



STATE OF MICHIGAN
DEPARTMENT OF TREASURY

RICK SNYDER
GOVERNOR

NICK A. KHOURI
STATE TREASURER

DATE: November 29, 2018

TO: Governor Rick Snyder

FROM: Shelbi Frayer, Executive Director
Chelan Burks-Andrews, Financial Specialist
Financial Review Commission

SUBJECT: Detroit Financial Review Commission (FRC) - Biannual Report for the Detroit Public Schools Community District (DPSCD) No. 5

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 June 21, 2016, the date the District became qualified as a District. The FRC has the legislative, fiscal, administrative authorities, and duties as prescribed by the Act.

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 submitted 122 applicable contracts. The FRC approved 122 applicable contracts.
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 CBAs that have been ratified, and 3 that required a letter of agreement to amend. The FRC approved 8 CBAs and 3 LOA.
Quarterly debt service certifications.	6(11)	Detroit Public Schools (DPS) provided all required quarterly certifications. The new District, DPSCD has not issued any debt.

FRC review of DPSCD revenue estimates.	7(a)	DPSCD 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)	DPS submitted one amendment to the FY 2018 budget and one amendment to the FY 2019 budget to the FRC, both amendments were approved by the FRC on June 25, 2018. DPSCD submitted its FY 2019 adopted general fund budget to the FRC and it was approved by the FRC on April 16, 2018. The FY 2018 and FY 2019 capital projects budgets and FY 2019 food service budget were submitted to the FRC and approved on June 25, 2018. DPSCD submitted one amendment to the FY 2018 general fund budget and one amendment to the FY 2018 food service budget, both amendments were approved by the FRC on June 25, 2018. DPSCD submitted one amendment to the FY 2019 capital projects budget and it was approved by the FRC on November 19, 2018.
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)	DPSCD submitted its appointment of its Chief Financial Officer. FRC approved the appointment on November 20, 2017.
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 124 reimbursement requests for out-of-state travel to the FRC. FRC approved 124 reimbursement requests.

Financial Update – DPSCD

Based on budget projections as of September 30, 2018, the District estimates it will finish the fiscal year ending June 30, 2019, with a general fund surplus of approximately \$8.0 million, and a general fund balance of approximately \$150.0 million.

The District's ending cash balance at the close of September 2018 was \$140.0 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.

Financial Update – DPS

As statutorily required, the District provided its quarterly debt obligation summary for DPS. According to the 3rd quarter report for FY 2019, DPS's principal balance for the reporting period was \$1.9 billion. A total of \$223.5 million of debt service payments are due in FY 2019 and the District paid \$59.0 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 2049 along with amounts owed to the School Loan 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 and 2019 Budget and Budget Amendment 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.

DPSCD FY 2018 Proposed Budget Amendment No. 3 – General Fund

The District's Chief Financial Officer (CFO) presented an overview of the proposed changes to the FY 2018 adopted budget (amendment No. 3) which was approved by the FRC at the June 25, 2018 meeting. The updated assumptions are as follows:

1. **Revenues:** A decrease in total revenue and sources of \$76.1 million, primarily due to a decrease of \$7.3 million in local sources due to a decrease in rent, private donations, investment revenue and to prevent an overpayment of Act 18 revenue, a decrease in state sources of \$5.8 million due to a decrease in 31a revenue, offset by an increase in Great Start and First Robotics revenue and a decrease in federal sources of \$63.1 million due to a decrease in Title IA, Title IIA and IDEA funding.
2. **Expenditures:** Expenditures have decreased based on the projected final expenditures for reimbursable grants, the reduction in general fund vacancies and contract services. Expenditures have decreased by \$40.0 million in the following areas:
 - \$20.9 million, Purchased services
 - \$7.6 million, Supplies
 - \$6.7 million, Equipment and capital
 - \$4.8 million, Title I restricted
3. **Vacancies:** Personnel savings from vacancies is projected to reduce the budgeted expenditures by \$51.6 million which has a positive impact on the general fund operational budget.
4. **Contingency:** The FY 2018 budget amendment No. 3 eliminated \$24.6 million in contingency; \$18.0 million general fund, \$3.3 million special education fund, \$2.8 million Act 18 fund and \$.5 million state transition fund.
5. **Operating Surplus and Fund Balance:** DPSCD's FY 2018 adopted budget amendment No. 2 projected an operating surplus of \$17.5 million and ending fund balance of \$96.4 million. The FY 2018 budget amendment No. 3 projects an operating surplus of \$55.7 million and ending fund balance of \$134.6 million.
6. **Transitional Fund Summary:** Of the \$25 million transitional funds allocated to DPSCD; \$4.8 million was expensed in FY 2017, \$3.7 million was expensed in FY 2018,

\$10.0 million was transferred to the capital projects budget in June 2018 and the remaining \$6.5 million is projected to be spent before June 30, 2019.

7. **Equipment and Capital:** The amended capital and equipment budget of \$3.3 million was decreased by \$6.7 million from \$10 million in FY 2018 budget amendment No. 3. One-time investments were removed from the operating budget and will be included in the capital projects budget.

DPSCD FY 2018 Proposed Budget - Capital Projects Fund

The District's CFO presented an overview of the proposed FY 2018 budget to the FRC which was approved by the FRC at the June 25, 2018 meeting. The capital projects proposed budget establishes the capital projects fund which will account for the necessary maintenance and repairs of the District's buildings and equipment. The District will budget non-recurring capital expenditures as part of the capital projects fund. This will shift one-time capital expenditures of \$1.0 million out of the general fund's restricted reserve. The capital projects fund budget includes projections for immediate health and safety expenditures related to the roof replacement of Palmer Park.

DPSCD FY 2019 Proposed Budget - Capital Projects Fund

The District's CFO presented an overview of the proposed FY 2019 budget to the FRC which was approved by the FRC at the June 25, 2018 meeting. The capital projects proposed budget is funded with restricted reserve from the general operating budget that includes bond settlement funds of \$0.7 million, EAA transition funds of \$0.9 million and state transition funds of \$7.5 million. The capital projects fund budget includes projections for immediate health and safety expenditures related to the roof replacement of six other schools, building maintenance and bond settlement repairs related to Cass Tech HVAC and football field.

DPSCD FY 2019 Proposed Budget Amendment No. 1 - Capital Projects Fund

The District's CFO presented an overview of the proposed changes to the FY 2019 adopted budget (amendment No. 1) which was approved by the FRC at the November 19, 2018 meeting. Budget amendment No. 1 transfers \$3.1 million from the general fund's surplus to the capital projects fund. The transfer will fund the purchase of the Elkay hydration stations, installation of the stations and site improvements associated with the water hydration stations. The District has raised \$2.5 million for the project through private funds and is working to fully fund the project through a fundraising partnership with United Way. The District will replenish the \$3.1 million from the general fund's surplus when United Way closes out the campaign.

DPSCD FY 2018 Proposed Budget Amendment No. 3 – Food Service Fund

The District's CFO presented an overview of the proposed changes to the FY 2018 adopted budget (amendment No. 3) which was approved by the FRC at the June 25, 2018 meeting. Budget amendment No. 3 increases the projected surplus to \$1.9 million at the end of the fiscal year due to a transfer from the general fund for a prior year adjustment. An increase in total

revenue and sources of \$0.043 million, primarily due to an increase in state sources due to an increase in lunches provided to the students. Total expenditures are decreased by \$0.043 million based on the projected final expenditures for the grants, expenses have been aligned with the revenues.

DPSCD FY 2019 Proposed Budget – Food Service Fund

The District's CFO presented an overview of the proposed FY 2019 budget to the FRC which was approved by the FRC at the June 25, 2018 meeting. The food service proposed budget is a balanced budget with substantial contingency and all positions are fully funded. The overall increase in revenue of \$1.4 million results from the increase in student enrollment. Total expenditures increase of \$1.4 million are associated with the increase in student enrollment.

DPS FY 2018 Proposed Budget Amendment No. 1

The District's CFO presented an overview of the proposed changes to the FY 2018 adopted budget (amendment No. 1) which was approved by the FRC at the June 25, 2018 meeting. Budget amendment No. 1 increases the projected surplus to \$1.1 million at the end of the fiscal year. A decrease in total revenue and sources of \$0.009 million, primarily due to a decrease in state sources from an adjustment in Renaissance Zone funding to reflect actual amounts collected. Total expenditures decreased by \$1.1 million, primarily due to a decrease in support services of \$0.3 million due to lower than anticipated audit fees and legal fees, an increase in the stabilization bonds of \$0.1 million due to the new tax policy which increases interest and a decrease in emergency loan debt service of \$0.9 million based on updated debt schedules.

DPS FY 2019 Proposed Budget Amendment No. 1

The District's CFO presented an overview of the proposed changes to the FY 2019 adopted budget (amendment No. 1) which was approved by the FRC at the June 25, 2018 meeting. Budget amendment No. 1 increases the projected surplus to \$7.2 million at the end of the fiscal year. An increase in total revenue and sources of \$0.3 million, primarily due to an increase in local sources based on conservative property tax value increase of .5 percent. Total expenditures are increased by \$0.3 million, primarily due to an increase in the stabilization bonds of \$0.3 million due to the new tax policy which increases interest and a decrease in MPSERS interest of \$0.9 million based on updated debt schedules.

Facility Condition Assessment

The District retained OHM Advisors to do a comprehensive needs assessment of the District's 100 school facilities. OHM Advisors conducted a facility-by-facility assessment and inspection to determine the condition of each facility including the playground. The July 2018 assessment reported that the District's school facilities have approximately \$526.7 million in capital improvements needs and deferred maintenance. The assessment projected that the figure will grow to \$1.502 billion by 2023 if no action is taken.

The District transferred \$10.0 million into the capital projects fund in June to address outstanding critical needs repairs and replacements related to roofs, HVACs and ground repairs. The District subsequently transferred \$3.0 million into the capital project fund in November for the water hydration stations. The District plans to allocate \$10.0 million in the fall of 2019 for the next phase of critical needs repairs and replacements related to roofs and HVACs. The work will start in the spring of 2020.

Final Audit Update - DPSCD

The District's FY 2018 audit report was filed by the required November 1st deadline. The District's audited FY 2018 financial statements reflect a surplus of \$49.0 million of revenue over expenditures and year end fund balance of \$141.0 million.

Audit Findings

The audit revealed that the District has material weaknesses and material noncompliance with laws and regulations. These material weaknesses and material noncompliance were primarily the result of poor general ledger (GL) internal controls and noncompliance with federal grant program spending and monitoring. The District has developed a corrective action plan to address the audit findings and implemented the necessary changes to ensure corrective action occurs by the end of FY 2019.

Final Audit Update - DPS

The District's FY 2018 audit is still ongoing as such the report was not filed by the required November 1st deadline.

Collective Bargaining Agreements (CBAs)

The District has been in an extensive and lengthy contract negotiation with the Detroit Organization of School Administrators and Supervisors (OSAS). OSAS submitted its first proposal for contract negotiations on March 27, 2017. The agreement goes far beyond the traditional surface level contract issues of wages and benefits, all 18 articles were rewritten and made more concise to better align with the District's core values and strategic initiatives. It was the last pending agreement to be settled among the District's eight unions, now all have three-year agreements. The District ratified the three-year OSAS collective bargaining agreement (CBA) on November 8, 2018.

On October 26, 2018, the Detroit Board of Education approved the 2018-2019 Letter of Agreement (LOA) reached with the American Federation of State, County and Municipal Employees Council, 25, Local 345 (AFSCME) and the Detroit Federation of Para-Professionals, Local 2350 (DFP). The LOA reached with AFSCME and DFP provided the terms and conditions that provides compensation enhancement of an additional dollar per hour worked for food preparation and serving workers. The CBA and the LOA were approved by the FRC on November 19, 2018.