Introduction

School districts across the commonwealth are in the midst of developing their 2020-21 budgets as the state develops its budget on a parallel track.

During this time, the PA Association of School Business Officials (PASBO) and the PA Association of School Administrators (PASA) issue an annual report articulating the financial health of Pennsylvania’s 500 school districts, highlighting their successes and challenges.

This report uses multiple sources of school district data to triangulate the composition of an accurate picture of the general financial health of school districts. This year’s report uses school district survey data—data collected in November and December 2019—to both understand more about the budgets that school districts finalized for the current school year and to assess the financial pressures that impact school district budget development for the next fiscal year.

The report also uses Annual Financial Report (AFR) data—detailed financial data submitted by school districts to the Pennsylvania Department of Education (PDE) each year. The most current AFR data available is from the 2017-18 fiscal year.

Additionally, we have pulled from school districts’ 2019-20 General Fund Budget submissions—school district budgets for the current fiscal year, as well as PDE staffing and enrollment reports. The AFR data, the General Fund Budget submissions and the staffing and enrollment data are publicly available on PDE’s website.

Examining these data sets individually and in conjunction with one another allows us to identify and confirm trends and to provide valuable context for the challenges identified and the capacity of school districts to overcome those challenges under existing circumstances.

It remains clear, and the multiple data sources data reaffirm the fact that a severe amount of fiscal stress exists across Pennsylvania’s school districts. This fiscal stress continues to have significant impact on our public education system.

As articulated in past reports, the current financial situation in many school districts is unsustainable to ensure maintenance of current educational program levels. And while continued increases in state funding for education have been helpful, mandated costs for charter school tuition, special education and pension costs are consuming most if not all of the additional investment the state is targeting to schools, and correspondingly requiring an increased reliance on property tax increases in the majority of school districts. It is the antithesis of the growing property tax relief debate.

Overall, there is little to no additional money heading into the classroom in many school districts across the state. Without needed policy changes to curb some mandated costs and meaningful efforts to increase the state’s share of k-12 education, fiscal stress will continue to impact school districts, the burden on property tax will grow and educational opportunities for school district students will diminish.
The Education Deficit

Our last two reports included an illustration of the Education Deficit—the difference between growth in mandated school district expenditures and increases in state funding to cover those cost increases. The Education Deficit represents the amount of mandated school district costs that must be covered at the local level—either through property tax increases, program cuts or both.

Focusing on the fastest growing mandated costs for school districts, we compared changes in mandated special education, charter school tuition and pension costs to the corresponding changes in state funding for those items. We excluded special education pension costs and special education charter tuition costs to avoid double-counting costs included under total pension and total charter tuition.

Figure 1 shows that between 2010-11 and 2017-18, these costs increased by more than $4.6 billion. During the same time, state support for these costs through increases in basic education funding, special education funding and pension reimbursement (we also factored in the elimination of the charter school reimbursement) resulted in a total state funding increase of $2.24 billion.

Figure 1 – The Education Deficit: Cumulative Dollar Change in Mandated Costs and State Funding Increases (2010-11 to 2017-18)

Source: PDE AFR data
Comparing the mandated costs increases to state funding increases, the Education Deficit added $2.43 billion directly to the local tax base. School districts covered this mandated cost-driven deficit through property taxes increases, cuts to programs, services and staff or both. Remember that this deficit only accounts for the three mandates listed above, all other cost increases are on top of this amount.

As we await 2018-19 AFR data, we anticipate that the Education Deficit will grow. While the state has invested additional dollars into education, the growth in mandated costs is outpacing the state’s contribution, widening the deficit, increasing the reliance on property taxes and keeping educational programs and services at risk in many school districts.

School District Budget Cost Drivers

In 2017-18, school district expenditures totaled about $30.2 billion, nearly $300 million less than the prior year. While the overall total expenditures fell for the first time since 2011-12 (mostly due to the infusion of backlogged PlanCon funding in 2016-17), school districts across the state continued to face fiscal pressure due to the three mandated costs that are responsible for driving school district budget increases from year to year: employee pension costs, special education costs and charter school tuition costs. The scope of these mandated costs is illustrated in Figure 2 below.

![Figure 2 – Charter School Tuition, Special Education and Retirement Contributions (2012-13 to 2017-18)]

<table>
<thead>
<tr>
<th></th>
<th>2017-18 Total</th>
<th>5-Year $ Change</th>
<th>Avg. Annual % Change</th>
</tr>
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<tbody>
<tr>
<td>Charter School Tuition</td>
<td>$1,823,405,695</td>
<td>$555,074,820</td>
<td>8.75%</td>
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<tr>
<td>Special Education</td>
<td>$5,280,458,269</td>
<td>$1,282,662,302</td>
<td>6.42%</td>
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<tr>
<td>Retirement Contributions</td>
<td>$3,740,297,469</td>
<td>$2,406,807,967</td>
<td>36.10%</td>
</tr>
</tbody>
</table>

Source: PDE AFR data

Employee Pensions

School districts spent more than 12% of their total expenditures on employee pension costs in 2017-18, or more than $3.74 billion, an increase of more than $360 million (a 10% increase over the prior year). Over the past five years (2012-13 to 2017-18), pension costs have increased by more than 180% for school districts, as the employer contribution rate has continued to increase each year.

Figure 3 below shows the actuarial projected total employer contribution rates (ECRs) for the Pennsylvania School Employees Retirement System (PSERS) through 2027-28. While the 2020-21 ECR has been set by the PSERS board, all other rates are subject to change based on complex actuarial metrics that will change annually and over-time.

Clearly, the rate of increase is slowing down, even as it continues to grow from the current rate of 34.29% in 2019-20 to a rate of 38.17% projected in 2027-28. While the slower rate of increase is good news, Figure 3 reflects that even at the lower pace of increase taxpayers will need to contribute an additional $1.3 billion dollars over the next seven years. It’s also important to remember that the ECR rate is a plateau, and while the rate of increase is slowing, pension funding policy is by no means fixed.
### Figure 3 – PSERS Future ECR Projections

<table>
<thead>
<tr>
<th>FY Ending</th>
<th>Total Employer Contribution Rate</th>
<th>ECR Rate Increase</th>
<th>ECR Rate Increase As a %</th>
<th>Employer Contributions Annual Dollar Increase ($ Thousands)</th>
<th>Employer Contributions Cumulative Increase ($ Thousands)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2021</td>
<td>34.51%</td>
<td>0.22%</td>
<td>0.64%</td>
<td>$98,866</td>
<td></td>
</tr>
<tr>
<td>2022</td>
<td>34.95%</td>
<td>0.44%</td>
<td>1.27%</td>
<td>$135,650</td>
<td>$234,516</td>
</tr>
<tr>
<td>2023</td>
<td>35.62%</td>
<td>0.67%</td>
<td>1.92%</td>
<td>$176,852</td>
<td>$411,368</td>
</tr>
<tr>
<td>2024</td>
<td>36.12%</td>
<td>0.50%</td>
<td>1.40%</td>
<td>$161,936</td>
<td>$573,304</td>
</tr>
<tr>
<td>2025</td>
<td>36.60%</td>
<td>0.48%</td>
<td>1.33%</td>
<td>$164,675</td>
<td>$737,979</td>
</tr>
<tr>
<td>2026</td>
<td>37.23%</td>
<td>0.63%</td>
<td>1.72%</td>
<td>$193,968</td>
<td>$931,947</td>
</tr>
<tr>
<td>2027</td>
<td>37.79%</td>
<td>0.56%</td>
<td>1.50%</td>
<td>$182,501</td>
<td>$1,114,448</td>
</tr>
<tr>
<td>2028</td>
<td>38.17%</td>
<td>0.38%</td>
<td>1.01%</td>
<td>$153,191</td>
<td>$1,267,639</td>
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</tbody>
</table>

Source: PSERS (as of June 30, 2019; PSERS Board approved Dec. 2019)

### Special Education

Another major area of mandated cost growth for school districts that contributes to the growing Education Deficit continues to be special education costs. State and federal special education mandates drive the provision of special education services to eligible students, and as a result, school districts have limited flexibility in controlling these costs. If a student requires special education services, programs, transportation or private placements, school districts must cover those costs.

In 2017-18, school districts spent more than $5.27 billion on special education programs and services. Of this total more than $4.55 billion was spent on special education instructional costs—86% of the total expenditure. The remaining $720 million represents the special education support services, which includes services such as special education transportation, guidance services, psychological services, social work and nursing services.

Growth in school district special education expenditures has been significant, and that impact is compounded by state special education subsidy that hasn’t kept pace. Special education costs across all 500 school districts increased by $1.28 billion between 2012-13 and 2017-18, with special education instructional costs increasing more than $1 billion during this time frame, and special education support services increasing by $185 million.

Based on 2019-20 General Fund Budgets submitted to PDE, school districts budgeted $4.93 billion in 2019-20 in special education instructional costs, a $368.7 million increase from the actual amount of special education instructional costs reported in AFRs for 2017-18.
What’s driving the cost growth? An overall increase in special education enrollment has been included by survey respondents as one of the top reasons for increased special education costs for the past two years. We see survey and hiring data that reveal an increase in the need for outside or private special education placements, an increase in the need to hire additional special education staff (including teachers, aides and nurses) and an increase in the need for special education transportation services. All of these are consistently reported by school districts as drivers of special education costs. Growth in charter school special education enrollment also exacerbates school district special education costs.

Looking first at enrollment growth, there have been significant increases in special education enrollment each year. This growth, as illustrated in Figure 4, is occurring at all categories of special education need.

Figure 4 – Special Education Act 16 Student Counts

<table>
<thead>
<tr>
<th></th>
<th>2013-14</th>
<th>2014-15</th>
<th>2015-16</th>
<th>2016-17</th>
<th>2017-18</th>
<th>Total Change</th>
<th>Average Annual % Change</th>
</tr>
</thead>
<tbody>
<tr>
<td>Cat. 1</td>
<td>278,297</td>
<td>271,977</td>
<td>279,307</td>
<td>290,360</td>
<td>303,525</td>
<td>25,228</td>
<td>2.27%</td>
</tr>
<tr>
<td>Cat. 2</td>
<td>18,026</td>
<td>20,512</td>
<td>21,838</td>
<td>21,965</td>
<td>22,180</td>
<td>4,154</td>
<td>5.76%</td>
</tr>
<tr>
<td>Cat. 3</td>
<td>6,754</td>
<td>6,899</td>
<td>7,504</td>
<td>8,430</td>
<td>9,104</td>
<td>2,350</td>
<td>8.70%</td>
</tr>
<tr>
<td>Total</td>
<td>303,077</td>
<td>299,388</td>
<td>308,649</td>
<td>320,755</td>
<td>334,809</td>
<td>31,732</td>
<td>2.62%</td>
</tr>
</tbody>
</table>

Source: PDE Special Education Data

Between 2016-17 and 2017-18, the number of special education students with the lowest cost special education needs (less than about $25,000 a year) increased by about 15,000 students. The average annual growth in the number of students in this category is 2.27%.

During that same time frame, the number of students with more significant special education needs (ranging in costs from about $25,000 to $50,000 per year) increased by about 220 students, and the average annual growth in the number of students in this category is 5.76%.

Finally, the number of students requiring the most extensive special education programs and services (generally costing in excess of $50,000 per year) increased by nearly 700 students. The average annual growth in the number of students in this category is 8.70%.

Obviously, as the number of students requiring special education programs and services increases, so does the associated costs. To accommodate the increases in special education enrollment, the data, captured in Figure 5 below, shows that school districts have hired additional special education staff, adding 356 special education teachers between 2017-18 and 2018-19 alone.

Additionally, school districts continue to report increases in the number of students requiring outside or private special education placements. School district special education payments to intermediate units grew $97.2 million or almost 13.5% between 2014-15 and 2017-18, while payments to Approved Private Schools and Chartered Schools for high-need special education students grew almost $37.5 million or 26.7% between 2014-15 and 2017-18.
Additionally, school districts continue to report increases in the number of students requiring outside or private special education placements. School district special education payments to intermediate units grew $97.2 million or almost 13.5% between 2014-15 and 2017-18, while payments to Approved Private Schools and Chartered Schools for high-need special education students grew almost $37.5 million or 26.7% between 2014-15 and 2017-18.

Figure 6 captures the three-year cost increases in some specific special education support services between 2014-15 and 2017-18 (as reported to PDE pursuant to Act 16). Total medical services costs increased by 40.3%, special and audiology services costs increased by 47.5%, social work services costs increased by 37.2%, guidance and psychological services costs increased by 18.1% and special education transportation costs increased by 17.3 %.

Overall, the data continues to tell the story of ongoing increases in special education costs for school districts. As this mandated cost appears to be growing on every front, there is no indication of any mitigation in sight. While the growth in special education costs has been minimally offset by small increases in state special education funding, the fact is that special education costs are growing far faster than state funding increases. The result is that the state’s share of funding special education continues to fall year over year, and school districts continue to shift resources from other areas of the budget, reduce or eliminate programs or raise property taxes to balance their budget.
Charter School Tuition

A third major cost driver of school district budgets and the growing Education Deficit is charter school tuition. We have been consistent in our message that school choice policy is here to stay; however, the controversy on this issue comes as a result of the commonwealth’s policy on how to pay for it.

The current charter school funding policy imposes serious fiscal stress on many school districts. In 2017-18, school districts paid $1.82 billion in charter school tuition. This cost increased by nearly $170 million between 2016-17 and 2017-18—a 10.18% increase in a single year. For reference, during that same year, the increase in state basic education funding was $100 million.

While we await PDE’s release 2018-19 AFR data this spring, our survey data as well as our review of the 2018-19 and 2019-20 General Fund Budget submissions provides an informed glimpse from which to estimate the impact of charter school tuition on school district budgets for this fiscal year and next year. While time will tell, our analyses of current trends strongly suggest that school districts will see a second and third consecutive year of double-digit increases in total charter school tuition.

The scope of the increase in charter school tuition, especially in the context of state funding and property tax increases, is startling. From 2011-12 to 2017-18, charter school tuition increased by more than $1 billion. During that same time period, the state eliminated $220 million in funding it had previously provided to school districts to help offset the impact of mandated charter school costs on the local tax base.

Charter School Enrollment vs. Tuition Rate

Many assume that the annual increases in charter school tuition are driven by increases in charter school enrollment. The answer is yes, but only in part.

The formula to determine the annual charter school tuition payment by each school district is heavily biased toward charter schools and has minimal correlation to actual school district financial cost data. For example, if a school district’s total costs increase from one year to the next and their total enrollment goes down (approximately 375 school districts have been experiencing declining enrollment), the result will be a charter school tuition calculation that has a larger numerator and a smaller denominator.

That means that the charter school tuition amount goes up—as does the total amount the school district sends to charter schools, even if charter school enrollment remains static—or even declines. The bottom line is that charter school enrollment growth represents only a fraction of the actual cost increase for many school districts.

School districts where charter enrollment has grown significantly are facing the compounding effect of the increasing enrollment, the increasing tuition rate and increasing counts in special education charter students, which carries a higher cost per student.
In terms of charter school tuition, the rate a school district pays to a charter school depends on whether the student is a regular education or a special education student. The special education tuition rate is significantly greater than the regular education tuition rate.

Figure 7 below shows the annual percentage increases in total charter school enrollment and in special education charter school enrollment. While there have been general increases in the number of special education students across school districts, charter schools have increasingly identified more special education students.

Figure 7 – Annual Changes in Total Charter School Enrollment vs. Special Education Charter School Enrollment

Source: PDE Data.
Figure 7 above uses actual trends in charter school enrollment (through 2018-19) and estimates the out years based on those trends. The ratio of special education identification to each new charter school student enrolled is over 70% in the past five years (2014-15 to 2018-19).

Where is all this policy taking us? Based on the data, we are at a crossroads with the current approach to charter school funding. Below we outline two scenarios for growth in charter school tuition costs.

Two Scenarios; One $3 Billion Inflection Point

As noted above, the 2017-18 AFR data showed a $1.82 billion total school district expenditure for charter tuition. As we assess school district fiscal stress and the factors driving it, we reviewed several data sources to estimate and project charter tuition cost through 2024-25—just five years from today.

We used prior year actual history of charter school tuition growth to run two different scenarios to project the impact of this mandated cost on school districts over the next several years. Figures 8a and 8b illustrate the similarities and differences in these scenarios. For both scenarios, we have assumed the charter school tuition calculation remains the same and enrollment trends remain similar as the past. The objective was to create a reliable projection for this cost consistent with reasonable assumptions supported by the data.

Scenario 1 uses our survey and budget data, which strongly indicate double-digit charter school tuition cost increases in 2018-19, and most likely for 2019-20 as well. We have estimated that the charter school tuition increase will be approximately 11.2% in 2018-19, and we have projected a 10% annual increase in the total cost from 2019-20 to 2024-25. We show actual charter school tuition growth for all years up to 2017-18 (see Figure 8a).

In Scenario 2, we utilized a more conservative approach for the rate of increases driving projections. As we believe all the data sources support the 11.2% cost increase for 2018-19, that assumption is built that into both scenarios. However, we have assumed single-digit percent increases in charter school tuition costs beginning in 2020-21. Such reductions could be driven by a move by the legislature to modify the tuition calculation itself or charter enrollment factors.

Figure 8a - Charter School Tuition Growth: Historical and Projected

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<th></th>
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</thead>
<tbody>
<tr>
<td>Scenario 1</td>
<td>11.20%</td>
<td>10.00%</td>
<td>10.00%</td>
<td>10.00%</td>
<td>10.00%</td>
<td>10.00%</td>
</tr>
<tr>
<td>Scenario 2</td>
<td>11.20%</td>
<td>8.00%</td>
<td>6.00%</td>
<td>5.50%</td>
<td>5.50%</td>
<td>5.50%</td>
</tr>
</tbody>
</table>

Source: PDE Data.
Figure 8b illustrates the impact of the projected annual percentage increases in total charter school tuition in Scenario 1 and Scenario 2. The result of the Scenario 1 projection is that in 2022-23 the total cost of charter school tuition reaches $3 billion, climbing to $3.62 billion by 2024-25. While Scenario 2 includes annual percentage increases in the charter school tuition rate that are half of those assumed in Scenario 1, Scenario 2 still shows significant cost increases. Under scenario 2, charter school tuition reaches $3 billion in 2024-25.

Figure 8b - Actual and Projected Total Charter School Tuition Costs

Figure 9 below illustrates the annual increase in charter school tuition required for school districts and taxpayers for each of the scenarios outlined above, highlighting the amount that must be raised by school districts each year—either from local property taxes, increases in state funding or school district program cuts.

Unless there is a significant change in charter school funding policy and/or a major change in school district funding, it’s likely that the reality of the growth in charter school tuition will fall somewhere between these two scenarios. However, what’s important to consider is that both scenarios strongly suggest school districts will hit the $3 billion charter school tuition mark by 2024-25. At that point, if not before, charter tuition annual increase will completely wipe out, in perpetuity, virtually all of any future annual increases in state basic education funding.

Figure 9 below illustrates the annual increase in charter school tuition required for school districts and taxpayers for each of the scenarios outlined above, highlighting the amount that must be raised by school districts each year—either from local property taxes, increases in state funding or school district program cuts.

Source: PDE AFR data and PASBO projections
Under Scenario 1, annual increases in charter tuition rapidly pass the $250 million per year mark and then exceed $300 million per year. Under Scenario 2, charter school tuition cost increases still result in massive annual increases for school districts, and when compared to increases in basic education funding (which was increased by $160 million for 2019-20), it demonstrates that the state is barely keeping pace with the growth in this mandated cost.

The reality is that even with conservative estimates, the new funding being provided to school districts in state basic education and special education subsidies is just a pass-through to charter schools in many school districts. Growth in charter school tuition is now so extreme that school district fiscal stress will continue to grow until a comprehensive solution or a significant change to funding policy is implemented.
Next, we turn to the strategies and challenges school districts navigate as they attempt to cover the Education Deficit driven by the mandated cost increases discussed above. The reality is that many school districts must turn to property taxes to raise the revenue necessary to balance their budgets. The ability to raise property tax revenue, however, is different for every school district, and this difference highlights another component that adds to widening disparity and school district fiscal stress.

To illustrate the measurement of board authority, Figure 10 examines a fictional school district that relied on property taxes to fund just 48.5% of its $54 million operating costs in 2019-20. With an Act 1 index for 2020-21 of 2.6%, the district’s board authority would be about $680,000—meaning, effectively, that for 2020-21, the district could raise up to the equivalent of 1.26% of its $54 million budget in additional property tax revenue (without exceptions) to cover mandated cost increases.

For most school districts, the amount that can be generated through their board authority doesn’t begin to cover increases in their mandated costs for pension, special education and charter school tuition, let alone pay for other needs or priorities. With limited board authority to generate additional property tax revenue, many school districts must rely on state revenue increases or cost avoidance/reductions to balance their budgets. They have little room to maneuver.

For 2019-20, the median board authority across all school districts was 1.19% of their total budget—meaning that a school district generally had the ability to raise revenue the equivalent of 1.19% of its 2018-19 budget to begin to cover its mandated and all other cost increases in the 2019-20 school year.

Board authority across school districts varies widely, and nearly 40% of school districts had a 2019-20 board authority less than 1.00% of their total 2018-19 budget, meaning they had minimal ability to cover mandated cost increases through property tax increases.

Shifting to 2020-21, Figure 11 below illustrates the flexibility of each school district in terms of their board authority to cover mandated cost increases for next year. As school districts are building their 2020-21 budgets, the board authority represents the percentage of their 2019-20 budget that can be raised by increased property taxes without Act 1 exceptions.

With the average increase in mandated costs statewide being 2.75% of total operating costs, for the school districts with minimal board authority, the fiscal stress related to mandated cost increases is most significant.
With the average increase in mandated costs statewide being 2.75% of total operating costs, for the school districts with minimal board authority, the fiscal stress related to mandated cost increases is most significant.

Furthermore, as discussed in our prior budget reports, school districts are not equal when it comes to their tax base. In examining assessed value (AV)—the value upon which property taxes are based—not all school districts experience AV growth from year to year.

In fact, on average over the last seven years, Figure 12 shows that about 20% of school districts experience an AV decline from one year to the next. This means that those school districts need to increase property tax rates just to generate the same property tax revenue as the prior year.

For these school districts, even before they examine the impact of rising mandated costs on their budgets, they are starting behind the prior year when it comes to revenue. On average, 106 districts had a decrease in AV each year from 2011-12 to 2019-20.

### Figure 12 – Annual Decline in Property Tax Assessed Value

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<tr>
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</thead>
<tbody>
<tr>
<td>Count</td>
<td>122</td>
<td>141</td>
<td>94</td>
<td>89</td>
<td>109</td>
<td>121</td>
<td>94</td>
<td>98</td>
<td>87</td>
<td>106</td>
</tr>
<tr>
<td>Percent</td>
<td>24.40%</td>
<td>28.20%</td>
<td>18.80%</td>
<td>17.80%</td>
<td>21.80%</td>
<td>24.20%</td>
<td>18.80%</td>
<td>19.60%</td>
<td>17.50%</td>
<td>21.00%</td>
</tr>
</tbody>
</table>

*Source: PDE General Fund Budget data and DCED data*
Figure 13 represents the number of school districts experiencing each type of annual change in AV between 2018-19 and 2019-20. Approximately half of school districts experienced at least some minimal growth in their 2019-20 AV, which could allow them to get a head start on covering some mandated cost increases through some natural growth in their tax base.

Other school districts, however, aren’t as lucky. While 7.7% of school districts observed no change in their AV between 2018-19 and 2019-20, about 17.5% of school districts observed their AV decline to some extent.

As school districts begin to build their 2020-21 budgets, they are currently grappling with how to mitigate the fiscal stress of mandated cost increases, how to move forward with educational or operational priorities and how to pay for all of it without overburdening taxpayers or reducing programming, services or staff. While this process and the priorities are different in all 500 school districts, one thing is universal: expenditures have to equal revenues—state law dictates that budgets must be balanced.

Figure 14 represents the property tax implications for school districts in 2019-20. To balance their budgets for 2019-20, about 69.2% of school districts raised property taxes to some degree, with 32.8% of school districts raising taxes at or above their Act 1 Index and the other 36.4% raising taxes below their Act 1 Index. At the other end, only 2.8% of school districts had a decrease in their effective property tax rate with the remaining 28.0% of school districts having no change compared to 2018-19.
While PDE’s 2019-20 annual report on Act 1 Referendum Exceptions indicates that 84 school districts received exception approval, only 47 school districts adopted a final budget with an increase exceeding their Act 1 index. The majority of those districts receiving an approved exception to raise property taxes above the Act 1 Index due to mandated special education costs, which comes as no surprise based on the discussion above.

Putting all of these factors together, the school districts facing AV decline and limited board authority will likely face the greatest challenges in developing their 2020-21 budgets. With limited board authority under Act 1, additional years with a decline in AV will mean that the district will continue to need to raise property tax rates just to maintain level revenue from the prior year. Depending on the extent of the AV decline, there may be no room to even begin to cover mandated cost increases through local revenue.

Overall, the growth in mandated costs is insurmountable at the local level for many districts. Even by maximizing board authority, without increasing state support each year, most school districts would have to turn to massive reductions to programs, services and staff just to cover mandated cost growth.

Zeroing in on the impact on the growth in mandated costs for special education and charter school tuition have had on property taxes can be easily observed in the data over five years from 2012-13 to 2017-18. During this time, mandated costs for charter school tuition and special education increased by $1.6 billion while state support for these costs, through the new special education and basic education funding formulas, grew $669.6 million.

This growth in the costs borne by local taxpayers meant that on average statewide, $0.76 of every new dollar raised in property taxes between 2012-13 and 2017-18 went directly to charter schools or special education. For school districts that had to raise property taxes to cover these costs, the average school district spent an additional $1.09 on special education and charter tuition for every $1 in increased property taxes during this time frame.

Alternatively, the net local share of mandated cost increases for charter school tuition and special education had an impact on the local property taxpayer to the tune of $706.15 per student or $433.67 per homestead property.

Unfortunately, the resulting impact of this state policy will likely continue to worsen. Recent studies published by the Center on Regional Politics at Temple University used current trends to simulate and estimate the financial impact of the state’s school finance policy by projecting out to 2021-22, finding that these mandated costs and the effect they are having on school districts’ level of fiscal stress is observed in the fact that 60% of districts will annually experience budget deficits/shortfalls and manage through continuous, tough financial scenarios.
Fund Balance

As many school districts struggle to cover their rising mandated costs through property tax increases each year, fund balances are often pointed to as a panacea. The reality is that, while a critical tool for school districts to plan for certain expenditures long-term, fund balances cannot cover the growth in mandated costs from year to year. Additionally, school district fund balances have been relatively static over the past several years, highlighting the facts that 1) there has been consistent use of school district fund balance and 2) mandated cost growth has diminished school districts’ ability to save long-term.

So, what is it? A fund balance, in most school districts, is the difference between current assets and current liabilities in a governmental fund on June 30. It includes cash, but it also includes many receivables the school district categorizes as current assets. It’s important to remember that fund balance is a snapshot of where a school district is on June 30 and represents the beginning balance for July 1.

Those receivables are comprised of a lot of assets the school district expects to receive sometime between July 1 and September 1, or even a little later. If taxes levied in May or June are arriving over the summer months (after June 30), they are counted in the fund balance number on June 30. If the state owes a school district money on June 30, but it won’t get to the district’s bank account until August 20, it is included in that ending fund balance number.

There are generally three types of fund balances: committed, assigned and unassigned. Committed and assigned fund balances set aside reserves for a specific project or cost that the district is currently implementing, planning to implement or knows is coming. The unassigned fund balance is the ending difference between current assets and liabilities—a district can use this reserve to support and protect school district operations from cost shocks and to moderate tax increases. As noted above, it is not all cash.

Figure 15 below shows school district fund balances equated to the number of operating days for committed and assigned fund balances, unassigned fund balance and total fund balance.

Figure 15 – Fund Balance in Number of Days and Percent of Current Expenditures

<table>
<thead>
<tr>
<th></th>
<th>Days</th>
<th>% Expenditures</th>
</tr>
</thead>
<tbody>
<tr>
<td>Unassigned</td>
<td>25</td>
<td>23</td>
</tr>
<tr>
<td>Committed + Assigned</td>
<td>32</td>
<td>34</td>
</tr>
<tr>
<td>Total</td>
<td>57</td>
<td>57</td>
</tr>
</tbody>
</table>

Source: PDE AFR data
Overall, Figure 15 illustrates that the total amount of school district fund balance has remained steady over the past five fiscal years in terms of operating days. Also, following our discussion of mandated cost increases, the scary reality is that school districts only have the equivalent of 22 days of operating expenses in their unassigned fund balance.

Additionally, as Figure 15 examines fund balance data as a percent of school district current expenditures over multiple fiscal years, and it’s clear that total fund balance as percent of current expenditures are holding steady as well. School districts are constrained by what they can raise in local revenue, and during this time frame, school districts have experienced greater growth in mandated costs than they have previously at any point in history.

School districts reported total unassigned fund balance of $1.9 billion in 2016-17 and $1.84 billion in 2017-18—about a 3% reduction. As noted above, unassigned fund balance includes receivables even though the money is not in a school district account at year-end.

Meanwhile, all the parts of fund balance composition have to be managed. For example, as shown in Figure 16, the amount owed to school districts from the state at year-end has consistently grown over the past several years.

For example, at the end of the fiscal year the state owed school districts $506.6 million in 2016-17 representing 26.7% of the reported the total unassigned fund balance for that year. Similarly, in 2017-18, the state owed school districts $596.5 million, representing 32.3% of the reported unassigned fund balance.

This state funding owed to school districts at year-end is included in school district unassigned fund balance even though the money is not yet in district bank accounts—and it may not be for 30, 60 or 90 days. School districts must implement complex cash flow strategies to ensure they can pay bills and make payroll over the summer months while they wait for the state funding and tax revenue to flow.
One of the major contributors to unassigned fund balance in many districts is state funding due for the pupil transportation reimbursement. Over the past several years, the state funding to school districts for their transportation costs has been level-funded, despite the fact that transportation costs, and the contractual state share, have grown. The state’s transportation reimbursement formula should be driving out increased funding to school districts. The state continues to under-budget this line over multiple years, and its share of support for pupil transporting is falling.

However, the result of underfunding this line item means that funding due to school districts falls further and further behind and stretches out over wider periods. The pupil transportation line item for school districts is estimated to be short by more than $100 million for 2019-20. All of this is captured in unassigned fund balances, despite the fact that school districts do not have this transportation funding until well after year-end close.

Figure 17 shows the fund balances for the last two fiscal years that reflect growth in the assigned fund balance and a reduction in the unassigned fund balance. By many measures, school district fund balances are being used as fiscal tools to pay for needed maintenance and other pay-as-you go needs requiring capital formation and diligent planning. Annual wear and tear, depreciation and upkeep on the major infrastructures of our commonwealth’s schools has to be planned for, but it also has to be funded. The ongoing moratorium on PlanCon projects means there is no state support. School districts either find way to cover their needs, or they defer, kicking the can and the price tag down the road.

Survey respondents indicated that they are using fund balance to address maintenance needs of aging infrastructure, to plan for future construction and renovation needs, to mitigate some mandated cost growth, prepare for assessment appeals or litigation and to plan for variations in healthcare spending.

Figure 17 – School District Fund Balances for 2016-17 and 2017-18

Source: PDE AFR data
Each district has different needs and different priorities along these fronts. State funding delays in actual subsidies, unknown funding allocations and changes to state funding in several line items can only be managed by districts within the confines of Act 1 tax restrictions and strategic fund balance management.

Further Challenges

While this report focuses on two of the biggest drivers of school district budgets—special education and charter school tuition, school districts continue to face additional priorities that further exacerbate the competition for revenue and resulting fiscal stress for school districts in many areas of the state. One growing area of fiscal concern is that related to school construction and maintenance needs. Our budget survey continues to tell the story of a growing disparity between those school districts that can address vital school construction, renovation or maintenance needs and those that cannot. The absence of funding for the PlanCon program for school construction and renovation reimbursement has had a chilling effect on school construction.

For the second year in a row, our survey responses indicate that school districts have massive school construction, renovation and maintenance needs. This year’s survey highlighted a need of more than $760 million in school district construction and maintenance needs in the next 18 months, while the total dollar amount of need climbs to more than $1.1 billion for those needs in the next 2 to 5 years. These numbers represent only the school construction and maintenance needs reported by survey respondents—not the universe of need in all 500 school districts.

Additionally, like last year, only about half of survey respondents expect to be able to move forward with these construction or maintenance needs in the absence of state funding. For those districts that don’t have FB committed or assigned for construction or maintenance needs, there is little capacity to fund even the most critical of maintenance needs until they reach a crisis. The lack of PlanCon funds on top of the growth in mandated costs is driving a growing wedge between school districts that can cover these costs locally and school districts that cannot.

Another major priority for school districts continues to be school safety and security. While the legislature has provided school districts with $60 million in school safety and security grants for both 2018-19 and 2019-20, school district prioritization of safety and security can be seen prior to that in school district AFR data.

Total school district spending on school security increased by more than $27 million between 2014-15 and 2017-18. This total increase includes the hiring of additional school security personnel, which increased by $7 million or 13% during this time frame, and the purchase of security services, which increased by 53% or $4.5 million during this pre-safety grant time frame.

Our survey data indicates that the hiring of school resource officers, school police officers and school security guards—in both full-time and part-time capacities—was a priority for many districts in both their 2018-19 and 2019-20 budgets.
In addition to the security focus, school districts have made some significant changes to their school and student safety and support staff. Between 2017-18 and 2018-19, according to staffing reports, school districts and intermediate units hired more social workers, school psychologists and school counselors, as illustrated in Figure 18 below.

Survey data indicates that districts have prioritized the hiring—both full-time and part-time—of school counselors, psychologists, social workers, behavioral therapists and other mental health professionals as part of their 2018-19 and 2019-20 budgets.

While these changes represent positive changes and improvements in school districts safety and security programs, there is still room for improvement across the commonwealth. School districts continue to identify the school safety and security needs of their individual districts, schools and student populations, and the needs continue to range from physical security assessments, security personnel and equipment to staff training, student support and mental health personnel and other resources targeted to implementation of trauma-informed educational programs.

Source: PDE Staffing data
While these needs are prioritized by school districts, funding them (and sustaining them) outside of the limited resources available through the safety and security grant program continues to present a challenge for many school districts. And while disparities should not exist across school districts, disparities in school safety and security across school districts is especially egregious.

It’s All One Conversation

This report has covered a lot of ground, from mandated costs to property tax implications and from fund balance changes to school construction and safety needs. So, what does it all mean, and how does it all fit together?

School district mandated costs are increasing and straining school district budgets. State funding is increasing, but it’s not keeping up with the growth, and the state’s share of funding in multiple line items continues to fall. Property taxes continue to be the default mechanism for school districts to fund mandated special education, charter school tuition, and pension increases. Other priorities continue to emerge. The fiscal health of many school districts declines. And the cycle continues year after year.

The math of the Education Deficit is getting worse for school districts, and fiscal stress is increasing at drastically different paces in school districts across the commonwealth. The result is new and widening disparities between commonwealth school districts, students and taxpayers.

The state should be focused on maintaining educational programs at adequate levels and chipping away at the many disparities that exist across school districts, the reality is that the whole system is unsustainable. Reform at multiple levels is necessary to ensure equity for school districts, students and taxpayers. How that reform happens, however, is important.

With mandated costs for special education and charter school tuition increasing by a combined quarter of a billion dollars each year, massive policy changes that include increased state support for education to significantly mitigate the annual growth in these two mandated costs are essential.

At the same time, the state has to tackle—meaningfully and effectively—the continued local funding reliance burden on taxpayers.

To make this work, however, policymakers have to understand and appreciate the connection between education finance, policy and property taxes. These conversations can’t lead to meaningful, long-term or effective policy change if they are had in silos.

Property tax reform is where charter school reform, special education costs, and the state funding discussion converge. More state funding for special education is property tax relief. Failure to address the charter school funding formula means increased property taxes.

It’s all one conversation. Success on these critical issues can’t be accomplished in a vacuum.
As school districts and the state continue on their parallel tracks to 2020-21 budgets, we encourage the General Assembly and other policymakers to recognize that a comprehensive solution is needed to address mandated cost increases within school funding and property tax reform discussions.

It’s a school district budget issue, a state budget issue, an Education Deficit issue, a property tax issue, a charter school tuition issue and a special education issue, and it can only be solved—to the long-term benefit of the commonwealth, students, school districts and taxpayers, if we tackle it as one.