



STATE OF MICHIGAN
DEPARTMENT OF TREASURY

RICK SNYDER
GOVERNOR

NICK A. KHOURI
STATE TREASURER

DATE: March 1, 2018
TO: House and Senate K-12 Appropriations Subcommittees
FROM: Nick A. Khouri, State Treasurer
SUBJECT: Quarterly Report to the Legislature on Deficit Districts

OVERVIEW

On July 7, 2015, the Governor signed into law PAs 109-114, giving the Department of Treasury (the Department) additional financial authority and responsibilities over K-12 school districts, intermediate school districts (ISDs), and public school academies (PSAs).

Pursuant to MCL §380.1220(2), the State Treasurer shall submit quarterly interim reports to the Legislature concerning school districts, ISDs, and PSAs that are subject to periodic financial status reports or are under an Enhanced Deficit Elimination Plan (EDEP). Moreover, on a quarterly basis, the State Treasurer shall publicly present those quarterly interim reports to the appropriations subcommittees of the Legislature responsible for K-12 state school aid appropriations. This is the Department's 10th quarterly report to the Legislature.

EARLY WARNING

Pursuant to MCL §380.1219(3), the State Treasurer is required to determine whether or not potential fiscal stress exists within a school district, ISD or PSA; that an operating deficit may arise within a school district, ISD, or PSA during the current school fiscal year or the following 2 school fiscal years; or that a school district, ISD or PSA may be unable to meet its financial obligations while also satisfying the districts, ISDs, or PSAs obligations to provide public education services in a manner that complies with state law.

The Department uses 2 methods to determine the existence of potential fiscal stress. First, a projection model that extrapolates enrollment, revenue, expenditure, and fund balance for the subsequent two school fiscal years using weighted historical trends. Second, a tri-annual budget review of all school districts, ISDs and PSAs scheduled to coincide with budget amendments in March, July, and October. The Department communicates with identified districts, ISDs, and PSAs before making a final determination of whether or not potential fiscal stress exists.

Pursuant to MCL §380.1219(5), if the State Treasurer declares that potential fiscal stress exists within a school district, ISD or PSA, then the governing body has 60 days to enter into a contract with an ISD or authorizer to perform an administrative review. Within 90 days after entering into the contract, the ISD shall complete the administrative review. School districts, ISDs, or PSAs that do not enter into a contract may be subject to Department periodic reporting.

2016 POTENTIAL STRESS

In 2016, 19 districts and PSAs were declared to have potential fiscal stress. Eighteen districts were identified using the financial projection model, and 1 district was identified through budget reviews. As of this report, only three of those districts remain subject to Department oversight:

| 2016 | School District/PSA | Administrative Review ISD/Authorizer |
|------|-----------------------------|--------------------------------------|
| 1 | Flat River Academy | Saginaw Valley State University |
| 2 | Kent City Community Schools | Kent Intermediate School District |

| 2016 | School District/PSA | Department Periodic Reporting ISD/Authorizer |
|------|-----------------------|--|
| 3 | Multicultural Academy | Bay Mills Community College |

2017 POTENTIAL STRESS

In 2017, 8 districts were declared to have the potential for fiscal stress. Seven districts were identified using the financial projection model, and 1 district was identified through budget reviews. As of this report:

- Algonac Community School District and Coloma Community Schools improved their financial position and are no longer subject to Department oversight.
- Menominee Area Public Schools and Gwinn Area Community Schools incurred general fund deficits placing them under MDE oversight.
- Michigan Technical Academy was closed by its authorizer Central Michigan University.

The remaining 3 districts continue to be subject to Department oversight:

| 2017 | School District/PSA | Administrative Review ISD/Authorizer |
|------|-------------------------|---|
| 1 | Bay City Public Schools | Bay-Arenac Intermediate School District |

| 2017 | School District/PSA | Department Periodic Reporting ISD/Authorizer |
|------|--------------------------------|--|
| 2 | Britton Deerfield Schools | Lenawee Intermediate School District |
| 3 | Ontonagon Area School District | Gogebic-Ontonagon Intermediate School District |

2018 POTENTIAL STRESS

In 2018, 7 districts were declared to have the potential for fiscal stress after being identified by the financial projection model.

The following school districts have been notified of the declaration and have 60 days to contract with an ISD or authorizer for an administrative review:

| 2018 | School District/PSA | ISD or Authorizer |
|-------------|--|--|
| 1 | Detroit Community Schools (PSA) | Bay Mills Community College |
| 2 | Macomb Academy | Central Michigan University |
| 3 | Midland Academy of Advanced and Creative Studies | Central Michigan University |
| 4 | New Beginnings Academy | Central Michigan University |
| 5 | Saranac Community Schools | Ionia Intermediate School District |
| 6 | Success Mile Academy | Grand Valley State University |
| 7 | Watersmeet Township School District | Gogebic-Ontonagon Intermediate School District |

PRELIMINARY REVIEW

Pursuant to MCL §141.1544(2), the Department shall conduct a preliminary review to determine the existence of probable financial stress for all school districts subject to a DEP that provides for the elimination of deficit over a period exceeding 5 years.

Eleven districts under MDE oversight became subject to the preliminary review process in 2016. Three of them were able to eliminate their deficit as of June 30, 2016 and were not subject to a preliminary review:

1. Clintondale Community Schools
2. Flint Community Schools
3. Southgate Community School District

A preliminary review was completed for the following 8 districts with the Emergency Loan Board (ELB) finding no probable financial stress.

1. Beecher Community School District
2. Bridgeport Spaulding Community School District
3. Hazel Park City School District
4. Mackinaw City Public Schools
5. Mt. Clemens Community School District
6. New Haven Community Schools
7. Vanderbilt Area Schools
8. Westwood Community Schools

- The following 2 districts eliminated their deficit as of June 30, 2017 and are no longer subject to EDEP reporting:

1. Bridgeport Spaulding Community School District
2. New Haven Community Schools

PENDING PRELIMINARY REVIEW

Two Districts previously under MDE oversight, Bay City Academy and Gwinn Area Community Schools are determined to have a deficit lasting longer than 5 years and will be transferred to Treasury oversight through an EDEP. Bay City is subject to a Preliminary Review in front of the Emergency Financial Assistance Loan Board, while Gwinn will move directly to treasury based on language in the statute (MCL 381.1220)

ENHANCED DEFICIT ELIMINATION PLANS

Pursuant to MCL §380.1220(5), a school district, ISD, or PSA currently operating under a DEP that has not completely eliminated its deficit within 5 years after the initial DEP was submitted to MDE is required to submit an EDEP to the Department of Treasury.

Eight school districts have undergone the preliminary review process. These districts are also required to submit an EDEP for Department approval. In addition to providing an EDEP, these districts are required to provide additional cash flow and budget-to-actual reporting on a monthly basis.

The 6 remaining school districts along with the year each is expected to eliminate its deficit are as follows:

| 2017-18 | School District/PSA | ISD or Authorizer | FY 2017-18 EDEP |
|----------------|---------------------------------------|--------------------------------------|------------------------|
| 1 | Vanderbilt Area School | Cheboygan-Otsego-Presque Isle ESD | \$6,712 |
| 2 | Westwood Community Schools | Wayne RESA | \$102,093 |
| 2018-19 | | | |
| 3 | Mackinaw City Public Schools | Cheboygan-Otsego-Presque Isle ESD | \$(138,390) |
| 4 | Mt. Clemens Community School District | Macomb Intermediate School District | \$(60,497) |
| 2020-21 | | | |
| 5 | Hazel Park City School District | Oakland Schools | \$(4,619,406)* |
| 6 | Beecher Community Schools | Genesee Intermediate School District | \$(1,060,401) |

*There are indications that this number will be much larger at the end of FY 18. We are working with the district on getting an updated EDEP and a preliminary figure for a FY 19 budget by May 1.

PA 436

EMERGENCY MANAGER

Highland Park Schools

Effective Date: January 15, 2014

Emergency Manager: Kevin A. Smith

- Emergency Manager's 18-month term ends in April 2018.
- District and Treasury are reviewing options to transition to a form of local control.
- District has entered into repayment agreements with ORS, MDE, Wayne RESA, and UIA. It is in negotiations with DTE, its remaining creditor.
- EM has drafted a District Educational Strategic Plan 2018-2023, which he expects to share with stakeholders in early March.

CONSENT AGREEMENT

Pontiac Schools

Effective Date: September 18, 2013

Consent Agreement Consultant: Vacant

- District is still working to refinance \$3.4 million in 2014 school building and site bonds and \$10.2 million in 2006 energy bonds.
- District is expected to restructure its emergency loans in early March.
- District is projected to eliminate its general fund deficit in 2023; and pay-off its emergency loans in 2036.
- Treasury is reviewing Consent Agreement amendments to transition the District back to local control effective June 1, 2020, which is consistent with the termination date of MDE's Partnership Agreement.

Benton Harbor Schools

Effective Date: September 23, 2014

Consent Agreement Consultant: Vacant

- District, in December 2017, hired Clark Hill to investigate the administration for alleged union contract violations, violations of student disciplinary procedures, and issues regarding Public Safety/Gang Prevention Grants. A final report on Gang Prevention Grants has been completed and presented to the board of education. The board has not authorized its release to the administration, Treasury, or MDE.
- District, in February 2018, hired Thrun Law to investigate student safety polices and whether or not the superintendent had followed board procedures.
- District placed Superintendent Shelly Mills-Walker on non-disciplinary, paid administrative leave pending the completion of the above-mentioned investigations. The superintendent has two years remaining on her contract and is pursuing other employment opportunities and a contract buy out.
- District CFO resigned effective March 2, 2018.
- District, at Treasury's insistence, hired Rehmann to oversee CFO operations from February 26 to June 1, 2018. Treasury agreed to reimburse the District for all related expenditures.

- Treasury is reviewing Consent Agreement amendments to transition the District back to local control effective June 1, 2021, which is consistent with the termination date of MDE's Partnership Agreement.

RECEIVERSHIP TRANSITION ADVISORY BOARD

Muskegon Heights Public Schools

Effective Date: August 8, 2012

RTAB: Established October 28, 2016

- The District is currently seeking a fourth emergency loan note to cover outstanding liabilities with interest rates untenable in the current financial situation.

- A meeting of the Emergency Loan Board to approve the fourth emergency note is tentatively scheduled for March 2018.
- District owes: Unemployment Insurance Agency \$967,863; Office of Retirement Services \$1,528,919; MDE \$371,435; this does not include bond or emergency loan debt service. The emergency loan will be used to pay these outstanding liabilities.
- The previous three emergency loan notes will also be amended and restated to reflect more efficient timelines in tax capture.

CONTACT

Additional questions about this report should be directed to Rodney Taylor, Administrator in the Bureau of Local Government and School Services at TaylorR23@michigan.gov or (517) 241-7029.