF Revenues	% Deficit is of Revenues
CATEGORY 4						
Districts that began FY2014 with a positive fund balance but project to end the year in deficit.						
Calhoun ISD						
Battle Creek Montessori Academy	NA	NA	($192,155)		$1,274,936	-15.07%
Dickinson-Iron ISD						
Iron Mountain Public Schools	$793,565	$247,143	($158,473)		$7,690,615	-2.06%
Macomb ISD						
South Lake Schools	$1,200,175	$689,515	($1,828,396)		$21,008,413	-8.70%
Wayne RESA						
Detroit Public Safety Academy	NA	NA	($667,456)		$819,380	-81.46%
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	($11,896,251)	TBD	$411,331	B,D	$1,494,181	27.53%
Wayne RESA						
Highland Park City Schools	($12,170,066)	($7,638,145)	($7,059,877)	B,D	$2,100,035	-336.18%

SUMMARY:

No. of Districts	Cat.	Description
8	1	Districts that project to eliminate their deficit by June 30, 2014
28	2	Districts that began FY2014 in deficit and project to end the year with a reduced deficit.
8	3	Districts that began FY2014 in deficit and project to end the year with a greater deficit.
4	4	Districts that began FY2014 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	As of 2/25/2014 district has not submitted DEPas required. State Aid payments have been withheld since December 20, 2013.
B	District has an emergency loan from Treasury.
C	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.
D	District exists as authorizer of an academy.