Amended Recovery Plan

Harrisburg School District

Dauphin County Pennsylvania

Prepared by the

Chief Recovery Officer

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With the Assistance of

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Harrisburg School District
Amended Act 141 Recovery Plan
January 21, 2014

An Act 141 Recovery Plan for the Harrisburg School District (District) was presented to the Harrisburg School Board on April 26, 2013. The plan was approved by the School Board on May 17, 2013 and by the Commonwealth's Department of Education on May 31, 2013. The School Board, the Chief Recovery Officer (CRO) and the District administration have operated under the provisions of the plan since its adoption.

In the period since May 2013, there have been a number of changes in financial circumstances facing the District and several of the requirements of the Act 141 Recovery Plan have been clarified. The purpose of this document is twofold:

1. To revise certain initiatives of the Recovery Plan to address the current financial circumstances and projections of the District.
2. To provide clarifying language for aspects of the Recovery Plan.

Unless changed or amended by this document, all other aspects of the Act 141 Recovery Plan as presented on April 26, 2013 and approved by the Harrisburg School Board and the Department of Education in May 2013 remain in effect.

<u>Amended Plan Initiatives</u>

Subsequent to the development and approval of the Recovery Plan, it was concluded that the District achieved better financial results in the 2012-13 year than forecast in the Plan. These financial results were confirmed by the 2012-13 audit, which was received in late December 2013 and approved by the School Board in January 2014. In addition, the CRO and his consultants, Public Financial Management (PFM), have worked with the District's CFO to review the District's 2013-14 budget. Based on 2012-13 financial results and information on 2013-14 year-to-date revenues and expenses, they have concluded that the estimated actual revenues and expenses for 2013-14 should be revised from the adopted budget.

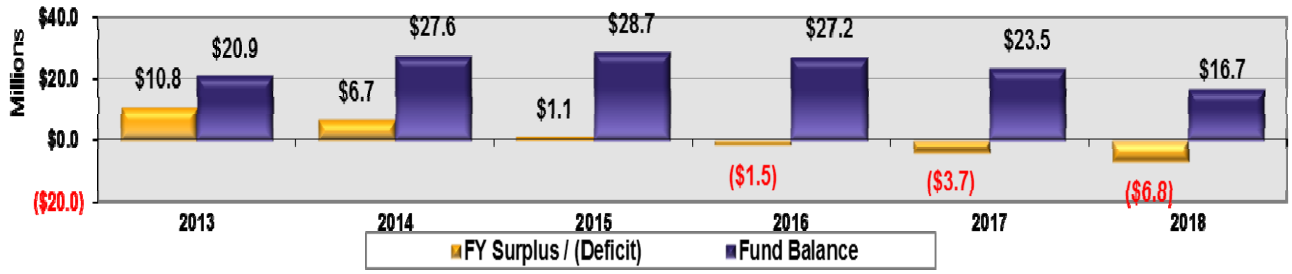
PFM has developed a new baseline forecast, intended to indicate the District's financial position if current trends and policies are maintained. The new baseline forecast uses the revised 2012-13 and 2013-14 information and the following assumptions:

- Charter school enrollment for the District will continue to grow by 13.7% annually from the 2013-14 school year to the 2017-18 school year.
- The 5% salary reduction for District staff that was implemented in July 2013 will remain in place, but the Recovery Plan's initiative to achieve an additional 5% salary reduction for July 2014 will be eliminated. The baseline forecast assumes salaries for all staff will be frozen at the 2013-14 level.
- There will be no District tax increases for the period 2014-15 to 2017-18.

- The District will not take the Act 141 Transitional Loan as proposed in the Recovery Plan.

Chart 1 below shows the revised baseline forecast based on these assumptions. The yellow or light gray bar on the left shows the positive or negative operating result for each year and the blue or dark gray bar on the right show the cumulative fund balance based on the annual operating results. The forecast fund balance excludes any portion of the fund balance that is not available for expenditure.

Chart 1
Baseline Forecast 2012-13 to 2017-18
Harrisburg School District



Act 141 requires the CRO to submit a Recovery Plan that attains long term fiscal stability for the District while improving academic performance. This Amended Plan is intended to meet this requirement while addressing interests of the District's students, taxpayers, employers and the staff and administration of the District.

As can be seen in Chart 1 above, the baseline forecast does not meet the financial stability requirements of Act 141 even given higher-than-expected reserves. Although the District has a fund balance in each of the projection years, the baseline forecast also shows declining performance each year and a worsening structural operating deficit in the years 2016 to 2018. The gap is caused by growing expenditures for such items as benefits and charter schools, while revenue sources are flat or growing only slightly.

As a result, the Board, the Administration and staff of the District must continue to take actions to attain and maintain financial stability. If the District successfully implements a number of cost saving and revenue enhancement initiatives, finances can improve and there will also be resources to provide for some academic program enhancements and address the pay cut implemented in July 2013. If the initiatives are not implemented, however, the enhancements are not affordable.

Recognizing that longer term forecasts are subject to change based on District actions and external factors, the Amended Plan provides a process for achieving enhancements if there are sufficient financial resources. The Amended Plan proposes a “shared savings” approach to future positive financial results.

Amended Act 141 Financial Recovery Plan and Initiatives

The key elements of this Amended Act 141 Recovery Plan for Harrisburg are as follows:

- Improve financial performance compared to the baseline, reversing the trend of growing annual shortfalls.
- Fund academic enhancements that will help the District’s academic performance and increase its ability to compete with charter schools for students.
- Focus the entire District on improving its performance so that it can retain and attract students in relation to charter school competition.
- Avoid increasing the tax burden on Harrisburg taxpayers.
- Restore salary cuts incurred by Harrisburg District staff to the degree such restoration is consistent with the requirement for long term fiscal stability.
- Provide a mechanism for revising the financial initiatives of the Plan based on changes in the financial conditions of the District.

The Amended Plan outlines a series of near term actions and provides for a “shared savings" approach in the longer term should the financial results of the District’s operation be better than the forecast.

Specific Initiatives of the Amended Act 141 Plan

The following are the specific initiatives of the Amended Recovery Plan, the year of expected implementation of the initiative and the anticipated financial impact.

Initiative: Restore Full Day Kindergarten (increased expenditure)

This initiative would fund an additional 15 teachers and related costs to expand kindergarten to the full school day for all students beginning in the 2014-15 school year.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact	$0	$1,125,000	$1,125,000	$1,125,000	$1,125,000	**$4,500,000**

Initiative: Increase Staff Salaries by 2.5% in 2013-14 and Freeze Thereafter (increased expenditure)

This initiative will restore 2.5% of the 5.0% salary reduction that District employees incurred at the beginning of 2012-13. The restoration of the 2.5% can be accomplished over the remainder of the 2013-14 fiscal year in a manner that is administratively efficient.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact	$977,068	$977,068	$977,068	$977,068	$977,068	**$4,885,340**

Initiative: Cap District Health Insurance Cost Increase at 5% Beginning in 2016-17 (reduced expenditure)

See initiative WF02 of the Recovery Plan for details. This initiative is intended to reduce the District's cost of employee health insurance. As outlined in initiative WF02 of the Recovery Plan, the growth in the District's cost of health care would be capped at 5% with employees absorbing any additional cost. If the health care plan is adjusted or the District's health care cost experience is such that health care costs grow at 5% or less, the District will continue to assume this cost.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact				($742,644)	($1,604,369)	**($2,347,012)**

Initiative: Reduce Health Insurance Opt-Out to Save $130,000 Annually Beginning in 2016-17 (reduced expenditure)

As described in the Recovery Plan, the District currently pays a bonus to employees who opt out of the District's health care plan. At present, the opt-out bonus is exorbitant and outside the norm for districts in the Harrisburg region. This initiative requires the renegotiation of the opt-out provision to cut the District's cost by 50%.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact				($130,000)	($130,000)	**($260,000)**

Initiative: Improve District Education and Limit Growth in Charter School Enrollment (net reduced expenditure)

Harrisburg School District faces a challenging competitive environment with local charter schools. The Recovery Plan focused on competition from cyber charter schools, but recently brick-and-mortar charter schools have emerged with faster enrollment growth. It is vital that the entire Harrisburg school community focus on improving its academic performance and present itself in a manner that will retain students in the face of the alternatives offered by charter schools. This initiative sets target growth rates for charter school enrollment and shows the financial impact of achieving the growth target versus the base case assumption of 13.7% per year charter school enrollment growth. The effect is a lower payment to charter schools and increased District direct education spending compared to the baseline, for a net reduced expenditure each year.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Growth Target		11%	8%	5%	3%	
Financial Impact		($127,215)	($779,796)	($1,729,655)	($3,270,043)	**($5,906,709)**

Initiative: Increase Property Tax to Act 1 Index Beginning in 2016-17 (increased revenue)

This initiative calls for the School Board to raise District real estate tax millage to the Act 1 index limit in the 2016-17 and 2017-18 fiscal years. The Act 1 index shown below is an estimate. If the actual Act 1 index is lower than shown below, the District shall apply for exceptions to allow the District to increase millage rate by the amount shown.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Percentage Increase in Tax Rate				3.5%	3.75%	
Financial Impact				$898,415	$2,055,470	**$2,953,885**

Initiative: Eliminate Food Service Fund Transfer from the General Fund (reduced expenditure)

See the Food Service Chapter of Recovery Plan for details.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact		($100,000)	($200,000)	($300,000)	($300,000)	**($900,000)**

Initiative: Increase Delinquent Real Estate, Earned Income and Occupation Tax Collection (revenue increase)

See initiatives RV01 and RV02 of Recovery Plan for details.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact		$250,000	$500,000	$550,000	$550,000	**$1,850,000**

Initiative: Optimize ACCESS Utilization (revenue increase)

See initiative RV06 of Recovery Plan for details.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact			$250,000	$300,000	$350,000	**$900,000**

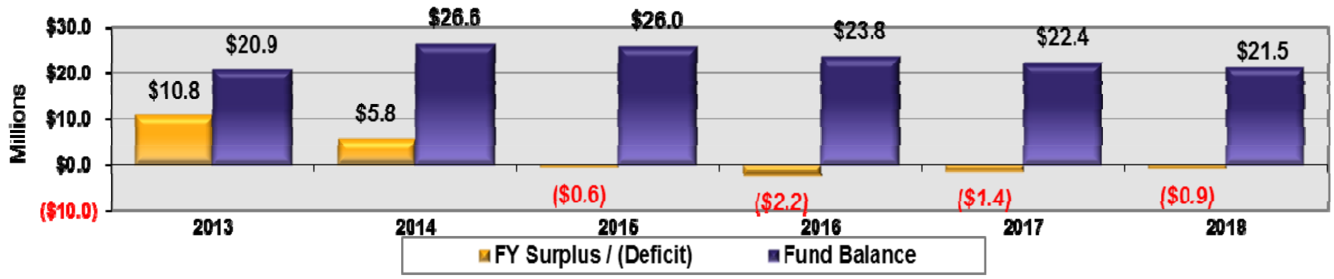
Initiative: Increase Energy Efficiency of District through Reduced Energy Consumption and Increased Building Efficiency (decreased expenditure)

See FA04, FA05, FA06 and FA07 of Recovery Plan for details.

Year	2013-14	2014-15	2015-16	2016-17	2017-18	**Total**
Financial Impact			($35,000)	($282,000)	($289,000)	**($606,000)**

Based upon the expected financial impact of the above initiatives, it is projected that the District's financial performance will be as shown in Chart 2 below. In contrast to the baseline forecast, which had declining annual results with negative operating balances for 2015-16 and subsequent years, this projection shows a near-balance position in all years and an improving annual operating trend after 2014-15. The forecast indicates a trend toward long-term fiscal stability as required by Act 141 and also retains adequate reserves to allow the District to operate without dramatic swings in operation from year to year.

Chart 2
Forecast with Initiatives 2012-13 to 2017-18
Harrisburg School District



Adapting to Changing Financial Results

As presented above, the Amended Act 141 Recovery Plan for the Harrisburg School District accomplishes a number of long term goals for the District while moving toward the long-term fiscal stability required by Act 141. However, there are also a number of other goals put forward by various District constituencies – including immediate full restoration of the 2013 salary reduction and elimination of all future tax increases – that have not been included in the Amended Plan. In the view of the CRO and his consultants, these other goals are not achievable within the currently forecast finances of the District.

It is also understood that the long term forecasts can be changed by District actions and outside forces, resulting in actual financial performance that is better or worse than expected. The CRO, the Board, the Harrisburg community and District administration and staff must be prepared for periodic reassessments of the Plan based on these changes in circumstances. Viewed optimistically, it may be the case that not all the expenditure reductions or revenue increases outlined above will need to take place and as a result additional District goals can be achieved. Recognizing this circumstance, the Amended Act 141 Recovery Plan includes a shared savings approach for managing variances in District financial performance from the Amended Plan.

Shared Savings Approach Defined

To the extent that the District improves academic performance and has better financial results than projected, there will be opportunities to fund programs or activities related to educational enrichment, and to also address employee salary and benefit issues and tax initiatives of the Amended Recovery Plan. As additional dollars are available, it is the intention of this Amended Plan to allocate a portion of these dollars for enhancements as follows:

- Supporting curriculum, training and technology investments
- Eliminating tax increases otherwise required in 2016-17 and 2017-18
- Restoring remaining portion of the 2013 salary cut and increasing employee salaries (which are otherwise frozen)
- Eliminating or moderating changes to employee health care provisions

Alternatively, if the District fails to meet its academic and financial goals, no dollars will be available for enhancements. Instead, further cost control efforts will have to be implemented as deemed necessary by the CRO, and this Amended Plan will be revised accordingly.

In order to share savings if results are better than anticipated in this Amended Recovery Plan, the District will assess its financial situation within 30 days of completion of the annual audit of the School District as required by 24 PS 24-2401. If the District has a positive fund balance, and if there is a positive annual operating result (revenues less expenditures for the year are positive), a sum up to the amount of the positive annual operating result may be allocated in the following manner.

Positive Financial Result

Objective	2014-15	2015-16	2016-17	2017-18
Support curriculum, training and technology investments or fund balance	50% (or more if full 50% is not needed for salary restoration)	50% (or more if full 50% is not needed for salary increase)	If tax and benefit goals are met, and funds remain, half may be used for these purposes	If tax and benefit goals are met, and funds remain, half may be used for these purposes
Eliminate tax increases*	Not Applicable	Not Applicable	Up to 50% of any available positive operating result	Up to 50% of any available positive operating result

Objective	2014-15	2015-16	2016-17	2017-18
Restoring the 2013-14 reductions in employee salaries and benefits and provide for future increases	Up to 50% of any available positive operating result may be used to restore the remaining 2.5% salary reduction from 2013-14	Up to 50% of any available positive operating result may be used for a salary increase of up to 2.5% over 2014-15 baseline salaries	If tax and benefit goals are met, and funds remain, half may be used for a salary increase of up to 2.5% if Plan academic goals are also met	If tax and benefit goals are met, and funds remain, half may be used for a salary increase of up to 2.5% if Plan academic goals are also met
Moderating employee health care changes (capping District health care growth at 5% and reducing size of opt-out benefit by ½)	Not Applicable	Not Applicable	Up to 50% of any available positive operating result may be used to moderate or eliminate the required 5% cap on District spending for employee health care and/or eliminate or moderate the reduction in the opt-out benefit	Up to 50% of any available positive operating result may be used to moderate or eliminate the required 5% cap on District spending for employee health care and/or eliminate or moderate the reduction in the opt-out benefit

*Note that the final determination of whether shared savings are available to abate the 2016-17 tax increase will be made in June 2016 after receipt of the 2014-15 audit and with the knowledge of the likely results for 2015-16. Therefore, the District may need to approve an increase in its preliminary budget proceedings to maintain its options as it moves through the budget process. A similar process will be necessary to abate the 2017-18 tax increase otherwise required in the Plan.

**Note that final audited results for each year will not be available until mid-year, so changes to pay and benefit provisions will be approved by the Board in January and retroactive to the previous July 1.

For example, if there is a positive net operating result in 2014-15, that amount would be allocated as follows: up to 50% toward restoring the remaining 2.5% salary and wage reduction imposed in 2013-14, with the remainder allocated for curriculum, training and technology. If the figure is large enough that a full 50% is not needed to restore the wage cut, more could be spent on District programs or retained in fund balance.

As another example, if there is a positive net operating result in 2016-17, that amount would be allocated as follows: up to 50% toward eliminating the tax increase included in the Plan, and 50% to funding for health care cost increases so that employees would not have to raise their health care contribution or reduce the opt out amount as required by the Plan. If 100% of the amount is not needed to achieve these goals, the remaining balance could go equally to salary increases of up to 2.5% and to District programs.

Notwithstanding any other provisions of this Plan, no portion of positive annual financial results shall be allocated to objectives other than increasing fund balance if they would cause the District's fund balance to be negative or the overall fund balance to drop below 5.0% of annual revenues. So that the District's annual financial performance is not overstated, the calculation of a positive annual operating result shall also exclude any revenue from an unfunded debt loan, Commonwealth Transitional Loan under Act 141, or other borrowing that the District uses to eliminate accumulated deficits. Note that for certain shared savings, the District must also meet its academic performance goals under the Plan.

Negative Financial Result

As noted above, if the District reports or projects to report a negative annual operating result (annual expenditures exceed annual revenues), no shared savings expenditures may be made. Moreover, the District is required under the Plan to take action to eliminate the deficit, considering all options including tax increases, other revenue enhancements, and expenditure cuts including salary and benefit reductions. This situation may also require the CRO to modify the Amended Recovery Plan.

<u>Other Provisions of Recovery Plan Dated April 26, 2013</u>

In addition to the above amendments and additions to the Harrisburg School District Act 141 Recovery Plan Dated April 26, 2013, the following amendments are made:

1. In regard to the Education Chapter of the April 26, 2013 plan, it is the explicit intent of the Recovery Plan that the District shall be accountable for attaining the minimum performance improvement benchmarks by year that are outlined on pages 32 and 33 of the Recovery Plan.

2. The April 26, 2013 Recovery Plan defined the new position of CEO and outlined duties and responsibilities for that position as well as the reporting relationship of the CEO to the Harrisburg School Board. The Plan is amended to substitute the title CFO (Chief Financial Officer) for any reference to CEO or COO (Chief Operating Officer). However, there are no changes to the plan in regard to the reporting relationships, responsibilities of the position or span of control of the CFO as discussed on pages 41 and 42 of the original plan. Based on recent academic results, including the School Performance Profiles released in December 2013, there is a specific concern that the Superintendent of Schools still does not have sufficient time to spend on the academic improvement required by the plan and therefore the original intent of the Recovery Plan to have a CFO to focus on finance and operation and a Superintendent of Schools to focus on academics is to be implemented with fidelity. A critical part of the entire Recovery Plan is the fact that both the Superintendent of Schools and the CFO report directly to the School Board in the operation of the District and in the implementation of the Recovery Plan.

All other provisions of the plan in so far as they are not in conflict with the initiatives outlined above remain in place and are part of Amended Recovery Plan of the Harrisburg School District.