BUDGET BRIEF:
2017 PROPOSED BUDGET

MILWAUKEE PUBLIC SCHOOLS

PUBLIC POLICY FORUM

Budget Brief:

2017 Proposed Budget
Milwaukee Public Schools

May 2016

Study authors:

Douglass Day, Researcher
Rob Henken, President

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We would like to thank the Greater Milwaukee Foundation and Northwestern Mutual Foundation for their generous support of our education research.

This analysis of MPS' 2017 proposed budget refers to the budget recently submitted to the Milwaukee Board of School Directors by the Milwaukee Public Schools Superintendent. The budget covers the school district's 2017 fiscal year, which takes effect on July 1, 2016, and runs through June 30, 2017. Also, it should be noted that while the School Board will adopt a tentative budget later this month and the fiscal year will begin in July, the budget will be revisited by the Superintendent and Board in the fall after the district receives final aid amounts from the State of Wisconsin.

Introduction

In last year's analysis of the proposed budget for the Milwaukee Public Schools (MPS), the Public Policy Forum remarked upon the improvement in the district's short-term fiscal stability. Yet, at the same time, we warned that "whether MPS can maintain and achieve both stability and the capacity to make strategic programmatic investments still is questionable, and still is largely contingent upon decision-making at other levels of government."

The MPS Superintendent's proposed 2017 budget, at first glance, appears to refute that warning. The budget contains a variety of investments in strategic plan initiatives and activities, including expansion of summer school and English as a Second Language services, "bridge" programs for ninth graders, an increase in Advanced Placement and International Baccalaureate programming, and free driver's education. It also adds 183 positions, is able to allocate $12 million for salary increases, and invests in additional elements of the Regional Development Plan.

Curiously, these investments are proposed despite continued revenue challenges. District revenues decline by $1.3 million, which constitutes a minimal 0.1% in a $1.2 billion budget, but which would seemingly preclude MPS' ability to invest in strategic plan initiatives, let alone accommodate inflationary increases in its fixed costs. Furthermore, a source of fiscal salvation in previous budgets – the decline in health care costs generated from health plan redesign and other changes – appears to have run its course, with overall fringe benefits spending projected to grow by $3.3 million in 2017.

So where did the wherewithal to invest in strategic initiatives come from? The answer lies largely in internal reallocation. Most notably, the 2017 proposed budget reduces by $31.2 million the contribution to reserves for retiree liabilities, thus freeing up an equivalent amount for investment in other budget priorities. It also transfers $8.5 million in property tax revenues from the construction fund to school operations. As a one-time maneuver, that move is not expected to reduce the district's capacity to address infrastructure challenges, and it would provide additional resources for the classroom.

The good news is that MPS' ability to invest in initiatives identified through strategic planning that hold promise to improve academic achievement and stem the loss of enrollment is maintained in the proposed budget. The bad news is that future-year challenges may be exacerbated, as the use of internal reallocation strategies may be more difficult to achieve in future years, and the $8.5 million transfer from the construction fund must be reversed. In fact, we project that MPS' expenditures may exceed continuing revenues by nearly $40 million heading into 2018.

In the pages that follow, we provide more detailed analysis of the major elements of the 2017 proposed budget, and the strategies the district is proposing to accommodate programmatic objectives within the confines of its continued fiscal challenges. Our objective is to provide an independent assessment of the district’s immediate fiscal circumstances – as well as its long-term outlook – that will encourage informed deliberations by policymakers in Milwaukee and Madison.

Budget Overview

For the second year in a row, MPS' 2017 proposed budget is able to accommodate large-scale investments in new activities despite stagnant revenues. The district accomplishes this feat by using internal funding reallocations – some of which were made possible by prior year savings – to fund new budget initiatives and continue implementation of its strategic plan.

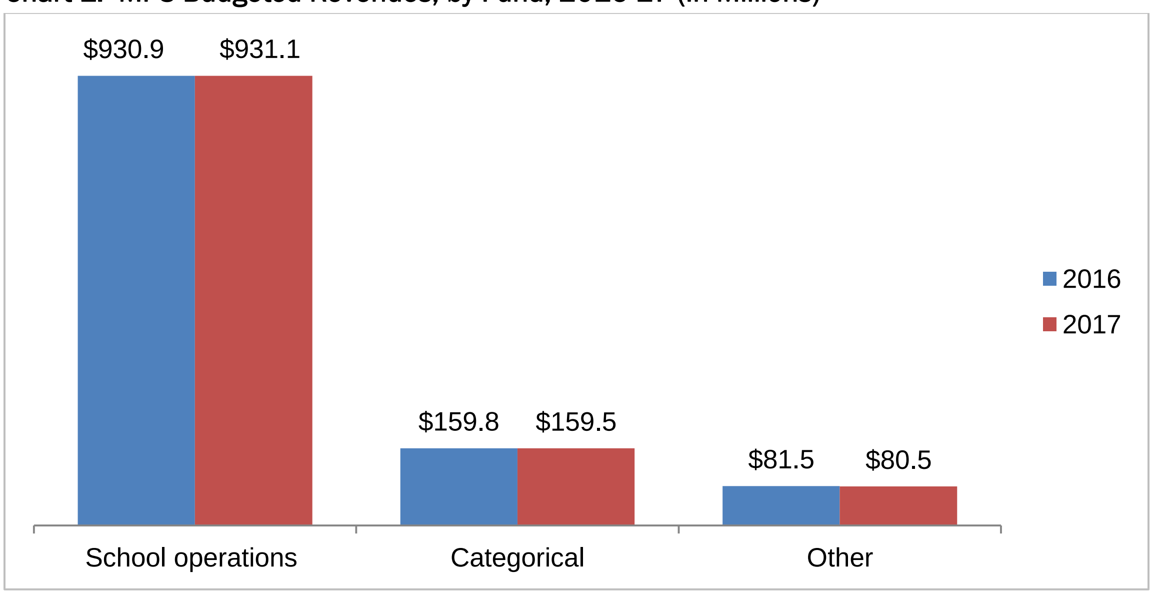
Below, we provide a high-level synopsis of the major revenue and expenditure issues that characterize the proposed budget. More detailed analysis of specific key budget items is provided in later sections of the report.

Revenue

The MPS superintendent proposes a budget for 2017 that differs little from the previous year in the overall amount of money available for district programs and operations. The budget anticipates that revenues will decline by $1.3 million, which represents a decrease of 0.1% from the 2016 adopted total.

As shown in **Chart 1**, the overall change in revenue in the proposed budget is reflected in each of its main funds. School operations, which constitutes 80% of MPS' budget and funds all school and administrative expenditures, shows a small increase of $280,000 over 2016. Categorical aids, which is the next largest fund and is comprised of state and (especially) federal grants, declines by $306,500. The smaller construction, school nutrition, and extension funds – which we combine in the chart – drop by $1 million.[1]

Chart 1: MPS Budgeted Revenues, by Fund, 2016-17 (In Millions)

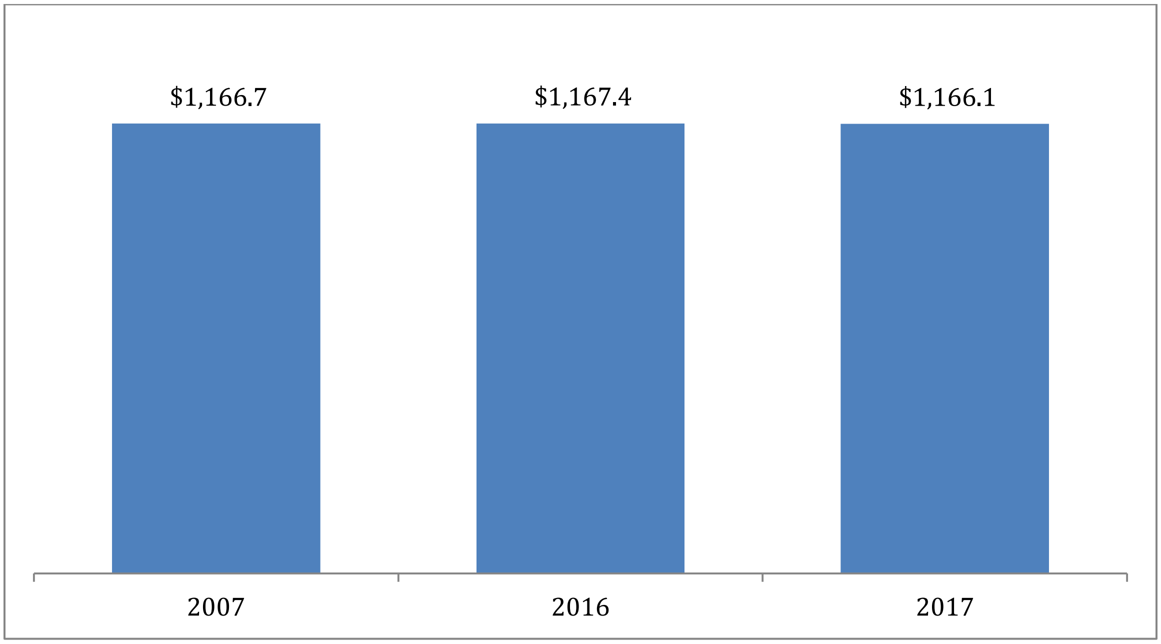


[1] MPS' extension fund finances adult education, social centers, playgrounds, and fee-based recreation programs for City of Milwaukee residents.

The minimal change in total revenue in each of the district's major funds should not obscure the substantial variation that occurs in *some* 2017 revenue sources. The most significant of these fiscal changes takes place in the school operations fund, where an estimated $11.2 million decrease in the combined amount of state equalization aids and property tax levy is somewhat offset by a $7.7 million increase in state per-pupil aid.

As shown in **Chart 2**, when viewed over a 10-year period, the trend line in total MPS revenues has been relatively flat. In fact, incoming revenues in 2017 are nearly identical to what they were in 2007.

Chart 2: MPS Total Budgeted Revenues (In Millions)



Lack of revenue growth has had a negative impact on the district's purchasing power and the fiscal health of the district in general.[2] The past decade has shown only a modest increase in prices, as the Consumer Price Index rose by an average of 1.5% each year. Still, if MPS' total budget had increased at the same rate as inflation during the past decade, MPS would have $217.9 million more in its budget today than it had in 2007.[3]

Expenditures

As shown in **Table 1**, major expenditures by object in the 2017 proposed budget do not vary substantially from 2016. Salaries and fringe benefits are up slightly, and purchased services and supplies are down.

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[2] The financial evaluation system of the International City/County Management Association, previously used in Forum fiscal analyses, uses a variety of indicators to assess the fiscal health of local governments. One indicator is whether incoming revenue is rising at about the rate of inflation.

[3] U.S. Department of Labor. Bureau of Labor Statistics CPI Inflation Calculator. Inflation calculated between 2006 and 2016 to correspond to the fiscal year 2007 and 2017 budgets.

Table 1: MPS Total Expenditures by Object, 2016-17, (In Millions)

Expenditures	2016 (Budgeted)	2017 (Proposed)	% Change
Salaries/other wages	$522.7	$523.1	0.1%
Benefits	$242.5	$245.8	1.4%
Purchased services	$319.6	$315.3	-1.3%
Supplies	$71.1	$68.3	-3.9%
Debt Service	$29.8	$31.1	4.4%
Other	($18.3)	($17.5)	-4.4%
Total	**$1,167.4**	**$1,166.1**	**-0.1%**

Source: MPS 2017 Proposed Budget

However, a closer look reveals that funding reallocations *are* proposed for the coming year. For example, an expansion of the number of MPS charter schools and charter school enrollment will increase the district's fiscal allocation to non-instrumentality charter schools by $16.2 million, even though overall funding for school operations remains nearly the same.[4]

This is an example of the extent to which MPS' expenditure budget can be impacted by competition from independent, publicly-funded charter schools, as well as private schools that participate in the Milwaukee Parental Choice Program. Such competition also has resulted in school closings and enrollment losses in previous years, as well as expenditures on new initiatives designed to enhance MPS' competitiveness in this fluid environment.

The rise and fall of fringe benefit expenditures also has significantly shaped the district's budget in recent years. A decade ago, MPS' pension and health care costs were growing at a rate substantially greater than inflation, forcing internal reallocation to pay for these costs. That changed in 2010, however, when fringe benefit expenditures were sent on a downward path because of a new four-year teachers' contract that included major changes in health care financing.

This cost trajectory accelerated with the passage of Wisconsin Act 10 in 2011. Under this legislation, a school district's fringe benefits were no longer subject to collective bargaining, and MPS was able to make additional, unilateral changes in employee benefits. In addition, public sector employees were required to pay a higher portion of their health care and pension costs.

The restructuring of employee benefits also served to indirectly curtail annual increases in salary expenditures, as retirements increased precipitously when employees sought to secure benefits that were being phased out, such as eligibility for retirement at age 55. As lower-salaried and less experienced employees took the place of higher-paid, retiring teachers and staff, cost savings resulted.

The combination of fringe benefit and salary/wage changes enabled MPS to budget $109 million less for personnel costs in 2016 than it spent in 2011. The savings not only helped to balance the budget, but also provided an opportunity to reallocate funds to address operational needs that had gone unmet in previous years.

[4] These funding increases are caused in large part by a doubling of enrollment at Milwaukee College Prep; the addition of a new charter school, Milwaukee Excellence; and a partnership between Carmen High School, a charter school, and Pulaski High School.

The impact of these savings and reallocations are seen in the current 2016 budget. Largely because of reductions in fringe and salary costs and a conscious strategy to leave open some vacant positions, MPS was able to fund 42 new positions, while also generating more than $30 million in savings to apply toward 2017 debt payments for other post-employment benefit (OPEB) liabilities for retirees (most of which relate to retiree health care obligations).

In 2017, MPS' five-year run of personnel cost reductions seems to have ended. With savings from that source exhausted, at least in the short-term, the district must look elsewhere in the 2017 proposed budget to support implementation of high-priority initiatives. One example is a decision to shift $8.5 million in property tax levy from the construction fund to school operations. Borrowed funds and an unassigned balance in the construction fund will make up for some but not all of the reduction from the construction account.

The budget proposes to reallocate $31.2 million freed up by a reduced payment to the district's reserve for future OPEB liabilities – plus funds secured from other internal reallocations – on a series of initiatives. The monies generated will be used for various purposes, including $12 million for salary increases, 183 new positions, and program enhancements related to the district's strategic plan. These actions will place financial strain on the 2018 budget, which budget officials contend will be addressed through future cost savings and efficiencies.

Eight Keys to Understanding MPS' 2017 Proposed Budget

Key #1: The State's Per-Student Revenue Limit Remains Flat

MPS' per-student revenue limit for 2017 is $10,122, the same as 2016. In the past five years, MPS' revenue limit has increased by $322 per student, or 3.3%, which is well below the rate of inflation.

<u>Why this is important</u>

The equalization aid formula governs the allocation of most state and local funding for public education in Wisconsin. The formula is complex, but its central purpose is to compensate for differences in property wealth. Poor districts receive more state equalization aid; wealthy districts receive less. However, for both types of districts, after state equalization aid is credited, local districts only can provide additional property tax funding up to their state-established revenue limit. A district's expenditures can exceed this limit only when approved by public referendum or for other technical reasons.

Consequently, the revenue limit is the key factor governing increases in a school district's combined amount of state equalization *and* local property tax levy. Together, these two revenues represent 89% of MPS' school operations budget and 71% of its total budget. It is important to note that even when the state allocates additional money for equalization aid, if the per-student revenue limit is not raised as well, then the new funds will not be used for educational purposes but instead will go for property tax relief.

Key #2: Limited Growth in Non-Formula School Aids

While general state aid increases by $7.7 million in the 2017 proposed budget, funding from federal and state categorical grants remains comparatively flat. These grants generally support services for disadvantaged and special needs students.

<u>Why this is important</u>

In the last few years, much of the increase in state funding has occurred outside of the equalization aid formula through a new form of per-pupil assistance that was adopted in 2011 to partially compensate for funding cutbacks instituted under Act 10. These general state aid monies go directly into a school district's school operations fund. In 2017, MPS will receive $19.7 million from this revenue source, or $7.7 million more than in 2016.

In contrast, there is little variation in grant funding in the proposed budget. Federal categorical revenues (and categorical revenues as a whole) essentially are flat; budget increases in some programs, such as Title I, are offset by revenue drop-offs in other areas. State programs that are budgeted under school operations – such as handicapped aid, transportation, and library aids – have changed little, if at all, as has state categorical funding.

For MPS, these forms of non-formula school aids provide critical support for school programs educating special populations. Students with disabilities constitute 20% of the district's total enrollment – compared to 14% for the state as a whole – and 80% of all MPS students fall within the income guidelines established by the federal subsidized school lunch program. MPS depends upon federal and state grants to offset the higher costs involved in educating these disadvantaged and special needs students.

MPS' reliance upon state and federal grants is shown in Department of Public Instruction data. These numbers reveal that in 2015, MPS received $2,387 per student in federal grants, placing it fifth among Wisconsin's 434 school districts. MPS also ranked 28th in state funding per student, though its high standing on this measure did not result from its receipt of equalization aid, where it placed 111th; rather, it resulted from the revenues that flowed into designated programs such as state handicapped aids and the Achievement Gap Reduction (formerly known as Student Achievement Guarantee in Education, or SAGE), which provide supplemental funds for the education of disadvantaged students.

Key #3: A Decline in MPS' Student Enrollment Contributes to a Loss of $11.2 Million

MPS' student enrollment, which is used to calculate equalization aid, is projected to fall by 700 students in 2017. This enrollment decrease represents a 5% reduction since 2014. MPS will lose $11.2 million in its estimated combined amount of equalization aid and property tax levy in 2017 as a consequence of recent and projected enrollment declines and the revenue limit freeze described above.

Why this is important

Student enrollment has a strong impact on school district finances, as many programs have allocation formulas predicated on numbers of students served. The revenue limit, as discussed above, is student-based.

MPS has experienced a 17% decline in enrollment (as measured by the equalization aid formula) in the past decade, and a 5.1% reduction since 2014, as shown in **Table 2**. Funding in MPS' 2017 proposed budget projects an enrollment drop of 700 students in the next year. In addition, as noted later in this report, MPS enrollment is projected to continue to fall over the next five years.

Table 2: MPS Enrollment, By School Type

School Type	2014	2015	2016	2017	One-year change	Four-year change
MPS-traditional schools	70,756	68,835	66,920	64,803	-3.2%	-8.2%
MPS-contracted schools	1,552	1,657	1,524	1,720	12.9%	9.8%
MPS charters	6,194	6,899	7,124	8,785	23.3%	56.7%
MPS sites total	**78,502**	**77,391**	**75,568**	**75,308**	**-0.3%**	**-4.1%**
Open enrollment/Chapter 220*	8,517	8,128	7,747	7,307	-5.7%	-14.3%
Total MPS membership	**87,019**	**85,519**	**83,315**	**82,615**	**-0.8%**	**-5.1%**

Source: MPS budget office

* Chapter 220 enrollment in suburban schools does not include intra-district MPS transfers

Competition from private schools and non-MPS charter schools contributes heavily to the district's enrollment plunge. Private school enrollment in Milwaukee – stimulated by the Milwaukee Parental Choice Program (MPCP) – has grown from 25,270 students in 2004 to 35,063 students in 2016. An even faster rate of growth is evidenced among the city's independent charter schools, whose student numbers more than doubled from 4,104 in 2005 to 8,839 in 2015.

A detailed analysis of the fiscal impact of MPS' enrollment losses is beyond the scope of this budget brief. It should be noted that the state equalization aid formula averages enrollment over a three-year period and seeks to moderate the financial impact of sharp enrollment losses in a given year. A continuous fall in enrollment ultimately leads to funding cutbacks, however. MPS budget officials report that this year's reduction is the largest negative enrollment funding adjustment in revenue limits they can recall.

Key #4: Total Fringe Benefit Costs Increase by $3.3 million

Why this is important

As explained above, fringe benefits have been the dominant force in MPS' budget during the past decade. Initially, this force was negative, as a variety of factors coalesced to drive pension and health care cost increases that were significantly above the rate of inflation. Some prophesized that out-of-control fringe benefits would even bankrupt the district and pointed as evidence to MPS' $2.8 billion unfunded OPEB liability, a figure exceeding the unfunded OPEB liabilities of other area governments, such as the City of Milwaukee and Milwaukee County.

However, starting in 2010, MPS began to bring its health care costs under control by instituting actions such as redesigning its medical, dental, and pharmaceutical plans, hiring a new third-party administrator, and differentiating premium costs by creating low- and high-cost plans. Subsequent changes followed, such as the district's decision to raise the employee threshold to receive fringe benefits from 20 to 30 hours a week, and the closing of the district's supplemental teacher retirement plan to new employees. MPS also increased the years of service and retirement age needed to qualify for retiree health care benefits.

Actual medical insurance expenditures plummeted from $155.4 million in 2011 to $83.1 million in 2015. Meanwhile, the district's unfunded OPEB liabilities now total $1.1 billion, a considerable sum but a much lower figure than just a few years ago.

The 2017 proposed budget marks the end of five consecutive years of falling fringe benefit expenditures, however. In the coming year, fringe benefit expenditures are budgeted to increase by $3.3 million (1.3%), with the increase mainly attributed to a rise in medical costs and a greater incidence of high-cost medical claims. The district's overall fringe benefit rate will increase from 43.2% of salary in 2016 to 46.6% in 2017. For teachers, budgeted average salaries stay constant at $59,320, but fringe benefits rise by $2,000 per teacher from $25,600 to $27,600.

The volatile recent history of MPS' fringe benefit expenditures makes it difficult to say for certain, but it appears that MPS now may be entering a period in which fringe benefits will grow at a more predictable rate, though one that will be above the rate of inflation. Such a circumstance would produce ongoing challenges in light of the district's flat revenue streams. Projections for fringe benefit expenditures in the next four years are reviewed later in this report.

Key #5: Reallocation of $8.5 Million in Property Tax Revenues from the Construction Fund to School Operations

In the 2017 proposed budget, MPS reallocates $8.5 million in property tax revenues from the construction fund to school operations, replacing most of the $11.2 million reduction in its combined state equalization aid and property tax levy.

Why this is important

The reallocation of $8.5 million from the construction fund to school operations averts a major funding reduction in school operations in 2017. To restore some of the lost revenue in the construction fund, the budget draws upon $2 million in unassigned surplus revenues and $1.5 million in borrowed funds. The $8.3 million construction fund budget proposed for 2017 is a decrease of $2.8 million from 2016, which may cause continued deferral of some maintenance projects. The district intends to repay this funding transfer in 2018.

MPS budget officials state that use of unassigned and borrowed funds for 2017 construction activity is fiscally appropriate since the district will not need to draw on some revenues in these funds for construction projects in the coming year. Also, they point out that MPS' overall level of borrowing is modest in comparison with similar urban school districts in the U.S. Recent data from the Council of Great City Schools show that the ratio of outstanding principal debt to annual district revenue is 68.4% for the median urban district, while that ratio stands at 31.1% for MPS.

The changes in MPS' construction budget are part of a planned two-year fiscal restructuring highlighted by an increase in expenditures to $45.1 million in 2018. The 2017 proposed budget notes that revenues in 2018 "will include several million dollars more of tax levy…and $34 million of borrowed funds." The primary purpose of the borrowed funds would be to address deferred major maintenance.

After the influx of substantial additional funding in 2018, budget officials anticipate establishing a rotating five-year schedule to fund these types of routine infrastructure costs. The level of funding established will be equivalent to 2016 expenditures ($11.1 million) and is intended to be sufficient to prevent future growth in deferred maintenance.

Key #6: A Reduced Retirement Liability Reserve Contribution Frees Up $31.2 million for Strategic Plan Investment

MPS anticipates reducing its 2017 contribution to its OPEB reserve by $31.2 million, thus freeing up an equivalent amount of funding for instructional investments.

Why this is important

MPS has generated unanticipated mid-year budget savings in the past few years that it has dedicated to building its reserve for future OPEB liabilities. According to budget officials, the build-up of reserves provides sufficient comfort to reduce the budgeted reserve contribution in 2017 by $31.2 million.

MPS' prior year savings were generated by lower-than-anticipated personnel expenditures caused mainly by position vacancies that remained open, as well as salary and fringe benefit costs that were below budgeted levels. Use of those savings allowed MPS to make contributions to its OPEB reserve that exceeded required levels, thus allowing for the reduced contribution in 2017.

Under the equalization aid formula, any unexpended monies that exist at the end of the year only can be used for debt service payments and other limited purposes. Any attempt to carry over funds to the next fiscal year for other purposes results in an equivalent reduction in a district's revenue limit. Consequently, MPS has employed the practice of dedicating its unanticipated surplus from the prior year to help finance a portion of the OPEB liability.

Key #7: Internal Reallocation for Salaries, New Positions, and Strategic Initiatives

With the addition of funding from the reallocations described above, as well as other reallocations from monies freed up in the 2017 school operations budget, MPS has substantial revenues available to invest in budgetary initiatives for 2017.

<u>Why this is important</u>

Despite its stagnant revenue streams, the proposed budget manages to set aside $12 million for employee raises (though the exact amount of the increase will be determined by collective bargaining negotiations). Also, the proposed budget funds 183 new positions, most of which are allocated to school operations.

As in 2016, the 2017 proposed budget allows MPS to move forward with implementing its new strategic plan, and it integrates that plan into the budget process. The plan is organized around "eight big ideas" for improving student outcomes. It also includes a Regional Development Plan for increasing the number of high-performing schools. In essence, MPS is attempting to raise the level of student achievement in schools with high student poverty, while at the same time seeking to increase the number of schools that can compete more successfully with private schools, thereby attempting to reverse the district's history of enrollment losses.

In 2016, MPS will complete most of Phase I of the Regional Development Plan, aimed at expanding facilities and operations in high-demand programs and strengthening feeder patterns that facilitate students' progression from one school (and one level of education) to the next. Accomplishments include:

- Building a new addition at Fernwood Montessori
- Remodeling a former middle school to facilitate the expansion of Rufus King International Middle School
- Developing a second campus for Milwaukee Spanish Immersion School
- Designating Victory School as an Italian language-immersion program
- Relocating Morse Middle School for the Gifted and Talented
- Creating a partnership between Carmen High School of Technology-South and Pulaski High School, thereby creating more seats for Carmen and bringing the International Baccalaureate program to Pulaski

MPS allocated $27.6 million in 2016 to implement Phase I of the Regional Development Plan. In 2017, the district will move on to less costly plan development, allocating $6.2 million for this purpose and freeing up $21 million for internal reallocation. Program initiatives funded from this and other reallocations include:

- Summer school expansion ($1.4 million)
- Expansion of ESL services ($0.65 million)
- Reduction of the district's adult-to-student ratio, including class size reduction ($11.1 million)
- Increase in the number of school counselors and counselor time ($0.73 million)
- Freshman "bridge" programs for all grade 9 students ($0.8 million)
- Expansion of after-school activities ($1.5 million)
- Free driver's education for all MPS students ($0.65 million)
- Increase in Advanced Placement & International Baccalaureate programming ($1.0 million)
- Expansion of career pathway programs in arts, health, and culinary arts ($1.8 million)
- Additional alternative high school options ($1.1 million)
- Expansion of funding for translation services ($1.0 million)

Key # 8: Expenditures in 2017 Will Exceed Continuing Revenues by Nearly $40 Million

MPS' plan to restore into the construction fund the $8.5 million in property taxes that will be transferred in 2017 to school operations – combined with its reduced payment of $31.2 million to the OPEB reserve and expansion of overall expenditures by that amount – creates a potential $40 million budget "hole" for 2018.

Why this is important

The district's use of this $40 million is part of an overall financial and program strategy that seeks to halt enrollment losses and the state equalization aid reductions associated with them. Also, the 2018 budget outlook will be shaped by unknown future factors and developments, such as the amount of new revenue provided by the next state budget. Nevertheless, the creation of this potential "hole" does set up a 2018 budget scenario that may be far more challenging than that experienced in the past two years.

In the coming year, budget officials will monitor expenditures and assess possibilities for again generating savings that can be reallocated to reduce the anticipated revenue shortfall in 2018. They also will look at possibilities for achieving more effective and efficient operations and otherwise reducing program costs. In this effort, district officials report they will examine potential savings in areas such as transportation costs, building use, right-sizing enrollment, and medical costs.

Fundamental Budget Components: Revenues and Positions

While the previous sections of this report provide broad analysis of the major issues that characterize the 2017 proposed budget, there are two budget categories that merit detailed analysis. That is the case not only because of their importance to 2017, but also because of what they portend for MPS' long-term fiscal solvency. In this section, we provide additional details on those categories: revenues and positions.

Revenues

School Operations

MPS' school and administrative expenses are financed through the school operations fund. This fund is distinct from other funds in the MPS budget in that those other funds have specialized purposes.

Table 3 shows that major individual revenue lines for school operations exhibit little change in the 2017 proposed budget when compared to 2016. General school aids, funded from both state aid and property taxes, fall by $3 million (0.4%). With the exception of general state aid (also referred to as per-pupil aid), which increases by $7.7 million, most other revenue lines are flat. It is important to note that because MPS will not receive final notification of general school aid payments until October, it estimates total school aid revenue, but it does not distinguish between state equalization aid and property taxes in its 2017 proposed budget.

Table 3: School operations, Budgeted Revenue, 2016 to 2017 (In millions)

	2016 Budgeted	2017 Proposed	Difference	% change
State				
General equalization aid	$570.2			
Integration aid	$31.7			
Poverty aid	$5.3	$822.8**	-$3.0	-0.4%
Computer aid	$6.5			
Charter/Choice deduction	($61.0)			
*General School Aids**	*$825.7*	*$822.8*	*-$2.9*	*-0.4%*
Handicapped	$50.0	$49.6	-$0.4	-0.8%
Transportation	$2.5	$2.0	-$0.5	-20.0%
Library	$4.7	$4.7	$0.0	0.0%
Bilingual aid	$1.9	$1.9	$0.0	0.0%
Tuition from state	$0.5	$0.5	$0.0	0.0%
General state aid	$12.0	$19.7	$7.7	64.2%
Other state aid	$0.1	$0.1	$0.0	0.0%
Non-School Aids total	$71.7	$78.5	$6.8	9.5%
State Total	*$624.5*	n/a	n/a	n/a
Federal				
Fed reimbursement	$3.3	$3.5	$0.2	6.1%
Indirect cost aids	$5.3	$5.0	-$0.3	-5.7%
Medicaid Reimbursements	$7.3	$7.3	$0.0	0.0%
Federal Total	*$15.9*	*$15.8*	*-$0.1*	*-0.6%*
Local				
Property tax	$273.0	***	n/a	n/a
Non-property taxes				
Tuition	$6.1	$9.0	$2.9	47.5%
Rental	$3.8	$3.8	$0.0	0.0%
Other	$7.7	$1.2	-$6.3	-84.0%
Local Total	*$290.6*	NA	n/a	n/a
School Operations Total** **	**$930.9**	**$931.1**	**$0.2**	**0.0%**

* Includes funding from property tax levy

** Property tax levy for 2017 school aids budget is not set until fall 2016

*** The total and component pieces of the school aids budget are not known until fall; until then, MPS budgets school aids revenues as a single sum

**** Totals may not add due to rounding, excludes carryover funding

Source: MPS 2017 Proposed Budget

Categorical Aid

MPS' second largest fund is for categorical aid, which consists largely of grant programs. The federal government provides about 80% of MPS' grant monies. As shown in **Table 4**, the change in categorical aids from 2016 to 2017 is minor, with total funds dropping by about $300,000 and federal funds declining by $400,000.

While not shown in the table, a five-year trend analysis indicates that categorical aids have decreased by 14.5% since 2013 (by contrast, school operations has seen a 2.8% *increase* in total revenue over the past five years). Decreases in federal grants, which dropped by $26.9 million, contributed to most of this revenue loss.

MPS budget officials report that a particular concern has been the district's drop in Title I funding for disadvantaged students, a program that MPS closely aligns with ongoing school operations. Title I funding has gone down for many reasons. Prominent among them are MPS' decrease in enrollment, which coupled with a statewide increase in poverty has prompted a redistribution of Title I revenues among Wisconsin school districts. In 2015, MPS Title I expenditures amounted to $75.2 million. Under the 2017 proposed budget, Title I aid is budgeted at $71.6 million.

Table 4: MPS Categorical Revenue, 2016-17, (In Millions)

Program	2016 Budgeted	2017 Budgeted	Difference	% Change
Federal				
ESEA, Title I-A	$69.5	$71.6	$2.1	3.0%
ESEA, Title II	$10.1	$9.8	-$0.3	-3.0%
ESEA, Title III	$1.6	$1.1	-$0.5	-31.3%
IDEA	$25.0	$25.5	$0.6	2.4%
Head Start	$8.7	$7.8	-$0.8	-9.2%
Other	$13.9	$12.6	-$1.6	-14.7%
Federal total	**$128.8**	**$128.4**	**-$0.4**	**-0.3%**
State				
SAGE*	$24.1	$24.1	$0.0	0.0%
Other	$3.4	$3.5	$0.1	2.9%
State total	**$27.5**	**$27.6**	**$0.1**	**0.4%**
Private/local				
GE Foundation	$3.2	$3.2	$0.1	3.2%
Other	$0.3	$0.3	$0.0	0.0%
Private/local total	**$3.5**	**$3.5**	**-$0.1**	**-2.9%**
Total Categorical**	**$159.8**	**$159.5**	**-$0.3**	**-0.2%**

* Student Achievement Guarantee in Education

** does not include indirect aid payments, subtotal and totals may not add due to rounding

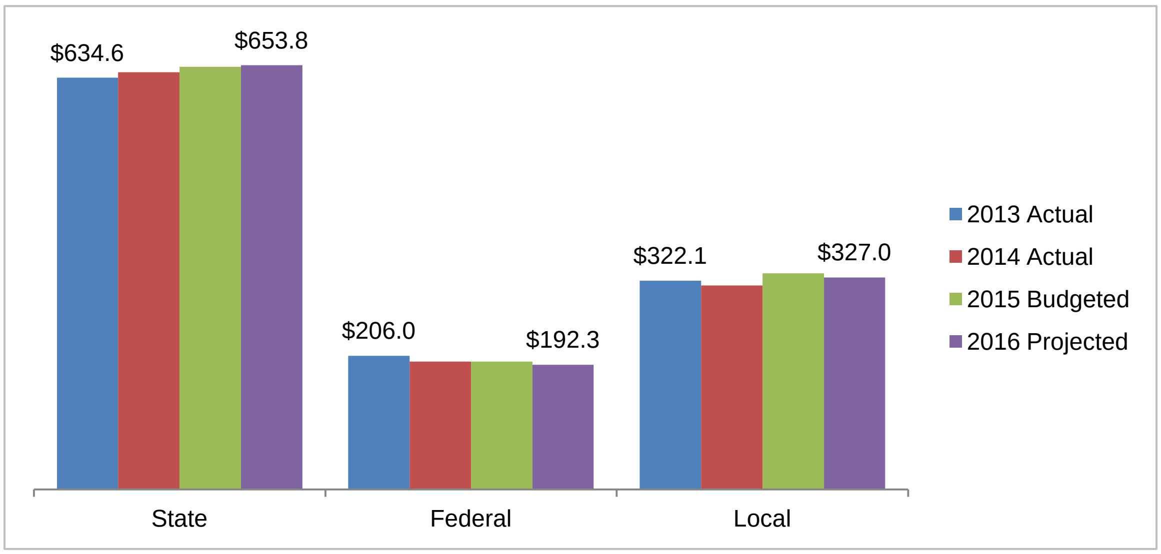
Source: MPS, 2017 Proposed Budget

Summary of State, Local, and Federal Revenues

With school operations and categorical programs as context, it is instructive to view MPS' revenue portfolio through the lens of its total breakdown of state, local, and federal revenues. **Chart 3** combines the revenue streams shown above in the school operations and categorical funds with revenues from the district's three smaller funds to provide complete state, local, and federal totals.

The table covers 2013-2016, as the unknown status of state general aids and property tax levy for 2017 prevents us from including that year in the chart. It indicates that during this period, state revenues increased by the largest amount of the three funding streams, growing by $19.2 million (3%). Federal revenues decreased by $13.7 million (6.7%), while local revenues grew marginally.

Chart 3: MPS State, Federal, and Local Revenues*, 2013 to 2016 (In Millions)



Position Changes

As shown in **Table 7**, the 2017 proposed budget shows a substantial increase in staff of 183 positions, with 139 of those positions allocated to school support. Some of the staffing changes represent typical annual personnel fluctuations, while others reflect conscious policy decisions to reorganize instructional operations and strengthen student services.

Table 7: MPS Positions, By Type, 2016 and 2017

Type	2016 Budgeted	2017 Budgeted	Difference	% Change
Certified school administrators	232	232	0	0.00%
Principals & assistant principals	253	267	14	5.50%
Teachers	4,987	4,959	-28	-0.60%
Licensed support professionals*	354	360	6	1.70%
School nurses	67	67	0	0.00%
Educational assistants	1,178	1,313	135	11.50%
Classified technical & administrative	357	376	19	5.30%
Trades & clerical	570	592	22	3.90%
Safety aides	250	258	8	3.20%
Building services, engineers,+ boiler attendants	617	620	3	0.50%
Food service	463	466	3	0.60%
Other	308	309	1	0.30%
Total	**9,636**	**9,819**	**183**	**1.90%**

* Includes therapists, social workers, & psychologists
Source: MPS 2017 Proposed Budget

A substantial group of position changes relates to a staff restructuring made possible by the elimination of the SAGE program and its reconstitution as AGR. Like SAGE, AGR focuses on improving the academic achievement of poor students. It differs, however, in that the state no longer requires schools receiving these revenues to meet specific class size thresholds. The new program provides roughly comparable funding for K5-3rd grade in schools previously receiving SAGE revenues.

According to the budget document, this program shift "has created flexibility in the 18:1 teacher-to-student ratio for K5 through 3rd grade classrooms." Consequently, the budget proposes to reduce teacher positions in those grades for schools eligible to receive AGR funding, while instead adding 135 educational assistant positions.

In other efforts to strengthen school and instructional performance, the budget proposes to add 14 assistant principals to focus on "school climate" and hire 19 teacher coaches at the district's central office to work with classroom teachers. In addition, it adds 18 school secretaries to improve service for parents and other constituents, and allocates resources to increase the number of school counselors and counselor time.

Perhaps the most remarkable aspect of MPS's proposed budget is that in just two years, total staff has risen by 256 positions, while budgeted enrollment at district schools has fallen by 2,085 students. Obviously, fiscal considerations will limit how long the district can pursue an expansive staffing strategy in the face of enrollment losses. MPS administrators are betting that – at least in the short term – an increase in school and instructional personnel, combined with other facility and academic improvements, will halt long-term enrollment losses and enhance the district's competitiveness.

Five-Year Budget Forecast

There was a time not long ago when MPS' fiscal forecast looked particularly dark: enrollments were falling, revenues were flat, and expenditures were spiraling upward because of escalating fringe benefit costs. The 2017 proposed budget shows that while some of those conditions have changed, the forecast is still far from sunny. Indeed, while the district has moderated expenditures substantially, student enrollments continue to fall and prospects for state revenue growth and increases in the revenue limit remain uncertain.

Table 8 shows the five-year fiscal forecast included in the 2017 proposed budget for school operations. The bottom line is a projected imbalance of revenues to expenditures (i.e. a projected deficit) of $114.2 million by 2021.

Table 8: Five-Year Projection, School Operation Expenditures, (In Millions)

	2016 Budgeted	2017 Proposed	2021 Projected	Five-year Difference	Five-year % change
Revenues (without applied surplus)	930.9	931.1	925.9	($5.0)	-0.5%
Expenditures					
Salaries/other wages	$427.1	$428.3	$443.5	$15.2	3.5%
Benefits	$192.2	$199.7	$249.3	$49.6	24.8%
Purchased services	$235.9	$258.6	$262.5	$3.9	1.5%
Supplies	$38.2	$32.7	$34.0	$1.3	4.0%
Debt Service	$29.8	$31.1	$36.8	$5.7	18.3%
Other	$38.0	$11.9	$14.0	$2.1	17.6%
Total Expenditures	$961.2	$962.3	$1,040.1	$77.8	8.1%
Balance Before Use of Prior Year Funds	($30.3)	($31.2)	($114.2)		
Use of Prior Year Funds for Legacy Costs	$30.3	$31.2	$0.0		
Balance/Deficit	**$0.0**	**$0.0**	**($114.2)**	**($114.20)**	**n/a**

Source: MPS 2017 Proposed Budget

The forecast estimates that total expenditures will rise by $77.8 million, or about 2% per year. Fringe benefit cost increases comprise about two thirds of the total at $49.6 million. MPS assumes that its medical expenditures will return to their historic pattern and will grow at an annual rate of 7%, substantially greater than the projected rate of inflation.

The five-year forecast's revenue projections are its most striking feature, as budget officials estimate that total revenues in school operations will fall by $5 million over the period. The $5 million reduction results from a projection that revenues will rise slightly by about $3 million, but these incoming funds will be offset by an $8.5 million repayment of the property tax revenues temporarily transferred in 2017 to school operations from the construction fund.

The revenue projection assumes that the per-student revenue limit will remain flat over the next four years and that MPS will receive no other additional state funding, including increases in per-pupil aid. These are very conservative assumptions; as shown in **Chart 3**, from 2013 to 2016, a time of tight state funding, MPS' state revenues grew by $19.2 million.

Certainly, a key factor in MPS' five-year revenue projection is a continuation of student enrollment declines. Despite the district's effort to stem enrollment losses through substantial investments in its strategic plan and expansion of its most popular and successful school programs, its long-range projection is for a fall-off in enrollment of 1,802 students from 2016 to 2021 at MPS schools.

Finally, MPS is budgeting no annual carryover of savings in its five-year forecast beyond 2017. Budget officials report that they would prefer to eschew this practice since careful budgeting and expenditure of total revenues maximizes fiscal and operational effectiveness. It is important to note, however, that in the three years before 2016 – when MPS was not consciously trying to produce carryover savings – it averaged $24 million of such savings, which became a source of incoming revenue for the next fiscal year.

MPS' fiscal forecast is hardly good news. However, it represents a conservative estimate and likely reflects a determination to proceed cautiously and prepare for adverse fiscal conditions. This type of financial projection is difficult to make because several of the major forces driving MPS revenues, such as state aid, and some of its major expenditure pressures, such as medical costs, are beyond the district's control. In light of this uncertainty, the proposed budget notes that the district is "pursuing options and alternatives to stabilize enrollment and contain cost, which will help MPS avoid the projected deficits if the status quo is maintained."

Conclusion

In any given year, the nature of a government budget is shaped by its projection of incoming revenue. In a “good year,” revenue streams show sufficient elasticity to accommodate pressing needs and perhaps allow for salary increases, new positions, and/or new programs. On the other hand, when revenue is tight, these types of initiatives usually do not occur. Raises may be foregone, outgoing staff are not replaced, and aging equipment is declared good enough to last one more year.

For the second consecutive year, the Milwaukee Public Schools’ proposed budget appears to counter that orthodoxy. MPS will have little new money in 2017. The budget anticipates that revenues will be flat, as they generally have been for the last decade. Overall district revenues are off by $1.3 million, a decrease of 0.1% in a $1.2 billion budget.

A closer look does reveal two major changes within the overall revenue mix: an influx of $7.7 million in state per-pupil aid and a downward adjustment in combined equalization aids and property tax levy of $11.2 million. There are few other significant revenue adjustments.

Yet, if the status quo is the watchword on the revenue side of the budget, it does not characterize what is happening on the expenditure side. Here, MPS is poised to undertake a variety of initiatives and to continue with the execution of its strategic plan. Major activities in the proposed budget include $12 million for employee salary adjustments, 183 new positions, and implementation of Phase II of the Regional Development Plan, which is aimed at expanding instructional high-demand offerings such as language immersion schools, charter schools, and Montessori education.

In addition, the budget provides funds for the growth of numerous programs and services such as summer school, English as a Second Language, Advanced Placement and International Baccalaureate, after-school activities, freshman bridge programs, and free driver's education. It also proposes to reduce class size and the adult-to-student ratio by an unspecified amount.

As we have discussed, the proposed budget is able to fund these new activities through internal reallocation. Most notably, the budget transfers $8.5 million in property tax revenues from the construction fund to school operations and reduces the contribution to retirement liability reserves by $31.2 million, thereby freeing up an equivalent amount for new initiatives. It also applies $21 million from the Regional Development Plan, which is made available by the plan's transition to a less costly phase.

Unlike the 2016 budget, which applies 2015 savings to debt payments and preserves the displaced funds for carryover to future years, the 2017 proposed budget uses the $31.2 million reduction in the OPEB reserve contribution to expand expenditures by that full amount. That action – combined with a decision to transfer $8.5 million in property tax levy from the construction fund – produces a level of 2017 expenditures that is $39.7 million above continuing revenues.

Whether creating a 2018 budget hole of that magnitude is advisable is a difficult question to answer. Certainly, a decision to create a funding imbalance heading into 2018 would weaken the district's financial position and place stress on budgets in subsequent years. On the other hand, an expenditure budget that maintains the status quo would forsake needed investments and, arguably, provide little opportunity to reverse MPS' decade-long trend of enrollment losses, which is having a highly detrimental impact on its allowable revenue limit.

MPS' overall approach for 2017 appears both financially defensible and strategically sound. Expanding the most competitive programs and strengthening instructional operations and services might be MPS' best course of action to curb enrollment losses. If enrollments do not pick up to justify proposed investment, then the district has shown the ability to generate internal savings by various means.

Yet, at some point, repurposing internal funding and instituting cost efficiencies will become more difficult. Cost reallocation can produce both winners and losers, and some types of program savings may not prove popular or feasible to achieve.