

Public Budget Workshops for the 2005-06 Budget:

Session 1:

***Background for
Understanding the
School District Budget***

Session Schedule:

CHS Library

January 12, 2005

7:00 PM

CHS Library

January 19, 2005

7:00 PM

Presented by the Board of Education Finance & Facilities Committee

Overview of budget workshops

Tonight:

- Introduction: the challenges we face
- Board-adopted budget goals and priorities for the 2005-06 budget
- Overview of this year's school district budget process
- School district accounting; uses and limitations of district financial statements
- Constraints on budget decision-making

Wednesday, January 19

- *Where we've been*: a review of historical and near-term trends
- *Where we are*: a more detailed look at the composition of the budget
- *Where we're going*: a recap of the three-year budget projections

Disclaimer

- This presentation was prepared by the Finance and Facilities Committee of the South Orange-Maplewood Board of Education,
- The contents of this presentation are the responsibility of the Finance and Facilities Committee. More particularly, any specific views expressed herein are not necessarily the views of the entire Board or the Committee, but should be attributed to Mr. Latz, the primary author of this presentation. No one should impute any view contained herein to other members of the Committee or the Board of Education as a whole.\

Background material available on the SOMSD district website

- 4 major Budget 101 workshops presented from July through December of 2003
- Several hundred pages of analysis and descriptive material produced from 11/03 to 4/04 as part of the 2004-05 budget process.
- All of that material is on the district's website:
 - Budget 101: <http://www.somsd.k12.nj.us/finance/budget101home.htm>
 - 2004-05 budget: <http://www.somsd.k12.nj.us/finance/financehome.htm>

The Challenges We Face

The Challenges We Face

- Budgeting for the 2005-06 school year promises to be even more difficult than the last several years because we're faced with challenges which threaten to undermine the vitality and viability of our school district.
- We face a major new constraint in the form of last June's S-1701 legislation, which puts stringent new restrictions on the rate of increase for N.J. school budgets
- A projected maintenance budget -- which would preserve all current programs and services -- would cost \$2-4 million more than we are allowed to spend by the State of New Jersey
- In these circumstances, despite our best efforts, some cuts in programs and services are highly likely.

How Did We Get Here?

- SOMSD mirrors national and state trends:
 - spending per student has quadrupled in real terms since 1950
 - our spending per student remains at or near the NJ state average
 - our rate of expenditure increase is less than comparable NJ districts
 - overall school budget increases continue to be driven by double-digit increases in the largest segments of the budget: healthcare, commercial insurance, energy and special education out-of-district tuitions
 - annual salary increases for the last seven years average 5%
- Due to anomalies in the state's wealth-sensitive aid formula, our district bears over 90% of the burden from local property taxes. Approx. 58% of local taxes go to the schools.
- South Orange-Maplewood has a narrow property tax base; with relatively little commercial property and significant areas of land that are tax-exempt. Our equalized property tax rates are already among the highest in the state.
- Despite significant belt-tightening in each of the last three years, costs of major components of our budget have risen sharply. Local taxpayers have had to dig deep to help maintain the quality of our school system.

South Orange-Maplewood is not alone in feeling the “tax stress”

- In June 2004, the Governor proposed -- and the legislature hurriedly passed – a package of measures in response to New Jersey’s property tax crisis:
 - establishment of a Tax Reform Task Force to study the question of a constitutional convention on property taxes
 - the “millionaire’s” tax
 - S-1701, which implements stringent budget caps on school districts and municipalities
- S-1701:
 - caps school budget increases at 2.5% or the rate of inflation, whichever is greater (this year approx. 3.01%);
 - “SGLA” adjustments are fewer and Separate Proposals are effectively precluded

Why is this year's budget climate so different?

- In prior years, we have:
 - struggled for efficiencies and cost containment
 - sought to demonstrate to the community that tax dollars are spent well and efficiently to support a high-quality school system
 - succeeded – most of the time – in demonstrating to the Board of School Estimate (and the community) that it was important to dig deep to support the schools, with tax increases of 4.65% in 2001-02, 8.90% in 2002-03 and 6.78% in 2003-04.
- S-1701 precludes us from raising more than the state-imposed 3% CAP, even if the Board of School Estimate were willing to do so.
- Our costs continue to rise at higher rates. The result: cuts that may impair our ability to deliver the quality education required by N.J.'s core standards.

*Budget Goals and Priorities
and Overview of this Year's
School District
Budget Process
(for the 2005-06 budget)*

Board-Adopted Budget Goals and Priorities

Goals: Subject to the constraints and requirements in S1701 as outlined in Board Resolution 1913, the Board of Education remains committed to goals outlined below:

- Provide educational programs and services that enable all students to succeed.
- Manage systemic changes that will increase the efficiency and cost effectiveness of operations.
- Continue maintenance and capital improvement efforts according to our long-term plan while managing debt service to minimize tax impact.
- Remain competitive with comparable public and private schools.
- Achieve a common understanding between the community, the board and the administration regarding the administration's budget recommendation and the rationale supporting it.

Board-Adopted Budget Goals and Priorities (cont.)

Priorities: Subject to the constraints imposed by S1701, we endorse these priorities in our attempt to preserve and maintain our educational program.

- Increase achievement for all students in language arts literacy and mathematics.
- Improve the effectiveness of academic interventions for student subgroups that do not meet, or are at risk of not meeting, the *No Child Left Behind Adequate Yearly Progress* as determined by the New Jersey Department of Education.
- Provide professional development, which focuses on increasing student learning so that all subgroups in all schools meet the *No Child Left Behind Adequate Yearly Progress* as determined by the New Jersey Department of Education
- Preserve the elective offerings at Columbia High School to meet the scheduling needs of a growing enrollment and increase student access to high-level courses.
- Utilize technology as an effective tool to enhance teaching and learning and maximize efficiency of administrative services.
- Provide a learning environment which is clean, safe and secure, and which will best support the delivery of the district's educational program.
- Continue to provide programs and services that support the goal of maintaining integrated schools.
- Strive for class sizes that best support the developmental and educational needs of students.

Budget Activities To Date

7/1/04	Administration began planning for the 2005-06 budget
11/15/04	•Board formally received and accepted Consolidated Annual Financial Report for 2003-04 (“CAFR” or the “audit”) •Administration presented Three-Year Budget Projections to the Board, together with supporting enrollment data
11/19/04	Three-Year Projections presented to So. Orange and Mplwd municipal officials at monthly Liaison Committee meeting
11/15/04 discussion 12/6/04 adoption	Board approved Finance Committee’s proposed list of budget analysis topics
12/20/04 discussion 1/3/05 disc/adopted	Board discussion and adoption of budget goals/priorities

Anticipated Budget Calendar

Jan. 12, 19, 2005	Background budget workshops presented by Finance Committee
1/24/05	Presentation of Superintendent’s preliminary draft budget to BOE
1/26/05 (tentative)	Budget workshop

Anticipated Budget Calendar (continued)

month of Feb.	Administration and Board solicit community input
2/7/05	BOE discussion of budget
2/23/05	BOE budget workshop
2/28/05	BOE adoption of preliminary budget to be sent to County Supt.
3/1/05	Preliminary Budget due to County Supt.
3/7/05	BOE receipt of budget back from the County Superintendent and approval of budget to be submitted to Board of School Estimate
3/9/05	BSE workshop conducted by BOE to establish understanding of district's proposed 2004-05 budget
3/10/05	Board-approved budget is advertised
3/16/05	BSE Public Hearing and action to levy 2005-06 school tax
3/21/05	BOE adoption of 2004-05 Budget as approved by Board of School Estimate

*Key Concepts of
School District
Accounting and Cost Analysis*

Financial reporting makes use of two basic types of statements

- The *balance sheet* reflects what an organization owns and controls, what it owes and what it owns free and clear *at some point in time*, typically the start or the end of a defined accounting period
- The *income statement* or *statement of activities* – A/K/A the *statement of revenues, expenditures and changes in fund balance* -- which describes a summary of revenues and expenditures over some period of time, typically one accounting period
- See the 7/23/03 Budget 101 presentation for a tutorial on these topics at:
<http://www.somds.k12.nj.us/finance/budget101home/budget101-072303.pdf>

It's Important To Understand Both The Extent and Limits of Current Financial Information

- N.J. school districts keep their books and records, and present their budgets, in strict accordance with state regulations, which in turn adhere to national standards (Generally Accepted Accounting Procedures, “**GAAP**”).
- **Accounting Funds** are used to segregate major activities (debt service, current operating expense, capital projects and proprietary activities are separated)
- Budgets are prepared in **line-item fashion**, according to a **Chart of Accounts** which is specified by the N.J. Department of Education
- The public budget is detailed. The Chart of Accounts categorizes expenditure by Fund/Program/Function/Object. **It is possible to see**, for example, that salaries and benefits represent 80% of expenditure, or that Special Education expenditures (including salaries), represent nearly 20% of the budget
- Line-item budgets help accountants track and summarize all financial events. They enable comparability from one year to the next and from one district to another (except that the Dept. of Ed. keeps changing the Chart of Accounts!)

In our district, we have found it necessary to augment the traditional line-item budget presentation

- A traditional line-item budget has limitations. Members of the public cannot:
 - determine how many people a given salary line represents, what their actual salaries are or how they're deployed
 - explain from a line-item itself the source of a variance in that line-item nor discern the main drivers of an increase from one year to the next
 - tell how much money goes to which specific services delivered to which specific students
- Using publicly-available information, it is possible to infer or compute answers to these questions but few have the time or expertise to do so
- For these reasons, we annotate our line-item budget and augment it with a variety of analyses and descriptive materials and publish them on the web.

Traditional Line-Item Budgets Are Not Especially Helpful To Policymakers Grappling With Budget Trade-offs

- Some experts characterize line-item budgets as creating an instructional blob – it's impossible to tell which resources are included on which line and it's also difficult to tell whether increases or decreases represent changes in the quantity of resources allocated or changes in the price of those resources
- Simpler presentations of the financial data in forms other than the official financial statements can be helpful in understanding where the money goes (what people and material resources are involved) and why certain costs go up (disentangling changes in the price of resources from changes in quantity)
- Such simpler presentations must be verifiable and must therefore *reconcile* to the financial statements. They must also be done using a consistent set of *cost concepts* according to a clear set of rules.

When Considering a Budget Decision, It's Important to Use the Relevant Cost Concept

- ***Total Cost vs. Net Cost:*** Elimination of a program/service does not always result in saving the total cost of that service. One must look at net costs when making specific budget decisions. A change in service delivery may trigger some new expense. Net costs take into account all factors.
- ***Marginal Cost:*** The cost of adding or removing the last unit of a program is usually smaller than the average unit cost of one unit of the program.
- ***Actual Cost vs. Average Cost*** When considering the cost of employees, especially, one must be clear which cost concept is relevant. The actual cost of a specific employee is of course different than the average cost for all employees, or even the average for all employees in a particular category.
- ***Allocated Cost.*** Some costs are *direct* and visible, others are *indirect* and are posted in a different part of the budget. When considering the cost of a resource, one must ***allocate the indirect costs*** in a way that allows one to understand the ***Total Cost*** of the resource. Employee benefits are one example. According to the Chart of Accounts, they are posted to the Business Office section of the budget, but need to be considered in cost analyses that consider the relative costs of program alternatives.

Examples of cost analyses done annually or periodically in the district in previous years

- All-in annual cost per seat to support computer workstations (1999)
- Cost per student mile of alternative bus routing/scheduling approaches (2001-02 budget planning)
- Cost for district-run routes versus contracted routes (2001-02 and 2003-04)
- Comparative program costs per pupil
- Level of scheduling efficiency in use of secondary staff
- 5-year energy audit by Mark Smith (April 1999)
- Insurance risk management
- Elementary school class size analysis/alternatives to pullout model (2003-04)
- Custodial Services (2003-04)
- Efficiency of Administrative Staffing (2003-04)
- Special Education Services (2003-04)

See: <http://www.somsd.k12.nj.us/finance/0405budgetlinks.htm>

This year's list of budget analysis topics, adopted by Board on 12/6/04:

For each of the topics listed below, explore the possibilities for budget savings, while describing the impact on the quantity and quality of services to be delivered in each alternative considered.

- Explore potential savings and other impacts from changes in scheduling and class size.
- Examine additional savings to be realized from the expansion of custodial outsourcing.
- Examine the potential for additional administrative efficiencies and savings from the reduction of administrative headcount.
- Explore alternative approaches to the delivery of secretarial services.
- Explore alternative approaches to the delivery of student services provided by non-certified personnel, including special education aides, technology aides and other instructional aides, as well as lunchroom aides.
- Explore potential savings to be realized from the possible creation of additional special education programs in-district.
- Present a range of options for savings in transportation.
- Identify actual costs related to community use of the schools.
- Provide an analysis of technology spending that builds on last year's report and explores additional options for savings.
- Provide an analysis of all stipends and explore ways to reduce them, together with an analysis of the full costs of co-curricular and extra-curricular activities, including transportation, insurance, supplies, etc.

*Understanding the
Constraints on Budget
Decision-Making*

Key Constraints

BOE Policy

**Federal
and
State
Mandates**

**N.J. State Imposed
Spending Cap**

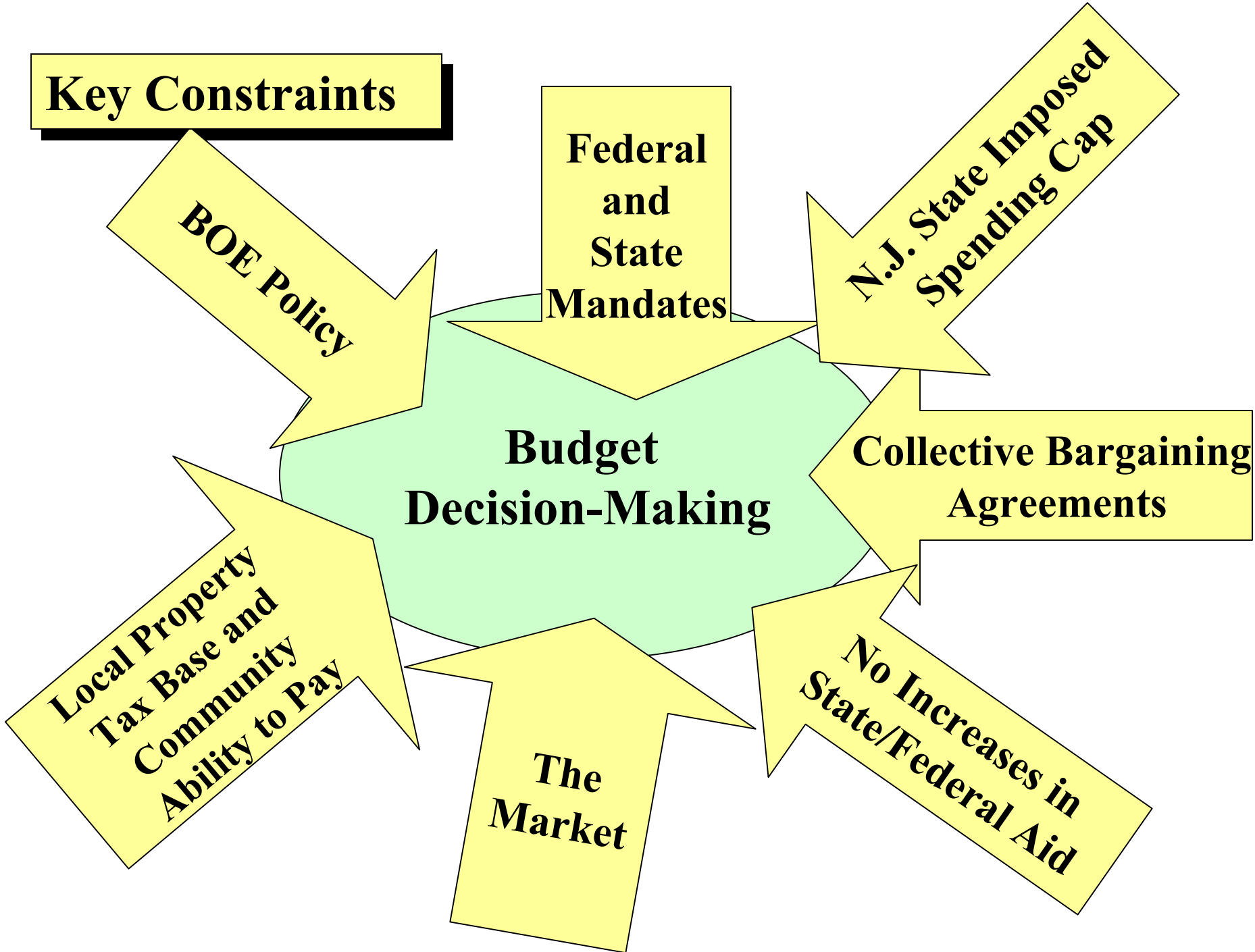
**Budget
Decision-Making**

**Collective Bargaining
Agreements**

**Local Property
Tax Base and
Community
Ability to Pay**

**The
Market**

**No Increases in
State/Federal Aid**



Constraints on the Revenue Side of the Budget Include A Narrow Property Tax Base . . .

- Local property tax base consists predominantly of residential property
– property wealth per pupil is at state average

Municipality	Percentage of total tax base contributed by top taxpayer (2001)	Percentage of total tax base contributed by top ten taxpayers (2001)
Montclair	.41%	2.06%
South Orange	.6%	3.7%
Maplewood	1.81%	3.86%
West Orange	1.41%	8.02%
Livingston (2002)	5.01%	10.8%
Millburn	8.41%	14.01%

Source: School District Consolidated Annual Financial Reports for year ended 6/30/02

Leading to Fiscal Stress . . .

- Our towns suffer increasingly from “fiscal stress” – equalized property tax rates that are among the highest in New Jersey.

Year 2000 equalized tax rates were:

	Equalized School Tax Rate	Rank in New Jersey (1 = highest)	Equalized Combined Tax Rate	Rank in New Jersey (1 = highest)
Maplewood	\$1.93	27th	\$3.17	56th
South Orange	\$1.92	28th	\$3.46	23rd
Montclair	\$1.78	74th	\$3.25	42nd
West Orange	\$1.74	93rd	\$3.14	62nd
Livingston	\$1.37	336th	\$2.42	247th
Millburn	\$0.74	526th	\$1.76	493rd

Source: Rutgers 2001 Legislative Data Book

... While State and Federal Aid Continues to Decline as a Proportion of Total Revenue

- State and Federal aid remains relatively frozen in dollar terms year after year (since 1987):
 - 1987-88: \$4.9 million
 - 2004-05: \$5.523 million
- Aid dollars offset only a portion of the mandated special needs for which they're intended
- Aid revenue represents an increasingly small proportion of total revenue

The state-defined *Maximum Net Permitted T&E Amount* (the “Cap”) imposes a revenue-raising limit.

- Total budget revenue for the General Fund and Special Revenue Fund from all sources is limited to the *Maximum Net Permitted T&E* amount, which is calculated as:
 - the prior year’s budget,
 - plus a 3% increase for inflation (the *Statutory Growth Limitation*),
 - plus possible additional adjustments (*Statutory Growth Limitation Adjustments*, or “SGLAs”), to allow for increases in enrollment, transportation cost and extraordinary special education costs
- Debt service is not included in the Max. Net T&E limit. A separate vote by the Board of Education and the Board of School Estimate is necessary each year. Our debt service is carefully managed to remain at \$3 million annually.

“We Can’t Spend the Money Even If We Wanted To”

- The state does not dictate that our school district raise revenue to fund a Maximum Net T&E budget; nor does it provide any extra money to do so. The Maximum Net T&E amount simply authorizes us to raise that much revenue if we choose
- In past years, a school district could raise additional revenue through a separately-approved *Separate Proposal*, which represents an amount over and above Maximum Net T&E, and requires a separate vote for approval (from both the Board of Education and the Board of School Estimate)
- S-1701 threatens significant restrictions on SGLAs and precludes most Separate Proposals

Constraints on Budget Expenditure Decisions Can Be Divided into Four Major Categories

- *State and Federal education mandates*
- *Collective bargaining agreements* that define salary, benefits, work hours and teaching workloads are negotiated by the Board with ASCA (administrators) and SOMEA (teachers and support staff)
- The “*market*”, which -- within a narrow range -- determines the *price for human and material resources* used by the school district, and the *level of programs and services* necessary to remain competitive as a community, as well as the tax burden the community is willing to bear
- *Board of Education policy*, and other decisions, reflecting educational judgment and community desires. Board policy imposes “soft” constraints –modifiable by board action

State and Federal Law Prescribe Many Requirements Precisely

- N.J. minimum of 180 days of instruction per year
- N.J. minimum of 240 instructional minutes that students must receive each day: “A school day shall consist of not less than 4 hours of actual school work, except that in an approved kindergarten one continuous session of 2.5 hours may be considered as a full day.” (N.J.A.C. 6:3-9:3)
- N.J. minimum of 110 high school credits required to graduate, 100 of which are in mandated subjects.

More State and Federal Requirements . . .

- Federal Individuals with Disabilities Education Act (“IDEA”) establishes standards for a Free and Appropriate Public Education (“FAPE”) for students with disabilities (similar to other districts, Special Education now accounts for approx. 20% of our budget)
- “Accommodations”, including barrier-free access, for students and employees with disabilities, regardless of whether they’re classified
- Services for students with Limited English Proficiency
- Aid in Lieu of Transportation for private-school students (\$751 per student in 2003-04, for a total of approximately \$500,000 per year)
- Stringent facilities codes

State and Federal Mandates Extend to Many Aspects of Employment, Particularly Collective Bargaining Agreements

- Tenure laws, see N.J.S.A. 18A:28
- N.J. Employer-Employee Relations Act of 1968, as amended, specifies the framework within which collective bargaining with public employees must occur, including specification of which terms and conditions of employment are subject to collective bargaining
- Level of local contributions to TPAF (certificated) and PERS (non-certificated) pension funds
- Federal Fair Labor Standards Act
- Federal FMLA (family leave act)

Other State/Federal Requirements

- In the past, success in meeting N.J. Core Curriculum Content Standards was measured principally through tests given at grades 4, 8 and 11 (the ESPA, GEPA and HSPA). N.J. required that a minimum percentage of students pass these tests (minimum percentage passing of 75%, 75% and 85%, respectively)
- Under the *No Child Left Behind Act* (“*NCLB*”) legislation, N.J. is required to switch from being accountable for general education students passing at specific rates to being accountable for all students by NCLB-defined subgroups passing at specific rates

The “No Child Left Behind” Act

- Impact of NCLB on school districts:
 - minimum *Adequate Yearly Progress* (“AYP”) in the scores of each subgroup in tested grades
 - all teachers must be “*highly-qualified*” by June 2006
 - see <http://www.somsd.k12.nj.us/finance/nclb.pdf>
- Meeting these mandates may require allocation of additional resources or re-allocation of existing resources

Collective Bargaining Agreements Establish:

- Salary guides
- Benefit levels, including healthcare, sick leave and personal leave
- Length and structure of the teacher's workday, including number of teaching minutes, amount of prep time, other duties required (e.g., lunch, tutorial in the high school)
- Required compensation for loss of prep time
- Differentials and stipends for additional and/or off-hours duties

The market acts as an invisible but real force in determining the prices we pay for goods and services

- Teachers and administrators bargain with knowledge of what other districts pay
- Failure to stay within the market range for salaries will, over time, result in an inability to attract and retain staff
- Healthcare premiums, commercial insurance, energy costs, construction services, transportation costs, out-of-district placement, etc., are all subject either to negotiation or low-bid requirements, but the market establishes their “*price-floor*” – which is *beyond our control*

Community Expectations Dictate the Level of Programs and Services We Must Provide Beyond the Mandated Minimum

- The attractiveness of the community is dependent upon a curriculum and extra-curricular offerings that are competitive with those of neighboring public school districts and private schools in proximity to our community
- Keeping our graduates competitive in the college admissions race requires a set of high-level courses in the high school
- Community expectations also dictate support for Project Ahead and other intervention programs for students at risk

Board of Education Policy and Other Board Decisions Establish:

- Class size maximums (the state imposes no requirements in this regard)
- Our Board policy goes beyond the N.J. requirement of 110 credits to require a minimum graduation requirement of 120 credits and a course load requirement of 35 credits per year for four years (implying 140 credits)
- Elementary attendance zones and minimum distance requirements for transportation
- Board policy is a “softer” constraint than the others (governmental mandates, collective bargaining agreements and market conditions); board has the ability to change its policy, although it does not do so without careful deliberation and is not driven by expedience

Summary

- The state must amend its S-1701 cost containment measures to take account of the realities of extraordinary rates of increase in areas of expenditure over which districts have no control.
- The Governor and the Legislature must also follow through on their pledge to effect property tax reform and ensure that a substantial portion of our school funding comes from state sources
- If the Governor and the Legislature want containment of healthcare costs, they must take the lead with the N.J. State Health Plan.
- In the meantime, we must make the best of a difficult situation, informed by the consensus around long-term goals that is emerging from the district's Strategic Planning Process.
- We understand the historical cost drivers and are attempting to manage them. The largest non-salary items include health benefits, special education (in particular, out-of-district tuition), purchased property services, transportation, supplies, energy and insurance. We must scrutinize each for savings and cost management opportunities.
- Understanding near-term opportunities for cost savings awaits delivery of the administration cost analyses.