



## Senate Education Committee

### Testimony by Secretary of Education Pedro A. Rivera

May 12, 2017

Good afternoon Chairman Eichelberger, Chairman Dinniman and members of the committee. Senator Laughlin, thank you for inviting the committee and Department to Erie to engage in this important conversation. As Pennsylvania's Secretary of Education, I oversee 500 school districts in the commonwealth, each with their own unique attributes and needs. These 500 school districts are comprised of more than 2,900 schools, ranging in size from 200 to 140,000 students, and serve communities located in the state's largest cities, rural regions, and everywhere between. My focus today will be on the process the Pennsylvania Department of Education (PDE) uses to identify and support financially struggling school districts.

Act 141 of 2012, the School District Financial Recovery Law, governs much of Pennsylvania's focus on assisting financially struggling school districts to get back on a path toward financial stability. The law requires the Department to monitor the fiscal health of school districts and allows the Secretary of Education to declare up to nine districts in Financial Recovery Status. This system for financially struggling school districts was implemented on the heels of the Great Recession, when families and communities were faced with significant economic challenges and at a time when schools faced drastic funding cuts. It was also enacted when state funding for schools was not appropriated through a formula that properly accounted for the additional costs of educating students with different needs, such as those living in poverty or learning English.

Financial security makes a difference for families, communities, and schools. While funding alone will not ensure students' success, schools cannot provide effective instruction and learning experiences aligned to the expectations of our interconnected, global economy without adequate resources. Over the past two years, Governor Wolf and the General Assembly have worked together to secure historic investments in Pennsylvania's public education system and established a new funding formula that provides for a more equitable distribution of state education funds. Despite the significant achievement of this new funding formula, inequities in funding across Pennsylvania's schools persist. Pennsylvania's per-pupil spending is severely disparate, ranging from \$10,303 in the lowest spending district to more than double that - \$25,234 - in the highest spending district.

This means that for many school districts - particularly those in poorer communities with less local resources but significant need, including those hit hardest by the economic downturn and decreased state funding - fiscal challenges continue to pose a real threat not only for financial solvency but for student success.

#### Financial Watch

Act 141 of 2012 amended the Public School Code to provide for a system of support and identification of school districts in Financial Watch and Financial Recovery. The law gave PDE authority to monitor the financial status of all school districts through an early warning system to identify at-risk school districts to be placed in Financial Watch Status.

Act 141 requires PDE to analyze data submitted by school districts to the Department in the Annual Financial Reports (AFR). Based on this data, PDE identifies trends which may indicate challenging financial circumstances and/or a troubling financial outlook for a school district, including an analysis of Fund Balance Ratio, Borrowing Base Capacity, and Debt Ratio. A Basic Education Funding (BEF) advance or a bond intercept payment may also be considered as indicators of financial distress. PDE is also authorized to review additional data relevant to financial conditions, such as fiscal measures and socioeconomic data; these measures include Market Value/MV/Personal Income Aid Ratio, Equalized Mills and School Tax Ratio. PDE can also consider whether any municipality located within the school district is declared as financially distressed under Act 47 of 1987 (Municipalities Financial Recovery Act).

The following components are considered in this initial analysis:<sup>1</sup>

- *Fund Balance Ratio.* Fund balance ratio indicates how much cash the school district has on hand in the event an unanticipated need arises. A higher fund balance ratio indicates a greater ability to meet fiscal obligations. The fund balance ratio is calculated by using a school district's total assets minus its total liabilities divided by the total general fund expenditures.
- *Borrowing Base Capacity Available.* Borrowing base capacity indicates to what extent a school district, according to law, can incur additional debt. A higher borrowing base capacity available indicates a greater ability to borrow more money. The borrowing base capacity is calculated by: a school district's total debt that can be incurred minus the total outstanding debt, divided by the total amount of debt that can be incurred, according to the Local Government Unit Debt Act (LGUDA).
- *Debt Ratio.* Debt ratio can be used to determine the school district's ability to be approved to add additional debt. A lower debt ratio indicates increased ability to incur more debt. Debt ratio is calculated by taking a school district's total debt service payments divided by total expenditures (for all funds). A three-year average is used to calculate this ratio.
- *Advance Basic Education Funding (BEF).* A BEF allocation payment made, pursuant to School Code section 2517(e), in advance of the dates set forth in section 2517(c) may indicate a decreased ability to meet fiscal obligations. BEF advances may be a warning sign that a school district is experiencing difficulties managing its cash flow.
- *Bond Intercept.* An agreement entered into between a school district, PDE, and a bond trustee to have the Department make bond payments directly to a trustee via deduction from the school district's subsidies. Bond intercept payments may indicate decreased ability to meet fiscal obligations.

As mentioned previously, the Department may also explore additional data relevant to financial condition, including the following:

- *Fiscal Measures and Socioeconomic Data.* The following other fiscal and socioeconomic components will be analyzed: Market Value/Personal Income Aid Ratio, Equalized Mills and School Tax Ratio.
  - *Market Value/Personal Income Aid Ratio.* A school district's combined market value (MV) and personal income (PI) wealth for each resident student as compared to the state average. The lower the MV/PI Aid Ratio, the less dependent the school district is on state funding. Market value/personal income aid ratio demonstrates the financial "wealth" of a school district.

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<sup>1</sup> Under section 611-A(c) of the Public School Code of 1949, the Secretary of Education is required to establish guidelines for the Early Warning System. The principal goal of the guidelines is to identify and provide technical assistance to school districts to prevent them from becoming Financial Recovery Status school districts. The Early Warning System Guidelines are operational upon publication in the *Pennsylvania Bulletin*. Please see [School District Financial Recovery Early Warning System](#), PA Department of Education, September 2012.

- *Equalized Mills*. A school district's total taxes collected divided by its taxable market value as certified by the State Tax Equalization Board. A higher equalized mills ranking indicates a greater taxation effort when compared to other school districts. High equalized mills indicate a decreased ability to raise additional funds via taxes. Equalized mills compare the tax burden based on the market value of taxable properties in the school district against all other school districts in Pennsylvania.
- *School Tax Ratio*. A school district's total taxes collected divided by the personal income of its resident taxpayers. A higher school tax ratio indicates a greater taxation effort on the part of taxpayers when compared to other school districts. High school tax ratio indicates a decreased ability to raise additional funds via taxes. School tax ratio compares the personal income tax burden in the school district against all other school districts in Pennsylvania.

After this preliminary analysis, PDE will determine whether a school district may be experiencing financial difficulty; for those that are identified, PDE will contact the district and ask for additional, up-to-date information about their financial status. This information includes, but is not limited to, the district's current budget, cash flow analysis, fund balances, and status of audits. During this second level of analysis, PDE works directly with the school district, and consults with school district officials, as needed. Based on the information gathered during this robust process, PDE may decide to monitor the district or designate the school district as being in Financial Watch Status. Currently, there are five school districts identified in Financial Watch Status in the commonwealth's Early Warning System: Reading School District, Aliquippa School District, Wilkesburg School District, and Steelton-Highspire School District. Erie City School District is also in Financial Watch Status as determined by Act 86 of 2016.

It is important to note that districts identified for Financial Watch Status are offered technical assistance before their financial issues require greater interventions prescribed by Act 141. Recognizing that financial and academic challenges are often intertwined in struggling districts, PDE provides both financial and academic technical assistance and supports to districts in Financial Watch Status to ensure students are receiving a high-quality education. The assistance provided by PDE is tailored to the needs of the specific district and may also include consultation with various agency staff, focusing on non-financial related issues such as special education, school safety, or curriculum and instruction. The Department has worked with Public Financial Management Group (PFM) to provide additional capacity and support for school districts under financial constraints, offering seminars and online webinars to district leadership teams.

### Financial Recovery

Act 141 also included both statutory and regulatory triggers for districts to be placed in a more significant Financial Recovery Status. Four school districts were placed in Financial Recovery when Act 141 was enacted due to statutory triggers: Chester Upland School District, Duquesne City School District, Harrisburg City School District, and City of York School District. The law also directed the State Board of Education to promulgate regulations establishing criteria which the Secretary of Education may consider in determining whether to issue a declaration that a school district is in Financial Recovery Status. Since the Title 22 Pa.Code Chapter 18 regulations were finalized in August 2016, PDE has worked to develop a thoughtful and meaningful way to place school districts in Financial Recovery Status, if necessary. No additional districts have been placed in Financial Recovery through regulatory triggers. Under the law, no more than nine school districts can be in Recovery Status at a time.

Once a school district is placed in Financial Recovery Status, the Secretary appoints a Chief Recovery Officer (CRO) to develop a financial recovery plan, in consultation with the district's superintendent. Act 141 spells out specific requirements for the financial recovery plan, which are included below:

- Provide for the delivery of effective educational services to all students enrolled in the financial recovery school district.

- Provide for the payment of lawful financial obligations of the financial recovery school district.
- Provide for the timely deposit of required payments to the Public School Employees' Retirement Fund.
- Provide a plan for the financial recovery school district's return to financial stability.
- Set forth a cash flow analysis for the financial recovery school district.
- State projections of revenues and expenditures for the current year and the next two years, both assuming the continuation of present operations and as impacted by the measures included in the financial recovery plan.
- State benchmarks and timelines for restoring the financial recovery school district to financial stability.
- Specify criteria that the financial recovery school district must satisfy before the secretary may terminate the financial recovery school district's Financial Recovery Status.

The CRO must develop the financial recovery plan in consultation with the superintendent, and copies of the plan must be shared with the district's business office, school board members, and solicitor. The financial recovery plan must also be made publicly available on the district's website and in hard copy form in the district's business office. After review and public inspection, the school board then must vote on the financial recovery plan. If a school board fails to approve the plan, the Secretary must go into the Court of Common Pleas and request the appointment of a receiver for the district. The receiver assumes all the powers of a school board, except raising and levying taxes.

In Harrisburg City and York City School Districts, the school boards approved the financial recovery plans and a Chief Recovery Officer stayed in place to oversee the implementation of the financial recovery plan. However, the school boards of Chester Upland and Duquesne failed to approve their plans, so the Secretary petitioned the Court of Common Pleas to appoint receivers in both districts. The initial three-year period of receiverships for Chester Upland and Duquesne expired and were extended for another three years in 2016.

### Erie

The Erie City School District (ECSD) was placed in Financial Watch Status on September 20, 2016. Section 694-A of the Public School Code, added by Act 86 of 2016, required school districts receiving \$2 million or more in Educational Access Program funding to be placed in Financial Watch Status and to "develop a plan to improve the school district's finances." ECSD received \$4 million in Educational Access Program funds through two \$2 million payments, one occurring in September 2016, the other in December 2016. Per the requirements of Act 86, ECSD was placed in Financial Watch Status and was required to develop a plan to improve the district's finances.

The process of creating and approving a plan for the financial health of ECSD has been ongoing, with extensive conversations between the district and the Department. ECSD submitted an initial plan to PDE on December 6. Based on Department requests for clarification, the school district submitted a revised financial plan to PDE on January 12. The Department undertook a thorough review of the revised plan. Multiple areas of the agency – including senior leadership and staff from the Bureau of Budget and Fiscal Management, the Bureau of Curriculum, Assessment, and Instruction – as well as independent financial consultants worked to evaluate information supplied by ECSD. The Department disapproved the plan on February 28 and requested that a revised plan be submitted within 60 days. That deadline has been extended an additional 30 days, until the end of May.

ECSD's initial plan relied upon the appropriation by the General Assembly of an additional \$31.8 million in annual state funding. Pennsylvania law does not authorize the Secretary of Education to approve the appropriation of additional state funding for the district. A viable plan cannot commit the current or future General Assemblies to appropriate the funds requested in the initial plan. PDE has communicated that any plan to improve the district's finances must be based on realistic projections for increased revenue,

reductions in spending, or both. The Department recognizes that these decisions are difficult for any school district, but they are decisions best made at the local level. PDE will continue to provide ECSD technical assistance to revise the district's plan to be resubmitted to the Department in the coming month.

In the February 28 letter to ECSD denying the initial plan submitted by the district, the Department urged the district to accept technical assistance offered by PDE as the district revises the plan and to further review the following strategies:

- Consider use of free curriculum development resources available through PDE's Standards Aligned System, or SAS portal, and the local intermediate unit.
- Implement a more focused, efficient, and pervasive professional development plan. Over-arching topics such as peer coaching, co-teaching, and differentiated instruction should be instituted and assessed regularly. Currently, professional development is largely self-selected without target goals or regular follow-up. Instituting more "train-the-trainer" models could increase internal capacity.
- Identify necessary staff and required services/support to build capacity to provide special education services to students with complex needs within the district.
- Develop/revise screening processes to reduce the demand for additional testing by the school psychologists during the special education evaluation.
- Consider additional opportunities to generate local revenue.
- Consider implementing new educational resources to coincide with the renovations of Collegiate and Central schools.

The Department will continue to provide technical support to the Erie City School District as the district makes decisions and implements policies that put them on more firm financial footing. I know that the district is making strategic investments in serving their students, and applaud their commitment to addressing the needs of the Erie community. The district recognizes that students often bring hunger, health or home issues with them to the classroom, and schools play an important role in ensuring that children's – and communities' – needs are met.

Unfortunately, the challenges faced in Erie are also found in communities across the commonwealth. Pennsylvania's students are increasingly living in poverty, and need a variety of supports and services to succeed in the classroom and beyond. Based on the most recently available data, we know that many children and communities across Pennsylvania face significant challenges:

- Nearly one in five children in Pennsylvania live below the federal poverty line;<sup>2</sup>
- More than 465,000 children live in households that were food insecure in the past year;<sup>3</sup>
- Pennsylvania schools serve 276,185 students with disabilities, and 221,000 students who speak a language other than English at home;
- 614,000 children (22 percent) in Pennsylvania have special health care needs because of increased risk of a chronic physical, developmental, behavioral, or emotional condition that requires health and related service above and beyond those of other children. The proportion of children with these health issues has increased substantially in the past decade; in 2001, only 13 percent (379,291) of children had special health care needs.<sup>4</sup>

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<sup>2</sup> The 2015 Federal Poverty Income Guideline for a family of four is \$24,250.

<sup>3</sup> Data Source: Population Reference Bureau, analysis of data from the U.S. Census Bureau, Current Population Survey, Food Security Supplement.

<sup>4</sup> National Survey of Children with Special Health Care Needs, U.S. Department of Health and Human Services,

- Nearly one in five children have one or more emotional, behavioral, or developmental conditions, including autism, depression or anxiety, ADD/ADHD, or behavioral/conduct problems.<sup>5</sup>

Recognizing the important link that student health and well-being have on academic performance, the Department applauds efforts of school districts like Erie, who are integrating student and community supports – such as mental health, food pantries, afterschool and out-of-school programs, and other services – as part of a community schools model.

### Conclusion

I appreciate the opportunity to provide information regarding the Department's efforts to meet its statutory and regulatory requirements related to identifying and supporting financially struggling school districts. We will continue to work with the General Assembly to secure the maximum amount of resources for financially struggling school districts, as well as all districts across the commonwealth. It is our hope that by securing additional investments in K-12 education and by addressing both fiscal and academic challenges in these districts, Pennsylvania can ensure more opportunities for young people to learn and succeed, regardless of where they live.

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<sup>5</sup> NSCH 2011-12 data, via the Kids Count Data Center, <http://datacenter.kidscount.org/data/tables/6031-children-who-have-one-or-more-emotional-behavioral-or-developmental-conditions?loc=40&loct=2#detailed/2/40/false/1021,18/any/12694,12695>.