Council Comments:

Citizens Research Council of Michigan
625 SHELBY STREET, SUITE 1B, DETROIT, MI 48226-3220
(313) 961-5377
1502 MICHIGAN NATIONAL TOWER, LANSING, MI 48933-1738
(517) 485-9444

No. 983 August 1989

DETROIT SCHOOL BALLOT ISSUES

Members of the Detroit Board of Education voted at a special meeting on July 13, 1989, to submit two ballot propositions to the voters at the municipal primary election on September 12, 1989: a request to approve the sale of up to $160 million of unlimited tax, general obligation bonds to fund the deficit, and a five-mill increase in the extra-voted property tax levy for school operations for the five-year period from July 1, 1989 through June 30, 1994.

A request to authorize the sale of up to $160 million in deficit funding bonds was defeated in November 19881, when voters also denied a request for six new extra-voted mills for operations. At that time, voters did approve a request to renew four extra-voted mills. Those ballot issues were explored in **Council Comments No. 976,** published in October 1988.

Background Detroit property on the ad valorem tax roll is now subject to taxation at the rate of $82.857 per $1,000 of assessed value. Of the existing 82.857 mill rate, 40.90 mills are levied by the Detroit School District. The school levy includes 5.0 mills for debt service on long-term debt; 8.65 allocated mills, of which 0.64 mills are passed through to the Detroit Public Library; and 27.25 extra-voted mills. In the spring, Detroit voters will be asked to approve the renewal of 3.5 mills that expire on June 30, 1990.

SCHOOL DISTRICT OF THE CITY OF DETROIT

Extra-Voted Mills	Years Duration	Expires as of June 30
3.50	10	1990
3.00	10	1992
7.50	10	1994
2.25	8	1994
7.00	6	1994
4.00	5	1994
27.25		

The Detroit Board of Education has pursued a strategy of scheduling the expiration of extra-voted millage for one date, June 30, 1994. Sometime before that date, voters in the city will be asked to renew all extra-voted mills at one time. This strategy, which has also been adopted by some Other Michigan school districts, precludes the ability of the voters to make incremental decisions on school funding. The proposed expiration date of the five mills being requested reflects the "all or nothing at all" strategy.

According to the most recent published data from the Michigan Department of Education, in 1987-88 the Detroit School District reported current operating expenditures per pupil of $3,864, 7.7% more than the $3,587 average current operating expenditures per pupil for the 524 Michigan K-12 school districts. In fact, Detroit spent more per pupil than 442 of the 524 K-12 districts. The average state equalized value (SEV) per pupil for those 524 districts was $66,607; there were only seven districts in the state with a lower SEV per pupil than Detroit's $27,078. The state school aid formula, which protects in-formula districts from the effects of declining tax base and rewards those districts for high millage rates, has enabled the Detroit School District to maintain a much higher rate of expenditures per pupil than would otherwise be possible with such a meager property tax base. Deficit spending also contributed to the high rate of expenditures per pupil: in spite of the $430 million provided by state school aid in fiscal 1988, the Detroit district in that year spent about $36 million more than it received in revenues.

In 1987-88, Detroit schools reported general fund revenue from local, state, intermediate, and federal sources of $3,718 per pupil, compared to a statewide average of $3,626 per pupil. Total general fund revenues per pupil, including transfers from other districts and funds and other transactions, were $3,718 for the Detroit district and $3,765 for the average of all districts.

SCHOOL DISTRICT OF THE CITY OF DETROIT
ACCUMULATED GENERAL FUND DEFICITS AS OF JUNE 30
BASED ON NORMAL SCHOOL ACCOUNTING PRACTICES

1979	$ 7.2 Million
1980	13.8 Million
1981	16.9 Million
1982	36.4 Million
1983	43.1 Million
1984	49.6 Million
1985	18.6 Million
1986	18.1 Million
1987	33.4 Million
1988	69.0 Million

The 1988 **Report on Audit of Financial Statements** disclosed: "If the District had accounted for property tax revenues and school bus costs in accordance with generally accepted accounting principles, the General Fund deficit reported by the District at June 30, 1988 would have been increased by $32,600,000 to approximately $101,600,000.'

Coopers and Lybrand in April 1988 projected that on June 30, 1989, the Detroit School District would have an accumulated deficit of about $109 million based on normal school accounting practices; that deficit estimate grew to about $160 million (subsequently revised to $151 million) when more stringent generally accepted accounting principals (GAAP) were applied.

Deficit Funding Bonds The School Code of 1976 as amended allows a school district to issue deficit funding bonds if the district's actual or projected operating deficit is in excess of $100 per membership pupil; if the district has made every available effort to offset the deficit, including requesting an increase in the millage rate in that year or the previous year; if the district school board has approved a plan which outlines actions to balance future budgets; and if the school board has set a maximum interest rate. The notes or bonds may not mature more than ten years from the date of issuance. The attorney general has opined that operating notes or bonds may not be issued by a school district without prior approval of the voters of the school district (Op Atty Gen, August 5, 1982, No. 6090).

The School Code of 1976 specifies in Section 1356 (3) that: "The existence of the operating or projected operating deficit and the amount thereof shall be determined by the Department of Treasury, using normal school accounting practices." Section 1356 (4) states in part: "The amount of a note or bond issued shall not exceed the amount of the operating deficit as shown by the determination." The state treasurer has informed the district that any deficit funding bonds sold must resolve the GAAP deficit, a position which is consistent with ongoing efforts at the state level to redefine normal school accounting practices to reflect generally accepted accounting principles.

The Detroit board is requesting authorization to issue up to $160 million of deficit funding bonds to be repaid from an unlimited tax levy, which the board estimates would result in an additional 1.5 mill levy annually for the next ten years. If the Detroit Board of Education were to sell $160 million of deficit funding bonds at about 8% for 10 years, the annual debt service would be approximately $24 million. Previous statements from the Detroit school system have indicated that a property tax levy of 1.5 mills, together with the state school aid generated by that 1.5 mill levy (the state treats deficit bond millage as operating millage for state aid purposes), would be sufficient to pay the principal and interest on that debt. The recently announced 198990 state school aid formula, which will guarantee receipts of $83.61 per mill per pupil (up from $77.71 in 1988-89), plus a flat grant of $310 per pupil (down from $350 in 1988-89), indicates that a 1.5 mill levy would generate about $23 million annually for the Detroit School District.

In November 1987 and October 1988, the Department of Treasury insisted on the inclusion of a special stipulation in authorizations allowing the Detroit School District to issue tax anticipation notes (TAN's). This stipulation required that state aid resulting from an increased millage rate applicable to deficit funding bonds would be used for debt service on the deficit bonds. Treasury officials are required to approve the issuance of deficit funding bonds by the Detroit School District, and intend to require the same stipulation as a condition for approval.

The State School Code requires that: 'The school district shall levy sufficient taxes annually, in addition to all other taxes, without limitation as to rate or amount in order to meet payments of principal and interest on the notes or bonds caning due before the next collection of taxes.0 (Section 1356 (4)) There has been some discussion as to whether generated state school aid may only be used to accelerate debt retirement, or whether such school aid could be used for operating purposes with the district levying each year for the entire amount of debt service. The Detroit School District would have to levy about five mills to generate $24 million from property taxes. The state aid generated from a five-mill annual levy could be about $50 million; if applied to early debt retirement rather than operations, it would allow the entire debt to be paid in about three years, rather than ten.

The Detroit School District had accumulated a $70 million deficit in 1972. Deficit funding bonds sold by the district at that time were retired with the proceeds of a 2.25 mill levy in 1974 through 1979, with the related state school aid used for operations rather than for debt retirement. The district received voter approval to continue levying the 2.25 mills after the deficit bonds had been retired; the proceeds from the levy as well as the generated state school aid then became part of the current operating budget. Other Michigan school districts that have or are selling deficit funding bonds have not been required to use generated state school aid for debt retirement.

If voters grant authorization to issue deficit funding bonds but do not approve an increase in the operating levy, it would not be surprising if the district challenged the legality of the state requirement to use generated state aid for debt retirement. Indeed, a report from Coopers and Lybrand dated April 13, 1989, describes a scenario in which deficit elimination bonds are approved but a requested increase in operating millage is defeated: "The current state rules require that property taxes and matching state aid be dedicated to provide for annual debt service.... If the district receives relief from this requirement the millage increase would be set so that revenue from additional property taxes would be sufficient to cover debt service and the additional revenue generated through state aid would be used for operating purposes."

The Contingency Budget As a condition for approval to issue up to $45 million of state aid notes necessary for the Detroit School District to meet the May 16 payroll and subsequent operating costs, the state treasurer required that prior to June 1, 1989, the district must approve an amendment to its deficit elimination plan. The contingency budget included in that amendment, whi6h assumed neither the sale of unlimited tax deficit elimination bonds nor an increase in the operating millage, was required to reduce appropriations to the level supported by actual revenues and, if limited tax deficit reduction bonds were not issued, was required to reduce the accumulated deficit by not less than 5% by the end of the 1989-90 school year. The specifics of the reduction plan had to be approved by the Michigan Department of Education and the Department of Treasury. If the Detroit School Board were unable to agree to a plan to achieve the required deficit reduction, the district general superintendent was empowered to order cuts to balance the budget.

The 1989-90 budget plan submitted by the Detroit district to the state eliminated 1,612 positions and $50.7 million in expenditures. Among the actions required to implement the reductions are improvements in facility utilization; reductions in administrative/support personnel, instructional personnel, and custodial services; transfers to specially funded programs; reductions in transportation programs; reduction of the instructional program for high school students to five classes (subsequently restored using state aid improvements) and elimination of extra curricular programs.

Five Extra-Voted Mills for Operations Imposition of five new mills would generate about $75 million for the Detroit School District in future years, but, due to the difference in state and school district fiscal years, only about $68 million in 1989-90. These projections acknowledge that in Detroit, the current year property tax collection rate is between 91% and 92%.

Of the $50.7 million removed in the contingency plan, about $7.5 million was for deficit reduction. Priority restorations include instrumental music and interscholastic athletics for elementary and middle school students, transportation for regular programs, custodial service, school staffing allocations, and new textbook allocations, and would cost about $22 million.

DETROIT SCHOOL DISTRICT
1987-88 AND 1988-89 TEACHER SALARY RANGES (39 WEEKS)

	Bachelors Degree	Masters Degree	Masters Plus 30	Doctorate Degree
Minimum	$21,261	$23,501	$23,801	$24,101
Maximum	33,620	38,576	39,276	39,576

In 1988-89, when unionized personnel received no pay raise, the district spent $370 million for salaries for teachers and administrators. On that base, a 3% arbitrated retroactive raise for teachers and administrators would cost $11 million, and a 6% raise for teachers and administrators in 1989-90 would cost $23 million. If teachers and administrators were to receive an arbitrated retroactive 3% raise and all instructional and support employees were to receive a 6% raise for 1989-90, the total cost would be about $42 million.

Thus it is clear that in 1989-90 five new mills for operations would barely fund requested arbitrated retroactive and negotiated prospective pay raises and restore priority programs. It is equally clear that some reductions, such as closing and selling under-utilized facilities, should be pursued. Indeed, the extent to which selected program reductions are pursued will in some measure determine the amount available for other program improvements, such as intervention strategies to improve student achievement, local school empowerment, additional resources for pre-school and elementary levels, initial implementation of the Detroit Compact, and dropout prevention.

Impact of Approval of only the Operating Millage Both the November 1987 and October 1988 Orders of Approval for issuance of tax anticipation notes by the Detroit School District require that if deficit reduction bonds are not issued, all property tax revenues from any increase in the operating millage must be applied to the general fund deficit. The increased state aid resulting from the increased millage rate would be available for operations. Since the penalty for violation of these conditions is calling the notes (one of which has al ready been retired), there is no guarantee that the district would comply with the state's requirements after the notes are repaid.

Local Taxes Paid by Detroiters The constitutional limitation of 'an aggregate of not to exceed 50 mills... for a period of not to exceed 20 years ... if approved by a majority of the electors' does not apply to property taxes imposed for debt service or "to taxes imposed for any other purpose by any city, village, charter county, charter township, charter authority or other authority, the tax limitations of which are provided by charter or by general law." (Article IX, Section 6) In the city of Detroit, in the charter county of Wayne, very nearly all the property tax except the school operating millage is exempt from the constitutional 50-mill limit.

Indeed, the state methodology for distribution of state income and single business taxes encourages and rewards cities that impose taxes at very high rates (a 3%/2%/1.5% municipal income tax and 5% utility users' excise tax may only be imposed by cities of over one million population). The state school aid formula encourages and rewards school districts that levy high millage rates, and the state homestead property tax credit reimburses homeowners for property taxes that are excessive in relation to household income.

Relative tax effort (RTE) and population are factors used in the distribution of state income and single business taxes to cities, villages, and townships. Relative tax effort as defined by the state includes municipal income tax (3% on Detroit resident individuals, 2% on corporations, and a portion of the 1.5% nonresident tax), excise tax (5% utility users' excise tax ' imposed only by Detroit), and city property tax (30.597 mills for Detroit in 1989-90). In 1989-90, the relative tax effort in Detroit is 6.33096; RTE in Detroit has been over six times the state average relative tax effort for the past seven years. The school property tax is not included in relative tax effort, but it is one component of the total tax burden on Detroiters, and as it increases, the disparity between the tax obligations borne by Detroiters and those borne by other Michiganians increases still further. Although school districts are held harmless from the effects of declining property values by the state school aid formula, the property tax base is clearly affected by very high rates of taxation.

If the requested authorization to sell deficit funding bonds and the operating millage increase are approved, the Detroit School District will impose 40.9 mills for operations (the statewide weighted average school tax is 34.59 mills for operations) and, if generated state aid is used for scheduled annual debt service, about 6.5 mills for debt, a total of about 47.4 mills.

CITY OF DETROIT PROPERTY TAXES

Market Value of Home	SEV (50% of Market)	Existing School Tax (40.9 mills)	Requested New School Tax (6.5 mills)	Potential Total Property Tax (89.357 Mills) (City, County, Schools)
$15,000	$ 7,500	$ 306.75	$ 48.75	$ 670.18
30,000	15,000	613.50	97.50	1,340.36
45,000	22,500	920.25	146.25	2,010.54
60,000	30,000	1,227.00	195.00	2,680.72

When the budgeted revenues from Detroit's income and utility users' excise taxes, adjusted to remove a portion of nonresident income tax payments (nonresident payments were about 27.1% of actual collections in the most recent year for which data are available) are divided by the state equalized value of the city, an equivalent property tax rate of 49.5 mills is derived. Thus, Detroiters are currently subject to 82.857 mills in property taxes plus additional taxes that translate into another 49.5 mills, for a total of 132.357 equivalent mills. If voters approve the requested five operating mills, the equivalent property tax rate would increase to 137.357 mills. Five new operating mills plus 1.5 mills for deficit funding bonds (assuming generated state aid were used for scheduled annual debt retirement) would produce an equivalent millage rate of 138.857 mills.

Detroiters currently bear an extraordinarily heavy tax burden, and are being asked to increase that burden substantially. They are being asked to do something even more difficult: decide whether to provide massive additional resources to the school system, or to further penalize students who are already perceived to be receiving an inadequate education.