

MEMO



MINNEAPOLIS
PUBLIC SCHOOLS
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Date: December 1, 2020

To: Board of Education, Minneapolis Public Schools

From: Ed Graff, Superintendent

RE: Pro-Forma Financial Projections – General Fund – Executive Summary

We have updated our 5-year pro-forma financial projections for the district's General Fund using, as our starting point, an adjusted forecast of this year's budget. (Refer to Table 1 to see the pro-forma by year). The pro-forma is a 5-year projection of the district's revenue and expenses based on a model that incorporates key assumptions.

We have taken a cautiously optimistic view and we assume that the Comprehensive District Design (CDD) will be successful. Our projections anticipate that enrollment will continue to decline, but decelerate, until the district begins increasing its enrollment again by the 25-26 school year. Our analysis finds that, regardless of whether the CDD succeeds, the district is burdened by an unsustainable fiscal structure and should urgently seek to identify and act on cost efficiencies to prevent entering statutory operating debt in the 2023-24 school year.

Key Findings

Our projections and the analysis of them have allowed us to reach several conclusions:

- The district operates under an unsustainable and inefficient cost structure, which, under current circumstances, will likely completely deplete the district's General Fund balance sometime during the 2023-24 school year.
- The district will be unable to solve its problems through enrollment increases alone. Adding the number of additional students needed to justify the current cost structure is unrealistic. A full analysis of the impact of enrollment increases and cost structure is included in the accompanying detailed report.
- The district will continue to assess its scope and footprint as it begins implementation of the Comprehensive District Design. Once the CDD has been fully implemented we will better be able to determine its impact on programming and enrollment across the District, and where adjustments may be needed.
- The district must set clear parameters and priorities to guide where funding should be maintained or increased and where disinvestment may need to occur. Constantly evaluating return on investment allows the District to maintain the future flexibility needed to ensure available funding for areas showing the most promising results.

Table 1 Millions of \$	Projected FY21	Pro-Forma Projection				
		FY22	FY23	FY24	FY25	FY26
Revenue	\$627.4	\$572.3	\$566.1	\$566.6	\$572.8	\$584.6
Expenses	\$650.4	\$603.2	\$602.8	\$610.9	\$631.9	\$652.0
Change in Fund Balance	(\$23.1)	(\$30.8)	(\$36.8)	(\$44.3)	(\$59.1)	(\$67.4)
Ending Fund Balance	\$83.2	\$52.4	\$15.6	(\$28.7)	(\$87.8)	(\$155.2)

Base Assumptions

Given the financial difficulties faced by the district as well as the State of Minnesota, we are assuming that the state's biennial budget will not include any increases to the funding formula. We are also assuming the district will be unable to agree to any increases in salaries in the next round of collective bargaining. In the just concluded current round of bargaining, when the district renegotiated contracts with its labor unions, the district was able to agree to 2.5% increases (about \$12M of current salary and benefits expense) in total compensation. Finally, we are assuming that enrollment continues to decline over the next three years as the CDD is implemented, but that this trend will reverse in FY25 and start to trend in a positive direction after the impacts of the CDD start to take root.

COVID-19 Response Expenses

Like most districts, we did not understand the significant impact that the Covid-19 Pandemic would have, both financially and in terms of its impact on students, families and staff. Unbudgeted expenditures to support distance learning, safe buildings and additional staffing are estimated to be \$58.7M this year, with additional expense in future years. While we are able to offset these expenses using additional state aid provided under the Coronavirus Aid, Relief, and Economics Act (CARES Act) and other sources, that aid will only cover about half of our anticipated costs.

This gap is further compounded by higher-than-expected enrollment declines in our schools as families look for alternatives to distance learning and other sources of daytime care for their children. These additional and unpredictable enrollment declines will reduce district revenue by about \$7.1 million this year, the 2020-21 school year. Finally, as a result of the distance learning mandate in the spring, the district was forced to move to a 'one-to-one' device program this year, providing laptops or tablets and often cellular hotspots to all families. We anticipate that this program will cost about \$20.1 million this year alone, with annual costs of \$8-\$12 million per year going forward to pay for additional staff, equipment replacement, filtering software, hotspots, and other costs needed to effectively operate such a program.

Legislative Response

While our pro-forma does not include any new funding from the state to offset the unfunded Covid-19 costs faced by the district, we did contemplate two potential scenarios in which the legislature responds to the needs of Minnesota's schools:

- First, we considered a scenario in which the legislature makes districts "whole" for any enrollment declines experienced this year. While this would not address the district's structural issues it would add about \$11.5M in revenue to our current year forecast.

- Second, we considered a projection that includes standard formula increases over the next two years, as our base projection does not include any formula increases.

Although both these scenarios improve the district's long-term financials (see Table 2), they do not solve the district's cost structure issues or lead to financial sustainability. Additionally, for a district already struggling with financial sustainability, the incremental costs arising from the COVID-19 pandemic only exacerbate these issues. Of the \$262 million in deficit spending projected in the current year and five years after, \$75 million represents unfunded spending required as a result of the Covid-19 pandemic. Many of these costs arise from state government mandates to provide devices to students, install expensive air filters in classrooms, and continue to pay employees who are not working.

While COVID-19 will eventually come to an end, many of these programs and pieces of equipment will long outlive it. These legacies of the pandemic – even though they may ultimately benefit staff and students – were unfunded, unplanned for and will be with us for many years. The new programs will need to be administered and equipment maintained and replaced. We do not anticipate any ongoing assistance from the state in addition to what we already receive.

There is also pending legislation (the “HEROES Act”) in the U.S. Congress to provide additional relief to schools. Current proposals include about \$105 billion for schools. While the amount that would flow to Minneapolis Public Schools is unclear, a similar program was created in 2009 with funding of about \$100 billion going to schools, and the district received \$19.8 million.

Table 2: Impact on Fund Balance Based on Action by State Legislature (Millions of Dollars)											
	Base Projection				Make Whole for FY21				2% Funding Increase		
	Rev	Exp	Chng	Balance	Rev	Exp	Chng	Balance	Rev	Exp	Chng
FY21	627.4	650.4	(23.1)	83.2	638.9	650.4	(11.5)	94.8	627.4	650.4	(23.1)
FY22	572.3	603.2	(30.9)	52.4	572.3	603.2	(30.9)	63.9	576.8	603.2	(26.4)
FY23	565.6	602.8	(37.3)	15.1	565.6	602.8	(37.3)	26.6	574.4	602.8	(28.4)
FY24	566.4	610.9	(44.5)	(29.4)	566.4	610.9	(44.5)	(17.9)	575.2	610.9	(35.7)
FY25	572.8	631.9	(59.1)	(88.5)	572.8	631.9	(59.1)	(77.0)	581.6	631.9	(50.3)
FY26	584.6	652.0	(67.4)	(155.9)	584.6	652.0	(67.4)	(144.4)	593.7	652.0	(58.3)
Total Change in Fund Bal			(262.2)				(250.6)				(222.1)
FY21 Starting Balance			106.3				106.3				106.3
FY26 Ending Fund Balance			(155.9)				(144.4)				(115.9)

Comprehensive District Design (CDD)

Our pro-forma includes all CDD-related costs included in the CDD Finance Presentation presented to the Board of Education at their meeting on May 12, 2020. This totals approximately \$11.5 million in FY22, with ongoing costs of \$10.7 million per year, adjusted for inflation. We are also including an offset of approximately (\$7.0 million) per year to account for anticipated transportation savings associated with the CDD.

Appendix 1: Pro-Forma Financial Projection
(Thousands of Dollars)

A more detailed breakdown of revenue and expenses than is presented in Table 1.

MPS Pro-Forma Financial Projection						
	'20-'21	'21-'22	'22-'23	'23-'24	'24-'25	'25-'26
Starting Fund Balance	106,286	83,226	52,404	15,649	(28,688)	(87,812)
State Aid	388,311	373,485	371,186	368,683	370,242	377,191
Levy	142,738	137,847	133,912	136,099	138,625	141,486
Grants	87,324	51,914	51,885	52,581	54,388	56,119
Funded Projects	9,000	9,090	9,085	9,207	9,523	9,826
Subtotal Revenue	627,373	572,336	566,068	566,569	572,779	584,623
Salaries	339,023	340,503	338,651	343,610	353,199	365,922
Extended Time	16,871	14,283	14,635	15,001	15,376	15,761
Reserves	18,102	6,019	6,080	6,140	6,202	6,264
Fringe	128,862	129,483	132,105	136,730	143,358	151,618
Purchased Services	95,172	75,534	74,912	72,587	74,814	75,108
Supplies	31,738	25,964	25,225	24,995	27,534	25,826
Capital Expenses	16,329	6,994	6,794	7,378	6,910	6,958
Misc	4,334	4,377	4,421	4,465	4,510	4,555
Subtotal Expense	650,432	603,159	602,823	610,905	631,903	652,012
Change in Fund Balance	(23,059)	(30,823)	(36,755)	(44,337)	(59,124)	(67,390)
Ending Fund Balance	83,226	52,404	15,649	(28,688)	(87,812)	(155,202)

Appendix 2: Enrollment Assumptions by Year

FY	ADM Est	Change	% Change	Adj. Pupil Units	% Change
FY21	31,645			34,212	
FY22	30,700	-945	-3.0%	33,187	-3.0%
FY23	29,700	-1,000	-3.3%	32,091	-3.3%
FY24	29,100	-600	-2.0%	31,350	-2.3%
FY25	29,101	0	0.0%	31,255	-0.3%
FY26	29,501	400	1.4%	31,600	1.1%

Appendix 3: COVID-19 Related Aid & Costs:

Table 3 Thousands of \$	Projected COVID-19 Related Revenue & Expenditures						Total
	FY21	FY22	FY23	FY24	FY25	FY26	
COVID-19 Related Aid	\$31,096	\$ -	\$ -	\$ -	\$ -	\$ -	\$31,096
<u>Expenditures</u>							
IT/Universal Tech Access	20,188	7,993	9,560	8,668	12,014	8,299	66,722
Human Resources *	16,307	-	-	-	-	-	16,307
Facilities	9,911	-	-	-	-	-	9,911
Transportation	6,608	-	-	-	-	-	6,608
Academics & Supports	5,418	114	117	120	124	128	6,022
Culinary	300	-	-	-	-	-	300
Subtotal Expenditures	58,732	8,106	9,677	8,788	12,139	8,427	105,870
Fund Increase/(Decrease)	(27,636)	(8,106)	(9,677)	(8,788)	(12,139)	(8,427)	(74,773)

Appendix 4: Statutory Operating Debt Definition

Minnesota Statutes, section 123B.81 – Statutory Operating Debt.

Subdivision 1. Operating debt. The "operating debt" of a school district means the net negative unreserved general fund balance calculated as of June 30 of each year in accordance with the uniform financial accounting and reporting standards for Minnesota school districts.

Subdivision 2. Statutory operating debt. If the amount of the operating debt is more than 2 ½ percent of the most recent fiscal year's expenditure amount for the funds considered under subdivision 1, the net negative undesignated fund balance is defined as "statutory operating debt".