



STATE OF MICHIGAN
DEPARTMENT OF TREASURY

RICK SNYDER
GOVERNOR

NICK A. KHOURI
STATE TREASURER

DATE: December 1, 2017

TO: Governor Rick Snyder

FROM: Romaneir Johnson, Executive Director
Financial Review Commission

**SUBJECT: Detroit Financial Review Commission (FRC) - Biannual Report for the
Detroit Public Schools Community District (DPSCD) No. 3**

Pursuant to the requirements of Section 6(8) of Public Act 181 of 2014, the Michigan Financial Review Commission Act (the “Act”), this report is being filed on behalf of the Detroit Financial Review Commission. A copy of this report will be delivered to the Senate Majority Leader, the Speaker of the House of Representatives, the Superintendent of the Detroit Public Schools Community District (“DPSCD”), and will be posted on the FRC’s Michigan Department of Treasury website located at <http://www.michigan.gov/treasury/>.

Pursuant to Section 6(1) of the Act, the FRC’s oversight of the DPSCD began on the date the District became a qualified as a District, which was June 21, 2016. The FRC has the legislative, fiscal, and administrative authorities and duties as prescribed by the Act. This is the FRC’s third Bi-annual report.

Statutory Oversight Activities

Sections 6 and 7 of the Act describe various duties and responsibilities for which the FRC are statutorily required to perform. Below is a summary of the status of these requirements.

Requirement	FRC Act Sec. No.	Compliance
FRC review and approval of all applicable contracts	6(6)	DPSCD has submitted (32) applicable contracts. All have been approved by the FRC.
DPSCD and its CFO provides needed information and documents to the FRC and attend FRC meetings as needed	6(7), 7(d), and 7(o)	DPSCD representatives have been responsive to requests for information, documents and have attended meetings when requested to attend.
FRC review and approval of collective bargaining agreements (CBAs)	6(9)	DPSCD have a total of (8) CBA’s to be ratified this year. A total of (7) CBA’s have been presented to the FRC and subsequently approved by the FRC. The last bargaining union is currently in negotiation with the District representatives and it is expected to be presented to the FRC in the near future.
Quarterly debt service certifications	6(11)	Detroit Public Schools (DPS) has provided all the required quarterly certifications. The new District, DPSCD has not issued any debt.

FRC review of DPSCD revenue estimates	7(a)	DPSCD has provided its revenue estimates to the FRC in connection with its budget submissions per subsection 7(c) of the Act.
FRC review and approval of the annual budget and accompanying budget amendments	7(c)	DPSCD submitted its FY 2018 adopted budget to the FRC and it was approved by the FRC membership on June 26, 2017. DPSCD submitted their first budget amendment for FY 2018 and it was approved by the FRC on October 30, 2017.
FRC review and approval of requests to issue debt	7(e)	DPSCD has not submitted any requests to issue debt.
FRC review compliance by a qualified school district with a deficit elimination plan under article I of the state school aid act of 1979.	7(f)	DPSCD has not been required to submit a deficit elimination plan.
FRC approval of the Chief Financial Officer's appointment	7(h)	The previous CFO resigned from the District effective June 30, 2017. DPSCD submitted a proposed appointment of a new Chief Financial Officer, Jeremy Vidito for the FRC's approval and he was approved at the November 20, 2017 FRC meeting.
FRC approval to alter the DPSCD Superintendent's contract or to terminate the DPSCD Superintendent	7(i)	FRC approved the proposed DPSCD Superintendent's contract on May 22, 2017.
FRC review and approval of reimbursements for out-of-state travel	7(q)	DPSCD submitted (6) reimbursement requests for out-of-state travel to the FRC. All have been approved.

Financial Update –DPSCD

Based on DPSCD's No. 1 FY 2018 budget amendment, they are projecting that the District will conclude the fiscal year, which ends on June 30, 2018, with a General fund surplus of approximately \$4.3 million, and a General fund balance of approximately \$92.8 million. The source of the General fund balance is expected to be primarily from one-time transfers, one-time asset sales, and underspending of personnel costs. Hiring qualified personnel continues to present a challenge for the District. Currently, vacancies supported by General funds total approximately \$38.2 million.

The District's ending cash balance at the close of September 2017 was \$64.4 million. The District has sufficient cash-on-hand to ensure timely payroll payments, payments to vendors, and support of other expenses for the remainder of the fiscal year. The district did not have to borrow against its' September State Aid payment for the first time in years.

At the time that this report was developed, DPSCD had no debt service payment requirements.

Financial Update –DPS

As statutorily required, the District provided its quarterly debt obligation summary for DPS. According to the 1st quarter report for FY 2018, DPS's principal balance for the reporting period was \$2.1 billion. A total of \$170.7 million of debt service payments are due in FY 2018 and the District paid \$15.8 million to-date against this obligation. DPS has a plan to pay off \$570 million

in operating debts over an 11-year period. The remaining bonded debt is projected to be paid by calendar year 2041 along with amounts owed to the School's Revolving Fund when debt service requirements fall below 7 mills. The FRC will continue to monitor DPS's management of debt to ensure payments continue to be made timely.

FY 2018 Budget Review

Pursuant to Section 7(c) of the Act, the FRC is required to review, modify, and approve proposed and amended operational budgets of a qualified city or qualified school district. A proposed budget or budget amendment does not take effect unless approved by the FRC.

Adopted FY 2018 Budget

Mr. Demetriou, previous CFO for DPSCD, presented a FY 2018 adopted budget to the FRC which projected an operating surplus of \$4.4 million for the fiscal year ending June 30, 2018. The FY 2018 adopted budget was approved at the June 26, 2017 meeting and included the following assumptions:

1. **Revenues:** Per Governor Snyder's FY 2018 spending plan, which was presented to Legislator on February 8, 2017, the District projected a \$99 increase in foundation allowance. The District projected \$475.7 million in State's revenues appropriation. This projection is based on an estimated DPSCD student enrollment of 47,148 (43,148 DPSCD & 4,000 Educational Achievement Authority (EAA)). Also, the District is projecting an additional increase in revenue of \$1.3 million from the enhancement millage due to the EAA student count.
2. **Expenditures:** The District's projected expenditures are based on the following assumptions:
 - Staffing costs were budgeted to increase by 3.0% across the board for all collective bargaining agreements that were in negotiation;
 - Health benefits were budgeted to increase by 5.5% effective January 1, 2018.
3. **Vacancies:** \$18.0 million was allocated in the budget to support vacancies. The FY 2018 adopted budget allocated \$8.0 million for DPSCD and \$10.0 million for the EAA to account for vacancies that will have an impact on the General fund operational budget.
4. **Contingency:** The FY 2018 adopted budget allocated \$10.0 million in contingency funding for unexpected costs.
5. **Operating Surplus and Fund Balance:** DPSCD's FY 2018 adopted budget includes a projected operating surplus of \$4.4 million and fund balance of \$80.1 million .
6. **Transitional Fund Summary:** Out of the \$25.0 million of transitional funds allocated to DPSCD, \$5.3 million was expensed in FY 2017, \$9.6 million is projected to be expensed in FY 2018, \$5.1 million is projected to be expensed in FY 2019, and a remaining minimum cash balance of 5.0 million.

7. **Equipment and Capital:** The FY 2018 adopted budget allocated \$8.0 million for capital and equipment.

Proposed FY 2018 Budget Amendment No. 1

The District's representative presented an update to the FY 2018 adopted budget that included proposed changes to the assumptions used to develop the FY 2018 budget amendment No.1, which was approved by the FRC at the October 30, 2017 meeting. The updated assumptions are as follows:

1. **Revenues:** A \$9.1 million increase in federal revenue, primarily due to Title IA. The student count has increased by 2,226; however, this increase is not addressed in this budget amendment. The projected increase resulting from a higher student enrollment approximately \$11.0 million in additional revenue.
2. **Expenditures:** Expenditures have increased by \$12.5 million in the following areas:
 - \$3.3 million, Information Technology;
 - \$1.3 million, Finance;
 - \$7.9 million, Operations

It should be noted that these increased expenditures are expected to be off-set by reductions of expenses in other areas.

3. **Vacancies:** Budget to support vacant positions increased over the FY 2018 adopted budget of \$8.0 million to support DPSCD and \$10.0 million for EAA to an amended combined budget of \$38.2M to account for all vacancies that has impact on General Fund (GF) operational budget.
4. **Contingency:** The FY 2018 adopted budget's General fund contingency funding went from 10.0 million to \$8.9 million in this budget amendment.
5. **Operating Surplus and Fund Balance:** DPSCD's FY 2018 adopted budget projects an operating surplus of \$4.4 million and ending fund balance of \$80.1 million. The FY 2018 budget amendment No.1 projects an operating surplus of \$4.3 million, and ending fund balance of \$92.8 million. This budget amendment is projecting an unaudited increase in beginning fund balance projection of \$12.8M from FY18 adopted beginning fund balance projection of \$75.7M to FY 2018 amendment budget No.1 beginning fund balance projection of \$88.5M.
6. **Transitional Fund Summary:** Of the \$25.0 million transitional funds allocated to DPSCD, \$5.3 million was expensed in FY 2017, \$9.6 million is projected to be expensed in FY 2018, \$5.1 million is projected to be expensed in FY 2019, and a remaining minimum cash balance of 5.0 million is projected.

7. **Equipment and Capital:** The amended capital and equipment budget was increased from \$8.0 million in the FY 2018 adopted budget to \$10.0 million in the FY 2018 budget amendment No. 1.

Summarization of DPSCD Budget Status as of the FY 2018 Budget Amendment No. 1:

According to the FY 2018 Budget Amendment No. 1, if the district does not fill vacant positions (\$38.2 million built in budget to support vacant positions), or spend the \$10.0 million of contingency funding by year end, the District's projected year end surplus will increase by \$48.2 million.

Collective Bargaining Agreements (CBA's)

This year, the District actively negotiated a total of 8 CBA groups. The District ratified the Detroit's Teacher Federation (DTF) CBA on June 12, 2017 and it was approved by the FRC on July 27, 2017. The District's representative presented an additional 6 unions (AFSCME, DAEEOE, Teamsters, Paras SSAS, Para NHA, & NISP) with ratified CBA's to the FRC. These CBA's were approved by the FRC on November 20, 2017. The aforementioned CBAs each have 3-year terms. The 3rd year term is non-economic and allows the each contract to be reopened for negotiations by March 2019. The cost of the ratified CBAs presented to-date have been below the approved FY 2018 adopted budget. The Detroit Organization of School Administrators and Supervisors (OSAS) CBA is currently being negotiated and is expected to be submitted to the FRC for approval in the near future.

District's Work Plan

The District's representative presented to the FRC a financial "Turn-Around" strategic/work plan, which will be implemented immediately. The highlights of the District's plan will address the following areas of concern:

- Reorganizing/restructuring timeline and projected budget development;
- Implementing zero-based budget for the FY 2019 adopted budget;
- Shifting from contracted services to district personnel;
- Implementing professional development for all employees;
- Establishing internal fiscal control, policies and procedures which promote efficiency and accountability;
- Implementing a district-wide audit to determine the physical infrastructure needs of schools;
- Developing and implementing a five-year capital budget and improvement plan; and
- Developing and implementing a metric based service delivery evaluation system (Key Performance Indicator system (KPI)).

This work plan will assist with the stabilization of the District during the restructuring process and is expected to address long-term strategic planning, enhance professional development, and resolve long-standing internal control issues.