

Overview of Budgeting & School Finance



PINE-RICHLAND SCHOOL DISTRICT

(UPDATED AS OF JANUARY 2015)

Purpose



- To provide a clear overview of school funding in Pennsylvania that highlights the impact of recent legislative changes and economic factors that impact school district operations

This presentation is intended to provide clear, proactive communication to our various stakeholder groups. We feel it is important to share factual information about education funding and the impact on school districts, including Pine-Richland School District.

School Funding in the News



- “Perfect Storm” of factors have put school budgets and education funding in the news
 - Slow economic recovery
 - State & federal funding cuts (e.g. School Based ACCESS funding)
 - Increasing school pension liabilities
- PASBO/PASA School Budget Reports
- PSBA Bulletin, *‘Skyrocketing Increases: Pension Crisis’*
- “Spending Money Wisely: Getting the Most From School District Budgets”, by The District Management Council
- Common misconception is that these issues are related only to Pine-Richland School District and not a national or state issue

School funding challenges have been reported extensively in the news. In recent years, public education has been impacted by the economy & funding cuts at both the state & federal levels.

Annually, the Pennsylvania Association of School Business Officials and the Pennsylvania Association of School Administrators report on the status of school finance statewide. The 2015 report will be issued in February. As stated in the December 2014, PASBO Report, of the respondent school districts in this year’s survey, 90% have furloughed staff or left key positions vacant in the last five years. Nearly 40% of respondents have done both. “Cost drivers for school budgets continue to be a state-wide problem and are not confined to particular regions or based on school size, type or tax base.” During these same years, school districts in Pennsylvania are facing substantial employer pension obligations. In April 2014, PSBA published an article *‘Proposals Aim to Mend Pennsylvania’s Pension Troubles.’* Legislators have been working to propose various pension reform plans. These include reductions to benefits for newly hired employees, state borrowing, voluntary modifications from current members of the plan, restrictions on future employer contribution rates. It was reported in the PA Independent in January 2015, even though the Public School Employees Retirement System reported almost double the projected investment earnings in 2014, the unfunded liability in the plan is still over \$35 billion in benefits beyond what its assets can cover.

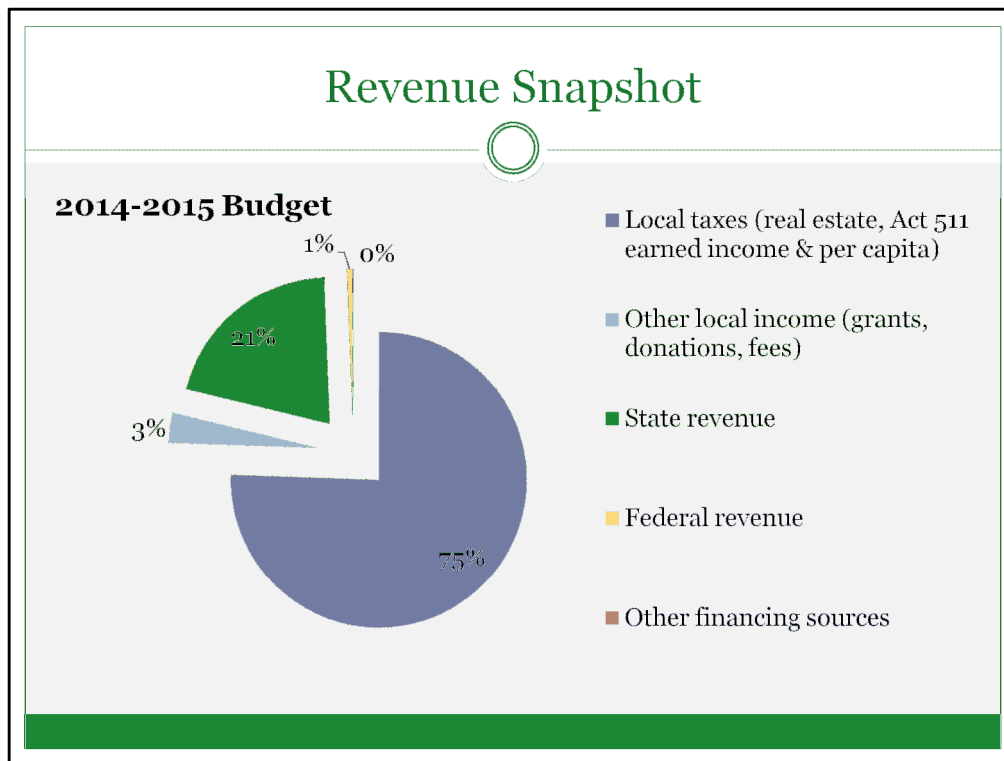
With all of these financial challenges facing school districts, any and all opportunities for cost savings need to be explored. The District Management Council published a book, “Spending Money Wisely: Getting the Most From School District Budgets”. The focus of the publication is on resource realignment and maximizing the impact of dollars spent. It is important to continually focus on meeting the needs of our students raising student achievement and implementing strategic direction with limited resources.

This situation is not unique to our community or even to the Commonwealth of Pennsylvania. School districts across the state and the country have been forced to reduce staff, close buildings, cut courses and extra-curricular activities, and increase class size, to name a few. It is important to emphasize this is a situation which is not unique to Pine-Richland. School districts across the state and nation are facing similar challenges.

Outline



- In this presentation, we will cover the following topics:
 - Revenue
 - Funding overview
 - Legislative changes
 - Expenditures
 - Implications for our school district & community



Pine-Richland School District's funding consists of local, state and federal sources. 78% of our revenue is derived from local sources, the largest of which is tax revenue from both real estate and earned income. Current real estate tax collections represent 65% of the school district's overall annual revenue; however, earned income tax only represents 8% of total revenue. The dependence upon local tax revenue is apparent from the chart shown.

In recent years, regulatory limitations at both the state and federal levels have created challenges for local school boards. Each year schools are faced with increasing mandated costs. The difficulty is managing unsustainable cost increases and limited revenue while continuing to offer a quality educational experience for our students.

Funding of Public Education



- Landscape for funding public education has changed significantly in recent years
- Legislative changes and regulatory limitations have impacted both school districts' revenues & expenditures
 - Indexed tax limits imposed on local school boards
 - Increasing mandated costs
- Emphasis has shifted to multi-year sustainability projections & long-term decision making
 - Limits to local revenue
 - Increasing fixed costs
- Significant program and personnel cuts have been necessary in Pine-Richland and in schools across the country

In the past few years, the landscape for how public education is funded in Pennsylvania has changed significantly. Regulatory limitations on real estate tax millage rates have restricted the ability of school boards to raise additional revenues through tax increase. As a result, the focus of financial decisions has shifted to long term sustainability. Even if the district is able to balance the next fiscal year budget without a tax increase, the school board is now faced with the compounded reality of indexed millage limitations imposed in the law. What was once an analysis of financial budgets on a yearly basis has now become an emphasis on multi-year projections and long term decision making.

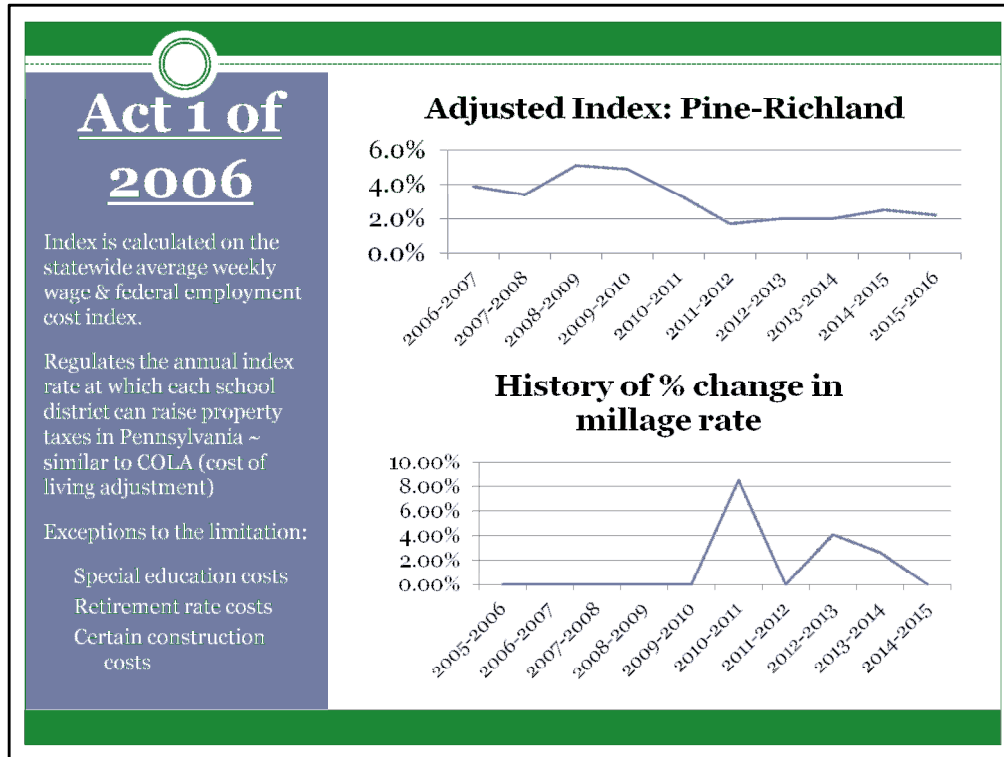
As noted in our most recent annual report, Pine-Richland has been active in addressing the financial climate by pursuing alternative revenue sources such as: grants, donations, facility rental agreements, student activity fees, parking fees, energy curtailment programs, and rebates. Furthermore, the district has reduced costs by: curtailing programs such as physical education, refinancing bond issues, eliminated post-employment medical benefits and not filled vacant staff positions.

Act 1 of 2006 – Taxpayer Relief Act

- Law was designed to provide state gaming revenue to local school districts, which is then used to lower property taxes to homeowners with approved homestead applications on file
 - In reality, a property owner with an approved homestead will receive a tax reduction in the amount of \$193.77 in 2014.
 - Tax reduction amount is the same ~ regardless of property valuation

In July 2006, the Governor of Pennsylvania signed into law Act 1 of 2006, the Taxpayer Relief Act. The law was later modified in June 2011 by Act 25 of 2011. The law imposes a limitation by which school board directors are not permitted to raise the real estate tax rate beyond a predetermined index or percentage each year. It does provide for some exceptions to exceed this limitation. Increases in tax rates beyond those permissible under the Act would require referendum approval by the voters of the Pine-Richland School District before budget adoption could occur.

Each year, the school board approves a Homestead and Farmstead Exclusion Resolution for the upcoming tax year. Residents with an approved application on file with Allegheny County will receive a reduction in assessed value for their school property tax. Each year the reduction amount has been decreasing slightly for residents since the passage of the Act. This is because the overall state gaming funds to Pine-Richland remains the consistent and is divided by a larger number of homesteads each year. In 2014, Pine-Richland has 6,488 approved homesteads.



The Act 1 Index is the state's measure for determining property tax increases justified by wage inflation. Each district's index is calculated separately for each fiscal year, and consists of two parts: the base index, and the district adjustment (if applicable). The statewide base index is the average of 1) the percentage changes in wages statewide, and 2) the percentage changes in school employee compensation costs nationwide. The base index reflects the rate of change in compensation costs. The state also provides for an adjustment to the index based on local environment. If a school district qualifies, a district's adjusted index is the base index plus an adjustment for lower wealth districts. The adjustment is based on a district's relative wealth, with the lowest wealth districts receiving the largest upward adjustments to the base index. Since the passage of Act 1, Pine-Richland School District has always been granted an adjustment to the base index because we are considered a lower wealth district. This is primarily a factor of our tax base, which is mostly residential with a high population of households with school age students in our district. The adjusted index for our district is 2.2% for the 2015-2016 budget year.

As shown on this slide, index limitations on tax increases have existed since 2006. Pine-Richland School District did not raise taxes for five consecutive years because of the rapid growth in our area. However, during three of those fiscal years, Pine-Richland utilized a total of over \$3 million of fund balance to cover increasing costs.

Currently, school districts still have the ability to file for exceptions to exceed the index. These have been and will continue to be phased out over time. Pine-Richland School District only qualifies for exceptions related to rising special education costs and increases in the employer contribution rate for the Pennsylvania Public School Employees Retirement System (PSERS).

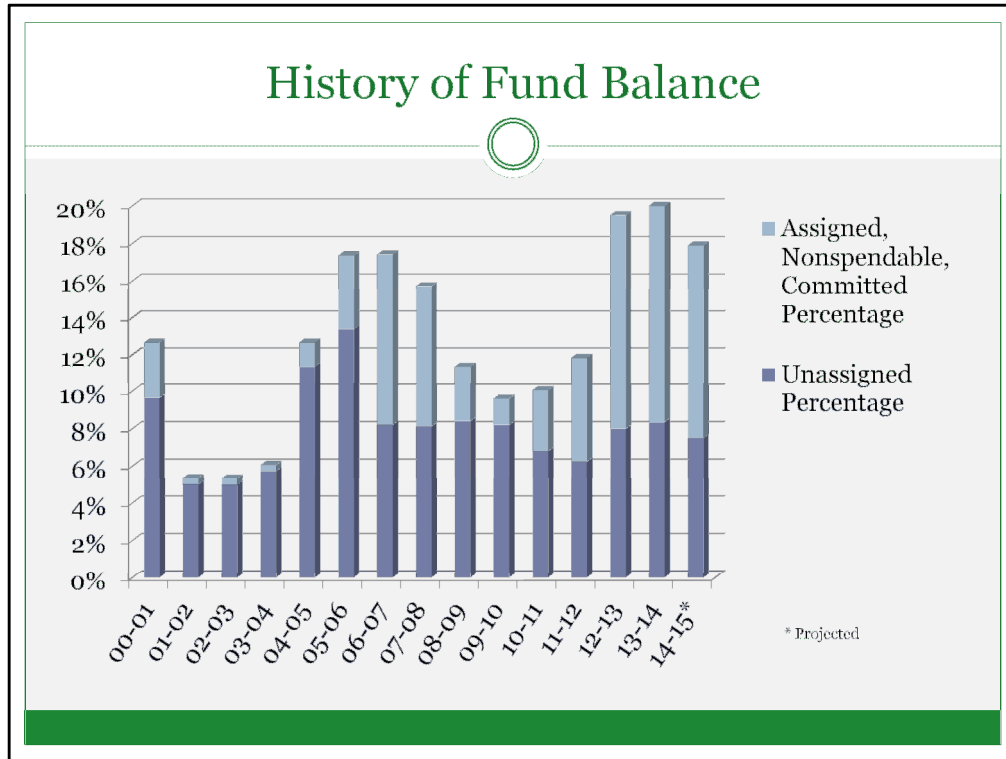
Market Value Aid Ratio	
Allegheny County	Pennsylvania
<ul style="list-style-type: none"> In Allegheny County, Pine-Richland School District is ranked 19th out of 43 school districts. 	<ul style="list-style-type: none"> Statewide, Pine-Richland School District is ranked 226th out of 500 school districts. This is a drop from the previous year ranking of 218th of 500 school districts across the State.
<small>Source: Pennsylvania Department of Education website - Financial Data Elements - market value per weighted average daily membership; http://www.education.state.pa.us/portal/server.pt/community/financial_data_elements/7672</small>	

As noted on the previous slide, school districts with a lower measure of wealth receive an adjustment to the statewide base index. Our school district has a higher amount of student enrollment in comparison to our taxable resources than other districts in our area.

On an annual basis, the Pennsylvania Department of Education (PDE) calculates aid ratios for each school district. This is the State's measure of the relative wealth of a school district based on market value and personal income for each pupil, in relation to the State average. The market value/personal income aid ratio is PDE's measure of a school district's ability to pay. Of these two primary components of local revenue, it is important to note market value is the most significant component in the school district's overall revenue sources.

Annually, PDE releases financial aid ratio spreadsheet for school districts across the State. We exported the most recent data from the PDE website and sorted all school districts from largest to smallest by market value per weighted average daily membership (MV per WADM). By just analyzing the school districts located in Allegheny County, we see the Pine-Richland School District is ranked 19th out of 43 districts for the value of our real estate tax base in Allegheny County. In other words, this represents the real estate market value divided by student enrollment. By expanding the analysis to the entire State for this same metric, Pine-Richland School District ranks 226th of 500 school districts within Pennsylvania. This has dropped from the previous year in which Pine-Richland was ranked 218th of 500 school districts in the State. Pine-Richland School District is not in the top 40% of wealth distribution in either the County or the State.

The purpose in presenting this information is to describe PDE's assessment of the relative wealth of Pine-Richland. By adjusting the index from 1.9% to 2.2%, PDE has recognized the potential need of the district to raise property taxes above the average the level of other school districts in the state.



A school district's fund balance represents the amount by which assets exceed liabilities. In recent years, restrictions have been placed on school districts regarding limitations imposed on unassigned fund balance reserves. If a school district maintains over 8% in fund balance, these reserves should be assigned or committed for a purpose. Assigned and committed fund balance at Pine-Richland School District has been established for future capital improvements, debt service expenditures and employee benefit obligations.

Bond rating agencies analyze the financial statements for school districts and put emphasis on levels of fund balances and reserves. In order to maintain a stable financial position, we need to be intentional about our utilization of fund balance for non-operational expenditures, when necessary. A school district's fund balance cannot be utilized for operational expenditures.

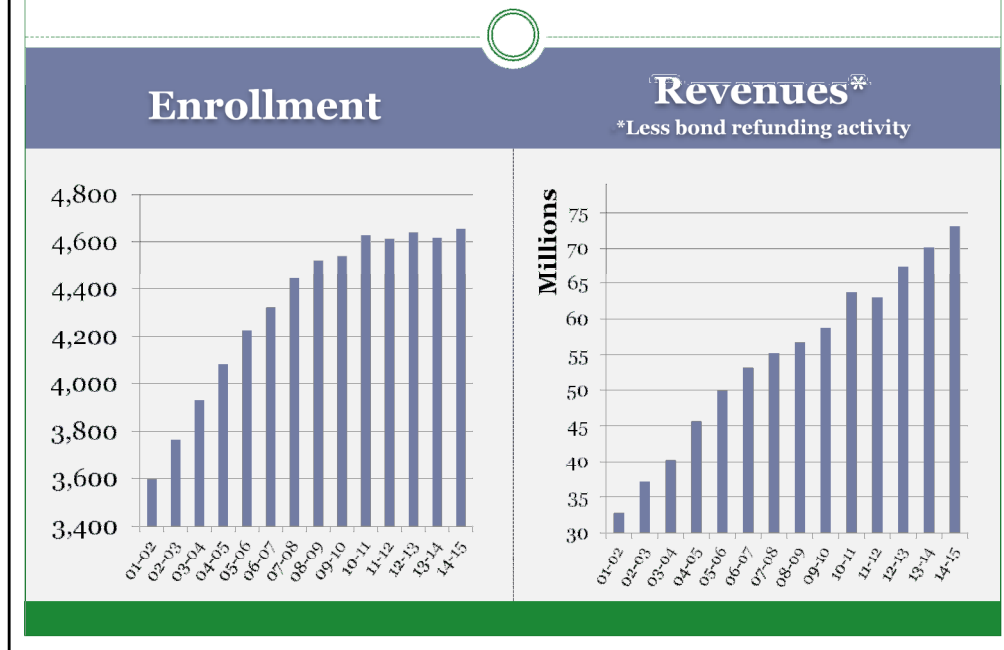
Projections reflect between \$2 and \$3 million in assigned reserves being utilized during the 2014-2015 school year to cover retroactivity for a collective bargaining agreement and capital funding items.

Fiscal Responsibility



Pine-Richland has been active in controlling costs where possible. School districts are faced with legislative mandates and fixed costs beyond our control.

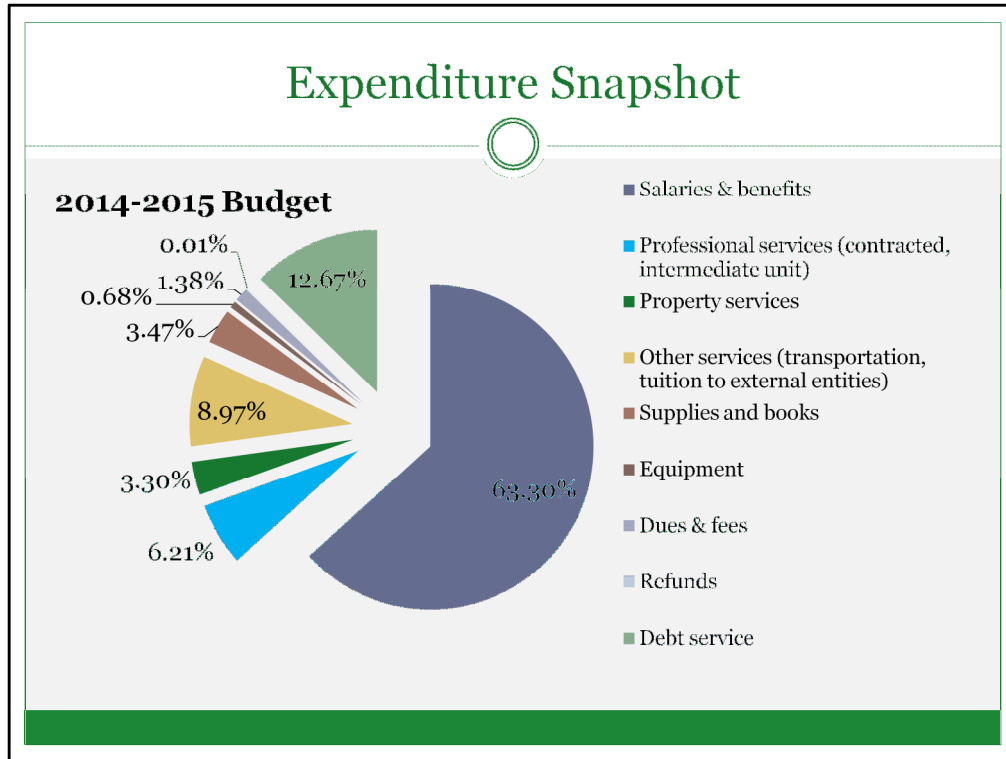
Community Growth



These charts demonstrate increasing enrollment has been a result of growth in our area which also results in increased revenue to our district. It would seem this correlation should cover any budget shortfalls which would occur. However, as noted later in the presentation, school districts are faced with increased mandated costs which are causing the financial challenges we see today.

Some would argue the annual index imposed by Act 1 creates a method by which school districts must 'live within their means'. However, in our district, we face the challenges of a growing community with many young families, as well as a number of families on a fixed income. With additional households, we do gain additional real estate and earned income tax revenue; however, we also gain additional students resulting in additional costs to the district with the challenges of providing a high quality educational experience.

Due to community growth in past years, the district's facilities reached a point where the classroom areas were not large enough to accommodate the number of students enrolled and some buildings had modular classrooms for a few years. In 2008-2009, the district opened a new upper elementary building for grades four through six to bring the district's primary schools back to a functional level of capacity. Eden Hall Upper Elementary was designed to provide common learning areas. The building is divided into biomes made up of grade level teams with common collaborative space for sharing of ideas and enhanced academic instruction. In 2012, the new STEAM addition was added to the high school to promote science, technology, engineering, arts & mathematics. The building has been designed to provide students with the opportunities for hands-on learning and the make our students more competitive in the global marketplace. However, the landscape for public education has changed since these buildings were constructed. As a result, we must understand these changes and make budgetary decisions which will be in the best interest of our students and community in the long term.



Salaries and benefits for administration, faculty & support staff represent 63.3% of total annual budgeted expenditures. The chart demonstrates the significance of personnel related costs to the overall district budget. We deliver educational services to our students through our staff.

The second most significant area of the district budget is debt service which represents 12.67% of total expenditures. As noted earlier, district facilities were constructed to accommodate the increasing growth in student enrollment. Bond issues were used to fund these projects and consequently the district is required to pay the principal and interest on an annual basis. During 2014, the Pine-Richland School District was able to reduce debt service expenditures through refunding bond issues and achieving savings in interest costs on these liabilities. This percentage shown is a reduction from 13.6% of total expenditures from 2013-2014.

In addition, the district has a number of contractual outsourced service agreements within the general operating budget for transportation, technology and substitute staffing.

Significant Cost Drivers

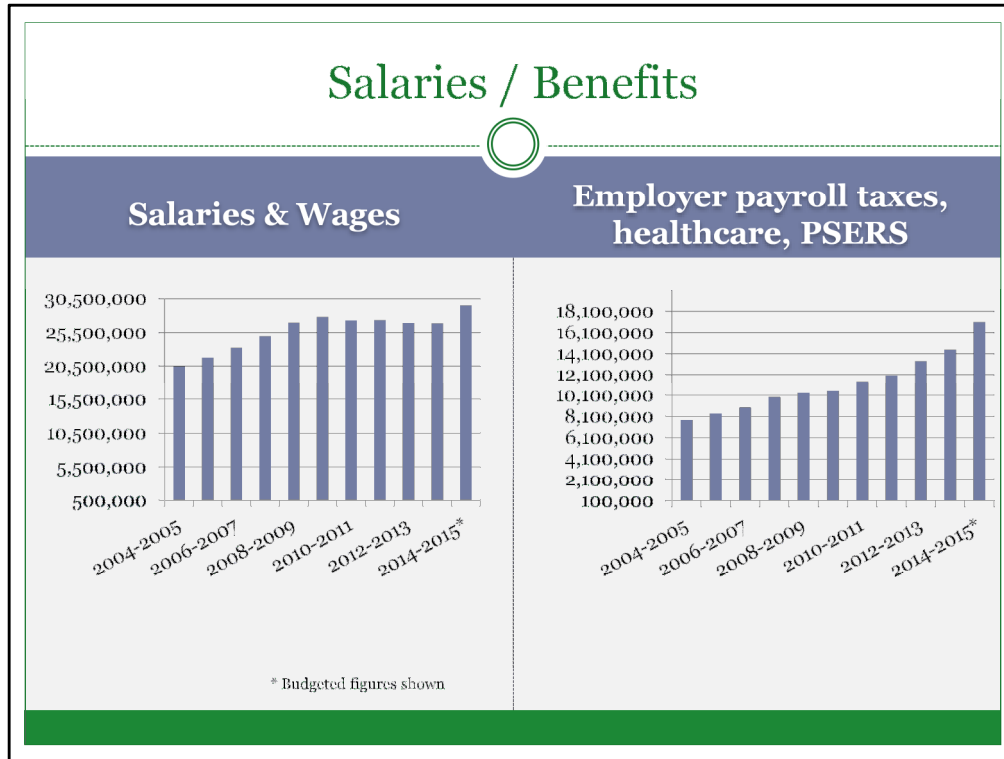


SALARIES & BENEFITS

RETIREMENT SYSTEM

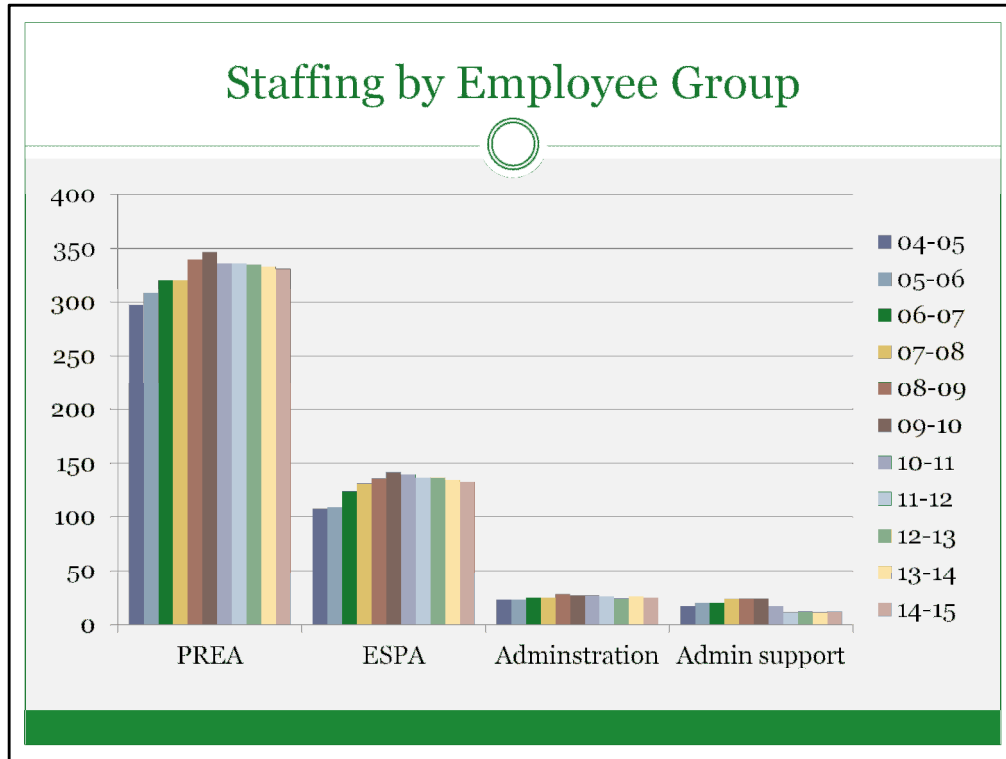
CONTRACTED SERVICES

TUITION – EXTERNAL ENTITIES



The district's annual personnel costs are dictated by various collective bargaining agreements and compensation plans. Salaries are controllable by decreasing the number of employees through attrition or the curtailment of programs that may lead to furlough. For the prior two fiscal years, salary cost has been held at status quo for a large portion of the staff at Pine-Richland School District due to ongoing negotiations with the teachers' union. Upon ratification of the agreement in September 2014, retroactive salaries were paid during the 2014-2015 fiscal year. This payment of salaries pertaining to previous fiscal years will be reflected as a draw down of fund balance in this year's financial statements.

Despite salaries remaining somewhat level in previous years, employee benefits have increased substantially each year. Pine-Richland School District does not have the ability to set the contribution rates for these expenditures. Employee retirement benefits through PSERS are mandated by legislation and healthcare premiums are established Allegheny County Schools Health Insurance Consortium.



By eliminating vacant positions and curtailing programs over the past few years, the district has been able to achieve cost savings for the long term.

PREA represents instructional faculty, guidance counselors, librarians, and nurses. ESPA includes all building secretaries, custodians and maintenance, instructional & library assistants, and paraeducators. Administration represents district-wide administrators, building principals, psychologists. Admin support includes central office, media personnel (PRTV), security, and college & career specialist.

Public School Employees' Retirement System

- Governmental, multi-employer, defined benefit pension plan for school employees in Pennsylvania
 - Operating parameters are defined by state legislation
- Funding mechanism:
 - Employer contributions (paid by school districts and the Commonwealth of Pennsylvania)
 - Employee contributions
 - Investment returns

PSERS was established on July 18, 1917 and is a governmental, multi-employer, defined benefit pension plan for school employees in Pennsylvania. This type of plan provides a specified formula for the annual pension benefit an employee will receive upon retirement. Funding is based upon the number of participants in the plan, their years of service, their expected earnings at retirement and the actuarially calculated rate of retirement, life expectancy and expected number of years of payments. The amount of a member's pension benefit is not tied to the investment performance of the fund.

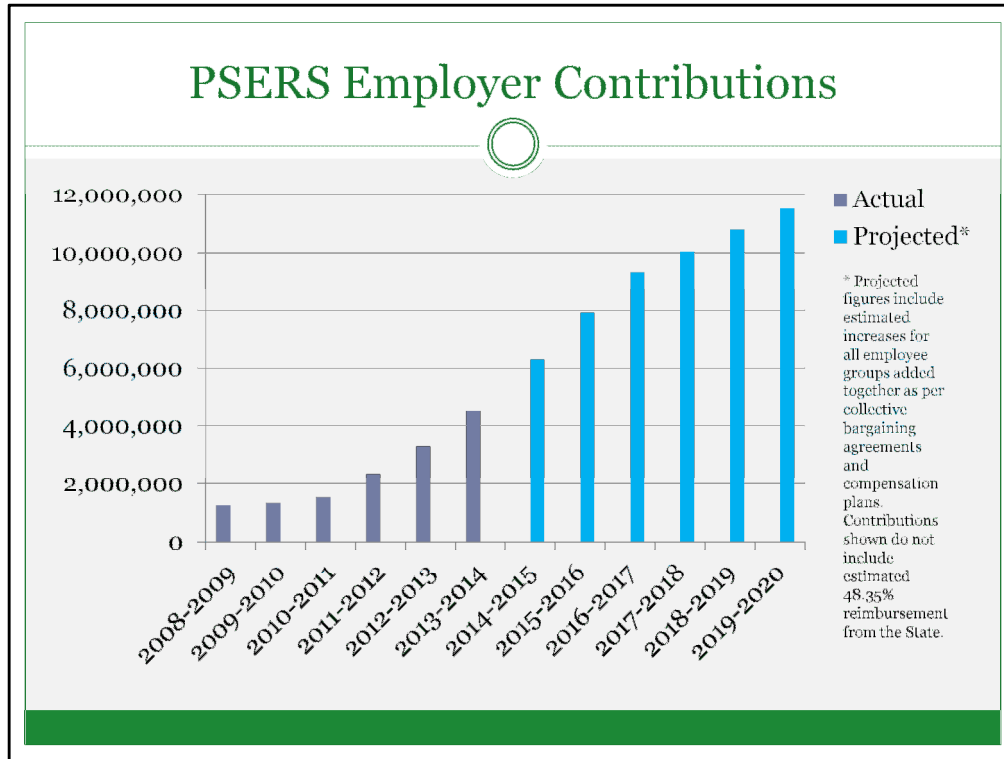
Investment Performance Risk

- Investment earnings are the primary source of funding for benefits.
- When investment performance was high in previous years, the employer contribution rate for both the state and school employers was lowered, as a result of state legislation
- Changes in the economy in recent years have negatively impacted the status of funding for the plan.

Over the last few decades, 71% of funding for the plan has been derived from investment earnings. The remaining 29% has come from employee contributions (12%) and employer contributions (17%). In a defined benefit plan, the members do not benefit when the investment performance of the fund is good. The Commonwealth of Pennsylvania and school employers benefit through a reduced employer contribution rate to PSERS. Likewise, the employees do not bear the investment risk of a down market. Investment risk is borne by the state and school employers through the employer contribution rate. Hence, the employer contribution rate rises when there is investment loss.

In 2011, legislation was passed to help alleviate some of the current funding issues of the PSERS plan. Effective July 1, 2011, new members to PSERS bear some of the investment risk via the shared risk provisions of Act 120.

As noted earlier in the presentation, investment earnings in recent years have been very positive for the plan. However, the unfunded liability remains over \$35 billion.

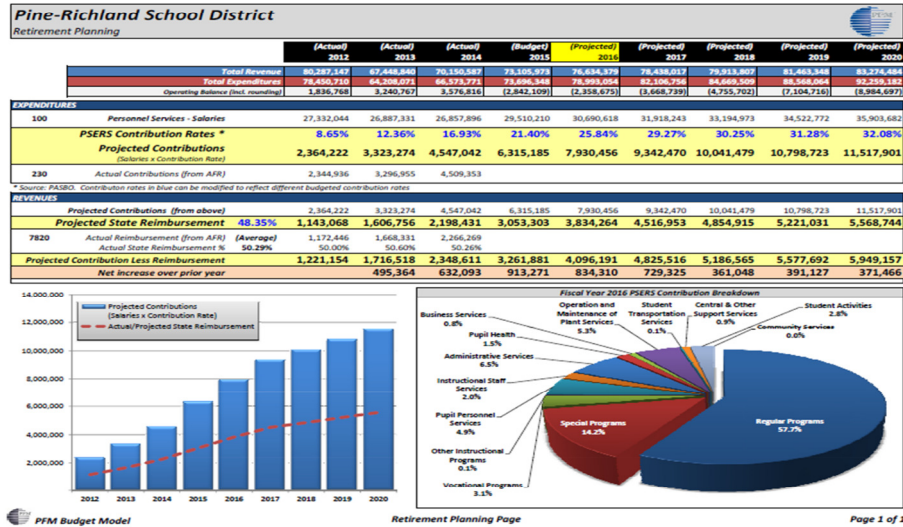


As a result of low investment performance, employer contribution rates for the Public School Employees' Retirement System (PSERS) have been increasing steadily. Although the burden of these increases is being shared by the state, the net increase to the district's budget on an annual basis is substantial. The contribution rate is set by the PSERS Board of Trustees and is mandated by state legislation. School employers do not have the ability to restructure benefits offered to retiring members and are mandated by the law to pay the employer contribution rates established by the PSERS Board.

For 2015-2016, the rate has been set to 25.84% of the salary cost for covered employees. Future projections of the employer contribution rate (as of the June 30, 2013 PSERS actuarial valuation) show a steady increase to about 32% of salary cost in the 2019-2020 fiscal year. At which point, the employer rate is expected to remain at or above this level.

Over the years, the school board has been working toward setting allocations aside in the district's fund balance to address these rising rates. By committing and assigning portions of fund balance, the district has been providing for a long-term plan to aim at lessening the annual impact of these increases in the annual general fund budget moving forward.

PSERS Employer Contributions



This slide represents an excerpt of the Pine-Richland School District's long-range budget model as of January 2015. Not only does this slide depict the annual employer contributions in relation to the overall General Fund Budget, but it also demonstrates the affect of state reimbursement. The year-over-year impact to the 2015-2016 budget is over \$830,000 just for PSERS contributions alone. The light tan bar in this graphic provides additional clarity around these significant year-over-year increases even if staffing were to remain constant.

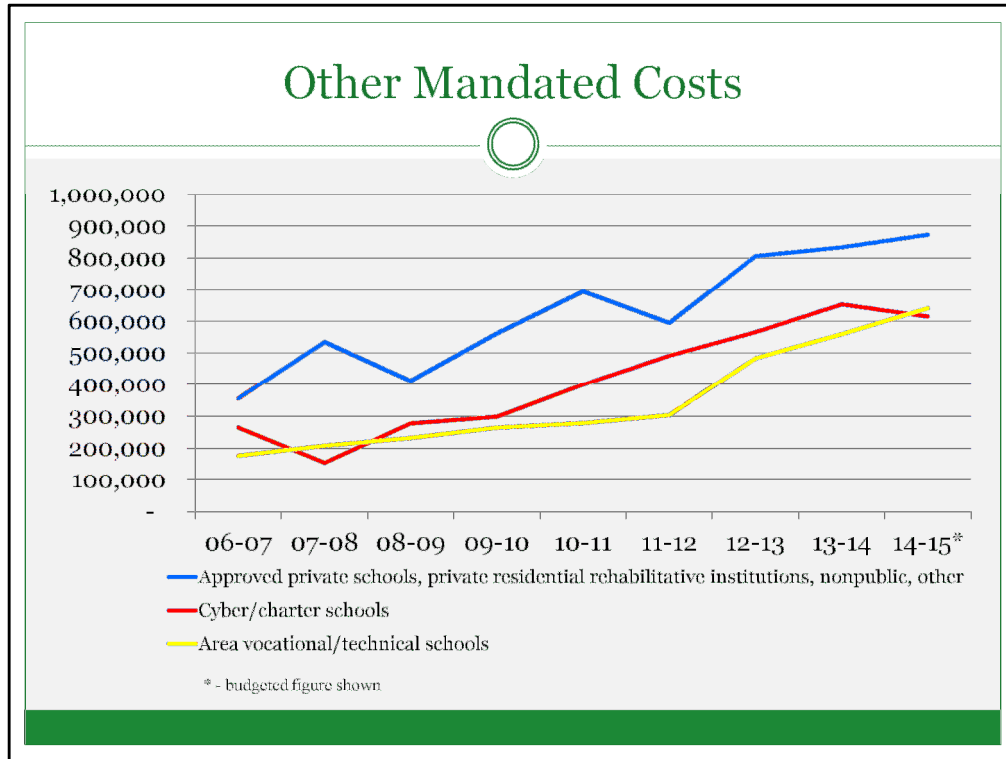
Outsourced Service Contracts

- General Fund
 - Transportation
 - Technology
 - Substitute Staffing
 - Copiers / Print Management Services
- Food Service Operations

Within the general operating budget, the district has outsourced service agreements for transportation, technology, substitute staffing and copiers/print management services. These contractual agreements combined represent about \$6.2 million of the district's overall expenditures, which is about 8.5% of total budgeted costs.

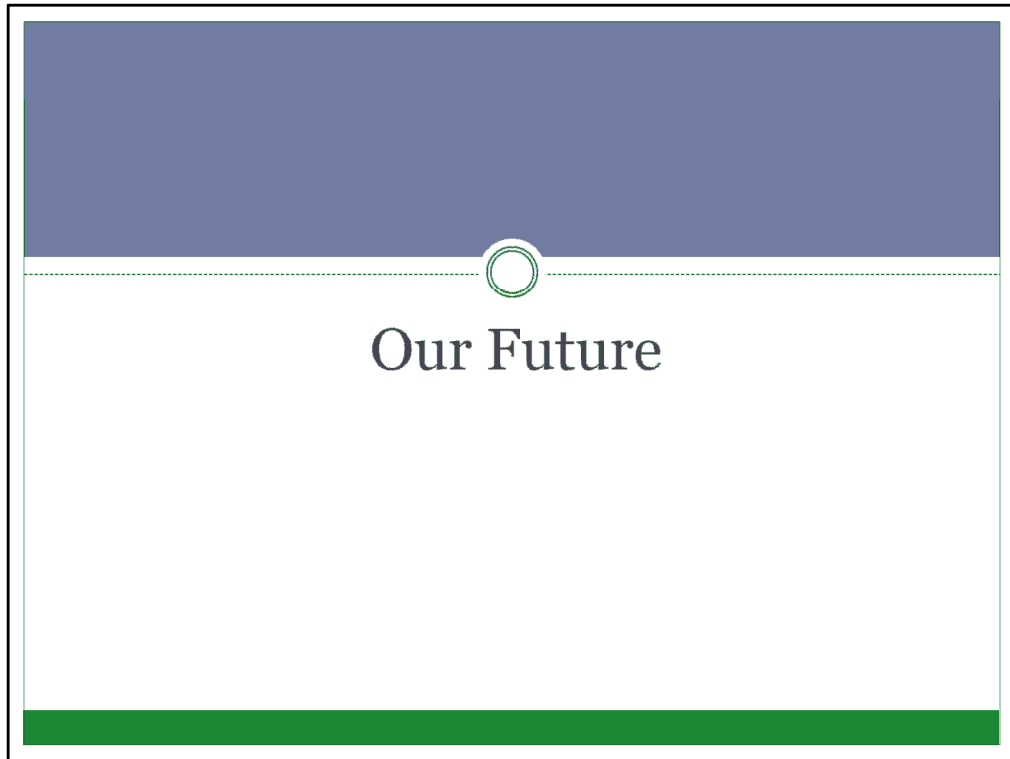
Food service operations are self-supporting and separate from the general operating budget.

The Pine-Richland School District has been actively and aggressively issuing requests for proposals and renegotiating contractual agreements in order to ensure competitive pricing for outsourced services.



The district is required by law to pay tuition costs for students who reside in the Pine-Richland community to attend cyber/charter schools. Over the past five years, the district's expenditures for cyber/charter school tuition have more than tripled. During the 2013-2014 fiscal year, the district paid \$653,148 to cyber/charter schools. Our obligation was \$8,960.96 for each general education student (43 students) and \$19,217.78 for each special education student (11 students) enrolled in these programs.

Pine-Richland's enrollment of students with special needs has been increasing steadily. The district is mandated to provide free and appropriate public education in the least restrictive environment for all students with disabilities regardless of cost. There are certain circumstances for which outplacement at a private institution is the best course of action. The district is required to incur the tuition expenditures for these students. As our enrollment increases, our costs related to specialized services continues to increase as well. Yet, our funding from the state for special education subsidy has remained somewhat level for many years. In 2013-2014, we paid over \$830,000 to approved private schools and other placements.



Economic Value of the School System



- District Vision Statement:
 - Pine-Richland School District is a community where learning is challenging, people are inspiring and students are enriched by their experience.
- Property values in our community are higher as a result of student achievement in our school system
- Growth in enrollment has been a result of new residential construction in both townships
- Pine-Richland has a strong reputation:
 - Academics
 - Course offerings
 - Special education
 - Athletics
 - Extra-curricular activities

The Winter 2013 issue of Scholastic Administrator included an article titled, '*Sell Your Schools.*' The core content of the article pertained to a community's return on investment in the school system as an economic entity. Property values have a direct correlation to the quality of the local school district. We cannot cut our way to excellence. When the quality of the service and educational experience we offer our students is impacted, there is a directly proportional effect to our community both short-term and long-term.

Future Financial Stability

- Annual budgetary challenges
- Fund balance
 - Capital improvements
 - Future benefit obligations
- District bond rating
- Alternative revenue and corporate partnerships
- Long range planning

The school board has been diligent over the past few fiscal years in approaching each annual budgetary gap with a balanced method of reducing operating costs, curtailing programs, eliminating vacant positions, utilizing assigned fund balance for capital improvements and increasing millage rates. It is imperative to recognize fund balance is maintained to provide for a stable foundation for the district's financial position. As mentioned earlier, fund balance cannot be utilized for operational expenditures. Assigned and committed portions of fund balance reflect long term financial planning.

The district's bond rating was recently upgraded in April 2014 to AA-/stable as determined by Standard & Poor's Ratings Services. Part of our rating is based on our financial stability. As stated by S&P, the district has 'sound finances, characterized by strong reserves'. Bond rating agencies monitor the financial statements for school districts and analyze reserves. In order to maintain a stable financial position, fund balance reserves cannot be depleted to fill annual budget shortfalls.

As we look toward the future, we will continue to review district expenditures for operational efficiencies and explore alternative revenue sources where feasible. We will also continue to work with the Pine-Richland Opportunities Fund to support teacher grants, scholarships and corporate partnerships to provide real world experiences for our students. It is important to make informed decisions and to focus on the long-term financial stability of the district.

Goals



- Continue to increase operational efficiencies
- Analyze staffing levels
- Evaluate multi-year impact of all decisions
- Balance challenges of providing a quality, educational experience for students with the economic impact on residents with fixed-income
- Team-based budgeting process

No one singular action can be done to solve these issues. Long-term financial planning is essential for the school district's sustainability.