Group paintings done by Drawing & Painting students at John Marshall High School, Milwaukee, MPS 2006-07 calendar

Challenges Today and Tomorrow

An Analysis of the Present and Future Financial Condition of MPS

wistax

Prepared for the Metropolitan Milwaukee Association of Commerce by the Wisconsin Taxpayers Alliance

Challenges Today and Tomorrow

An Analysis of the Present and Future Financial Condition of the Milwaukee Public Schools (MPS)

March 2007

To the Metropolitan Milwaukee Association of Commerce:

At the heart of every forward-looking state is a great city. And nothing is more essential to the growth and prosperity of a major city than its schools. So it is with Milwaukee and the Milwaukee Public Schools.

For that reason, the research team at the Wisconsin Taxpayers Alliance (WISTAX) and I were honored and excited when MMAC approached us to examine the financial condition of and prospects for the city's schools.

It was a daunting task. Obtaining and analyzing financial data for the state's largest and most complex district was problematic. To the uninitiated, the size, scope, and diversity of MPS are hard to grasp; the district is like no other in Wisconsin.

For that reason, we are most grateful to MPS Superintendent Bill Andrekopoulos and Chief Financial Officer Michelle Nate for their support. We also appreciate the interest of the MMAC education committee, and particularly the valuable insights of committee chair Bob O'Toole and MMAC president Tim Sheehy. On a personal note, I must thank WISTAX's dedicated and indefatigable Research Director, Dale Knapp.

As will be seen, MPS already has many challenges:

- Declining student numbers and a host of viable options for K12 students and their families;

- Rising and, in some cases, difficult to control costs. Though MPS's finances are similar to other large, diverse districts, its salaries relative to staff experience and its benefit expenditures are relatively high. The size of middle management within schools is also atypical.

- Highly aided by both the state and federal governments, the Milwaukee district is unusually vulnerable to political decisions and policy made elsewhere. An anticipated decline in federal monies will directly impact MPS's bottom line. And, any slowdown or reduction in state aid, has a direct property-tax impact in a high-tax city.

WISTAX projections show the future to be even more difficult. All these factors combine to suggest a future where revenue growth will be modest, at best, while costs will grow inexorably. If no further budget adjustments are made—and some have already been implemented—the Milwaukee school district faces a recurring and growing gap between slowing revenues and growing expenditures.

Needless to say, MPS has difficult years in its immediate future. From our work, we know that district, MMAC, and community leaders are passionate about improving education for all Milwaukee's children. We wish them only the very best.

Todd A. Berry
President, Wisconsin Taxpayers Alliance

Now in its eighth decade and widely respected for its objective, nonpartisan work, the Wisconsin Taxpayers Alliance (WISTAX) is Wisconsin's only private, independent statewide organization dedicated to public policy research and analysis.

wistax

EXECUTIVE SUMMARY: THE MPS STORY

Milwaukee leaders are increasingly concerned about the financial future of the Milwaukee Public Schools (MPS). Despite budget challenges and rising state and federal aid, property taxes continue to grow. The combined effect of lost market share, district spending choices (particularly in the fringe benefit area), tightening state revenue controls, and uncertain federal funding means that the expenditure demands MPS faces will grow faster than available revenues. Annual rounds of budget retrenchment are inevitable.

Study Aims

In light of these and other issues facing MPS, the Metropolitan Milwaukee Association of Commerce (MMAC) asked the Wisconsin Taxpayers Alliance (WISTAX), a nonpartisan research group, to study MPS's finances. Underlying the request was a desire to understand why, despite steady growth in per pupil expenditures, budget discussions are dominated by "deficits" and reductions. Key questions asked were:

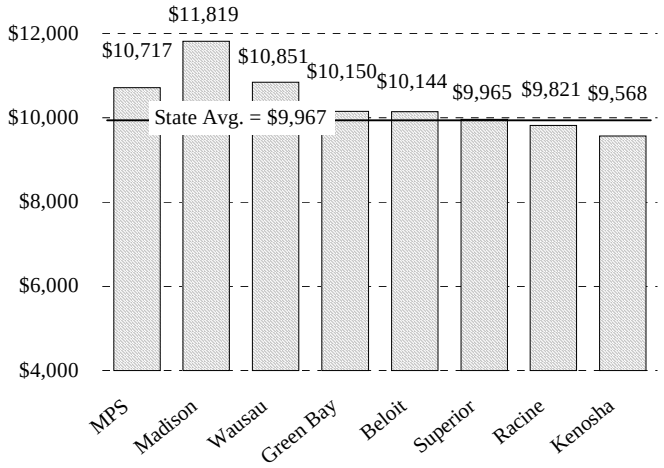
- What are the sources and uses of MPS's funds?
- What are the main factors driving district revenues and costs? and
- What will the district's finances look like in three to five years?

The goal of the study was to provide an objective, third-party review of MPS from experienced analysts of Wisconsin school finance. WISTAX has a long history of providing unbiased information, and its researchers have extensive backgrounds in Wisconsin school finance.

Key Factors Include Spending

Several factors contributed to the projections presented here: expenditure decisions, declining district market share, and changing—and less predictable—revenue sources. Of these, spending is the factor over which MPS has control.

MPS Spending Above Average
Per Student Spending, Selected Districts, 2004



MPS's 2004 per student spending was $10,717, or 7.5% more than the state average.

Among some casual observers, there is a perception that MPS's spending is out of line with other districts statewide. While the district's per student spending is above the state average, it is similar to other large urban districts.

WISTAX compared MPS spending to seven other districts and the state average. The seven districts were chosen based on size (the largest districts in the state) and demography. Although Beloit and Superior are not among the largest districts, their student characteristics are similar to MPS's.

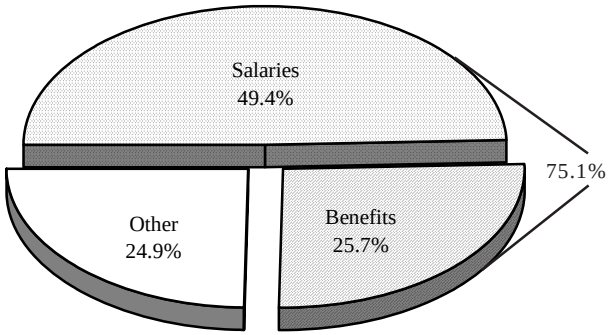
The chart above shows MPS's 2004 per student spending was $10,717, or 7.5% more than the state average. However, the district's expenditures were more in line with the seven "comparable" districts. Like MPS, four of them spent more than $10,000 per student (Beloit, Madison, Wausau, and Green Bay). Madison and Wausau spent more per pupil than MPS.

The district's spending was "more in line" with other large districts that had student characteristics similar to MPS's.

Compensation. Although MPS was generally above comparable districts in spending, more striking were spending differences by category. In many cases, MPS made different choices about how best to use their resources. Some of these differences were due to having a different student population than the other districts.

The district's compensation costs were more than 75% of total education spending in 2004.

Compensation 75% of Education Spending
MPS Spending by Broad Category, 2004

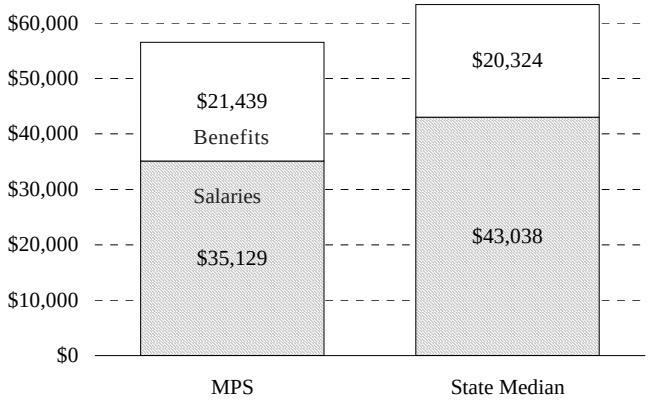


Compensation is a key driver of district costs. As with other districts, it is the largest cost for MPS. The chart above shows that MPS's compensation costs (salaries plus benefits) were more than 75% of total education spending in 2004. Salaries were about half and benefits were another quarter of the total.

Since 1995, benefit costs rose nearly three times as fast as salaries and about 50% faster than other spending. During the 1995-through-2004 period, benefit costs climbed 83%, salaries were up 30%, and other spending rose 56%.

Since 1995, benefit costs have risen nearly three times as fast as salaries, and about 50% faster than other spending.

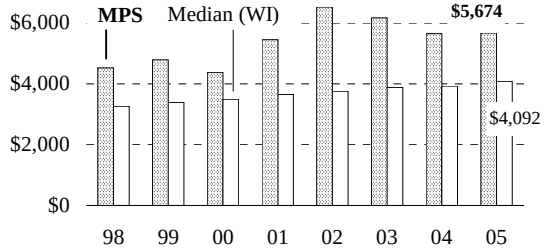
Benefits Stand Out at MPS
Avg. Teacher Salaries and Benefits, MPS and State Median, 2005



Teacher Compensation. Comparing teacher compensation at MPS with other districts statewide shows MPS to be low or high, depending on the comparison.

The chart below (below, left) shows average 2005 teacher salary and benefits for MPS, and for the median (half lower, half higher) district statewide. According to the Wisconsin Department of Public Instruction (DPI), average teacher compensation at MPS ($56,568) was below the median ($63,362). While the average MPS salary was lower ($35,129 vs. $43,038), average benefit costs were higher ($21,439 vs. $20,324) than the median.

Compensation Costs Per Year of Experience
Avg. Teacher Pay and Benefits: MPS vs. Wis. Median



However, MPS teachers were younger and less experienced than teachers statewide. Since salary schedules are based partly on experience levels, MPS salaries should be lower. MPS's teachers averaged 10.0 years of experience vs. 15.3 years for the median district. Adjusting reported salaries for experience, the average MPS teacher was paid $3,523 per year of experience, or 25.5% more than the state median ($2,807). When the focus shifts to salary *and* benefits, as the chart above shows, the gap in *total* compensation was over 38% ($5,674, MPS vs. $4,092).

In short, MPS is paying relatively more for less experienced teachers; and, regardless of salary level, paying out more in benefits, as well.

could be due to age/experience differences, similar to what was found with teachers. It could also be that MPS's job mix in this catch-all category is atypical.

The biggest difference between administration at MPS and at other districts is the number of assistant principals (AP). In 2005, MPS had 541 students per AP. The seven comparable districts averaged 1,177. Thus, relative to its student count, MPS had more than twice as many AP's.

A second way to look at the number of AP's is relative to the number of principals. MPS had more AP's than principals in 2005; the other districts had one AP for every two principals.

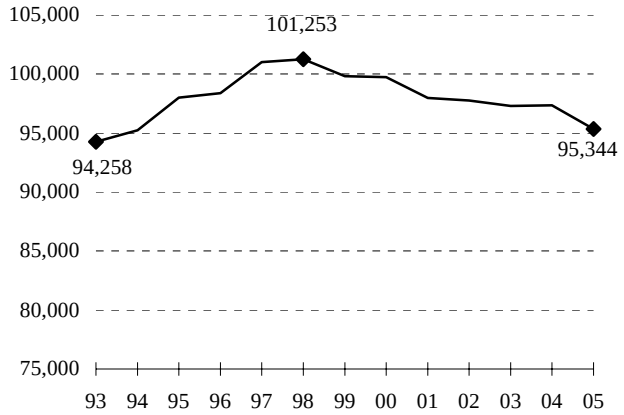
Declining Market Share

Another key factor driving projections is enrollment change and its impacts, under state law, on state aid and allowable revenues. Since the 1998-99 (hereafter, 1999) school year, MPS's enrollments have eroded. After peaking at 101,253 (see chart), fall enrollments declined a total of 5.8% over the following six years, reaching 95,344 in 2005.

Administration: Districts Differ on Asst. Principals
No. of Students per Administrator and Avg. Compensation, MPS and "Comparable" Districts, 2005

	MPS	Comp. Districts
District Admistrator		
Compensation	$171,405	$170,105
Principals		
Compensation	$105,653	$107,780
Students per admin.	641	575
Asst. Principals		
Compensation	$91,918	$95,463
Students per admin.	541	1,177
Asst's. per Principal	1.18	0.49
Other Admin.		
Compensation	$93,093	$113,918
Students per admin.	1,119	1,154

MPS Enrollments Declining
September Head Counts, 1993-2005



Due partly to increasing competition, the number of students MPS serves has been declining since 1999. MPS is losing "market share."

Market forces were a factor in the decline. The Milwaukee area is a competitive one for K-12 education. Parents and students have a number of options in addition to MPS, including parochial schools, charter schools, and several "choice" programs.

The state's "choice" options include: Chapter 220 transfers between Milwaukee and suburban public schools; the Milwaukee Parental Choice Program (MPCP), which provides public funds to low-income students to attend private schools; and public school open enrollment.

While the total number of students in the Milwaukee market has remained nearly unchanged since the late 1990's, MPS's share of that market has declined from nearly 83% to less than 79%.

With state revenue limits tied to enrollment, MPS's future revenue growth will be moderate, at best.

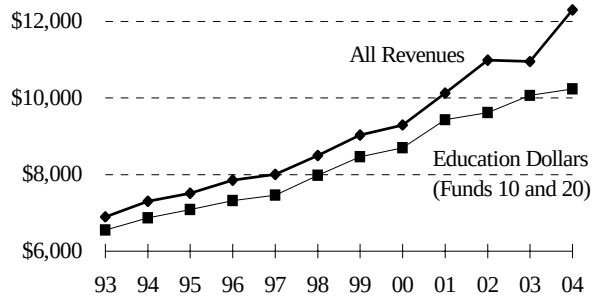
Revenues: Slow Growth, Outside Sources

While enrollments have fallen with eroding market share, revenues have increased moderately. However, since it receives the bulk of its revenue from state and federal governments, MPS is affected by political decisions made elsewhere.

Total per student revenues rose 78.6% from $6,891 in 1993 to $12,306 in 2004 (see chart on page four, top

Per Student Revenues Rising

Per Student Revenues, 1993-2004



With state and federal aids comprising more than four of every five education dollars at MPS, the district has become increasingly reliant on the financial decisions of others.

line). Part of the increase was due to bond revenue used to fund the district's Neighborhood Schools Initiative. "Education dollars"—revenues after subtracting funding for community programs, food service, and capital expenditures—grew at a slower rate. They rose 56.4% (bottom line in the chart above) from $6,542 to $10,232 per student during the period studied.

While per student revenues continue to climb, there are two areas of concern. The first is a slowdown in the growth of "education dollars." From 1993 to 2001, these per student revenues climbed an average of 4.7% per year. From 2001 through 2004, they grew only 2.8% annually.

And, second, as mentioned, MPS is increasingly reliant on state and federal dollars. In 2004, only 16.7% of the district's "education" revenues were raised locally (see chart above right). Aids from state (69.0%) and federal (13.5%) governments accounted for more than four of every five education dollars at MPS.

During 1993-2001, average annual revenue growth at MPS was 4.7%. From 2001 through 2004, it was 2.8%.

These percentages have changed significantly since 1993. In that year, state (56.0%) and federal (7.2%) funding was less than two-thirds of the total.

With growing federal dollars becoming more important to MPS, the district became more dependent on financial decisions made in Washington D.C. A slowdown in federal aid increases will impact the amount of revenue the district has available.

Changes in state aid do not affect the district's bottom line as much. State-imposed revenue limits are more important in determining total district revenue. However, the combined effect of the two can result in significant school tax increases when the state faces fiscal problems.

Looking Ahead

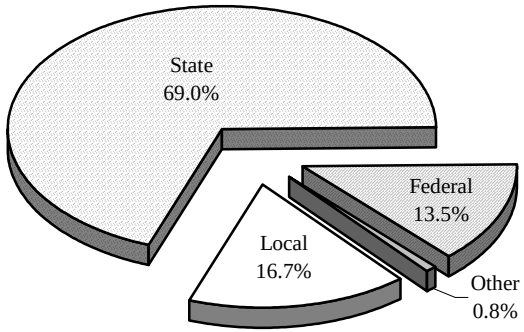
With enrollments falling, benefit pressures growing, and finances increasingly vulnerable, what does the future hold for MPS? Answering this question is difficult because it requires forecasting future enrollments, state and federal aid policy and politics, and spending decisions at the district level. All of these can be unstable, even volatile.

Assumptions. To forecast future finances, assumptions about enrollments, federal aids, and state aids were made. For enrollments, a commonly-used forecast method—"grade progression ratios"—was used. This technique compares the number of students in each grade with the number in the previous grade the prior year. Those ratios are then used to project future enrollments.

MPS's progression ratios are generally less than one, i.e., there are fewer students in fourth grade than were in third grade the year before. Hypothetical reasons for such ratios can vary, e.g., declining birth rates, student dropout, and loss of market share. MPS's current progression ra-

Local Revenues Less Than 20% of MPS Total

Revenue Sources, 2004



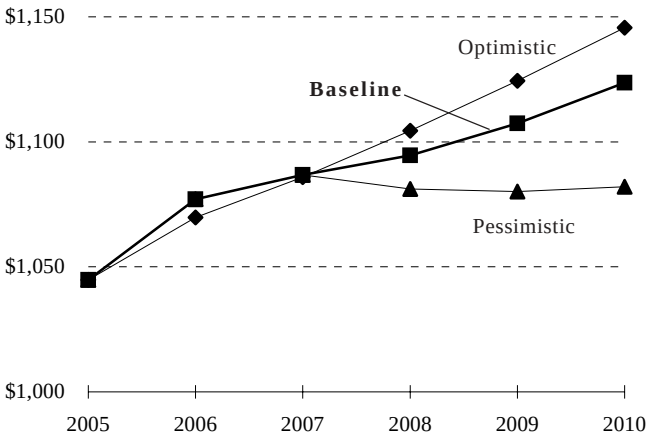
tios mean student counts are estimated to fall from more than 98,000 in 2003-04 to 92,400 in 2009-10.

After years of growth, national forecasts of federal school aids suggest they will decline slightly over the next several years. Our forecasts assume the same for MPS's per student federal aids.

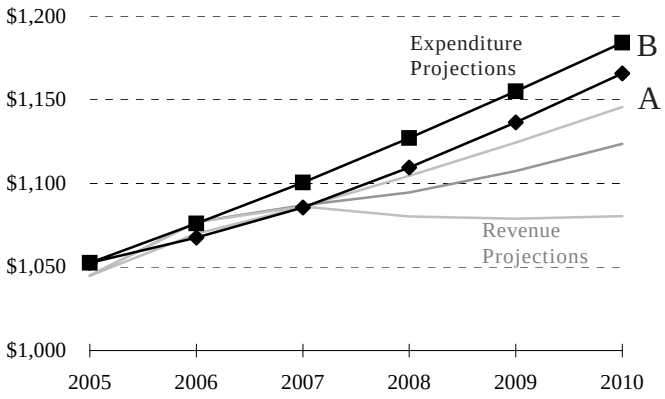
Given state budget difficulties in recent years, state aids and revenue limits are even more difficult to estimate. We provide several scenarios: one in which state revenue-cap and aid policies remain as is; and a second more pessimistic one in which allowable revenue-cap increases are approximately one-half of current law.

Revenue Forecasts. The chart below shows three revenue forecasts for the district through 2010. The baseline scenario assumes current state aid and revenue cap policy, unchanged federal revenues, and the predicted enrollment trends. The optimistic scenario uses the same assumptions, except enrollments are assumed to be unchanged and federal aids increase slightly. Finally, the pessimistic scenario uses baseline assumptions, but revenue-cap policy is more stringent ($120 per student annual increases, or slightly less than half the baseline scenario).

MPS Projected Revenues: Rising Slowly?
"Education Dollars" (Funds 10 and 20), 2005-2010



MPS Projected Expenditures and Revenues
"Education Dollars" (Funds 10 and 20), 2005-2010



The most-likely scenario for MPS's revenues is a modest increase of 1.5% per year through 2010.

Although revenues are projected to grow each year under two of the scenarios, the increases are not large. Under the baseline scenario, revenues increase an average of 1.5% per year. Under the optimistic scenario, the increase is 2.1%.

Spending. Revenues are difficult to project, but expenditures are more problematic. The district tries to adjust expenditures to revenues each year. In years of slow revenue growth, this may mean reductions in some areas.

The expenditure forecasts provided here (see above) use a different approach. Expenditures are not adjusted to match revenues. Rather, past expenditure trends are used to forecast future spending.

Under both spending projections, expenditures are greater than revenues for all years through 2010.

Using this method, the study can estimate the likely gap between revenues and expenditures, i.e. the dollar amounts that will likely have to be cut from current trends.

Two spending trends are used. The first ("A" in the chart above) uses recent per student spending and assumes modest increases (2.9% per year). The second ("B" in the chart) separates compensation and non-compensation, and

assumes they grow at different rates (lower for compensation, 2.5%, and higher for other spending, 3.1%).

The chart on page five summarizes the two projections (dark lines) and also displays the three revenue forecasts already described (gray lines). Under both spending projections, spending exceeds revenues. Line A represents per student expenditures growing 2.9% per year. Under this assumption, expenditures are $42.2 million above baseline revenues in 2010. That figure is 3.6% of expenditures.

Under baseline projections, revenues could be $40 million to $60 million less than expenditures by 2010. More pessimistic assumptions could push the gap over $100 million.

Under the alternative spending forecast (B), which assumes compensation grows 2.5% and non-compensation 3.1%, the gap between expenditures and baseline revenues would be $60.6 million, or 5.1% of expenditures in 2010.

Summary

MPS faces challenges as this research and accompanying forecasts suggest. The expenditure side of the equation is problematic. Like any school district, MPS's costs are heavily skewed toward compensation (75% of total spending). At first glance, the district's salaries are not out-of-line with other districts. A different picture emerges when staff experience is factored in. The average MPS teacher has 35% less total teaching experience than the state average. When compensation per year of experience is calculated, MPS is 39% above the average.

Another more significant factor is fringe benefits, which tend to be paid regardless of experience. Although MPS's teacher corps is relatively young with a lower average salary than the state as a whole, average benefits are more than $1,100 per teacher more than the state median. And, due to rapidly-rising health care costs and state law, benefits are growing much faster than salaries.

Covering the cost of post-retirement benefits "could increase the revenue-spending gap to more than $200 million in 2010."

A challenge that many districts across the state face is school-age populations that are not growing. This is generally true in Milwaukee with an added wrinkle: MPS is losing market share to other K-12 options. With enrollment adversely affecting state-imposed revenue limits and state aid calculations, falling student counts make MPS vulnerable on the revenue side of the ledger. Fewer students means that allowable revenue growth will be limited and state aid increases may not be as robust as in the past. In recent years, federal aid to MPS has grown considerably. Current federal finances make that unlikely to continue.

When the slowing and vulnerability of revenues is combined with cost pressures, particularly salaries relative to experience and fringe benefits, the gap between revenues and spending is expected to grow. Baseline forecasts suggest that gap could be $40 million to $60 million by 2010. More pessimistic assumptions it could exceed $100 million.

A final issue that MPS will need to address in the near future is the cost of post-retirement benefits. New accounting rules will require the district to account for the future cost of many post-retirement benefits—particularly health care. The best estimates available put the present cost of these benefits at $1.45 billion, or about 40% more than the district's total 2005 expenditures. Should the district issue bonds to fund these future costs, an additional $115 million would be added to MPS's budget. The addition of this expenditure could increase the district's revenue-spending gap to more than $200 million in 2010.

The last few years have been challenging for MPS and and confusing to the tax-weary public. WISTAX analysis and forecasts suggest more challenges lie ahead.

Final Note

Work on this study began with WISTAX staff and MMAC members discussing the scope of the study. We also met with Superintendent William Andrekopoulus and Chief Financial Officer Michelle Nate to seek advice, outline study goals, and obtain MPS data. MMAC staff briefed key union leaders on the project. We thank them all.

We hope this study helps MPS staff, the press, public, and interest groups to understand better the challenges Wisconsin's largest and most diverse district faces. □

INTRODUCTION

Over the last several years, the Milwaukee Public Schools (MPS) have reduced the number of teaching positions in an attempt to limit cost increases. At the same time, school property taxes have risen. In particular, the 2004-05 school levy rose nearly 15%. Few people outside of the education community understand this seeming contradiction.

In light of this and other issues facing MPS, the Metropolitan Milwaukee Association of Commerce (MMAC) asked the Wisconsin Taxpayers Alliance (WISTAX) to study MPS's finances. Key questions were:

- What are the sources and uses of MPS's funds?
- What are the main factors driving district costs? and
- What will the district's finances look like in three to five years?

Background

Work on this study began with a series of meetings. First, WISTAX met with MMAC members to discuss the scope of the study. It was agreed that the work should proceed in three phases, as discussed below. WISTAX also met with Superintendent William Andrekopoulos and Chief Financial and Operations Officer Michelle Nate to seek advice, outline the structure and goals of the study, and obtain MPS data. MMAC staff contacted key union leaders to brief them on the project.

Phases

The study was organized into three phases.

Phase 1. The initial section of this study was the product of the first phase, which examined broad trends affecting MPS. In particular, it explored changes in enrollments, property values, revenues and spending from 1993 through 2004. This phase of the study was completed in early 2005, so 2004 data were the latest available.

There were several goals to this phase. First, it served to provide a common base of information. Because it is a broad overview, we believe that interested parties should be able to agree on the basic trends facing the district.

Second, this phase also served to raise questions. Although part one answers some general questions, the intent was to generate questions that could only be answered by narrowing the focus to specific areas.

Third, these questions helped us focus the second phase of the study. Although the WISTAX proposal outlined specific areas of study for part 2, we looked to the questions raised in part 1 to determine where time and resources would be best expended.

Phase II. The second phase of the study drilled down to specifics. In terms of enrollments, the impact of Chapter 220 and Milwaukee school choice on district finances were explored. More detail on MPS's revenue limit are provided.

Of particular interest was MPS's spending, which was disaggregated in several ways. Expenditures in several categories were analyzed to determine the areas that are driving MPS's costs. To put MPS's costs in context, comparisons were made with other "similar" districts in the state.

Phase III. The third phase was primarily forecasting. The main focus was using the information gathered in the first two phases to make predictions about MPS's finances over the next three to five years.

Expectations

The overall goal of this study was to provide an objective, third-party review of MPS from respected analysts of school finance. WISTAX has a long history of providing unbiased information and its researchers have extensive backgrounds in Wisconsin school finance.

The study should serve to educate MPS staff, the general public, press, and interest groups about the district, and should also serve as a resource for problem-solving.

The study was done in three phases:

- ***a broad overview of district trends;***
- ***a comparison of MPS's spending in specific categories with other districts;***
- ***forecasts of district revenues and expenditures through 2010.***

PART 1: A VIEW FROM 10,000 FEET

SCHOOL FINANCE OVERVIEW

To understand a school district's finances, one must have a general understanding of where school districts get their money and the interplay between state school aids, local property taxes and school district revenue limits.

Revenue Sources

School district revenues come from four main sources: the federal government; state government; local sources; and other sources.

Most federal dollars are funds associated with the No Child Left Behind Act (NCLB) or the Individuals with Disabilities Education Act (IDEA). Both funding sources have increased significantly over the last several years.

State dollars are mostly equalization (or general) aids, which are distributed to districts based on their spending levels and per student property values. The state also provides categorical aids, which must be used for specific purposes. Special education and student transportation aids are two such categoricals.

Local revenues are primarily property taxes. They also include student fees and revenues from ticket sales for extracurricular activities. In MPS, local revenues also include payments in lieu of taxes from the city for city property not on the property tax rolls.

The "other" category is typically fairly small, and can include revenues from other school districts (for open enrollment or special education programs, e.g.), CESA's, or other organizations.

Accounting

The Wisconsin Department of Public Instruction (DPI) requires school districts to account for their revenues and spending in several different funds. MPS primarily uses six funds. Funds 10, 20, 30 and 40 are used to account for transactions generally associated with educating students. The first two report transactions for instruction, support services, administration, maintenance of buildings and student transportation. Fund 10 is for the general student population and fund 20 is for special projects, particularly special education. Funds 30 and 40 are used to account for transactions involving debt service and capital projects, respectively.

Food service transactions are recorded in Fund 50. Revenues in this fund are generally from food service sales and federal aids. Fund 80 is the community service fund and reports transactions related to programs provided for the general public, e.g., community recreation programs. The majority of revenues for this fund come from the property tax levy and activity fees.

At MPS, more than 95% of revenues and expenditures are accounted for in funds 10 through 40. These funds will be the primary focus of this study.

State Aids

Wisconsin school districts receive two types of state aid payments: general school aids (primarily equalization aids) and categorical aids. Equalization aids are paid to school districts based on spending and per student property values. In general, the lower a district's per student property values, the higher its equalization aids.

Equalization By Spending. The chart on page 10 shows how per student equalization aids change as per student spending and property values change. Each line represents a specific level of per student property values. As you move from left to right on a particular line, per student costs are increasing.

For districts with below-average property values (top line), state aids rise as spending goes up, although the increases slow when spending climbs above $7,531 (for 2003-04). For districts with average values (heavy line), aids rise until spending reaches $7,531 and then stabilize. Districts with above average property values (bottom two

School District Accounting

Fund 10. Commonly referred to as the general fund, Fund 10 is used to account for most of the district's current operations.

Fund 20. The sum of Funds 23 and 27 are referred to as Fund 20 in this report. Fund 23 (TEACH fund) is used to account for programs funded from the TEACH Wisconsin Board. Fund 27 is used to account for revenues and spending associated with special education services.

Fund 30. This is the sum of Funds 38 and 39, which are used to account for debt service.

Fund 40. This is the sum of several capital projects funds.

Fund 50. The food service fund is generally funded with federal dollars and local charges. Any deficit here must be covered with money from Fund 10.

Fund 80. The community service fund is used to account for activities such as adult education, community recreation programs, and other community programs. The school district can levy a property tax to help fund these programs. The tax is outside the district's revenue limit.

lines) experience declining aids as spending climbs above $7,531.

Equalization By Property Wealth. A second way to look at the aid system is to examine aids for districts with similar spending but different property wealth. For example, a district spending $8,000 per student (see vertical line in graph) would receive different amounts of aid depending on its property values. The lower its values, the higher its aids. This is true for any level of per student spending; i.e., for any vertical line we draw.

Other State Aids. Districts with declining enrollments are also eligible for special adjustment aids, which help limit declines in state equalization aids as enrollments fall.

Categorical aids are paid to districts based on specific criteria. The state has more than 20 categorical aid programs, though total funding is less than 15% of total general aids. The largest categorical aid program is special education, which topped $315 million in 2003-04. Among the other categorical aids are transportation funding, Student Achievement Guarantee in Education (SAGE) and school library aids.

Since 1993-94, the state has imposed revenue limits on school districts. Federal dollars, student fees and taxes for community programs are outside these caps.

Revenue Limits

Beginning with the 1993-94 school year, Wisconsin has placed limits on the amount of revenue school districts can raise from the sum of local property taxes and state general aids. Each year, a district's limit depends on its prior-year limit, its current three-year enrollment average, and a state-imposed allowable per-student increase. For 2004-05, the per student increase was $241, or approximately 3% for an average district. School districts can exceed their revenue limits with voter approval in a referendum.

The revenue limit amount is not the district's total revenues. Money from the federal government, state categorical aids, student fees and community service property tax levies are not subject to the limits. Thus, a district's total operating revenues are higher than the state-imposed limits.

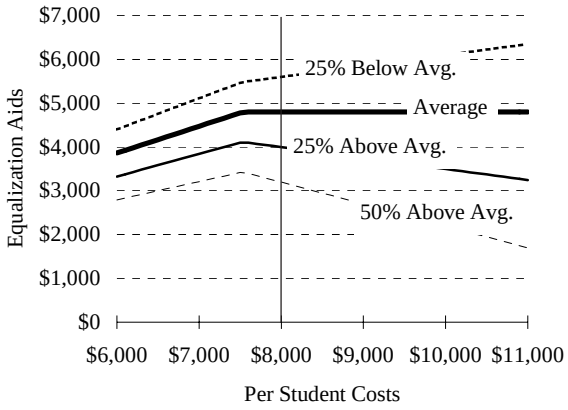
Enrollment is an important factor in a district's total revenue limit. Although all districts received the same per student increase ($241 in 2004-05), a district's enrollment will determine the change in its total revenues. For an average district with no change in enrollment, the $241 per student increase translates to about a 3% increase in per student revenues.

However, districts with rising enrollments and average spending will experience a more than 3% increase in *total* allowable revenues due to the rise in student numbers. Declining enrollment districts will see total revenues subject to the caps rise less than 3%, and possibly decline, depending on the severity of the student decline.

School Aids and Revenue Limits. Because the revenues associated with the limits are state aids and property taxes, increases in school property taxes are largely determined by the state. Once a district knows the amount of its general school aids and its revenue limit, it can determine the maximum property tax it can levy.

State Aids Change With Spending, Wealth

Per Student Equalization Aids at Various Property Wealth Levels



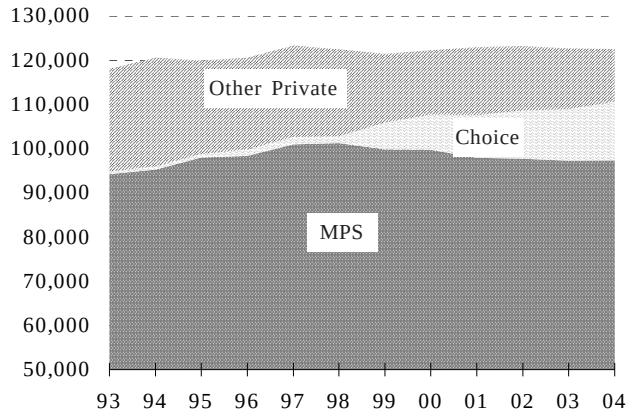
The chart at right shows the relationship between aid changes and property tax changes for three hypothetical districts. The only differences between the districts are general aids as a percent of their revenue limit. The 75%-aided district would be relative property poor; the state provides significant aids to equalize property tax rates. The 30%-aided district would be fairly wealthy, and thus is supported primarily through local property taxes. The 60% district is somewhat average.

As the chart shows, each of these districts would have a levy increase of 3% if their aids also rose by 3%. However, when state aid growth is limited (less than a 3% aid change), the highly aided (property poor) district can experience much higher property tax increases. For example, if the property-rich district experiences a 1% drop in state aids, its levy rises 5%. If the property-poor district experienced the same 1% drop in aids, its levy would have to rise 15% to fully fund the revenue limit.

At MPS, state general aids account for approximately 75% of its revenue limit. Thus, relatively small fluctuations in aid can have disproportionate impacts on property tax levies. In years when state aid increases are limited, MPS's property taxes will tend to rise more than other districts. This is part of the reason for the large property tax increase in 2004-05. Conversely, large increases in state aids translate to small property tax increases, or possibly declines, for MPS.

MPS Enrollments Fall

Fall Enrollments for MPS, "Choice" Schools and Other Private Schools in Milwaukee



ENROLLMENT TRENDS

MPS, like many school districts statewide, is dealing with annual declines in the number of students it serves, although the causes seem to be more market-driven, rather than demographic. Fall enrollments have generally declined since 1998, when they topped 101,000. In 2003-04, September enrollments at MPS were just over 97,000.

Declining enrollment districts face unique financial challenges. As enrollments fall, costs do not necessarily decline proportionally. School districts have significant fixed costs for items such as buildings, and to a lesser degree administration. Further, proportional reductions in staffing is difficult because changes in student populations are stretched throughout many grades.

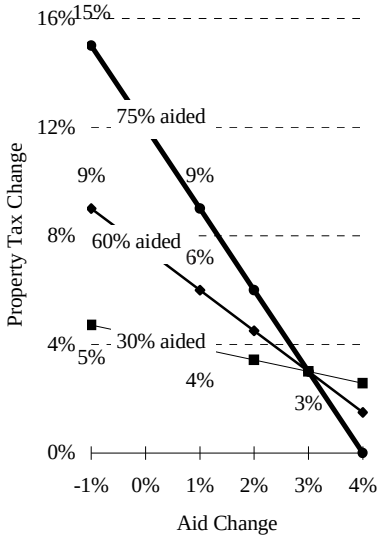
MPS is in a unique market. The Milwaukee area is probably the most competitive market in the state for K-12 education due to several educational options. First, the Chapter 220 program allows certain Milwaukee students to transfer to one of many suburban public schools. Likewise, suburban students can transfer to MPS, although nearly eight students transfer out of MPS for every student that transfers in.

Second, the Milwaukee Parental Choice Program (MPCP) provides public funding for low-income students to attend private schools. Public school open enrollment provides a third option for MPS students to attend an alternative district. Finally, Milwaukee has many private schools that compete with MPS.

The chart at left shows annual enrollments for MPS, private schools in Milwaukee and MPCP schools from 1993 through 2004. MPS is in a market with relatively stagnant

School Property Taxes Depend on State Aids

% Changes in Property Taxes, Aids for Selected District Types



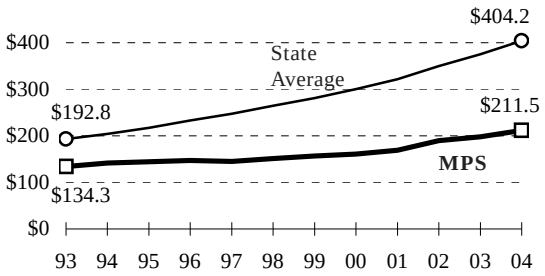
enrollments. The total number of students attending school in Milwaukee has fluctuated between about 120,000 to 123,000 since 1996.

PROPERTY VALUES

MPS's per student property values have fallen from 30% below the state average in 1993 to 50% below in 2004. As a result, the district has become more reliant on state aid for funding.

Per student property values are important for determining the amount of equalization aid a district receives.

Property Wealth Low, Rising
Equalized Values Per Student, ($ Thousands)



The chart on page 10 shows how property values and spending interact to determine state aids.

MPS's per student values have been below the state average for at least the last 11 years (see chart above) and are falling further behind. In 1993, MPS's equalized values were approximately 30% below the statewide average. By 2004, they had fallen to almost 50% below.

Because property values are below average, MPS receives a significant amount of state aid. As the district falls further behind in property values, it becomes more dependent on state aids for its revenues.

REVENUES

By Source

Total revenues collected by MPS in 2003-04 were $1.23 billion. A small portion ($21.9 million) was used for community service activities (Fund 80). Another $29.6 million funded food services (Fund 50). The remaining 96% was used for general education purposes, including capital projects and debt service.

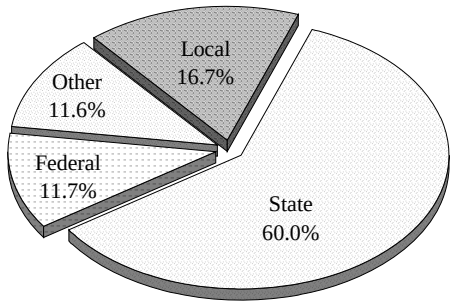
MPS is funded primarily with federal and state revenues. As the chart below shows, in 2003-04, these two sources accounted for nearly three of every four "education" dollars the district took in. State funding comprised 60.0% of MPS revenues, while federal dollars were another 11.7%. Local revenues, including the property tax, accounted for approximately one of every six dollars collected.

State Funding. Most of MPS's 2003-04 state revenues were general aids. These aids accounted for 81.6% of all state dollars and 48.9% of all education dollars. Nearly all of the remaining state funding was categorical aids, which are designated for certain programs. MPS's largest categorical aid was for special education.

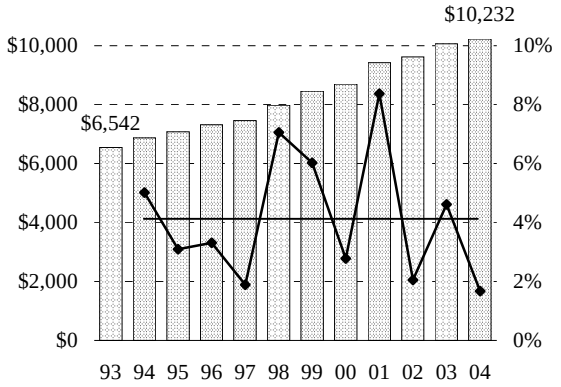
Local Funding. Most MPS local funding is from the property tax. Of the $196.7 million in 2003-04 local revenues, $175.3 million was from property taxes; another $11.7 million was city of Milwaukee payments in lieu of taxes.

Other Funding. MPS received other revenues from school districts participating in the open enrollment program and other miscellaneous revenues. However, the largest "other" revenue source was long term bond revenues to fund the neighborhood schools initiative.

Milwaukee Public Schools Revenue Mix
General Education Funds, 2003-04
$1.179 billion



Revenues Rise, Growth Slows
Per Student Revenues Funds 10 and 20 and
% Change, 1993 - 2004



Per Student Revenues

MPS's capital budget (Fund 40) has varied widely since 1993. In this section we eliminate that source of variation and look only at trends in non-capital education funds—Funds 10 and 20.

Per student revenues climbed from $6,542 in 1993 to $10,232 in 2004 (see bars in chart above). On average, they rose 4.1% per year during this period (the horizontal line in the chart).

Annual percentage increases fluctuated significantly during these years. In 2001, per student revenues jumped more than 8%, while the 2004 increase was less than 2%. Large increases in federal aids in 1998, 2001 and 2003 helped to significantly raise per student revenues in those years.

In two of the last three years studied, per student revenue increases were below average. In 2002, revenues climbed 2.0%; in 2004, they were up 1.7%.

Trends

As previously mentioned, MPS's revenues increasingly come from non-local sources. The pie chart on page 12 shows 2003-04 figures for all educational funds. The chart at right shows trends in funding for the non-capital funds.

Several important trends are displayed in the chart. First, the impact of the increased state aid due to the state's shift to 2/3 funding in 1997 is apparent. State funding of MPS rose from less than 60% prior to the shift to 70.1% in 1998. Local funded dropped from approximately one-third of all revenues to less than 20%.

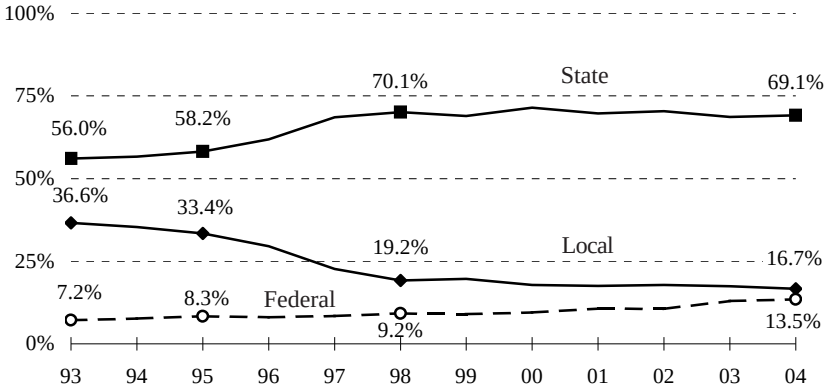
Since 1998, the state share of MPS's revenues has remained fairly steady. However, because total revenues have risen, state dollars have also gone up. Per student state funding climbed 26.3% from $5,598 in 1998 to $7,069 in 2004.

The federal share of funding rose significantly since 1998. As funding for special education rose, federal dollars climbed from 9.2% of the total in 1998 to 13.5% in 2004. On a per student basis, federal dollars nearly doubled, rising from $735 to $1,381 over the six years.

Local dollars increased slightly since 1998. In that year, they totalled $1,530 per student. In 2004, they were slightly higher ($1,704). However, because local funding did not rise as fast as federal and state dollars, it declined as a share of the total. By 2004, local dollars accounted for only 16.7% of revenues.

Per student state funding of MPS climbed 26.3% from $5,598 in 1998 to $7,069 in 2004. Federal dollars nearly doubled from $735 to $1,381.

MPS Revenues Increasingly From State, Feds
Revenues* as Percent of Total, Funds 10 and 20, 1993 - 2004



*Other revenue sources not shown include funds from other school districts, CESA's, etc.

In MPS, compensation (salaries plus benefits) were 75% of educational expenditures in 2003-04.

Consequences. MPS's high levels of state and federal funding has consequences. First, it allows the district to operate without an overly-burdensome property tax. The goal of Wisconsin's equalization aid program is exactly that—to allow property-poor districts to operate with tax rates similar to wealthier districts. Recent increases in federal monies, particularly special education aids, have allowed MPS to meet their growing special education costs using fewer general fund revenues.

There is, however, a down side for the district. Increasingly, MPS's financial situation is placed in the hands of state and federal officials, rather than local officials. If the federal government should cut back on federal education aids, MPS will be affected more than most districts because it relies to a greater extent on these dollars.

Finally, the graphic on page 11 shows the impact on property taxes of a slowdown or reduction in state aids. For a district like MPS that relies significantly on state support, large fluctuations in state dollars can lead to larger fluctuations in property taxes.

SPENDING

Spending trends are examined in two ways. First, a breakdown into compensation—salaries and benefits—and other spending are analyzed. Then, spending trends by broad category are explored.

Compensation

In 2004, approximately half of MPS's education expenditures (excluding capital expenditures and debt) were for salaries (see chart at right). Benefits were another 26% of spending, bringing total compensation to approximately 75% of expenditures. The district also paid approximately $33 million to other entities for purchased instruction. One example would be payments for open enrollment students. While these expenditures do not show up as personnel costs (compensation), most of the money is funding personnel at other school districts or at private entities.

A second important observation can be made from the chart. In these two funds (Funds 10 and 20), benefits averaged more than 34% of total compensation. Based on previous WISTAX research, this percentage is approximately five percentage points above the statewide average.

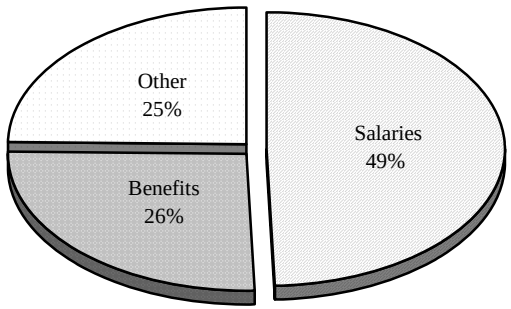
Longer term, there are two important trends affecting MPS. First, contrary to statewide norms, compensation is declining as a share of education spending. The reason is due to the second trend: Benefits are increasing as a percentage of total compensation.

Statewide, compensation costs are generally rising faster than revenues. The main reason is that revenue limits generally keep total revenue growth to around 3%. The Qualified Economic Offer (QEO) law allows compensation to rise approximately 4% per year. Due to salary schedules, individual compensation changes can vary widely from this number. In districts that do not impose the QEO, compensation can rise faster. Due to the differing growth rates, compensation tends to take an ever-growing portion of revenues.

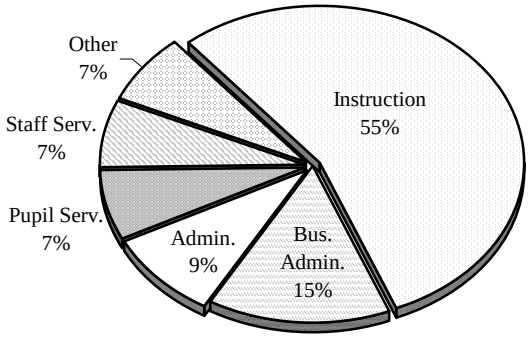
In MPS, the opposite is happening. In 1992-93, compensation was 83.0% of education expenditures. By 2004, that figure had fallen to 75.2%.

Because of the QEO, benefits are an increasing share of total compensation. Under the QEO, total compensation is allowed to rise approximately 4% per year. How-

Compensation is 75% of Spending
Education Spending by Compensation/Non-Compensation, 2003-04



Instruction Spending Over Half of Total
Spending by Category, 2003-04



ever, if the QEO is imposed, the district cannot change the employee benefit plan. Thus, when benefit costs rise rapidly, as they have over the last several years, salary increases grow slower. The result: benefit costs become a larger share of total compensation.

In MPS, benefit costs were approximately 26% of total compensation in 1995. That percentage increased steadily, reaching 34.2% in 2004.

By Category

Just over half (55%) of MPS's 2003-04 "educational" spending was on instruction (see pie chart above). The next largest category was business administration (15% of the total). Included in the business administration category is student transportation. District and school administration was next, accounting for 9% of spending. Pupil and staff services each were about 7% of the total.

Recent trends show per student instructional spending lagging increases in other areas. Spending on instruction rose 4.4% per year from 2000 through 2004. Of the major spending categories, only business administration rose slower. Staff services rose fastest, climbing 5.8% annually. Administration, pupil services and central services all rose more than 5% per year.

FUND BALANCE

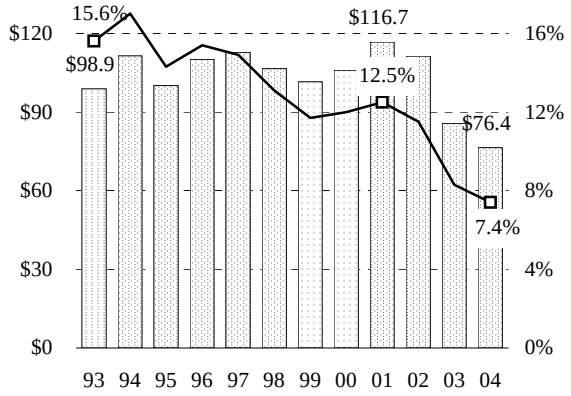
A final major trend affecting MPS's finances is its declining fund balance. School districts keep a fund balance (or savings account) for several reasons. Receipt of revenues do not always match expenditure timing and the fund balance can be used to balance out these discrepancies. Further, in some years a district's expenditures may exceed revenues. Districts will draw down their fund balance during these years to cover the spending gap.

MPS's fund balance dropped from more than 15% of spending in 1993 to 7.4% in 2004.

The chart below shows MPS's fund balance (bars) from 1993 through 2004. The balance fluctuated between $100 million and $120 million from 1993 through 2002. However, it has dropped every year since 2001 and was less than $80 million in 2004.

One way to compare the size of a fund balance is relative to spending. Statewide, fund balances averaged about 14% of spending in 2004. As a share of its spending, MPS's fund balance fell steadily from 1994 to 2004 (see line in graph). In 2004, MPS's balance was less than 8% of its expenditures. □

Fund Balance Declining
Fund Balance Total (bars, $ Millions) and Percent of Spending (line)



PART 1I: FOCUSING IN

Part II of this study examines enrollment and spending in more detail. The first section looks at the impacts of declining enrollment, MPCP, and the Student Achievement Guarantee in Education (SAGE) program on district finances.

The second part focuses on spending. In addition to examining specific spending categories, we also compare MPS spending with several benchmarks. As we began to examine areas of spending, it became clear that we could detail MPS's per student expenditures, but could not answer the following question: How would we know if MPS's spending was "too high" or "too low?" To attempt an answer to that question, the spending analysis here compares MPS's expenditures in various areas against the state average as well as several "comparable" districts. Those comparables are detailed beginning on page 20.

IMPACTS ON FINANCES

The number of students enrolled in MPS affects district finances. The most direct impact is through state-imposed revenue caps. State law limits the amount of revenue a district can raise through the sum of property taxes and state general aids. Since the limits are based on a three-year average of district enrollment and the previous year's limit, districts with declining enrollment will generally experience stagnation or outright decline in these revenues.

In addition to state revenue caps, other programs that impact MPS finances include MPCP and SAGE, a program that provides additional state funding to districts that reduce class sizes in lower grades.

Declining Enrollment

As outlined in Part I, due to lost market share, MPS has experienced falling student counts since 1998. In that year, district enrollments topped 101,000. As of 2003-04, September enrollments were 97,359.

Revenue Limits. Declining enrollments primarily impact a school district's finances through their effect on the revenue limit. The revenue limit is calculated using a three-year rolling average of September enrollments. Each year, districts are allowed to increase their per student limit by a legislated amount. This increase has gradually risen from $190.00 in 1993-94 to $241.01 in 2004-05.

Declining enrollments primarily impact a school district's finances through their effect on the revenue limit.

The table below shows how changing enrollments affected MPS's revenues. First, the year-by-year figures show MPS's enrollments (three-year averages) for calculating revenue limits rose each year from 1994-95 through 1998-99. During each of those years, MPS's total revenue limit increase (column 7) was higher than the legislated per student increase (column 5).

From 1999-2000 through 2002-03, revenue limit enrollments fell. During each of these years, MPS's total revenue limit rose slower than the legislated increase. Finally, in 2003-04, enrollments were nearly unchanged

MPS's Changing Revenues
Revenue Limits and Total Revenues, 1994 - 2004

			Revenue Limit					
Year	Members	% Chg.	Per Member	% Chg.	Total	% Chg.	Total Revenues	% Chg.
1993-94	95,284		$5,804		$553,028,336		$678,301,573	
1994-95	96,525	1.3%	$5,952	2.5%	$574,501,356	3.9%	$703,968,074	3.9%
1995-96	97,880	1.4%	$6,142	3.2%	$601,208,324	4.6%	$748,004,951	4.6%
1996-97	98,321	0.5%	$6,425	4.6%	$631,691,778	5.1%	$782,322,846	5.1%
1997-98	100,052	1.8%	$6,608	2.8%	$661,117,602	4.7%	$829,401,654	4.7%
1998-99	102,461	2.4%	$6,852	3.7%	$702,037,157	6.2%	$889,475,559	6.2%
1999-2000	101,260	-1.2%	$7,155	4.4%	$724,486,947	3.2%	$913,171,772	3.2%
2000-01	100,239	-1.0%	$7,433	3.9%	$745,125,604	2.8%	$983,658,423	2.8%
2001-02	99,372	-0.9%	$7,595	2.2%	$754,753,196	1.3%	$1,050,891,096	1.3%
2002-03	98,577	-0.8%	$7,830	3.1%	$771,843,123	2.3%	$1,043,650,716	2.3%
2003-04	98,663	0.1%	$8,043	2.7%	$793,517,773	2.8%	$1,178,801,920	2.8%
1994-98		1.2%		3.3%		4.6%		5.2%
1998-2001		0.1%		4.0%		4.1%		5.9%
2001-04		-0.5%		2.7%		2.1%		6.2%

Large increases in federal revenues since 1998 have helped increase MPS's total budget above what revenue limits allowed.

and total revenues rose about the same as the per student increase.

The bottom three rows of the table summarize the findings. The 1994-98 period was a time of increasing enrollments and the district's total revenue limit climbed 4.6% per year. The middle years saw enrollments rise and then fall, and growth in revenue limit dollars slowed somewhat. Finally, revenue growth during the 2001-04 period—a time of declining enrollment—was about half the growth in the preceding three years. Should MPS continue to experience declining student numbers, its total revenue limit will stagnate or decline.

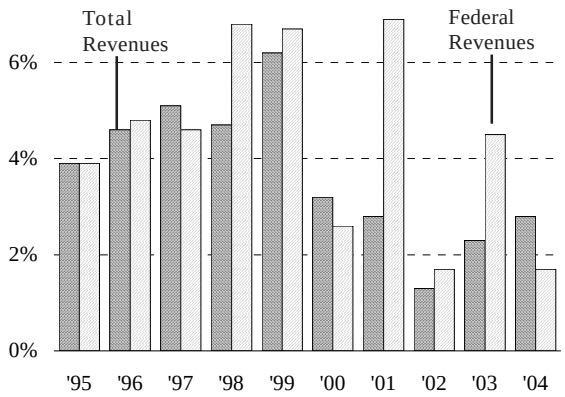
Other Revenues. While declining enrollments have affected a portion of MPS's revenues over the last several years, much of that impact has been muted by increased revenues from other sources. For example, from 1998-99 through 2003-04, federal aids to MPS rose 12.2% per year. These are primarily aids for special education. The chart above right shows annual increases in total Funds 10 and 20 revenues (dark bars) and federal aids (light bars). In 1997-98, 1998-99, 2000-01 and 2002-03, large increases in federal dollars help pull up increases in total MPS revenues.

In addition, borrowing and other revenues to fund capital expenditures outside the revenue limits were up sharply in 2001-02 and 2003-04. As a result, while MPS's revenue limit rose only 2.5% per year from 1998-99 through 2003-04, its total revenues (Funds 10 through 40) climbed 5.8% annually during those years.

Because of the surge in revenues outside the revenue limits, MPS's revenue limit has had slightly less impact on district finances in recent years. In 1993-94, revenues covered by the limits were 81.5% of all Funds 10 through 40 revenues (see chart on page 19). By 2001-02, that percentage was down to 71.8% and in 2003-04 it was 67.3%.

Federal Dollars Aid District

Revenue Limit as % of Total Revenues, 1994 - 2004



Part of the decline in recent years resulted from increased borrowing. In 2001-02 and 2003-04, MPS issued $70 million and $86 million in bonds. These amounts were significantly higher than the average $17.5 million issued from 1998-99 through 2000-01. Some of the bonds were issued as part of the Neighborhood Schools Initiative.

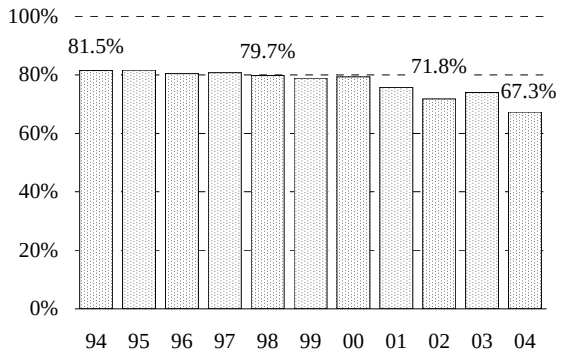
However, even after removing capital expenditures and borrowing costs and examining only revenues for current educational spending (Funds 10 and 20), total revenues climbed faster than the revenue limit totals. While revenue limit totals climbed 2.5% per year from 1998-99 through 2003-04, total Fund 10 and 20 revenues were up 3.4% annually. The difference was primarily due to rapidly-rising federal dollars.

Milwaukee Parental Choice Program

MPCP provides vouchers for some Milwaukee students from low-income families to attend private schools in the city. Participating students are not counted as MPS students for state aid purposes. As a result, the district's per student property values are higher than they would be without the program. Higher per student values mean less equalization aid for the district. In addition, MPS pays

Rev. Limit Declines Relative to Total Revenues

Revenue Limit as % of Total Revenues, 1994 - 2004



45% of the programs costs through a reduction in its state aids, though it can recoup those costs through higher property taxes.

MPCP affects MPS's finances through several channels. First, part of the change in revenue limit membership discussed previously was due to changes in MPCP in 1999. In that year, the state altered how MPCP students were counted for revenue limit purposes. In addition, there were changes in the way the program was funded.

Revenue Limit Effects. Prior to the 1999-2000 school year, a portion of MPCP students were counted in MPS's revenue limit calculation. Effectively, the difference between the number of current-year MPCP students and the number four years earlier was added to MPS's fall membership for revenue limit purposes. Since MPCP enrollments were rising during this period, MPS's revenue limit enrollments were higher than if the MPCP students were not counted. The additional students increased MPS's total revenue limit.

Beginning in 2000, MPCP students were not counted for revenue limit purposes. Much of the decline in revenue limit membership in that year (see table on page 17) was due to the legal change.

Further, many of the MPCP enrollments were students that would have attended MPS. Thus, increasing MPCP student counts played a role in MPS's continuing enrollment decline. This, in turn, affected MPS's revenue cap total from 2000 through 2004.

State Aids and Property Taxes. By law, MPS is required to pay 45% of the cost of MPCP. This is done through a reduction in its state equalization aids. However, because the district's total revenue limit is the sum of its state aids and property taxes, it can recoup the lost aids through the property tax levy. Thus, the cost of MPCP does not necessarily affect district finances, though it impacts the property tax burden.

The cost of MPCP does not necessarily affect district finances, though it impacts the property tax burden.

Reduced Class Sizes (SAGE)

The SAGE program was created by the state in 1996-97 to reduce class sizes in early grades, particularly for children from lower-income families. In the first year, 30 schools in 21 districts statewide participated. Of those, seven were from MPS.

The program was significantly expanded in 2000-01. In that year, a total of 576 schools participated in the program, compared to 78 the year before. A total of 88 MPS schools were in the SAGE program in that year. In recent years, the number of participating schools statewide has declined. In 2004-05, 524 schools statewide were in the program; 87 from MPS.

Finances. As of 2003-04, districts in SAGE receive $2,000 per participant. Each district must sign a five-year contract that requires it to:

- reduce class sizes to 15:1 in grades K-3;
- implement a rigorous, high-expectations curriculum;
- keep the school building open beyond regular school hours for community or student use; and
- give attention to professional development and staff evaluation practices.

In 2003-04, MPS received less SAGE aid than was required to fully fund the program. The additional funding came from general fund revenues.

There is concern among MPS officials that the $2,000 per student received from the state does not cover the costs of the program. If it costs MPS more than $2,000 per student, then the district must evaluate whether those extra expenditures are best served in the SAGE program or somewhere else.

The SAGE program is a school, rather than a district, program. Under the original legislation, a school was eligible to participate if at least 50% of its students were from low-income families. In 2000-01, the law was changed so that all schools were eligible. However, a district only receives SAGE aid for low-income students in participating schools. This makes a difference for whether or not the $2,000 per student covers a district's additional costs.

Consider an example: two schools, each with 75 students in each grade kindergarten through third. If these schools staffed their classes at 25 students per teacher, each would need 12 teachers. At 15 students per teacher, they would need 20 teachers. If the salary plus benefits cost of a teacher is $55,000, the additional eight teachers needed to bring the schools in compliance with SAGE would cost $440,000.

Now suppose that one school has 225 low-income students and the other has 150. The first school would receive $450,000 in SAGE aid, which is more than enough to cover the cost of the additional teachers. The second school would receive only $300,000, or about two-thirds of the additional costs.

To analyze the impact of SAGE on district finances, we examine the impact by school. We assume the cost of an additional teacher is $57,600 (salary plus benefits) and the student-teacher ratio would be 25-to-1 if the school did not participate in SAGE.

Under these assumptions, only 45 of the 87 participating schools received sufficient SAGE aid to cover their additional compensation costs in 2004-05; 42 received aid less than their costs. This does not account for the additional costs incurred for the other requirements of the law. Districtwide, additional compensation costs for SAGE are approximately $1 million more than the district receives in aid. MPS's internal analysis puts the SAGE gap for 2004-05 at more $13 million.

DISTRICT SPENDING

To understand MPS's cost drivers, we examine district spending by category, starting with the largest spending category, instruction. However, to evaluate whether district spending may be "too high" or "too low," some type of baseline is needed.

To put the district's spending in perspective, we compare MPS's expenditures with statewide averages (excluding Milwaukee) and with several comparable districts. The comparables are generally the largest districts in the state (Green Bay, Kenosha, Madison and Racine) and several smaller districts with "similar" demography (Beloit, Superior and Wausau).

Instruction

MPS's instructional spending is significantly above the state average, but below two of the six comparable districts (see table below). In 2003-04, MPS spent $6,416

MPS Instructional Spending High
Per Student Instructional Spending For Selected Districts, 2003-04

	Total Inst.	Spec. Ed.	Fund 10
MPS	$6,416	$6,512	$5,355
Beloit	6,351	7,471	4,917
Green Bay	6,054	8,090	4,414
Kenosha	5,941	8,263	4,707
Madison	7,035	10,383	5,131
Racine	6,130	9,115	4,479
Superior	5,613	9,654	4,390
Wausau	6,491	8,360	5,276
All Dist. ex. Mke	$5,835	$7,673	$4,715

per student on instruction. That was 10.0% more than the average of other districts statewide.

Relative to comparables, only Madison ($7,035) and Wausau ($6,491) were higher. MPS's instructional spending was 6.0% higher than Green Bay's ($6,054), 8.0% above Kenosha's ($5,941), 4.7% higher than Racine's ($6,130) and 14.3% above Superior's ($5,613).

To better understand why MPS is high, we break out instruction into several components. First, it can be separated into two broad areas. Most spending comes from the general fund (Fund 10) for "regular instruction." Districts also spend significant amounts on special education (Fund 27). Those two areas are examined next.

Special Education. MPS has a higher percentage of students classified as disabled than other districts (16.5% vs. 14.3%). Since the cost of educating disabled students is generally higher than for educating others, one might expect this to be one area driving MPS's higher instructional costs. However, the data show MPS's instructional spending on disabled students is significantly below average.

In 2003-04, MPS identified 16,017 children as having some form of disability. The district allocated $104.3 million to its special education fund, or $6,512 per student. The statewide average (excluding Milwaukee) was $7,673. Thus, MPS's per student special education instruction expenditures were 15.1% less than other districts.

Among the "comparable" districts, all had per student instructional spending for special education above MPS's. Beloit ($7,471) was nearest to MPS and the only district among the comparables that was below the state average. Madison ($10,383) was highest, more than 35% higher than the statewide norm.

There can be several reasons for these differentials. First, not all students identified as needing special education services receive them from the district. Thus, if a smaller share of MPS special needs students actually receive services, their costs per student served would be higher than estimated here.

Further, some students with special needs receive limited special education services. In these cases, the district would account for a large portion of their instructional costs in the general fund. Thus, if MPS has more of these students, their cost per special education student would be lower.

MPS's reported per student special education instructional expenditures were 15% below the state average.

Finally, MPS administration notes that many special education services provided by the district are provided by staff that are not certified in specific areas. Only salary and benefit costs for certified personnel are eligible for reimbursement through special education categorical aids. Thus, these costs, even though they may be "special education" costs, are accounted for in Fund 10 rather than Fund 27. Thus, MPS's *reported* special education costs are below its incurred costs.

General Fund. As the table on page 20 shows, MPS's per student general fund instructional spending was 13.5% above the statewide average and higher than all comparable districts. MPS's spending was approximately 20% higher than in Green Bay, Racine and Superior.

MPS Per Student Compensation Above Average

Per Student Instructional Salary and Benefit Costs
For Selected Districts, Fund 10, 2003-04

	Total Comp.	Salaries	Benefits
MPS	$4,392	$2,908	$1,484
Beloit	4,544	3,173	1,371
Green Bay	4,063	2,881	1,182
Kenosha	4,417	2,887	1,530
Madison	4,830	3,465	1,366
Racine	4,156	2,755	1,401
Superior	4,164	2,952	1,212
Wausau	4,666	3,370	1,296
All Dist. ex. Mke	$4,306	$3,020	$1,286

Per student benefit costs at MPS were nearly $200 above other districts statewide.

A detailed breakdown of Fund 10 spending highlights the areas in which MPS spending differs from the state average and from other comparable districts.

Compensation comprises the majority of instructional spending. In the districts studied, it ranged from 82.0% in MPS to 94.9% in Superior.

Only a small portion (13.4%) of MPS's higher instructional spending is due to above average total compensation. The district spent $4,392 per student on instructional salaries and benefits in 2003-04, 2.0% above the state average and higher than three of the seven comparable districts (see table on page 21). Madison's instructional compensation was highest among the districts studied.

The table shows MPS was below the state average in per student salary costs (instruction only), but above in benefits. Per student instructional salaries were $112 less than the state average. Relative to comparable districts, MPS was in the middle. Three districts (Green Bay, Kenosha and Racine) had lower salary costs; the other four had higher.

Per student benefit costs at MPS were significantly higher than the state average. The district was nearly $200 per student (15.4%) above other districts statewide. Among the comparable districts, only Kenosha had higher per student benefit costs. A more detailed examination of compensation costs across all funds begins on page 25.

Two other spending categories accounted for most of the remaining difference between MPS instructional spending and spending statewide. Purchased instruction was one-third of the difference; purchased services was 43% of the gap.

Purchased instruction is mainly tuition payments to other districts for open enrollment students or to other agencies for non-open enrollment students. MPS spent $212 per student more on purchased instruction than districts statewide. Of that amount, $164 (77.2%) was payments for instructional services provided by private or nonprofit organizations. The remainder was payments for open enrollment students ($5,446 per participating student).

MPS also spent $330 per student on purchased services, which was above the statewide average of $53. Nearly all of the difference can be accounted for in spending on "personal services" for undifferentiated curriculum. Personal services are defined as "services performed by individuals, not district employees, with specialized skills and knowledge." Undifferentiated curriculum is for grades in which faculty teach all subject areas (generally K-6).

MPS spent $312 per student for these personal services, compared to only $10 statewide. Even among the comparable districts, the highest spending in this area was in Wausau ($26 per student).

Administration

MPS's per student spending for administration was 18.7% above the state average in 2003-04. At $899 per student, administration costs were above all comparable districts by at least $110. The table below shows these expenditures for MPS and for the comparable districts.

Spending for administration comprises three parts: general administration; school building administration; and fiscal operations.

MPS Administration Spending Above Average
Per Student Administration Spending For Selected Districts, 2003-04

	Tot. Adm.	Gen'l	School	Other
MPS	$899	$212	$615	$72
Beloit	752	122	521	109
Green Bay	587	71	463	53
Kenosha	579	47	477	55
Madison	786	82	625	79
Racine	644	110	478	56
Superior	730	170	493	67
Wausau	591	53	460	78
State ex. MPS	$757	$180	$470	$107

General Administration. Spending on general administration includes activities of the school board, district administrator, community relations administrators, and state and federal relations, including grant procurements. MPS spent $212 per student on general administration, or 17.4% more than other districts. All of the comparable districts spent less than the state average.

Most of the general administration expenditures were for salaries and benefits. At MPS, 87.0% of these expenditures are compensation, significantly above the state average (72.1%). Salary expenditures per student at MPS were $121 per student ($11.9 million total) compared to an average of $95 at other districts. Among the comparable districts, the highest per student salary expenditure was in Superior ($78).

Benefit costs were $63 per student compared to $35 elsewhere. Benefit costs were 52% of salaries at MPS. Only Kenosha (51.6%) was similarly high. The state average was 37.4% and all other comparable districts, except Beloit (43.6%), were near that percentage.

School Administration. On average, costs associated with school building administration were 62% of total administration costs. At MPS, they were slightly higher, 68.5%.

MPS's ($615) expenditures for school building administration were 30.9% higher than the average of other districts statewide ($470). Among comparable districts, only Madison ($625) was higher.

Nearly all (97.2%) of MPS's expenditures for school building administration are salaries and benefits. Per student salaries for school building administration were $396 at MPS, compared to $306 statewide. MPS's benefit costs were $202 compared to $132 elsewhere.

Numbers of Administrators. While MPS's administration costs tend to be above average, the number of administrators appears to be more in line with other districts. The table at right shows numbers of administrators, students per administrator and average compensation.

Several items stand out in the tables. First, MPS has significantly more assistant principals, given its size, than other districts. At one per 541 students, MPS has at least double the number of most other comparable districts. A low number of students per administrator translates to more administrators given a districts student count. Wausau (875 students per assistant principal) is the only other district under 1,000.

Administrators and Compensation

Numbers of Administrators and Average Compensation, 2003-04

	District Administer					Principal				
			Average Compensation					Average Compensation		
	No.	Stud's Per Adm.	Sal.	Ben.	Total	No.	Stud's Per Adm.	Sal.	Ben.	Total
MPS	1.0	97,359	$122,360	$49,045	$171,405	152.0	641	$71,705	$33,948	$105,653
Beloit	1.0	6,941	104,143	20,800	124,943	14.0	496	73,626	14,845	88,471
Green Bay	1.0	20,297	130,246	39,143	169,389	35.0	580	79,217	28,112	107,329
Kenosha	1.0	21,426	130,000	34,069	164,069	36.8	583	84,427	24,294	108,721
Madison	1.0	24,913	159,276	63,710	222,986	47.0	530	83,383	33,353	116,736
Racine	1.0	21,457	140,100	53,028	193,128	30.3	709	74,500	30,566	105,066
Superior	1.0	4,938	106,972	43,336	150,308	10.0	494	72,853	29,419	102,272
Wausau	1.0	8,746	125,107	40,808	165,915	16.2	540	78,503	28,456	106,960

	Assistant Principal					Other Administrators				
			Average Compensation					Average Compensation		
	No.	Stud's Per Adm.	Sal.	Ben.	Total	No.	Stud's Per Adm.	Sal.	Ben.	Total
MPS	180.0	541	$61,088	$30,830	$91,918	87.0	1,119	$63,736	$29,358	$93,093
Beloit	5.9	1,176	69,616	14,221	83,837	9.0	771	75,955	15,318	91,274
Green Bay	16.0	1,269	74,936	27,740	102,676	12.0	1,691	90,203	29,925	120,128
Kenosha	13.0	1,648	76,114	25,476	101,590	10.0	2,143	99,991	28,901	128,892
Madison	23.0	1,083	71,988	28,795	100,783	30.3	824	82,122	32,849	114,971
Racine	20.5	1,047	60,208	24,259	84,467	20.0	1,073	77,696	32,758	110,454
Superior	4.0	1,235	65,397	27,792	93,189	3.0	1,646	85,172	35,058	120,230
Wausau	10.0	875	67,836	26,201	94,037	10.0	875	84,794	28,928	113,722

MPS had 1.2 assistant principals for every principal in the district. The next highest ratio was Racine with 0.7. Part of the reason for the high number of assistant principals could be the district's move to decentralization. Also, the assistant principals may be doing some of the duties that other administrators perform in other districts. For example, if we calculate the number of students relative to the total number of administrators, MPS (232) is more in line with the other districts: Beloit (232), Green Bay (317), Kenosha (353), Madison (246), Racine (299), Superior (274) and Wausau (235).

MPS spends its student services dollars differently than other districts. It focuses on social work and psychological services; other districts spent significant amounts on guidance.

The second item that stands out is related to compensation. MPS administrator compensation seems to be in line with other districts—it generally falls in the middle of the group. However, benefit costs are among the highest. For example, average benefits for principals and assistant principals are highest among the districts studied.

Transportation

MPS's student transportation costs were more than 50% above the average of other districts statewide. The district spent $600 per student, or more than 60% above the average of other districts ($373). Among the comparable districts, Superior ($439) and Racine ($433) had the highest spending. Beloit only spent $179 per student.

Unfortunately, transportation spending is not disaggregated enough to determine where significant differences come from.

Student Services

Student service expenditures are for items such as social work, guidance counseling, health and psychological services, attendance, and occupational and physical therapy.

Although MPS's expenditures were above the state average in this category, they were less than the most comparable districts. MPS spent $485 per student on student services, or 15.1% above the average of other districts statewide ($421). However, among comparable districts, only Racine ($463) and Wausau ($400) spent less than MPS (see table below).

It appears that special education student services are driving the higher costs for MPS and the comparable districts relative to the state. Statewide, student services costs for special education students were approximately 40% of the total. Among the seven comparables plus MPS they were about 60%, and at MPS they were 72%.

The average special education student service cost for the eight districts was $315 per student, compared to a statewide average of $168. MPS spent $349 per student here.

Among the various components of pupil services, MPS tends to spend their dollars in different ways than other districts. Statewide, districts spent $36 per student on social work and $70 per student on psychological services. MPS spent more than three times ($118) the state average on social work and nearly double ($131) on psychological services. Most of the comparable districts spent much less. Madison ($179 and $132) was the exception. The Madison school district spent 56% more than MPS on all student services.

Student Services Spending

Total Per Student Spending on Pupil Services and Its Components, 2003-04

	Pup. Serv.	Dir. of Pup. Serv.	Soc. Work	Guidance	Health	Psych. Serv.	Speech/ Audio.	Attend.	Occ./Phys. Therapy	Other
MPS	$485	$0	$118	$62	$28	$131	$1	$27	$34	$83
Beloit	535	8	95	167	66	98	0	0	49	51
Green Bay	534	10	109	191	9	64	4	1	78	69
Kenosha	544	8	64	213	45	63	0	48	41	62
Madison	758	1	179	138	146	132	0	3	158	0
Racine	463	0	89	169	41	87	0	1	62	15
Superior	503	88	0	240	49	70	0	0	57	0
Wausau	400	0	51	197	32	71	0	20	28	0
State ex. MPS	$421	$8	$36	$192	$36	$70	$0	$8	$50	$20

Instructional Support

Instructional support services include spending on the supervision and coordination of athletics and special education, among others, and library and staff services. The latter includes curriculum development and staff training.

The table on page 25 shows per student instructional support spending for the districts studied. Similar to other spending categories, MPS spending was among the highest—only Madison was higher.

However, what is more interesting is the distribution of spending. MPS spent more than half (56%) of their instructional support dollars on staff services. In the other districts, that percentage ranged from 22% to 44%.

Further, MPS allocated only 11% of their instructional support dollars to library services. All other districts spent at least one third there. Nearly half of MPS's staff services spending was in the "other" category; only Green Bay had a similarly high percentage for that category. Other districts spent less than 19% there.

MPS spending on library services was comparatively low. At $64 per student, the district spent less than one half the next lowest-spending district (Superior, $141).

Instructional Support Spending

Total Per Student Spending on Instr. Supp. Services and Its Components, 2003-04

	Instr. Supp.	Staff Serv.	Library	Super./ Coord.	Other
MPS	$581	$328	$64	$175	$13
Beloit	561	213	218	130	0
Green Bay	539	122	187	205	24
Kenosha	507	125	292	81	9
Madison	652	284	199	165	4
Racine	450	148	187	66	49
Superior	269	71	141	50	7
Wausau	411	134	154	112	11
State ex. MPS	459	120	217	104	17

COMPENSATION

Compensation is by far the largest cost for a school district. In some districts, these costs top 80% of expenditures. Because they are a major driver of spending, we analyze them separately here.

Compensation is examined in several ways. Each is dependent on the type of data available. First is a broad examination of compensation—both salaries and benefits—within the context of various spending categories. Second is a discussion of salary and benefits per student for instructional personnel. Finally, average teacher salaries and benefits are explored along with average experience levels. In addition to examining the MPS situation, compensation is compared statewide. This will provide a better understanding of how MPS compares with other school districts.

In 2004, approximately 75% of MPS's Funds 10 and 20 spending was for compensation. That figure was down from more than 80% in 1992-93.

By Spending Category

In 2004, approximately 75% of MPS's Funds 10 and 20 spending was for compensation. Nearly half (49.4%) of all spending was for salaries, and an additional 25.7% was for employee benefits.

These percentages have changed significantly over the last 11 years. Total compensation as a share of total expenditures has fallen, as has the share devoted to salaries. However, benefits have risen as a share of total spending.

In 1992-93, compensation costs were 80.9% of MPS's expenditures (Funds 10 and 20). That percentage has fallen steadily, reaching 75.2% in 2003-04. One reason for the decline is an increase in the amount of purchased services. While Fund 10 expenditures rose 37.4% from 1992-93 through 2003-04, purchased services rose 486% during these years. By purchasing these services, the district indirectly pays compensation costs, but it does not show up in the accounting.

While total compensation has become a smaller portion of the district's expenditures, salaries and benefits have

moved in opposite directions. This is largely a result of the interaction between the Qualified Economic Offer (QEO) law and rising health care costs.

From 1992-93 through 2003-04, salaries as a share of Funds 10 and 20 expenditures declined from 59.4% to 49.4%. During those same years, expenditures on benefits rose from 21.4% of the total to 25.7%.

From 1999 through 2004, per student compensation costs at MPS increased 17.3%. That increase was less than the state average (21.4%).

Instruction. Instruction is MPS's largest spending category. Compensation accounts for a significant share of that spending. At MPS, compensation was 88.9% of instructional costs in 2003-04. However, that was well below the state average (93.2%) and placed MPS 399th out of 426 school districts.

At MPS, less than 60% of instructional spending was for salaries, placing the district 408th. However, spending for fringe benefits was 30.1% of spending, 121st highest in the state. In many of the comparisons, we find benefit costs high relative to other districts, but costs for salaries relatively low.

Per Student

A second way to examine compensation costs is on a per student basis. Using instructional salaries and benefits, we calculate per student compensation costs. These figures not only account for average salaries and benefits, but also for the number of instructional personnel relative to the number of students. Thus, higher per student figures can be the result of higher compensation or more instructional personnel.

Since 1999, benefit costs have risen more than four times faster than salaries.

In 2003-04, MPS's total instructional compensation costs per student totalled $5,407. That ranked the district 127th and was 2.0% above the state average ($5,299). Again, salary costs were relatively low ($3,579, 190th and 2.7% below average) but benefits were high ($1,820, 76th and 12.3% above average).

Since 1999, benefit costs have risen more than four times faster than salaries. However, the per student changes were all below the state average. At MPS, total compensation per student climbed 17.3% over the five years. That was less than the state average (21.4%) and 311th highest.

During the period, per student benefit costs rose 34.4% (354th), which was below the state average (43.6%). Salaries per student rose only 10.2%. That was 293rd in the state and also below the state average (13.7%).

The QEO along with rising benefit costs clearly affect the salary increase. However, teacher turnover may account for part of the below average increases. That is discussed below.

Teacher Compensation

Wisconsin DPI reports information on average teacher salaries and benefits for each school district. In addition, they provide information on average experience levels. This allows for several comparisons of MPS with the rest of the state. The data are for all teachers with at least a nine month contract and a full-time equivalency of at least 84%.

Average Compensation. According to DPI figures, the average 2005 teacher salary in MPS was $35,129 (see table on page 27). That ranked MPS (419) among the lowest districts in the state and was well below the median district ($43,038). These figures show the average salary declining since 2002. Part of this could be due to a general decline in experience levels (see page 27).

Benefits for the average teacher were $21,439, or approximately 61% of salary. MPS's state rank on benefits (136) was above its salary rank. The median district paid $20,324 per teacher in benefits.

Combined, MPS's average total compensation was $56,568, or 382nd statewide. In the median district, compensation averaged $62,955.

Experience. While MPS is near the average in salaries and benefits, its teachers have significantly less experience than teachers in other districts. DPI reports both local

and total experience. (Note that in 2001 and 2002, MPS reported the same figures for local experience as for total experience.)

In 2004-05, the average MPS teacher had 9.94 years of local experience and 9.97 years of total teaching experience. The average teacher in the median school district had 12.83 years of local experience and 15.33 years of total teaching experience. Thus, the average MPS teacher had about 23% less local experience and 35% less total experience that the average teacher in the median district.

Further, while average experience levels have been generally declining statewide, experience in MPS has fallen faster. Average local experience statewide dropped 4.6% from 13.45 years in 1998 to 12.83 years in 2005. MPS's decline during those years was 15.2% (11.72 to 9.94). This provides some evidence that turnover at MPS is significantly higher than in other districts. As newer teachers replace those with more experience, salary and benefit costs are generally reduced. That is one reason total compensation costs at MPS have risen more slowly than the state average.

Relative Compensation. Combining the average total compensation (salaries plus benefits) figures with average experience levels shows MPS ranks high in compensation per year of experience.

In 2005, total compensation per year of local experience at MPS was $5,930, more than 20% above the state average ($4,885). Relative to total experience, compensation at MPS averaged $5,674 per year, 38.7% above the state average of $4,092.

Average experience levels at MPS are lower and have declined faster than the statewide average.

Salary Schedules

A final way to examine teacher pay is to compare salary schedules. Teachers are paid based on negotiated schedules that provide pay rates that depend on a teacher's education and experience. Portions of these schedules are published by the Wisconsin Association of School Boards (WASB). The last year for which WASB published MPS data was 2002-03.

In that year, starting pay for an MPS teacher with no experience was $29,224, or about $1,700 more than the median district ($27,534). The maximum that a teacher without a master's degree could earn was $45,802, or $7,148 more than average ($38,654).

The base salary for an MPS teacher with a master's degree was 32,910. Statewide, the median was $30,718. The maximum salary at MPS ($62,368) was 22.5% higher than the statewide median ($50,893).

Average Teacher Pay, Benefits and Experience
MPS and Statewide Median, 1998 - 2005

	Average Salary			Average Benefits			Average Local Exp.			Average Total Exp.			Comp. Per Loc Exp.			Comp. Per Exp. Year		
Year	MPS	Rk.	Median	MPS	Rk.	Median	MPS	Rk.	Median	MPS	Rk.	Median	MPS	Rk.	Median	MPS	Rk.	Median
1998	$39,941	113	$37,330	$14,397	95	$13,333	11.72	342	13.45	12.00	407	15.78	$4,636	44	$3,767	$4,528	10	$3,264
1999	$41,788	99	$38,690	$14,303	152	$13,871	11.48	345	13.29	11.71	411	15.70	$4,886	39	$3,956	$4,790	8	$3,399
2000	$42,736	85	$39,254	$14,943	118	$14,072	11.58	324	12.99	13.16	376	15.45	$4,981	47	$4,107	$4,383	20	$3,501
2001	$44,017	76	$40,222	$17,452	21	$14,737	11.26	321	12.65	11.26	405	15.15	$5,459	42	$4,345	$5,459	4	$3,657
2002	$42,791	120	$40,633	$23,595	1	$15,787	10.17	377	12.63	10.17	417	15.11	$6,528	10	$4,467	$6,528	1	$3,765
2003	$41,842	180	$41,099	$18,777	164	$18,237	9.83	386	12.69	9.83	425	15.27	$6,167	31	$4,678	$6,167	2	$3,888
2004	$36,173	389	$41,183	$21,827	67	$19,644	9.82	396	12.73	10.26	422	15.39	$5,906	9	$4,780	$5,653	1	$3,928
2005	$35,129	419	$43,038	$21,439	136	$20,324	9.94	401	12.83	9.97	422	15.33	$5,930	58	$4,885	$5,674	13	$4,092

MPS's base salary schedule for teachers with bachelor's degrees or master's degrees were 6% to 7% above the state-

PART III: LOOKING AHEAD

FINANCIAL FORECASTING

Estimating MPS's future revenues and expenditures is difficult. Revenues are largely determined by state-imposed limits that depend on hard-to-predict enrollments. MPS also relies more on state categorical aids and federal dollars than most districts. Projecting these requires assumptions about future policy and political decisions.

Forecasting expenditures is even more difficult, particularly with MPS in a period of flux and transition. To avoid some problems, we project expenditures in aggregate, rather than by individual spending category. We also provide several scenarios, each with its own assumptions.

We know that MPS is likely to have to pare expenditures to match revenues. Thus, this section begins with an estimate of district revenues. Then, given past trends and predicted enrollment changes, expenditures are projected. Finally, we show the kinds of reductions that may be required to match expenditures and revenues.

What Are We Forecasting?

Ideally, we want to forecast all revenues and expenditures. However, several factors make it more reasonable to limit the forecasts to "education dollars," i.e., Funds 10 and 20.

First, MPS's debt issuance has been volatile. Trying to project debt issuance three or four years out will only add significant error to forecasts. Second, the food service account is typically funded with state and federal dollars. In some years, MPS supplemented those dollars with education dollars, but that has been limited; and we believe it is not likely to occur in the future.

Thus, our forecasts are limited to Funds 10 and 20, which account for more than 80% of all MPS revenues and expenditures.

Revenues

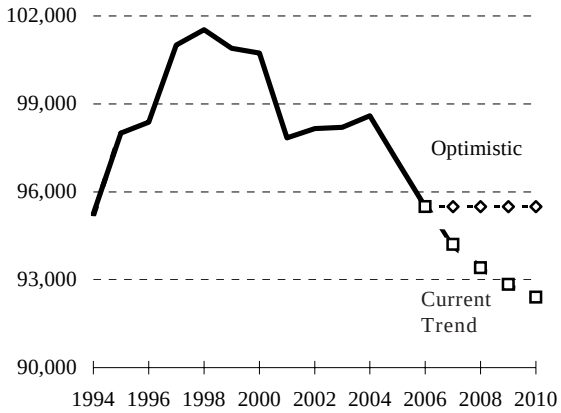
At MPS, dollars regulated by state revenue limits are approximately 77% of funds 10 and 20 revenues. Federal and state categorical aids account for much of the rest. The total amount MPS is able to generate through its revenue cap depends on its fall enrollment, as well as state law. To forecast these amounts, we first need to estimate future enrollments and state revenue-limit policy.

MPS's enrollments are projected to decline from more than 97,000 in 2003-04 to 92,399 in 2009-10.

Student Counts. The MPS enrollment projections presented here are based on student counts by grade from 1999-2000 through 2004-05. Data through 2003-04 are from DPI; 2004-05 data are from MPS.

Projections are based on "grade-progression ratios," i.e. enrollment in each grade relative to enrollment in the previous grade for the prior year. For example, 2003-04 second grade enrollments totalled 6,868. In 2002-03, the number of first-graders was 7,152. Thus, the 2003-04 2nd grade ratio was 0.96 (6,868 / 7,152). These ratios are calculated for each grade (except pre-kindergarten and four-year-old kindergarten) and for all years. Pre-K and K4 (four-year-old kindergarten) are estimated separately. We

MPS Student Counts To Continue Falling?
Enrollments and Projections, 1994 - 2010



Federal school aids are projected to decline over the next several years.

then apply the median progression ratio for each grade to forecast enrollments.

Based on this analysis, MPS enrollments are projected to decline from more than 97,000 in 2003-04 to 92,399 in 2009-10 (see chart on page 29). These estimates are sensitive to changes in assumptions. For example, we assume K4 enrollments increase 2% per year. However, should they rise 3% per year, total enrollments in 2009-10 increase to 93,488, or about 1,000 more students. Similarly, if they grow only 1%, 2009-10 enrollments fall to 91,388.

The forecasts do not account for recent changes to MPCP (Choice). While the expansion of the program will likely affect MPS enrollments in some way, the magnitude of the effect is unknown.

Revenue Limit Policy. For 2005-06, the state-mandated increase in per student revenue limits was $248.48, or 3.1% more than the 2004-05 figure. Without law changes, the increase grows at the rate of inflation (March over March). Based on January 2006 estimates, the 2006-07 percentage change in the allowable increase would be approximately 3.5%. At that rate, the allowable increase would rise to $257.18 in 2006-07. We assume a 2.5% increase in subsequent years, consistent with inflation forecasts in the Wisconsin Department of Revenue's most recent economic outlook.

Due to recent state financial problems, the 2005-07 budget originally passed by the state legislature provided allowable revenue-limit increases of $120 in 2005-06 and $100 in 2006-07. These amounts were increased by gubernatorial veto. Considering the state continues to have fiscal challenges, it is possible that the lower limits could be approved in the 2007-09 budget. To account for this, we also forecast revenues assuming a more pessimistic revenue-limit increase of $120 per year in 2007-08 through 2009-10.

Other Revenues. In addition to dollars subject to revenue limits, MPS receives significant amounts from state categorical aids and federal dollars that are not limited. The district also has miscellaneous revenues. Increases in each of these categories have fluctuated from year to year.

To forecast these amounts, we used several approaches. First, we examined the per student increases from 2000 through 2005. Because per student amounts were also somewhat volatile, we examined the two-year averages for the same time period (1999-2000 through 2004-05). Second, we examined trends in total state categorical aids and federal aids.

MPS's categorical aid history is mixed. From 2002-03 through 2004-05, the total was roughly unchanged. However, it increased in the three years prior to 2002-03. On a per student basis, it rose significantly in 2000-01 and 2001-02, before falling in the most recent three years studied.

Revenue Assumptions

Baseline:

- Enrollments decline from more than 97,000 in 2003-04 to 92,399 in 2009-10.
- Revenue-limit policy remains as is and per student revenue increases grow at the rate of inflation.
- Per student state categorical aids remain constant at their 2002-03 through 2004-05 average.
- Per student federal aids decrease at the national rate.

Optimistic:

- ***Enrollments remain unchanged***.
- Revenue-limit policy remains as is and per student revenue increases grow at the rate of inflation.
- Per student state categorical aids remain constant at their 2002-03 through 2004-05 average.
- ***Per student federal aids remain unchanged.***

Pessimistic:

- Enrollments decline from more than 97,000 in 2003-04 to 92,399 in 2009-10.
- ***Per student revenue limits increase $120 per year.***
- Per student state categorical aids remain constant at their 2002-03 through 2004-05 average.
- Per student federal aids decrease at the national rate.

Statewide, these aids rose 8% from 2000-01 to 2002-03, but have since declined to near their 2000-01 level. Given this uneven history, we assume that per student categorical aids remain constant at the average of their 2002-03 through 2004-05 level. Since we are projecting a decline in enrollments, total categorical aids to MPS would fall slightly.

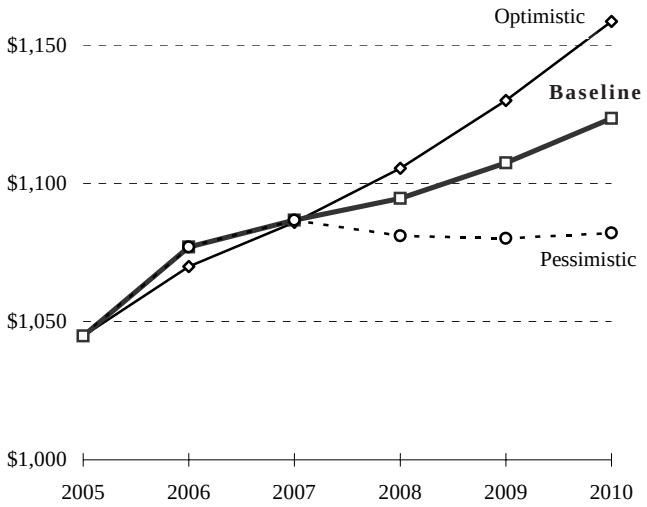
Receipt of federal dollars is also uneven. MPS had some years with large increases and others with small ones. However, changes in MPS's total federal dollars tracked nationwide changes. From 2000 through 2005, total federal aids were up 86%; MPS had a 71% increase.

The White House budget office projects that, after a 5% increase in 2005-06, federal education spending will decline between 2.1% and 3.1% in each year until 2010. We assume MPS's per student amounts change by the same percentage as total federal expenditures.

Forecasts. The chart below shows three revenue forecasts: a middle or baseline projection, plus two alternatives, one optimistic, one pessimistic.

Revenues to Rise ... Slowly

Projected Revenues, 2005 - 2010 ($ Millions)



Baseline. District revenues climbed 3.3% per year from 1999-2000 through 2004-05. Under baseline assumptions of declining enrollment, current state revenue-limit policy, and the federal and state aid changes outlined above, revenues would increase an average of 1.5% per year from 2004-05 through 2009-10 (see middle, bold line in chart).

Under baseline assumptions, MPS's revenues would grow an average of 1.5% per year through 2009-10.

Optimistic. The optimistic scenario assumes student counts and federal per student revenues are both unchanged after 2005-06 (they decline slightly under the baseline scenario). Under these assumptions, MPS's revenues rise an average of 2.1% per year through 2009-10, or 0.6 percentage points above the baseline.

Pessimistic. The pessimistic (lowest of the three lines) estimate assumes enrollment growth is one percentage point less than baseline assumption and per student revenue limit increases beginning in 2007-08 are only $120 per student. The lower revenue-limit assumption has a large impact because affected dollars—state aids and property taxes—comprise about three-fourths of district revenues. Under these assumptions, total revenues rise through 2007 and then remain largely unchanged through 2010.

Expenditures

Typically, the district estimates its revenues, and adjusts its expenditures accordingly. We assume MPS will continue this practice. However, we forecast expenditures using a different approach. Spending is not automatically tied to revenues. Rather, for each expenditure forecast, we examine past trends and carry them forward. The result is an estimate of future spending if current trends hold.

An alternative approach distinguishes compensation (total salaries and benefits) and noncompensation (e.g. the purchase of books or the leasing of copy machines). This is useful because we know something about compensation trends. Under the state's QEO law, compensation will grow about 4% if staff size remains the same. With staff

Expenditures are projected to be above revenues for the next several years.

Expenditure Forecast Assumptions
Avg. Annual Increases

	Method	
	A	B
Per Student Spending	2.9%	na
Compensation	na	2.5%
Noncompensation	na	3.5%
Enrollment	-1.0%	0.0%

reductions, the total would increase less. We make assumptions about total compensation and noncompensation growth to forecast expenditures through 2010 (see table below, left).

Spending Trends. The first (Method A) of two expenditure forecasts is based on assumptions about trends in per student expenditures. From 1993 through 2005, annual increases in per student expenditures ranged from 0.6% in 2004 to 7.8% in both 1999 and 2001. The median increase during the period was 3.1%; the average was 4.1%. For 2000-2005 only, the median increase in per student expenditures was 2.9%; the average was 4.3%.

We are conservative and apply the lowest growth rate (2.9%) to per student expenditures. The forecasted per student amounts are multiplied by the projected number of students to arrive at total expenditures.

The second (Method B) forecast treats compensation and non-compensation separately. From 2000 through 2005, total compensation rose an average of 3.1% per year. On a per student basis, the increase was 3.6%. On a per-staff basis, the annual increase was 3.0%.

However, in 2004 and 2005, increases were smaller. In 2004, total compensation declined 1.3%; in 2005, it was up only 1.5%. During those same years, non-compensation costs rose 6.8% and 5.1%, respectively. Staff reductions were responsible for the small change in compensation. However, given recent staff cuts, large reductions in the near future seem less likely.

Based on these past trends, we assume total compensation will grow 2.5% annually. Implicit in this assumption is total compensation increases in line with the QEO. To restrain compensation costs to a 2.5% increase, there would also have to be some staffing reductions.

Non-compensation costs are growing faster than compensation. Again to be conservative, we assume per student increases of these expenditures at half the 2003-2005 rate. We then multiply the per student forecasts by the projected number of students to arrive at total non-compensation spending.

Spending Projections. Two spending projections are presented here. Method A assumes a 2.9% annual increase in per student expenditures along with our baseline decline in enrollments. Method B assumes a 2.5% annual increase in total compensation and a 3.1% annual increase in non-compensation costs per student (see table at left).

The first chart on page 33 (left) shows expenditure projections using Method A (heavy line) along with our previous revenue projections (light lines). Expenditures are projected to grow significantly faster than revenues under baseline and pessimistic assumptions.

Caution should be used when interpreting the chart. The expenditure forecast assumes declining enrollment, consistent with the baseline and pessimistic revenue assumptions. The optimistic revenue scenario assumes stable enrollments. If we were to assume stable enrollments in our expenditure forecasts, spending would be higher than shown on the chart.

The second chart (page 33, right) displays costs if compensation rises 2.5% per year and noncompensation increased 3.5% annually. Under these assumptions, spending obligations grow faster than under previous assumptions. In 2010, Method B spending would be $1.184 billion compared to $1.166 billion with Method A.

Since spending is higher, the gap between projected revenues and expenditures is also greater than under the previous scenario (Method A). These revenue-spending gaps are now addressed.

Revenue-Spending Gaps

As seen in the two charts on page 33, under three plausible revenue scenarios, MPS expenditures exceed revenue over the next several years. This section focuses on those gaps under various scenarios.

The three charts on page 34 show the gaps between projected revenues and expenditures for each of the three revenue assumptions: baseline, pessimistic, and optimistic. Within each chart, the revenue-expenditure gap is shown for each of the two expenditure forecasts (A, solid bar; B, dashed)

Baseline Revenues. Under the baseline revenue scenario (top chart on page 34), the gap between revenues and expenditures grows from 2007 through 2010. Should per student expenditures increase at 2.9% per year (Method A), the gap grows to $42.3 million in 2010. Under the alternate spending assumptions (Method B), where compensation climbs 2.5% annually and noncompensation 3.5%, the gap would reach $60.6 million in 2010.

Pessimistic Revenues. Under the pessimistic revenue scenario (middle chart on page 34), the revenue-spending gaps are much greater than under the baseline assumptions. With revenues essentially unchanged from 2007 through 2010 (see chart, page 31), the revenue-spending gaps in 2010 reach $83.8 million (Method A spending assumptions) and $102.1 million (Method B assumptions).

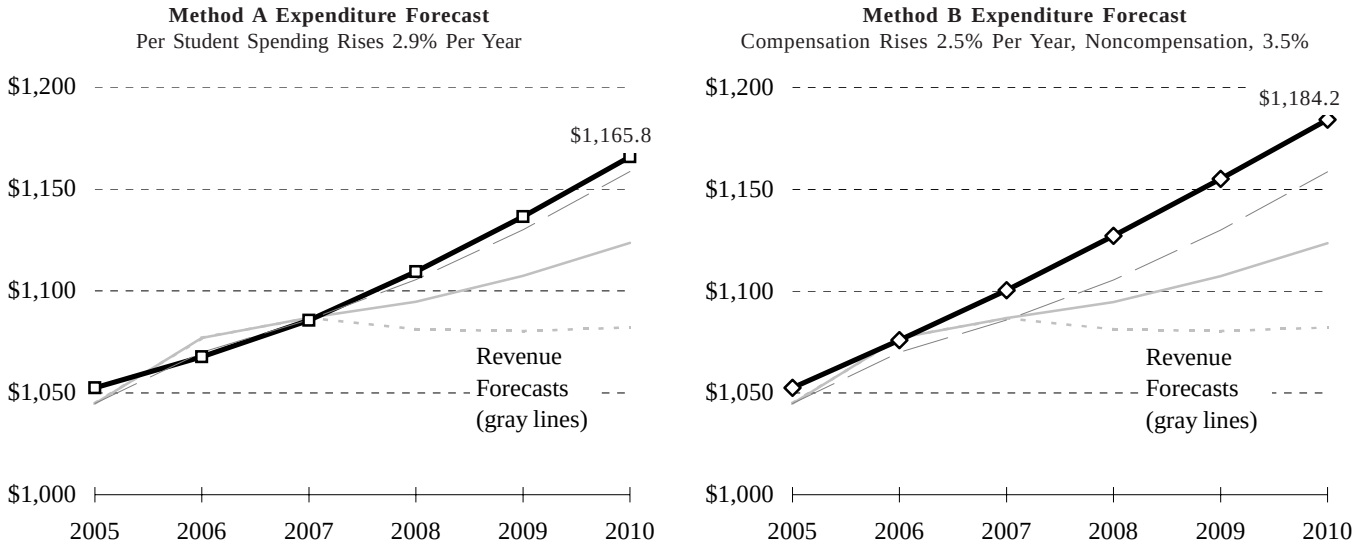
Optimistic Revenues. Even under the optimistic revenue scenario, MPS expenditures are projected to exceed revenues. As the bottom chart on page 34 shows, even if enrollment remains unchanged, the gap between revenues and spending could reach $67.3 million in 2010. Under the alternative spending scenario (Method B), the gap would be less than $30 million.

Under most plausible scenarios, MPS would have an increasing gap between revenues and expenditures.

Summary

Under any realistic projection, MPS's spending will increase faster than available revenues if current trends are continued. Due to demography and market dynamics, the number of students MPS serves is likely to continue declining over the next several years. Since the district's revenue limits as set by the state are tied to enrollment,

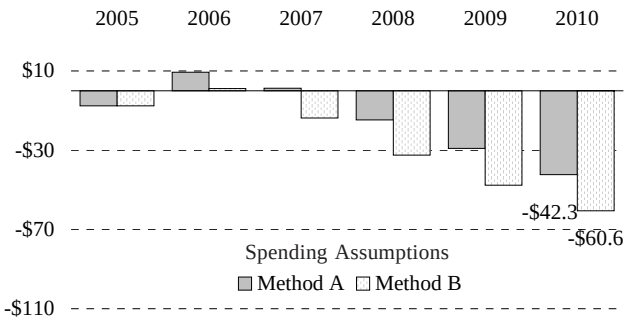
Expenditures To Rise Faster Than Revenues?
Projected Expenditures, 2005 - 2010 ($ Millions)



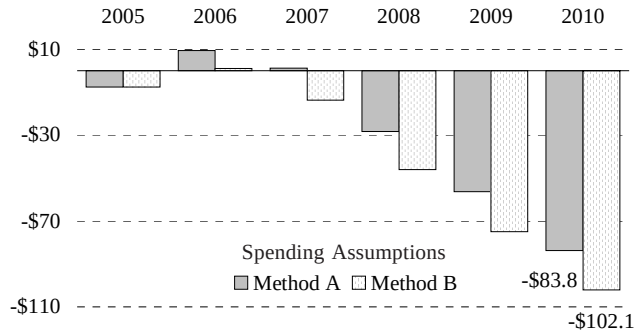
MPS's allowable revenues will likely grow slowly. In addition, slowing federal dollars would impact MPS disproportionately because it relies more on these dollars than most districts.

Given recent cost trends, district spending is likely to grow faster than revenues over the next several years. As it has in the past, MPS will, no doubt, avoid deficits by continuing to restrain expenditures so that they matches available revenue. However, as the analysis presented here indicates, spending will have to be even more tightly controlled than it has been in recent years or wholesale systemic changes/reforms will have to be implemented. □

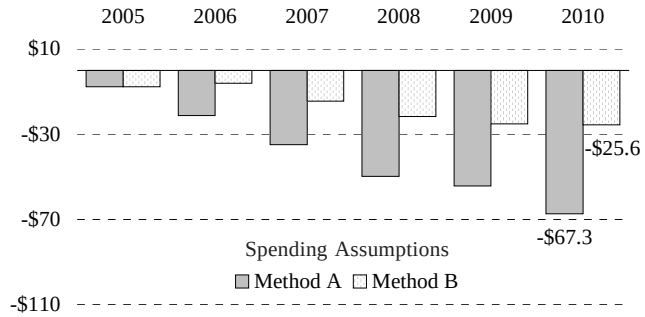
Projected Deficits, Baseline Revenue Assumptions
Projected Revenues-Expenditures, 2005 - 2010 ($ Millions)



Projected Deficits, Pessimistic Revenue Assumptions
Projected Revenues-Expenditures, 2005 - 2010 ($ Millions)



Projected Deficits, Optimistic Revenue Assumptions
Projected Revenues-Expenditures, 2005 - 2010 ($ Millions)



PART IV: EMERGING ISSUES

Since this study was completed, several new pieces of information have become available that impact MPS's future financial situation. First, enrollments in the 2006-07 school year are significantly less than were forecasted in the model. Second, data on estimated unfunded liabilities, particularly those for health care became available. They could negatively impact the district.

ENROLLMENTS

To forecast future finances required an estimate of future enrollments. We describe our estimates on pages 29 and 30. For the 2006-07 school year, our baseline forecast was for 94,528 students. The pessimistic forecast was for 93,030. Recent figures from DPI show MPS's enrollments for revenue cap purposes are 92,409, or 621 students less than our pessimistic forecast.

These new figures indicate MPS is on a path below the "baseline." Using the new enrollment figures with our forecasting model indicates that district revenues will be as much as 3% below our baseline forecast by 2010.

UNFUNDED LIABILITIES

In addition to the costs outlined in this report, MPS has several unfunded liabilities for health insurance and for retirement benefits.

Retirement

MPS's largest pension liability is for the Wisconsin Retirement System (WRS). The liability was funded in 2003 with a bond issuance. There is currently $170.7 million outstanding, but the payments are accounted for in our earlier financial analysis.

The district also has two smaller liabilities, both of which are now unfunded. One is an early retirement benefit that has an actuarial accrued liability of $49.5 million; $10.9 million of that amount is unfunded. A second early retirement plan has an actuarial accrued liability of $174.4 million. Of that amount, $113.8 million is unfunded. The table on page 36 shows MPS's post-retirement liabilities and the unfunded amounts.

Other Post-Retirement Benefits

MPS's unfunded health benefit liabilities are estimated to be nearly $1.5 billion.

MPS, like other public school districts, is required to report its financial condition using accounting rules from the Governmental Accounting Standards Board (GASB). GASB recently instituted new rules to account for certain post-retirement benefits. For MPS, the present value of all post-retirement health insurance costs as well as other smaller costs must be accounted for beginning with their 2008 financial statements. These do not include pension costs.

Although MPS does not have a current estimate of these costs, a 2002 actuarial study showed the present-value cost of these future benefits was $1.45 billion. To put that amount in some perspective, it is nearly 40% more than the district's 2005 expenditures and about 20 times the district's fund balance.

Financial Impact

The retirement payments and other post-retirement employee benefits (OPEB's) are liabilities that MPS will incur in the future. Some of the costs will occur within the next several years. e.g., health benefits for current retirees and for those who choose to retire during this time frame. Others, such as the future obligations for younger employees, will be incurred outside the time frame of this study.

The new GASB standards require governments, including school districts, to account for the actuarial cost of OPEB's (they do not have to account for the unfunded pension liability). The new standards do not require districts to fully fund these liabilities. They can continue to "pay as you go" as most districts currently do. However, some bond-rating agencies have noted that failure to fund liabilities fully could adversely affect a district's bond rat-

If MPS were to borrow to fund its unfunded liabilities, it would incur an additional annual expense of approximately $115 million, or about 11% of the district's current expenditures.

ing, meaning the district would have to pay a higher interest rate for any bonds it issues.

Costs of Full Funding. One way to assess the impact that these costs ultimately will have on the district is to estimate the annual cost to the district of borrowing these amounts. For example, if MPS were to issue $1.45 billion of bonds to fund its OPEB liability, the district would have the funds available to pay those benefits as they arose. However, the current cost of that strategy would be the annual payment required to pay the interest and principal on the bonds. If the bonds were issued at a 5% interest rate over 20 years, the annual cost to the district would be approximately $115 million, or about 11% of the district's current expenditures.

Should the district borrow to fund both its OPEB liability and its pension liabilities, annual payments of approximately $125 million would be required.

Impact on Forecasts. As previously mentioned, there is no requirement that the district borrow to fund these liabilities. However, it is instructive to show the impact that borrowing for these liabilities might have on financial forecasts.

MPS's Post-Retirement Liabilities
$ millions

Plan	Liability	Funded	Unfunded
Pension			
Wisconsin Retirement System	$170.7	$170.7	$0.0
Early Retirement Supp. And Benefit Improvement Plan	$49.5	$39.4	$10.0
Supplemental Early Retirement Plan for Teachers	$174.4	$60.6	$113.8
Healthcare			
GASB 45 OPEB	$1,450.0	$0.0	$1,450.0
Total	$1,844.5	$270.7	$1,573.8

We assume the MPS issues bonds to cover all of the unfunded liabilities listed in the table below. At a 5% interest rate, this would increase the district's costs $125 million. Adding that amount to the previous expenditure forecasts and using our pessimistic revenue assumptions yields the revenue-expenditure gap displayed in the chart below. In every year, the gap is at least $100 million and grows to more than $206 million by 2010. □

Projected Deficits, Pessimistic Revenue Assumptions
Projected Revenues-Expenditures, 2005 - 2010 ($ Millions)