AN INDEPENDENT VIEW OF THE FINANCIAL POSITION OF THE MT. VERNON COMMUNITY SCHOOL CORPORATION

FALL, 2011

PRESENTED BY:

EDUCATIONAL SERVICES COMPANY
3535 E. 96th Street, Suite 126
Indianapolis, IN 46240
317-818-3535 (Phone)
317-351-3535 (Toll Free)
317-818-3533 (FAX)
www.educationalservicesco.com

REPRESENTED BY: Timothy L. Armstrong, Consultant

INTRODUCTION

The Mt. Vernon Community School Corporation is in financial crisis. This statement certainly comes as “old news” to the Board of Education, professional staff, and community of the school corporation. They have been collaboratively working to reduce expenditures and generate additional revenue (in what few ways they can) for the past three school years.

The Superintendent and Board of Education have asked Educational Services Company to review their overall financial picture, including the measures of cost reduction and revenue enhancement that have been implemented, with the goal of answering the question “have we missed anything?”

Following initial review of the recent financial history of the corporation, this question will be very difficult to answer. This consultant has seen very few cost reduction plans as complete and comprehensive as the one already implemented by Mt. Vernon Community Schools.

OUTLINE

This brief report will include the following sections:

- **What caused this financial crisis to occur?**

- **Could it have been avoided?**

- **What has been the response from the district to this point?**

- **What next?**

- **Summary**

WHAT CAUSED THE PROBLEM?

In a nutshell, the financial problems being faced by Mt. Vernon Community Schools were caused by the same factor that has hampered every public school district in Indiana—financial decisions were made on the assurance of certain revenues that, in the end, were taken away. One can agree or disagree with the reasons why the revenue promises made were lowered so significantly, but the fact remains that the loss of funding **came after important decisions were made**, leaving every school district with huge financial struggles—you are not alone.

It is important to note that the situation was not caused by reckless spending, inappropriate actions or illegal transactions. All the revenue and expenditures are properly documented and accounted for.

The two areas where these revenues were promised and then reduced are the General Fund and the tax-supported funds (Debt Service, Pension Debt Service, Capital Projects, Transportation, and Bus Replacement). We will briefly look at what happened in both areas.

THE SCHOOL GENERAL FUND IN INDIANA

The General Fund of an Indiana public school corporation is used for all revenue and expenses of a current nature except for student transportation. General Fund expenditures include salaries and benefits, supplies, purchased services, utilities, and those expenses normal to the daily operation of the school corporation.

The landscape of General Fund revenue for all school corporations in Indiana changed dramatically on January 1, 2009, when the school General Fund property tax levy was eliminated and the state took over responsibility for the majority of school operating revenue. Prior to that date, the school General Fund received its revenue from a combination of local property taxes and state funding, with the two combining to fund the amount required by the school funding formula set by the legislature.

The concept of taking the school General Fund off of the property tax rolls had been discussed for many years prior to its removal. During those discussions, most school organizations, such as the Indiana Association of School Business Officials, raised concerns about this for one main reason—what happens to school funding when state revenues are down?

THE SCHOOL GENERAL FUND IN INDIANA (CONTINUED)

Given the recent economic status of Indiana, the nation, and the world, we have found the answer to this question. The answer is less revenue for schools.

For calendar year 2010, the school funding formula passed by the legislature indicated that Mt. Vernon Community Schools would receive just under $19.3 million from the state to operate their General Fund. However, through executive order, the Governor reduced that amount to just over $18.3 million. The same $1 million reduction is now in place for 2011 and will continue. Additionally, legislation was passed to eliminate New Facility Appeals which provided funds for the heating, cooling and care of new square footage, and it was applied retroactively. Thus, Mt. Vernon lost an additional $369,933 that would have become a part of their basic grant. **<u>These are permanent cuts to the funding formula, a revenue promise that was significantly lowered after financial decisions were made.</u>** While the political explanation may differ from this consultant's opinion, the General Fund for the State of Indiana was balanced in part by taking away significant funding from public schools. The projected General Fund balance for the State of Indiana at the end of fiscal year 2012 is **$1.2 billion.**

The projected General Fund deficit for the Mt. Vernon Community School Corporation is $5.1 million at the end of 2011 and $4.6 million at the end of 2012. A comparison of the projected deficit for 2011 and 2012 indicates the cost cutting measures implemented to date have stopped the growth of the deficit. The problem is how to eliminate the remaining deficit.

THE PROPERTY TAX SUPPORTED FUNDS

The major funds that remain supported by property taxes for Indiana school corporations are the Debt Service Fund, the Pension Debt Service Fund, the Capital Projects Fund, the Transportation Fund, and the Bus Replacement Fund. Each of these funds are limited as to how much tax may be collected. The two Debt funds are limited to 18 months of debt payment; the Capital Projects Fund has a rate cap; the Transportation Fund has a levy cap (allowable increase for 2012 is 2.2%), and the Bus Replacement Fund is limited to the 12-year plan submitted by the district. In other words, property tax limits were already in place. Additionally, many communities have restricted, reduced, or eliminated property taxes in an effort to attract more businesses (Tax Increment Financing and Property Tax Abatements). Many of these have been issued in Hancock County.

However, in a move to further decrease property taxes after the school General Fund was removed, the legislature passed a bill limiting the amount of property tax that may be collected to a percentage of assessed valuation. For individual homeowners the limit is 1% of AV; 2% of AV for farmland, and 3% of AV for commercial property. In 2010, these cap limits were made a part of the Indiana Constitution through a voter referendum.

THE PROPERTY TAX SUPPORTED FUNDS (CONTINUED)

Over the past three years, the amount of property tax revenue lost by the Mt. Vernon Community Schools due to the property tax caps has been in excess of $3.6 million. As a comparison, neighboring Warren Township Schools in Marion county, a district almost four times as large, has an anticipated cap loss of $2.5 million for the same three year period. As many school districts have found, little tax revenue remains for Capital Projects, Transportation, and Bus Replacement after debt payments are made. While increases in property values could increase the amount of tax collected, that prospect was also severely damaged by overall economic conditions. In 2008, Mt. Vernon's A.V. was $1,027,316,569 and in 2011 Mt. Vernon's A.V. is $804,895,660, a 22% decrease in value.

Once again, the loss of significant property tax revenue took place **after important decisions were made.** The recent building projects undertaken by the Mt. Vernon schools were approved prior to 2008 at both local and state levels on the assumption of property tax revenue that is lost forever.

COULD THIS CRISIS HAVE BEEN AVOIDED?

What, if anything, could the Mt. Vernon Community Schools have done to avoid or limit the financial crisis they currently face? With a functioning crystal ball allowing them to see the future, they could possibly have done some things differently:

1. From 2000 through 2009, district enrollment grew at an average of 107 students per year, an increase of 48%. In the last year of this period, the increase was over 150 students. This type of growth for a district like Mt. Vernon puts tremendous pressure on all resources—physical, financial, and human. In order to address the physical space, some significant construction projects (approximately 402,000 total sq. ft. of classroom space in four different buildings) were undertaken and the amount of debt grew as a result. The amount of debt and corresponding payment schedules were approved at all levels **assuming certain levels of property tax rate and levy.** As already explained, those taxes have been greatly reduced. Would they have "built less" with a functioning crystal ball?

COULD THIS CRISIS HAVE BEEN AVOIDED (CONTINUED)

2. The overall economy of the world, our country, and our state began experiencing a variety of serious problems for a variety of serious reasons about the same time the Mt. Vernon schools were experiencing their growth spurt. More students require more services—teachers, administrators, and support staff. The district responded on behalf of their students by increasing these services at a cost to the General Fund **<u>and assuming certain levels of funding.</u>** Then, as already explained, the amount of revenue to the General Fund began declining for reasons beyond their control. Would they have "hired less" with a functioning crystal ball?

The crystal ball wasn't there and the decisions made by the district and the community were made with the best information available at the time. It is no longer of any value to look back, what remains a huge challenge for this community is dealing with the future.

WHAT HAS BEEN THE RESPONSE FROM THE DISTRICT TO THIS POINT?

As mentioned earlier in the report, this consultant has reviewed many cost reduction plans implemented by school districts across the state. The work done to this point by the Mt. Vernon Community Schools is, in the consultant's opinion, exemplary. It touches all areas—personnel (certified, support, administrative), energy, supplies, professional development, technology, employee benefits, maintenance, substitute teachers, vehicle usage, extra-curricular, and the list goes on. In addition to cost reduction, the staff and Board of Education have been actively engaging both state legislators and Department of Education staff to seek any and all assistance so that they may continue to meet the needs of the students in this community. It is also no secret that a general fund tax referendum, a vehicle to increase revenue outside of the property tax caps, was defeated by the voters in the community.

Regrettably, despite the many cost-reduction efforts, the crisis has not been solved. What remains, short of some type of involvement from the state, is more significant cost reductions , passage of a general fund tax referendum, or bankruptcy (whatever that looks like for an Indiana school district).

WHAT NEXT?

The final section of this report will deal with suggestions where additional expenditure reductions might be made. Some are severe, and many have a negative impact on students. As a career public educator, it pains the consultant to include some of these recommendations; however, they reflect the reality of the situation. The recommendations are in no particular order.

- **<u>Class Size</u>**-The number that teachers, parents, and administrators throughout the State of Indiana must come to grips with is **30+.** Not only Mt. Vernon, but all districts. With the changes to funding outlined in this report, that is the future for Indiana public schools unless the legislature increases per pupil funding in a significant fashion. Mt. Vernon is not currently at this number, but they must quickly move in that direction. Reduction-in-force notifications should be given next Spring to bring class sizes to this level. Alternative methods of delivering instruction in small specialty or upper level high school classes must be examined. The number of sections taught each day by secondary teachers may also need to increase.
- **<u>Transportation</u>**-Suspension, as soon as possible, of all bus transportation beyond that required by law (certain special education students). Daily transportation to and from school is a service that Indiana districts **<u>may</u>** provide. It is no longer financially feasible for the Mt. Vernon Schools to offer this service.

WHAT NEXT? (CONTINUED)

- **Employee Benefits**-It seems very likely that the Mt. Vernon Community Schools will be moving their health insurance to the State of Indiana plan as required by new legislation. Unless dramatic reductions in current costs can be realized, this move is imminent. A complete and thorough evaluation of the current plan should be conducted with the goal of reducing costs (to both employees and district). A Dependent Audit should be conducted and a Spousal Carve-Out highly considered (if a member's spouse has the option of health insurance through their employer, they should be taken off of the Mt. Vernon plan). Changes to benefits must also be on the table.

Employer contributions to any 403B, 401A, and VEBA accounts should be suspended. A plan as to when contributions would start again and if missed payments will be made up would need to be negotiated. Certain financial goals would need to be met before these contributions can return.

WHAT NEXT? (CONTINUED)

- **<u>Hiring</u>**-With rare exception, a complete hiring freeze should be continued. Following any resignation or retirement, a plan to absorb that position should be formulated.
- **<u>Accounts Payable</u>**-Invoices should be paid on-time if absolutely necessary, held if possible, and never early. The district should continue to work with vendors to possibly extend some payments dates. This does not save money, but can assist with the tenuous cash-flow position of the district. By statute, no late payment fees can be paid by the school corporation and therefore must be avoided or negotiated away.
- **<u>Professional Leave, Substitute Teachers</u>**-No professional leave requiring staff to be away from the job should be approved. The district's policy of not paying for professional leave and field trips from the General Fund should be continued, and no field trips should be paid from the Transportation Fund. The use of substitute teachers for any reason must be limited. Other staff, including administrative, must cover absences as much as possible.
- **<u>Custodial and Maintenance</u>**-Staffing in these categories must be carefully controlled. While the increase in square footage per custodian from 20,000 sq. ft. to 36,000 sq. ft. is a step in the right direction, one custodian per 50,000-60,000 sq. ft. of space many have to be the normal. "Fix only what is broken" may need to be the approach of the maintenance staff, even though not doing preventive maintenance can be costly in the future.

WHAT NEXT? (CONTINUED)

- **Outsourcing**-Consideration to the outsourcing of custodial, grounds, and maintenance, should be reviewed each year. As long as the Food Service program continues to be self supporting, outsourcing may not be necessary. However, if it ever has to be supplemented by the General Fund, outsourcing may become necessary. While the hard costs for these positions may not be less, removing a significant number of employees from worker's compensation insurance, FICA, and potential unemployment claims can save money. In addition, payments to these vendors can be made monthly which helps cash flow. Many companies who offer these services to school corporations will consider hiring current staff as part of their proposal.
- **Property/Casualty Insurance**-Any changes that will reduce premiums should be discussed with agent and insurer. Higher deductibles, creative self-insurance options, etc., must be examined. If not already self-insured on Worker's Compensation, that move can also lead to significant savings.
- **Current cooperative agreements**-All educational services currently provided through cooperative agreements must be continually evaluated. These would include special education and vocational services. In addition, if the district maintains membership in one of the Educational Service Centers, that must be evaluated on a cost vs. benefit basis. If large lump sum payments are being made for these services, perhaps a payment plan can be negotiated to assist with cash flow.
- **Facility Use**-The district should continue to charge the full operational cost of the facility to any group who uses space regardless of the nature of the group (not-for-profit, youth programs, etc., as well as for-profit groups).

WHAT NEXT? (CONTINUED)

- **Salaries and Wages**-All employee groups, including those with negotiated agreements, must weigh the unfortunate choice of jobs versus compensation. At this time, the Mt. Vernon Community Schools do not have the means to offer salary increases of any type, including those previously negotiated (step increases). In fact, without revenue increases from either a referendum or legislative changes, salaries and wages must be **decreased**, as they were for bus drivers this school year. A decrease can only come from fewer employees, lower salaries and wages, or some combination of both. With either or both options, all employees groups must be included. In addition, length of work day may need to be reduced for all hourly employees, as they have been for custodial and maintenance staff.

SUMMARY

The conclusion of this report is the same as the beginning—the Mt. Vernon Community School Corporation is in financial crisis. Some final thoughts:

- **Cuts won't be enough**-Despite the numerous budget reductions already implemented and even with those suggested in this report, the Mt. Vernon Schools likely cannot "cut" their way out of this problem. Some type of additional revenue must be found. If not by local referendum, then from the State of Indiana through legislative action. Revenue growth through increased enrollment and/or increased assessed valuation will not be enough, and current trends have both of these declining.
- **Community Impact**-As some or all of the additional cuts are implemented, what impact does that have on this community? Will student achievement drop? Will families move out of the district? Will employees seek opportunities elsewhere? The community must ponder these questions very carefully.
- **The District is not alone**-Although the unfortunate timing of events have put the Mt. Vernon schools in financial crisis earlier than others, many will follow in 2013. All public entities in Indiana—cities, towns, libraries, school districts—are being choked financially.