State and Regional Support for District Financial Stability, JF

Agency: 350 Office of Superintendent of Public Instruction
Budget Period: 2011 Supplemental Session

Recommendation Summary Text (Short Description):
Superintendent Dorn requests $1.655 million to expand Educational Service Districts (ESDs) and the Office of Superintendent of Public Instruction (OSPI) fiscal support to school districts, as districts enter a period of severe financial distress.

Most school districts across the state face severe financial shortfalls in this biennium. State and local revenue increases are being outpaced by increases in salary, benefit, retirement, and utilities and fuel costs. Added to this are pressures to expand remediation for struggling students, buy new curriculum, train teachers to meet higher expectations, respond to the needs for the classes of 2010 and 2011 in order to increase graduation rates further, and reduce teacher and staff workloads. Statewide school districts' ending fund balances are dropping and further increases in costs without a commensurate increase in funding will cripple many. Districts need more support from regional finance experts, and OSPI must provide state oversight for many more districts that will likely fall under state-imposed conditions for financial operations.

Fiscal Detail

Operating Expenditures		FY 2010	FY 2011	Total
ESD Regional Support	001-01	$0	$1,366,073	$1,366,073
OSPI Finance Support	001-01	$0	$289,602	$289,602
Total Cost		**$0**	**$1,655,675**	**$1,655,675**

Staffing	FY 2010	FY 2011	Annual Avg.
Total FTEs Requested	**0**	**1.3**	**.65**

Package Description

Background
Districts are required by state law to expend only as much as their revenue and cash balances will cover. When districts cannot balance their budget, state law permits them to budget future receivables to cover current expenses. However, this step put districts into Binding Conditions status. Binding Conditions subject the district to financial oversight by the state; OSPI typically assigns day-to-day oversight to the regional Educational Service District (ESD) staff. Where districts do not maintain requirements of the Binding Conditions, OSPI can withhold apportionment payments.

Six districts are on Binding Conditions for the 2009-10 school year. Typically 1-2 districts are on Binding Conditions at any one time.

Districts are on the brink of financial emergency in many areas of the state. Ending fund balances (EFB) for most districts are budgeted at an all-time low for the 2009-10 school year, and well below prudent levels on a statewide average. Districts do not have the state funding budget capacity to cover new costs; local levy funds are subsidizing state funding inadequacies and are growing too slowly to absorb new costs.

- Four districts that are not currently on Binding Conditions have an ending fund balance of less than 1% of total operating funds. The risk associated with these districts is extreme; the total operating budgets of the 4 districts is $454 million while reserves total $2 million.
- Districts with less than 1,000 students have EFBs that have dropped from 15.8% in 1999-00 to 7.8% in 2009-10 school year (budgeted). (Small districts need much larger EFB as emergency costs are frequently a greater percentage of their budget.)
- The state average EFB has dropped from about 6% in prior years to 4.6% for the 2009-10 school year (budgeted).
- In December 2009, 2008-09 EFB will be final and therefore we will have a clearer picture of 2009-10 EFB. We are carefully watching an additional 3 districts to determine if Binding Conditions are required once 2008-09 EFB is known.

Clearly, there are diminishing EFB cushions to fall back on. If a significant increase in state funding is not provided in the 2010-11 school year, many districts face insolvency unless they undertake deep reductions in staffing and services. Districts will likely have to deeply reduce transportation programs, increase class sizes, and close schools. These are very divisive issues within communities. Districts will need ESD support to develop budgets earlier in the cycle in order to notify and work with their community and hold community input meetings. The ESDs are regularly called into serve a mediation role with vocal community groups.

When districts' EFBs fall, districts must manage not only total revenue compared to expenditure, but also manage cash balances more carefully. For many districts this is a new level of complexity. Districts report that they more frequently must borrow interest-bearing funds at points during the school year in order to temporarily meet payroll requirements.

Anecdotally we understand a few districts are beginning to consider consolidation with neighboring districts. Financial insolvency will require additional districts to consider this. Consolidation is a very time intensive process for districts, ESD fiscal officers, ESD Superintendents, and for OSPI. The intensity of the process will be exacerbated by the simple fact that most districts will be reticent to consolidate with a financially insolvent district.

In summary, ESD fiscal offices must have additional capacity to provide: expanded and in depth analysis of financial position, projections of revenue and expenditures for future years, development of budget reduction scenarios and assistance in negotiating consolidations and/or other appropriate solvency solutions. ESD fiscal offices often work with staff and community members and groups in communicating and implementing cuts to programs or building(s) closure.

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OSPI must provide districts and ESDs with regular support around the development of budgets, implementation of Binding Conditions, advice and consultation about projecting district costs and revenue, routes to and implications of consolidation. There is a growing demand on the part of community groups for the Superintendent to intervene in district budget deliberations. The Superintendent must then work with groups to understand the law and local control, districts' budget capacity, and school closure process. Finally, as districts must budget more closely there is more work associated with compliance and implementation of current rules and formulas.

Proposed Solution
Expanded staff support is required at each of 9 ESDs and at OSPI. 10 finance experts are required statewide, and are covered by this request. Legal support to OSPI by the Attorney General will also need to expand (as legal considerations for consolidation expand).

Contact person
Jennifer Priddy, Assistant Superintendent, Financial Resources, (360) 725-6292
Jennifer.Priddy@k12.wa.us

Narrative Justification and Impact Statement

What specific performance outcomes does the agency expect?
The state interest is to have districts remain financially solvent. Financial solvency is improved when school districts receive good financial advice and support for community process to reduce budgets. For some, financial solvency may only be obtained when the districts voluntarily consolidate; a time consuming process that takes constant support of boards, superintendents, and staff.

Performance Measure Detail

Is this decision package essential to implement a strategy identified in the agency's strategic plan?
The agency strategic plan addresses additional resources for school districts:
Sufficient state resources are provided for every student to succeed through an efficient, equitable, and responsive K-12 funding system. However, the package alignment to the agency's strategic plan is a secondary and a relatively unimportant alignment. More critical is that the state address an emerging crisis in a core obligation to its citizenry. It is becoming more certain that one or more districts will become financially insolvent and will not continue to operate, turning over debt, assets, and future operations to the state or other districts. While some may want to dismiss this as a small-district problem, we cannot rule out that this failure may occur in one of the largest districts in the state.

Reason for change:
The change is required based on clear signals of financial distress in the school system.

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Does this decision package provide essential support to one of the Governor's priorities?
Yes, the Governor has placed a high emphasis on district financial well-being.

Does this decision package make key contributions to statewide results? Would it rate as a high priority in the Priorities of Government process?
Unknown. The level of financial distress that drives this request has not been contemplated in prior POG efforts. Certainly a stable education system is implicit in state priorities.

Impact on Clients and Services

Communities, students, parents, and school staff are immediately impacted by school district financial distress. Any assistance to help districts more evenly reduce services or thoughtfully consolidate will have a positive impact. Unfortunately, any positive impact only lessens the real negative impact clients will experience rather than eliminate the negative impact.

Impact on Other State Programs

None.

What alternatives were explored by the agency, and why was this alternative chosen?
There are no alternatives to the request.

What are the consequences of not funding this package?
In an operation the size of our public schools, serving 1 million students in 2,000 buildings with 100,000 staff, it is impossible to predict the exact impact. However, if support is not provided to districts, navigation through the upcoming school years will not benefit from independent expert advice and counsel about how to reduce services or consolidate with neighbors.

What is the relationship, if any, to the state's capital budget?
There is not direct relationship to the state's capital budget. However, there is an indirect relationship at the district level. Technically operating and capital funds of a district are separate and distinct. However, where districts reach a desperate financial situation, the relative solvency of capital funds compared to operating funds will require expertise to ensure that capital programs are not compromised. In addition, where consolidation conversations must take place, a district's capital assets and debt are a significant area of concern or opportunity in negotiations.

What changes would be required to existing statutes, rules, or contracts, in order to implement the change?
No statute change is required by funding this request. However, the Superintendent is committed to working with policymakers to improve and simplify decades-old statutes related to district consolidation. The Superintendent will undertake a WAC review for

possible revision during 2009-10 in order to implement any new rules by September 2010.

Expenditure Calculations and Assumptions:
Cost assumptions are based on: (1) current costs to attract appropriately qualified staff into finance positions and (2) ESD salary schedules. All other costs are standard employment costs.

Object Detail

		FY 2010	FY 2011	Total
A	Salary and Wages	$0	$83,044	$83,044
B	Employee Benefits	$0	$23,027	$23,027
C	Contracts	$0	$104,100	$104,100
E	Goods/Services	$0	$63,431	$63,431
G	Travel	$0	$10,000	$10,000
J	Equipment	$0	$6,000	$6,000
N	Grants	$0	$1,366,073	$1,366,073
	Interagency Reimbursement	$0	$0	$0
	Other	$0	$0	$0
	Total Objects	**$0**	**$1,655,675**	**$1,655,675**

Expenditures & FTEs by Program

Activity Inventory Item	Prog	Staffing			Operating Expenditures		
		FY 2010	FY 2011	Avg	FY 2010	FY 2011	Total
A002 Administration	021	0	1.3	.65	$0	$289,602	$289,602
A010 Educational Service Districts	028	0	0	0	$0	$1,366,073	$1,366,073
Total Activities		**0**	**1.3**	**.65**	$0	$1,655,675	$1,655,675

Six-Year Expenditure Estimates

Fund	09-11 Total	11-13 Total	13-15 Total
General Fund-State	$1,655,675	$3,308,350	$3,308,350
Expenditure Total	**$1,655,675**	**$3,308,350**	**$3,308,350**
FTEs	**1.3**	**1.3**	**1.3**

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Distinction between one-time and ongoing costs:
All operating costs are on-going until state funding improves substantially and district ending fund balances return to prior levels.

Budget impacts in future biennia:
The amounts will increase with inflation and cost of living adjustments.