

PHILOMATH SCHOOL DISTRICT 17J
MEMORANDUM
February 15, 2011

TO: Board of Trustees
PREPARED BY: Kelly Howard, Business Manager
SUBJECT: 2011-12 Budget Shortfall

As you know, we like many school districts, have struggled with budget issues in the past and particularly so the last 3 years. As I have been preparing for next year's budget, I find the magnitude of these challenges has grown to a level I was not totally prepared for. At this time, I estimate that we need to reduce expenses by about \$2 million. There are a number of contributing factors but they combine to create what people commonly refer to now as the "perfect storm". The major factors include:

- Increased operating costs, including payroll costs
- A decade of declining enrollment
- Reduced state revenues stemming from a national recession, high unemployment and falling income tax revenues

Over the last few years as we have grappled with revenue declines, we have to a large degree, avoided the most difficult choices by doing the minimum to get by. The reasoning behind this I believe is twofold. First, there has been a fear that if we cut programs, we may never get them back. It has been reasoned that if we could outlast the economic downturn, then when things got better, we would still have our programs. We all know that once eliminated, a program is difficult to bring back. Second, over the last three years, we have received significant federal stimulus money that has bailed us out. We have used the stimulus money for its designed and intended purpose, to create or retain jobs. In doing so, we plugged large budget holes. Now this money is drying up at a time when state revenues are diving and the percentage of funds Oregon distributes to K-12 education has declined from 44% to 38%. This is largely due to increased demands from the human and social services sector.

District enrollment in 2002-03 stood at 1905 (1855-net of 50 KVCS students). Today total enrollment is 1648 (1485-net of 163 KVCS students). Excluding the KVCS students, we have sustained a 20% student loss. This trend is expected to continue for at least 5 more years. Over the last 6-7 years, we have not resized or downsized our district to match the rate of reduction in State School Fund (SSF) revenues and enrollment declines. One reason for this has been the goal to reduce class size. In addition, over the last two years, Oregon has had one of the highest unemployment rates in that nation and we have been reluctant to send more people unemployment through staff reductions.

Another major factor is the district's liability for post employment benefits. Benefits for early retirement were negotiated in the early 1980's when health insurance was a relatively small portion of the compensation package. Now these costs are eating us alive. In the last 10 years, it has cost the district \$3.656 million dollars for retirement stipends and health insurance for former employees. We have paid out over \$2 million in just the last 5 years. These are dollars that have

been diverted from the classroom or from increasing the district insurance contribution for current staff.

Following is a chart listing the historical student count (ADM), the amount funded per student and the total SSF revenue since the 2004-05 fiscal year. In terms of state funding, we are back at the same level as 2004-05 and we are \$1.5 million less than what we received in 2007-08.

Historical SSF Formula – PSD17J

Factor	04-05	05-06	06-07	07-08	08-09	09-10	10-11	11-12
ADMr	1703.6	1677.9	1656.4	1645.0	1604.9	1567.0	1526.0	1530.0
Weighting	252.2	251.7	251.6	248.5	266.6	259.9	256.6	250.0
ADMw	1955.8	1929.6	1908.0	1893.5	1871.5	1826.9	1782.6	1780.0
ADMw (Prior Yr)	2013.1	1955.8	1929.6	1908.0	1907.9	1871.4	1826.9	1782.6
Net Funding	\$5,155	\$5,600	\$5,959	\$6,313	\$6,163	\$6,092	\$5,941	\$5,898
SSF revenue	\$10,377,184	\$10,952,251	\$11,498,878	\$12,044,487	\$11,758,249	\$11,203,468	\$10,853,613	\$10,513,546

The impact of federal stimulus funds and supplemental money from the state has been significant. The primary purpose of these funds was to retain jobs and the expectation was to use them to accomplish that goal. During the last few years, the adopted budget showed that the Fund Balance would be spent down to balance the budget. Along with cost cutting, federal stimulus money has been an important factor in being able to increase the Fund Balance back up so that there was a sufficient balance to carry over to the next year. This was not the case for the 2010-11 fiscal year. Following is a breakdown of supplemental funding by source and amount.

Description	2007-08	2008-09	2009-10	2010-11	2011-12
School Improvement	\$345,941	\$344,578	\$17,950	\$0	\$0
Sch.Day Restoration		\$134,683			
St.Fiscal Stabilization		\$319,841	\$429,092	\$178,071	
Education Jobs				\$317,613	
Total-General Fund	\$345,941	\$799,102	\$447,042	\$495,684	\$0
ARRA-IDEA		\$138,411	\$138,228		
ARRA-Title I		\$87,222			
Total-Special Revenue	\$0	\$225,633	\$138,228	\$0	\$0

PERS has been a thorn in the side of all who have attempted to solve the problem of its unsustainable cost increases that impact employers. Investment rates of return and employer contributions are the two largest factors that influence the rates. The rates charged to employers for the 2011-13 biennium were established from the PERS portfolio value as of 12/31/09. Returns for that year were down 27%. PERS has certain yearly payout requirements to retirees, regardless of the investment return of the portfolio. In a bad year, employer rates are jacked up to compensate for the reduced investment income. Our new rates, effective 7/1/2011 increased 7.48% for Tier ½ employee and 5.45% for OPSRP (the new PERS program) employees. Assuming an average rate increase of 6.75% would increase our PERS cost about \$441,548 on estimated “PERS subject wages” of \$6.5 million. Following is a table of current and new PERS rates.

HISTORIC and PROJECTED FUTURE PERS RATES

	<u>Rates for 09-10 & 10-11</u>		<u>Rates for 11-12 & 12-13</u>		
	7/1/2009		7/1/2011		
	<u>T1/T2</u>	<u>OPSRP</u>	<u>T1/T2</u>	<u>OPSRP</u>	
Normal cost rate	14.22%	14.74%	19.48%	17.97%	1
Side Account Relief	-10.02%	10.02%	-7.80%	-7.80%	2
Net Contribution rate	4.20%	4.72%	11.68%	10.17%	3
PERS Pick up	6.00%	6.00%	6.00%	6.00%	4
	10.20%	10.72%	17.68%	16.17%	5
PERS Bond (1)	5.62%	5.62%	5.85%	6.06%	6
(2)	15.82%	16.34%	23.53%	22.23%	7

(3)

T1 = Tier 1

T2 = Tier 2

- (1) Rate is set by District at a level that will generate enough to make debt service payment on PERS Bond.
- (2) Note the wild fluctuations in total PERS rates and the potential negative impact of General Fund expenditures.
- (3) Cost of 6.75% rate increase - Estimated 2011-12 PERS subject payroll \$6,541,457 x 6.75% = \$441,548, each year.

In addition to the historical factors described above, other contributing factors are driving the immediate need to reduce spending by approximately \$2 million.

Spend down of Beginning Fund Balance during the 2010-11 school year	\$977,837
PERS rate increase effective 7/1/2011	441,548
Revenue loss due to enrollment decline	261,281
Cost increases (incl. payroll step advances)	<u>319,334</u>
Total	\$2,000,000

I suggest that we schedule a board work session at the earliest possible time to begin looking at options for responding to this crisis. By that time Budget Committee members should be on board as well.