DPS debt swells $18.7M, looks at cutting costs

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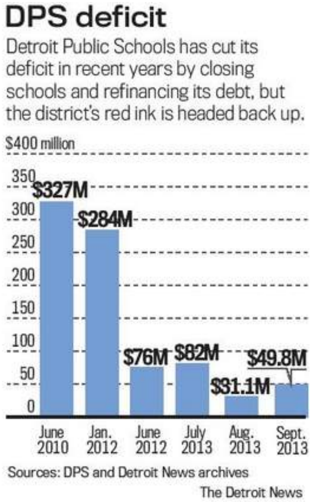

Detroit— The cash-strapped Detroit Public Schools racked up an additional $18.7 million in debt from July through September after its plan to boost enrollment failed, and it spent above budgeted amounts on security, transportation and maintenance.

In its first quarterly interim financial report filed Oct. 15 to state school and treasury officials, DPS Emergency Manager Jack Martin cited declining enrollment, high teacher costs and cash flow demands as factors contributing to the district's financial woes. DPS has been under state control since 2009, when its deficit reached $327 million.

While a series of refinancing efforts cut the district's deficit to $31.1 million in August, the red ink jumped to $49.8 million as of Sept. 30.

Financial experts said the quarterly report, the first of the 2013-14 fiscal year, is a danger sign for the state's largest school district.

"They kicked the can down the road," said Van Conway, CEO of Conway MacKenzie, a financial advisory firm working on the city of Detroit's restructuring. "Is that going to happen every quarter?"

The report covers the district's first fiscal quarter, when DPS experienced a $7.4 million revenue shortfall — mostly state funding — after its student count came in at 48,800, about 2,200 under its budgeted amount. The district also spent $10.5 million more than it had planned on certain expenditures and lost $743,448 in other funding.

Although the district reported an uptick in enrollment at some of its general admission high schools, overall enrollment is down and came in under budgeted targets set for this school year.

DPS has been battling enormous legacy deficits since 2009 after losing 100,000 students in a decade and millions of dollars in state aid.

In 2012, DPS officials refinanced $300 million of its short-term debt, leaving the district with $53 million in annual debt service obligations. In August, Martin borrowed $92 million — this time to cover cash-flow requirements — and saw the district's deficit drop from $82 million to $31 million.

But with the red ink growing since then, the district is preparing an amended budget and is planning to make unspecified spending cuts, according to the report, filed with state school superintendent Mike Flanagan and then-state Treasurer Andy Dillon.

"The amended budget will require the district to make significant expenditure reductions to keep the current fiscal year budget in balance and reduce the legacy deficit by approximately $4 million this fiscal year," Martin wrote in the report.

Martin took office on July 15, inheriting a budget approved by former emergency manager Roy Roberts.

Asked to detail what those cuts will be in a district that has closed nearly 200 buildings since 2000, DPS spokesman Steve Wasko said: “No decisions have been made.”

DPS officials spent $1.8 million on a new transportation plan this fall, hoping to attract more students and the state aid dollars that go with them. Four specialized bus routes go outside the city to collect new students — many of whom live in nearby suburbs — at 10 different stops.

Some of the increased expenditures came from costs to secure closed schools due to vandalism, updates to meet ADA requirements including an elevator replacement, and replacement of HVAC units vandalized at two schools, Wasko said.

State educations officials said they are working on an amended deficit elimination plan with DPS this week and expect it to be finalized soon. The state has ordered DPS to erase its debt within five years, but the latest plan has the district in the black by 2016, which is seven years after it filed its initial plan under then-emergency manager Robert Bobb.

“We are working with them to approve a new DEP and get it back down,” Martin Ackley, spokesman for the Michigan Department of Education, said of the deficit elimination plan. “They have been hemorrhaging kids by the thousands. We were more encouraged it wasn’t as dramatic (this fall) as it was in the past.”

The largest school district in the state, DPS had 300,000 students in the mid-1960s. After decades of steep enrollment drops, demographers told DPS as it prepared its 2013-14 budget in June to expect another enrollment drop of 5,000 students and to budget for 46,000 students.

Instead, the district announced it would attract 5,000 new students, for a total of 51,000, and approved a budget of $687 million.

Financial experts said that was DPS’s biggest mistake.

Conway said he struggled to understand DPS’ decision to budget an increase in students and revenues when the city is in decline. “You just added to the pile of debt,” he said. “You are building a bigger mountain to climb.”

James McTevia, who operates McTevia and Associates, a Bingham Farms-based financial turnaround company, said DPS’ decision to keep borrowing money to move its negative balances into later years on its financial sheet is the same solution the federal government keeps attempting.

“They’ve created a longer-term problem,” McTevia said. “You can’t solve financial problems by borrowing money.”

McTevia also questioned DPS’ rationale in expecting more students at a time when the city is in bankruptcy proceedings.

“This enrollment comes from students that are in a city that is in bankruptcy, how could you not expect enrollment to decline?” McTevia said. “They are unable or unwilling to do the tough things that have to be done: closing schools and firing teachers.”

DPS has told the state it will erase its deficit by 2016, the first step toward lifting the financial emergency under Public Act 436. Only Michigan’s governor has the authority to remove a local school district from receivership.