




RICK SNYDER  
GOVERNOR

STATE OF MICHIGAN  
DEPARTMENT OF EDUCATION  
LANSING

MICHAEL P. FLANAGAN  
SUPERINTENDENT OF  
PUBLIC INSTRUCTION

**DATE:** August 11, 2011  
**TO:** Rick Snyder, Governor  
**FROM:** Mike Flanagan, Superintendent of Public Instruction   
**SUBJECT:** Preliminary Review of the School District of the City of Highland Park

The following represents the Preliminary Review under 2011 PA 4 for the School District of the City of Highland Park. We appreciate the level of cooperation received from the district's administration during this process.

**I. Background**

In a letter dated July 25, 2011, I advised the School District of the City of Highland Park (Highland Park Schools) that pursuant to my authority vested under PA 4 of 2011, I initiated a Preliminary Review of the district's finances to determine if a finding of probable financial stress is warranted. Section 12(1) of the Act states that the state financial authority of a local government (the Superintendent of Public Instruction in the case of a school district) may conduct a preliminary review to determine the existence of a local government financial problem if one or more of the criteria listed in Section 12(1) are met. The Preliminary Review of the Highland Park Schools resulted from the condition enumerated in subdivision(r) of Section 12(1), which requires the existence of "other facts and circumstances...that in the Superintendent of Public Instruction's sole discretion...are indicative of school district's financial stress."

**II. Preliminary Review Findings**

The Department has developed six (6) critical factors to determine if a finding of probable financial stress is warranted. The factors are:

- 1) The district has been in deficit for three or more consecutive years (including the current year); and
- 2) The district's existing deficit is greater than \$1,000,000; and

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- 3) The district's existing deficit is greater than 15% of general fund revenues excluding incoming transfers; and
- 4) A fiscal review by one of the Department's program offices or an external auditor has revealed one or more material internal control weaknesses as evidenced by notes/findings in the financial audit related to:
  - a) Lack of written policies and procedures or failure to follow the written policies and procedures
  - b) Poor cash management
  - c) Failure to provide Personnel Activity Reports (PAR) for employees paid with federal funds
  - d) History of spending outside the appropriations established by the local school board (Violation of Uniform Budgeting and Accounting Act)
  - e) Use of grant funds on unallowable expenditures
  - f) Going Concern/Qualified Opinion; and
- 5) District has shown unsatisfactory progress in eliminating a deficit. This is determined by identifying one or more of the following conditions:
  - a) A deficit increase from the previous year
  - b) Lack of cooperation from the district in submitting deficit information (i.e., late submission of Deficit Elimination Plans (DEP), delinquent return of phone calls or correspondence relating to the DEP, chronic late submission of Monthly Budgetary Control Reports)
  - c) History of supplying the Department with DEP information that is inaccurate or inconsistent with actual revenues and expenditures at year end; and/or
- 6) District's failure to comply with bond or note covenants or failure to make pension fund deposits.

The Department assessed the Highland Park Schools with regard to the above six (6) factors. The results of the assessment are as follows:

- 1) The Highland Park Schools ended the 2008-09 and the 2009-10 fiscal years in deficit. The district projected that it will remain in deficit in the 2010-11, 2011-12, 2012-13 and the 2013-14 fiscal years. Although it had a very modest fund balance of \$7,282 in fiscal year 2007-08, the district was also in deficit in 2006-07.
- 2) The Highland Park Schools' fund balance confirmed by an independent public accounting audit at June 30, 2010, was a negative \$7,467,527. The district's fund balance deficit has exceeded \$3,000,000 since 2008-09.
- 3) The Highland Park Schools' fund balance expressed as a percentage of their general fund revenues is projected to be a negative 54%. This is the highest negative percentage of all districts in the state. The percentage far exceeds the Department's parameter of a negative 15% to indicate concern.
- 4) The Highland Park Schools' audited financial report for the year ended June 30, 2010, included 19 findings of material weaknesses, significant deficiencies, or non-compliance. The findings included failure to obtain a bond audit and poor cash management. The district's June 30, 2009, audit included 22 findings, 16 of which were repeated in the June 30, 2010, report. See Attachment A for more information.
- 5) The district has shown unsatisfactory progress in eliminating the deficit. The deficit has increased from \$3,000,000 at June 30, 2009, to over \$7,000,000 at June 30, 2010. The deficit is expected to increase further, to over \$10,000,000 at June 20, 2011.
- 6) On July 11, 2011, Highland Park Schools' Superintendent Edith Hightower wrote to State Superintendent Mike Flanagan advising that the district currently has a short-term state aid note outstanding with the Department of Treasury in the amount of \$11,152,865 that it is not able to pay to the Michigan Finance Authority. In order to avoid a default, the district requested a state school aid adjustment of \$4,190,000 to be paid back over a four (4) year period. I approved the district's hardship request under Section 15 of the State School Aid Act to allow this adjustment.

In addition to the assessment above related to Highland Park Schools and the six (6) critical factors that the Department developed to assist in analyzing a district's level of financial stress, the following factors were also considered:

- The Highland Park School's blended pupil count used per statute for the purpose of calculating state school aid dropped from 1,858 in

2009-10 to 1,331 in 2010-11. That represents a decrease of 527 pupils or 28%. The next highest percent decrease in pupil counts between 2009-10 and 2010-11 for a district with more than 10 pupils is 17%. The precipitous decline in pupils is critical as school funding in Michigan continues to be based on the number of pupils. Based on the Highland Park Schools' per pupil foundation of \$7,936 for the 2010-11 school year, the 527 pupil loss represents a reduction of \$4,182,272 which equates to 20% of the prior year's revenue.

- As a result of the district's failure to meet federal procurement standards, the district has lost approximately \$230,000 in federal food and nutrition funds. Consequently, the corresponding food and nutrition costs have been covered with general funds which further exacerbates the general fund deficit.

### **III. Conclusion**

Section 12(4) of 2011 PA 4, the "Local Government and School District Fiscal Accountability Act", states that the purpose of a Preliminary Review is to determine if a finding of probable financial stress is warranted. It further states that if a finding of probable financial stress is made, the Governor shall appoint a Review Team to undertake a "school district's financial management review." The Department determined six (6) critical factors to use as a basis for determining a school district's financial stress. As outlined in the Preliminary Review Findings above, the Highland Park Schools meet all six (6) factors. Also, the district's precipitous decline in the number of pupils educated, the most important factor in generating /determining a school district's revenue, weighs heavily in this determination. Finally, the fact that the district is in violation of Sections 17 to 20 of the Uniform Budgeting and Accounting Act, another possible trigger of a Preliminary Review, has been taken into consideration. Based on the above information, as the State Financial Authority for a school district under PA 4, I have determined that a finding of probable financial stress exists. PA 4 now requires that the Governor appoint a Review Team.

Attachment

cc: Andy Dillon, State Treasurer  
John Nixon, State Budget Director  
James Bolger, Speaker of the House  
Randy Richardville, Senate Majority Leader  
Edith Hightower, Superintendent, Highland Park Schools  
Alma Greer, Highland Park Schools Board Chair

## Highland Park Schools – Audit Summary

The Department's Office of Audits notes the following issues in the audits of the School District of the City of Highland Park.

- Consistent findings in internal control areas:
  - Lack of timely review and reconciliation of general ledger
  - Bank Reconciliations not prepared timely
  - Lack of segregation of duties in reconciling of cash receipts, payroll and wire transfers
  - No supervisory journal entry review
  - Untimely deposits of cash
  - Lack of reconciliations in Food Service between cash collected and recorded and amounts deposited in the bank
  - Inefficient internal controls in the collections of Athletic Funds and the deposits of cash
  - Lack of physical inventory of fixed assets and discrepancies between the fixed asset ledger and the general ledger
  - Inadequate support for 3<sup>rd</sup> party service providers by Board approved written contracts
  - Comingling of funds
- Total findings are consistently increasing in severity. Many of the findings are repeated in subsequent years.
  - 2005 – 8 findings
  - 2006 – 16 findings (6 repeated from prior year); 6 material weaknesses and 4 material noncompliance; questioned costs of \$12,674
  - 2007 – 23 findings (10 repeated); 9 material weaknesses and 13 material noncompliance; questioned costs of \$1,718,153
  - 2008 – 23 findings (16 repeated); 13 material weaknesses and 9 material noncompliance; questioned costs of \$40,418
  - 2009 – 22 findings (15 repeated); 14 material weaknesses and 9 material noncompliance; questioned costs of \$122,331
  - 2010 – 19 findings (16 repeated); 12 material weaknesses and 7 material noncompliance; \$287,533 questioned costs.