



CITIZENS RESEARCH COUNCIL OF MICHIGAN

# School Finance in Michigan

Municipal Advisory Council of Michigan Fall Conference  
*Livonia, Michigan*

December 9, 2014



## About The Citizens Research Council

- Founded in 1916
- Statewide
- Non-partisan
- Private not-for-profit
- Promotes sound policy for state and local governments through factual research
- Relies on charitable contributions of Michigan foundations, businesses, and individuals
- [www.crcmich.org](http://www.crcmich.org)



# Recent Trends in School Finance



## Quick Quiz: School Funding

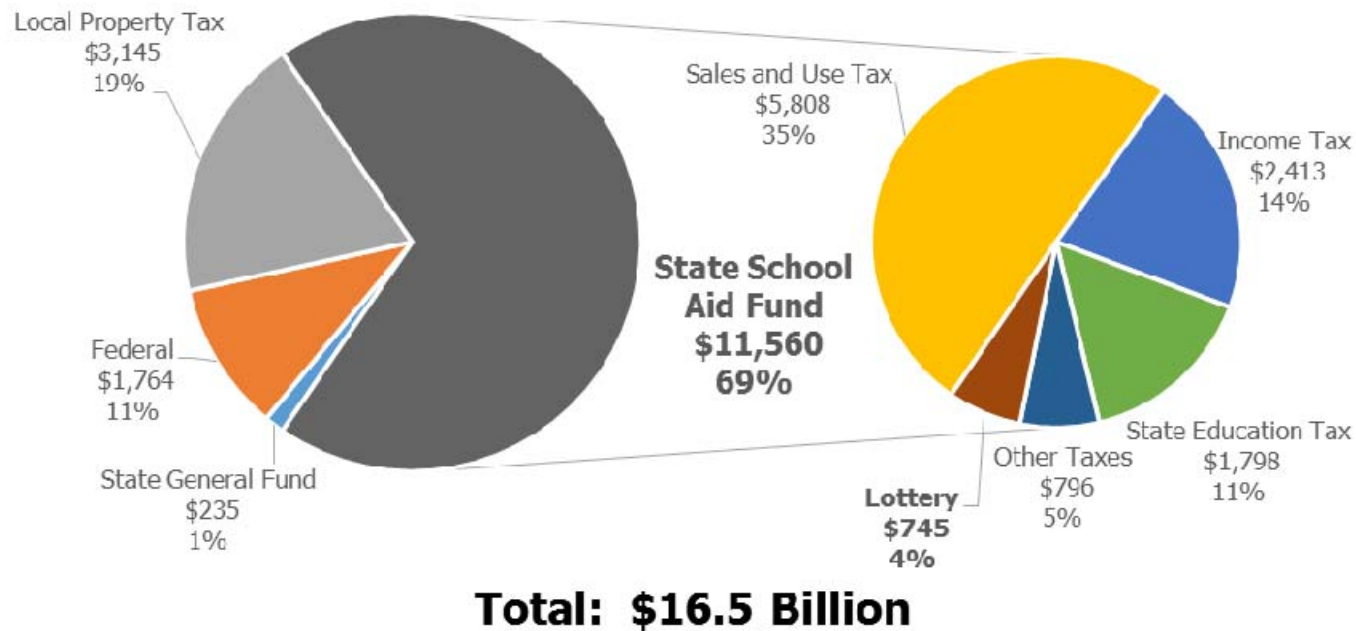
**Question:** What role does the lottery play in funding public schools?

- A. 50 percent
- B. 25 percent
- C. 10 percent
- D. Less than 5 percent



**Answer:** *D – less than 5 percent*

**2014 Operating Funding for Public Schools  
(millions)**





# Last Decade Was an Economic Disaster

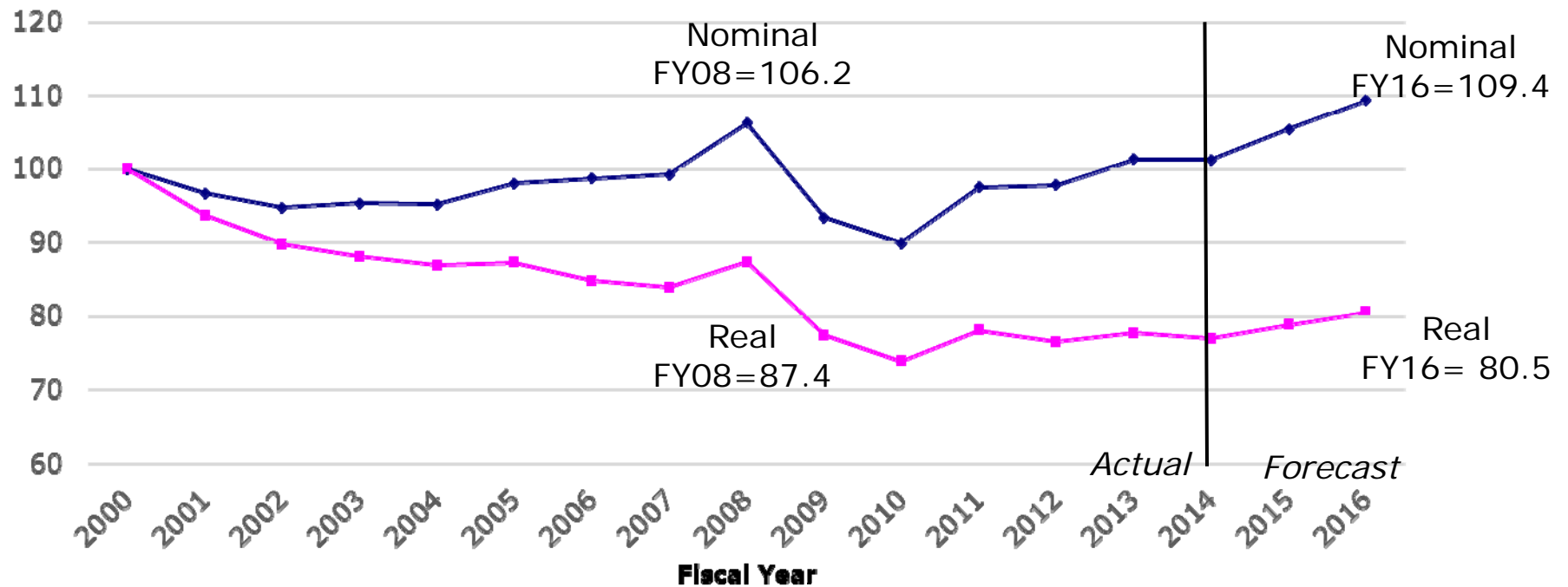
*School funding in larger context*

	Growth 2000 to 2010		Michigan
	<u>U.S.</u>	<u>Michigan</u>	<u>Rank</u>
Population	9.6%	-0.8%	51
Real Per Capita GDP	5.0%	-10.4%	51
Employment	-1.5%	-17.4%	51
Real Per Capita Income*	4.9%	-5.6%	50



# Nominal Revenues Nearing FY08 Level But Real Revenues Still Down

Combined GF/SAF Revenues (2000 = 100)





# State Spending From State Resources Down in Most Categories

	FY 2002 <u>(millions\$)</u>	FY 2013 <u>(millions\$)</u>	Nominal % <u>Change</u>
Medicaid/DCH	\$3,066	\$4,976	62.3%
Corrections	\$1,653	\$2,009	21.5%
Human Services	\$1,230	\$1,117	-9.2%
<b>K-12</b>	<b>\$11,221</b>	<b>\$11,244</b>	<b>0.2%</b>
Community College	\$320	\$294	-8.2%
Universities/Fin Aid	\$1,941	\$1,302	-32.9%
Revenue Sharing	\$1,517	\$1,084	-28.6%
All Other	<u>\$5,139</u>	<u>\$5,787</u>	<u>12.6%</u>
Total	\$26,087	\$27,812	6.6%
U.S. CPI - U	178.9	232.7	30.1%

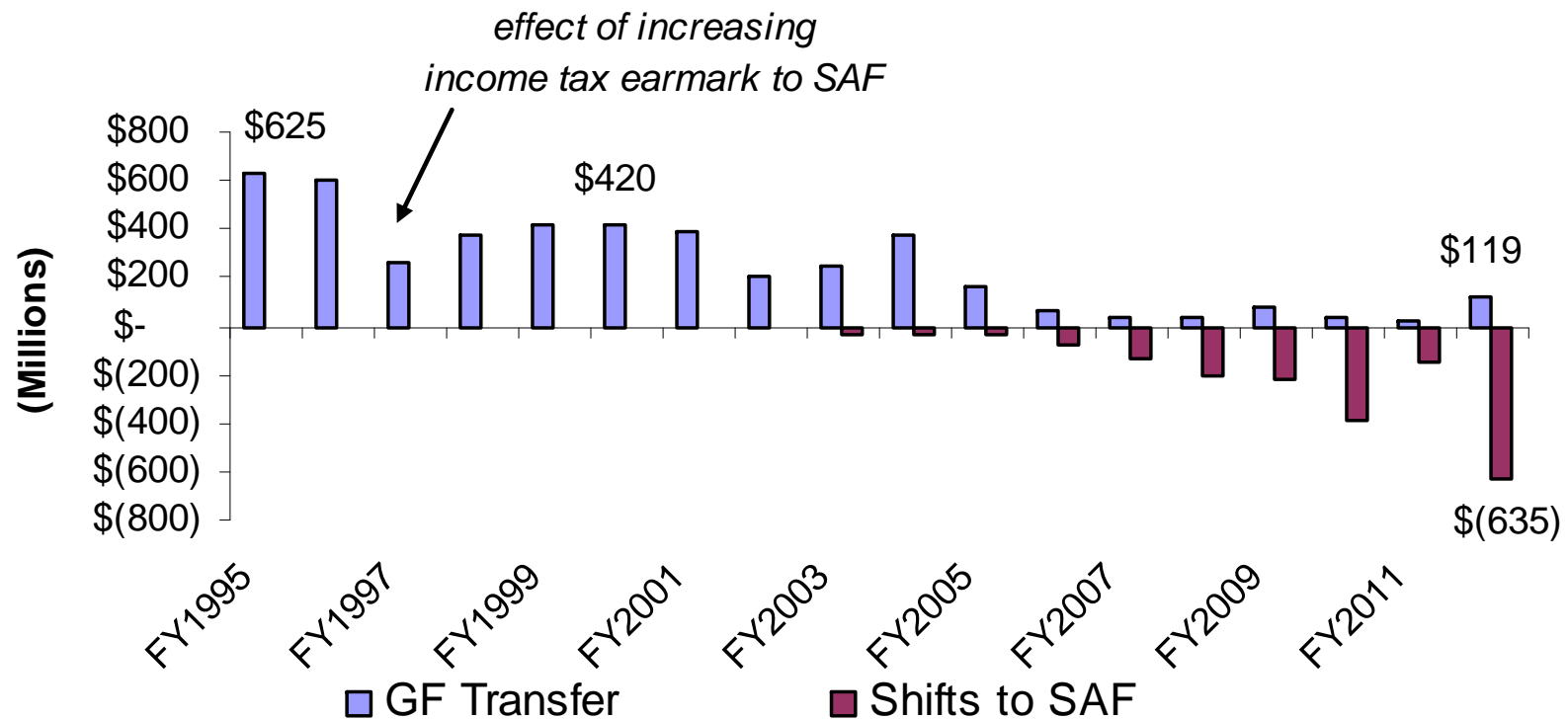




# General Fund Problems Spill Over

*Budget decisions reduce K-12 funding*

**General Fund Transfers and Cost Shifts - School Aid Fund**

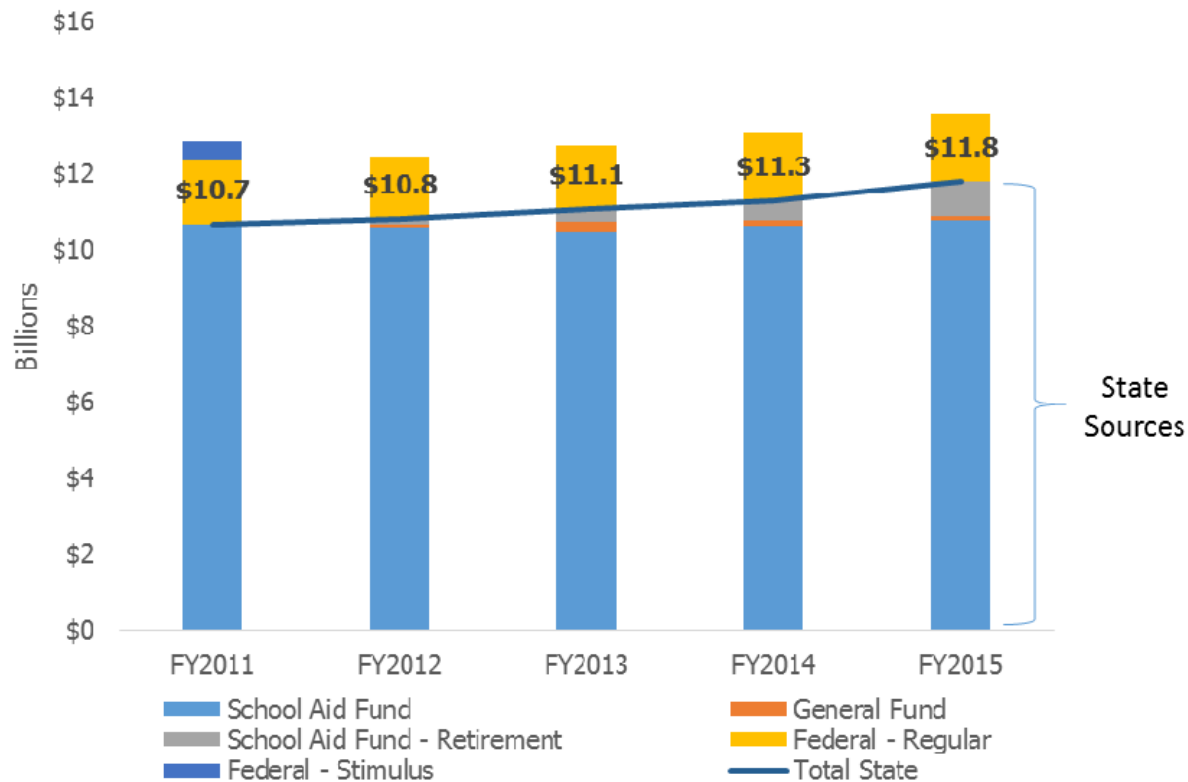


Source: Michigan Department of Education; House Fiscal Agency



# State Funding Up \$1B Since FY2011

*But, most of the increase is for retirement costs*



Source: Senate Fiscal Agency and House Fiscal Agency reports



# **Current Fiscal Challenges Facing Public Schools**



## Factors Affecting K-12 Finances

### *Structural Issues*

- Changing demographics
- Improving recovery from Great Recession
- Growing legacy costs

### *Policy Decisions*

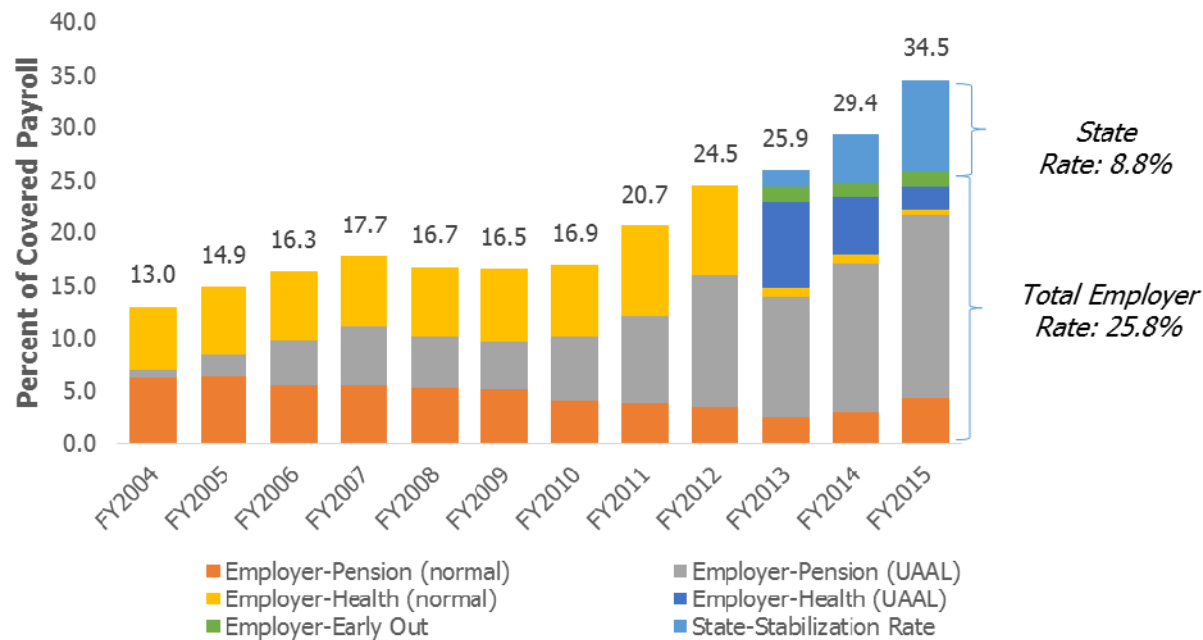
- Growth in number of educational providers
  - More charters and new cyber/online options
- State tax policy decisions
- State budget decisions
- State policy for dealing with districts in distress



# Employer Retirement Contributions Rise

*Rate cap instituted in FY13 to provide predictability*

**MPSERS Contribution Rates**



Source: Office of Retirement Services

*Contributions Grew from \$1.3B in FY04 to \$2.3B in FY13*



## Effects of Retirement Cost Growth

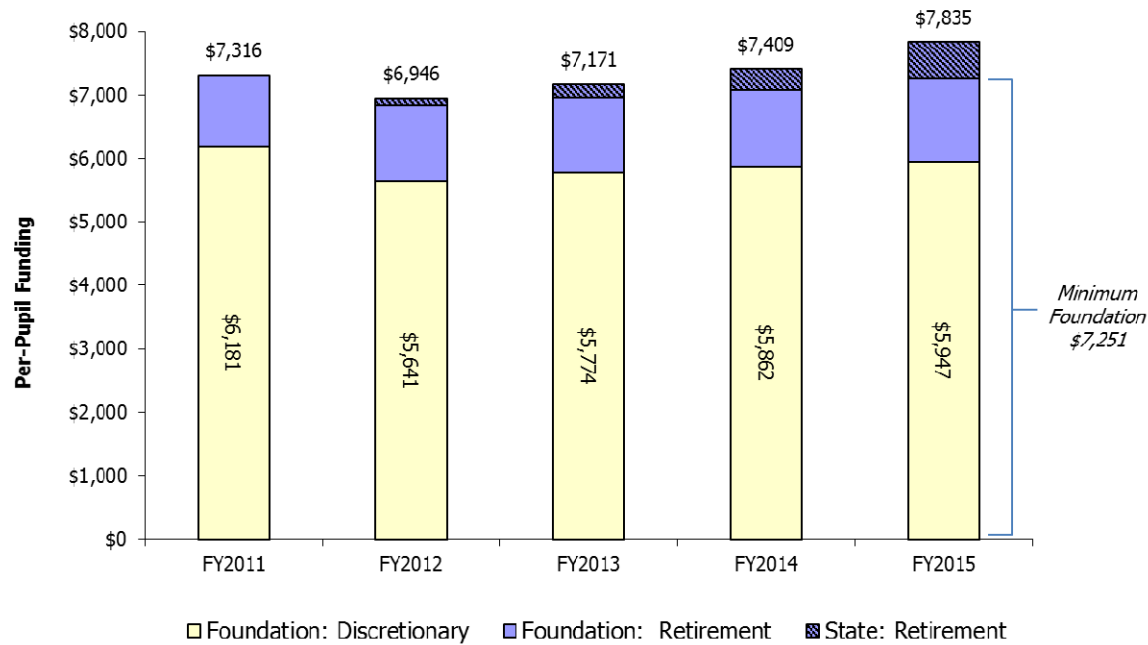
### *Funding increases eaten up*

- Primarily a problem for traditional public schools, most charters not members of system
- Increases in state funding have been eroded by growing retirement contributions
  - Employer costs have stabilized because of various system reforms
  - State picking up portion of the cost (\$883M) – these funds unavailable for other purposes
- Crowd outs other school spending
- Results in flat per-pupil classroom funding



# Retirement Costs and Per-Pupil Funding

*Estimated impact on minimum foundation grant*



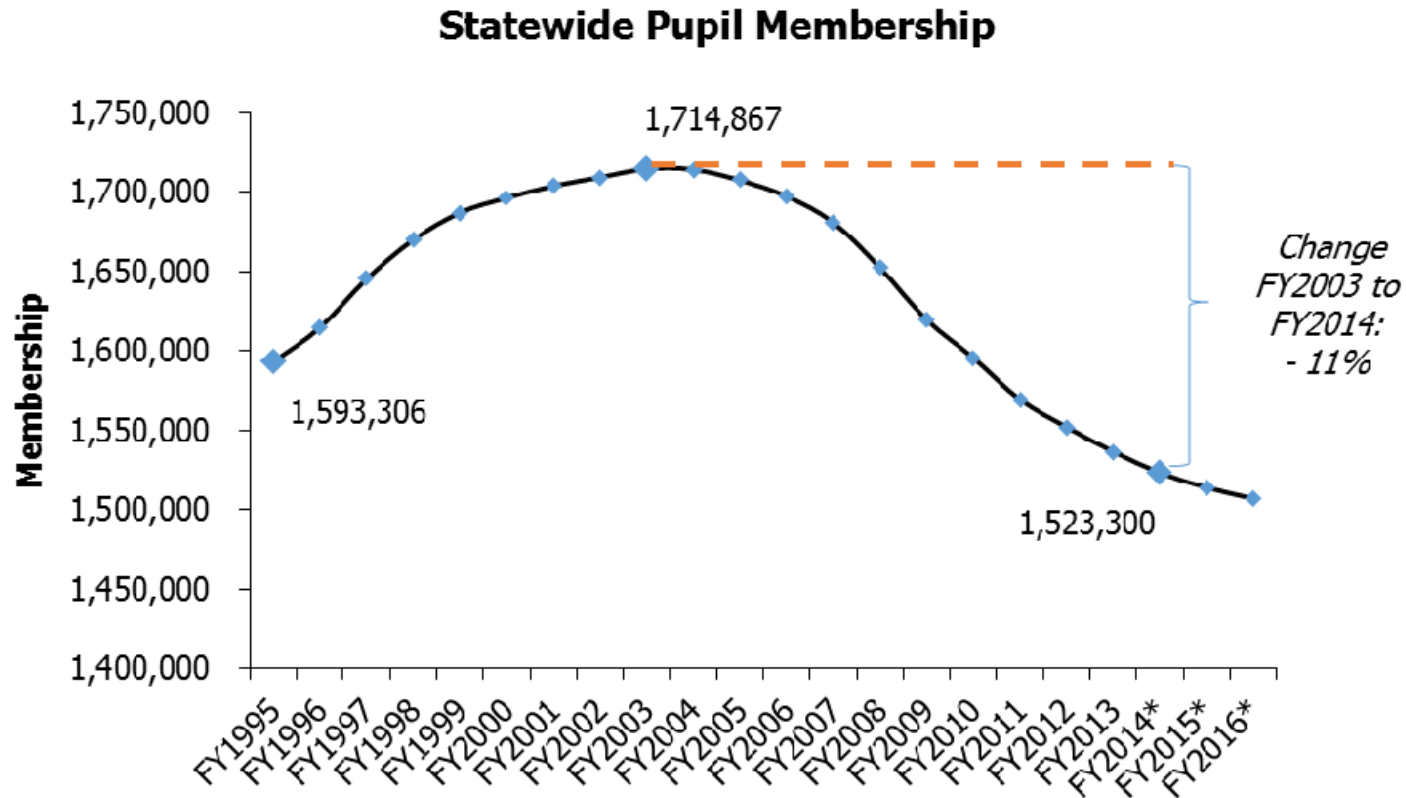
Source: Senate Fiscal Agency and House Fiscal Agency Reports; Office of Retirement Services

*Total Retirement Contribution: \$1,888 per pupil in FY15*



# Era of Declining Enrollment

*Trend expected to continue*



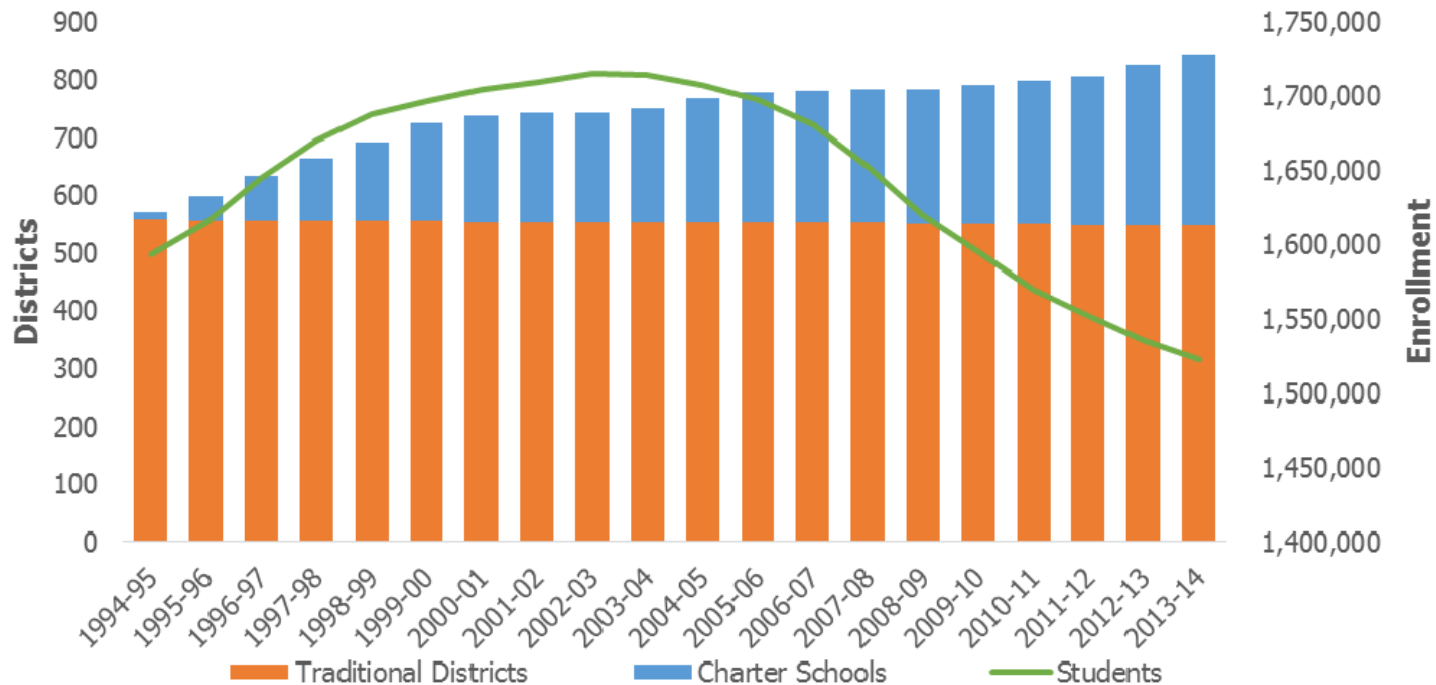
\* FY2014 through FY2016 based on January 2014 consensus estimates





# Number of Districts Increase Despite Declining Enrollment

Michigan School Districts and Student Enrollment



Source: Michigan Department of Education  
Note: Excludes Intermediate School Districts (56 in 2012)



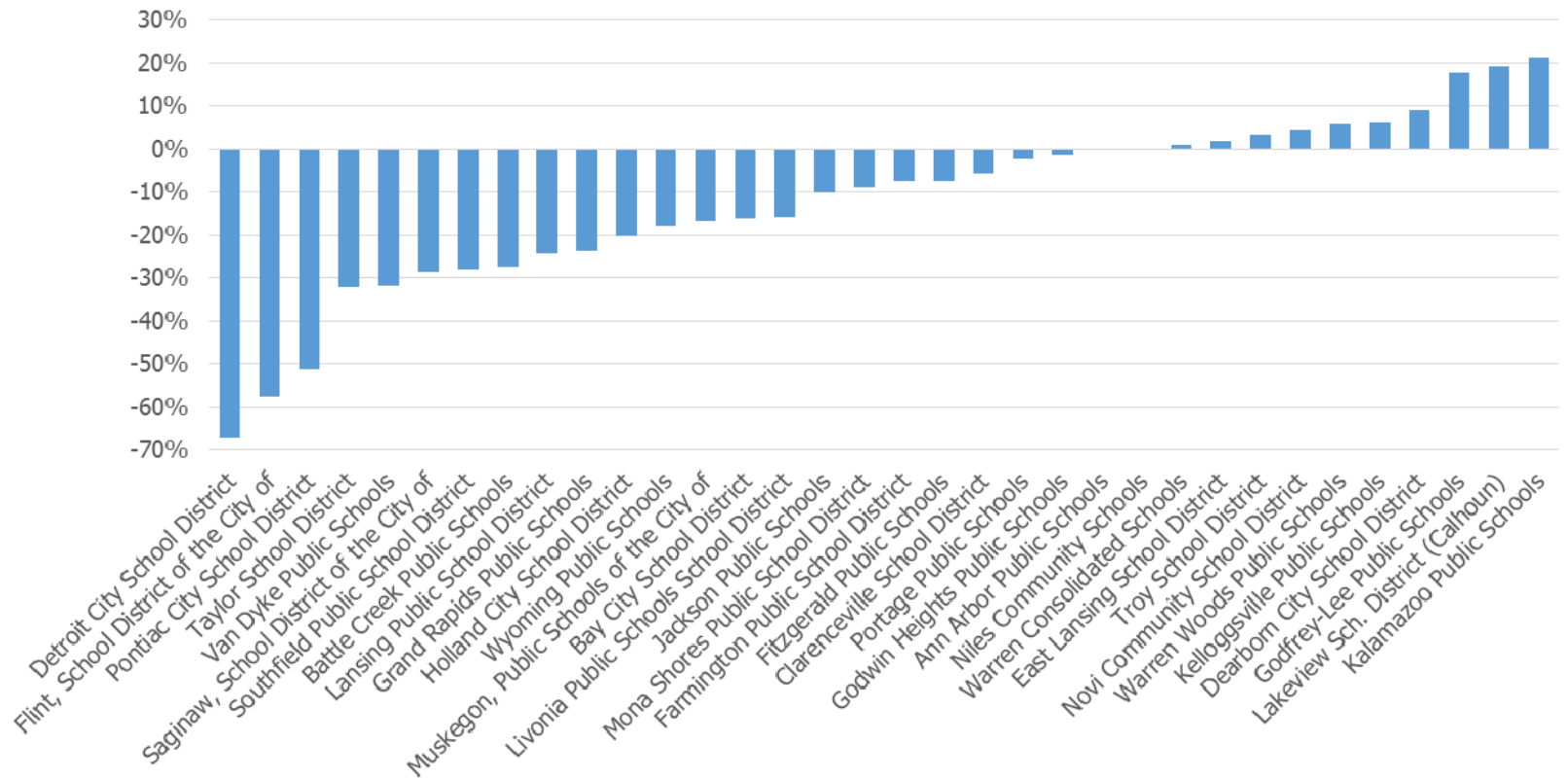
# Declining Enrollment . . . Not Just an Urban Issue

Enrollment Change from Fall 2003 to Fall 2012	District Locale			
	City	Suburb	Town	Rural
Gain	10	50	10	55
Loss				
greater than 50%	3	0	1	6
25% to 50%	5	14	5	61
10% to 25%	8	25	44	114
0 to 10%	8	46	23	57
Districts with Loss	<b>24</b>	<b>85</b>	<b>73</b>	<b>238</b>
Total # of Districts	34	135	83	293
Total Pupil Loss / % Loss	133,520 -32%	24,756 -4%	23,244 -12%	38,271 -12%



# Large Urban Districts Experience Massive Enrollment Loss

Enrollment Change in City School Districts: 2003 to 2012





# Effects of Declining Enrollment

## *Two narratives*

- State-level effects
  - Fewer students in the system allows the per-pupil foundation grant to increase, even if there are no new dollars in the system
- District-level effects
  - Per-pupil foundation grant might increase, **BUT**
  - Effects of grant increase are offset by the loss of students – result in fewer resources overall
  - Challenges of “managing down” when majority of costs are relatively fixed in near term



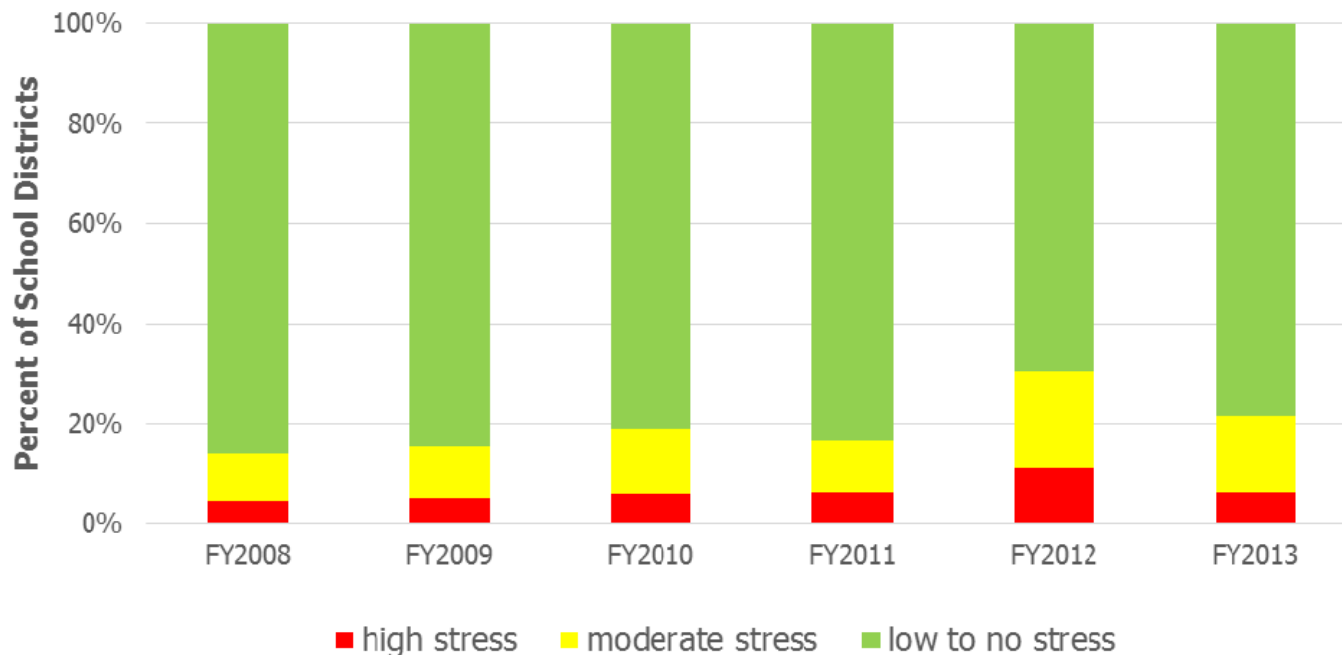
# Fiscal Stress



# Fiscal Stress Increased Through FY2012

*Improvements in FY2013 and projected for FY2014*

**Fiscal Stress Among Traditional Public Schools**



Source: Munetrix LLC



## Districts Tap Rainy Day Resources

*Record number of deficit districts in 2012*

	<u>2007-08</u>	<u>2008-09</u>	<u>2009-10</u>	<u>2010-11</u>	<u>2011-12</u>	<u>2012-13</u>
Statewide Average	10.81%	9.34%	7.19%	8.42%	8.96%	8.37%
<b>Fund Balance as % of Revenue</b>						
0% to 5%	57	63	73	44	50	78
5% to 10%	106	108	99	101	117	127
10% to 15%	114	119	131	127	136	106
Above 15%	<u>249</u>	<u>231</u>	<u>211</u>	<u>237</u>	<u>201</u>	<u>186</u>
Districts	526	521	514	509	502	497*
<b>Deficit (Negative)</b>	<b>21</b>	<b>29</b>	<b>36</b>	<b>41</b>	<b>47</b>	<b>42</b>

Source: Michigan School Business Officials; Michigan Department of Education (deficit districts).

Note: Traditional public school districts only (excludes ISDs and PSAs). Not all districts reporting for 2012-13.



## Why be Concerned with Fiscal Stress in Public Schools?

- Directly effects the quality of educational offerings
  - If not dealt with, can lead to “death spiral”
- Accountability for public funds – majority of school funding comes from state taxes
- Ensure that vendors get paid in timely fashion
- Avoid emergency manager law
- Avoid state bailout where other schools pay price
- Protect the credit ranking of the state





## Range of State Responses

- For majority of districts in distress, current Deficit Elimination Plan process functions well
- However, for those hardest hit, state lacks consistent policy and responses have varied:
  - “Charterized” districts (Muskegon Heights and Highland Park)
  - Dissolution used for two districts (Buena Vista and Inkster)
  - PA 436 used for Detroit (emergency manager) and Pontiac (consent agreement)
- *State needs “Early Warning” system*



## Consequences of Current Approach

- Interruption of student learning – sometimes abruptly and at mid-year
- Some state responses “socialize” deficit elimination solutions through the provision of additional funds
- Under dissolution scenario (new option), the learning environment that students are assigned to may not be any better than the dissolved district
- Diminished accountability for state taxes used to finance K-12 education



# Recommendations



## Examine Declining Enrollment

1. For those districts hardest hit, **establish policy and early warning strategies** to head off “death spiral”
2. **Restore state strategies** designed to ease immediate negative effects of declining enrollment
3. **Reconsider state messaging** – consolidation vs. expansion of educational providers
4. **Reexamine the structure** of the per-pupil foundation grant
  - Recognize that there are “school-based” costs
  - Differentiate foundation grant to take into account student/school characteristics



## Adopt Policy for Distressed Districts

1. Move away from current ad hoc approach and establish a **clear, transparent, and consistent policy** based on early intervention
2. Acknowledge that some districts would need **additional resources** (financial and technical) to address their financial challenges - these dollars should come earlier, but with “strings attached” to avoid recurring problems
3. There must be an **educational component**, not merely a financial solution



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