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Kansas City 33 School
District
Financial Condition and
Projections

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YELLOW SHEET

Findings in the audit of the Kansas City 33 School District, Financial Condition and Projections

Financial Position

Significant decreases in state funding and a failure to significantly reduce expenditures have led to the Kansas City 33 School District's current financial position. Expenditures exceeded revenues (excluding other financing sources) in the operating funds for the years ended June 30, 2008, 2009, and 2010, resulting in the reduction of district undesignated reserves. Several factors have contributed to the decline in the district's financial position, including but not limited to, decreased funding from the state, the declining student population, declining property valuations, and increased enrollment in charter schools in the Kansas City area.

School closings were proposed by the district's administration to the Board every year since June 2006 with minimal action taken, all while the district's enrollment continued to decline. On March 10, 2010, the Board approved a plan to close, mothball, or reconstitute over 50 percent of district facilities. This plan was updated May 26, 2010, with the district planning to close or reconstitute 29 of its 61 facilities, including 26 schools. To further reduce the district's budgeted expenditures, district administration proposed eliminating approximately 900 full-time equivalent positions. Finally, district administration proposed cancelling and/or renegotiating various district contracts to reduce the district's expenditures.

Subsequent Report

The State Auditor's office is continuing to audit the operations of the district and any findings and recommendations will be included in a subsequent report.

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Kansas City 33 School District

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To the Board of Education
Kansas City 33 School District

The State Auditor conducted an audit of the Kansas City 33 School District, Financial Condition and Projections, under authority granted in Section 29.205, RSMo. The district engaged McGladrey & Pullen, Certified Public Accountants (CPAs), to audit the district's financial statements for the years ended June 30, 2009 and 2010. To minimize duplication of effort, we reviewed the CPA firm's audit report for the 2009 audit, since the 2010 audit had not been completed. The scope of our audit was the 2 years ended June 30, 2010. The objective of our audit was to evaluate the financial position of the district's operating funds including budgetary projections.

Our methodology included reviewing minutes of meetings, written policies and procedures, financial records, and other pertinent documents; and interviewing various personnel of the district, as well as certain external parties. We obtained an understanding of the assumptions used during the development of budget projections and verified applicable data from which various assumptions were based. In addition, we reviewed detailed historical budget and actual financial data for the 4 years ended June 30, 2010.

We conducted our audit in accordance with the standards applicable to performance audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform our audit to obtain sufficient, appropriate evidence to provide a reasonable basis for our conclusions based on our audit objectives. We believe that the evidence obtained provides such a basis.

The accompanying Organizational and Statistical Information is presented for informational purposes. This information was obtained from the district's management, accounting records, and Comprehensive Annual Financial Reports and was not subjected to the procedures applied in the audit of the district.

While this report contains no specific recommendations an audit of Kansas City 33 School District operations is still in process, and any additional findings and recommendations will be included in a subsequent report.



Susan Montee, JD, CPA
State Auditor

The following auditors participated in the preparation of this report:

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Kansas City 33 School District

Financial Position

Financial Position

Significant decreases in state funding and a failure to significantly reduce expenditures have led to the Kansas City 33 School District's current financial position. Expenditures exceeded revenues (excluding other financing sources) in the operating funds for the years ended June 30, 2008, 2009, and 2010, resulting in the reduction of district undesignated reserves (see Appendix A). The fund balance of the district's undesignated operating funds decreased approximately \$25.9 million from approximately \$74.3 million at July 1, 2006, to \$48.4 million at June 28, 2010.¹ Significant changes have been approved by the Board of Education to reduce expenditures and improve the financial position.

The district defines its operating funds as the General, Teachers, and Capital Projects - Operating Funds. The district also maintains several other funds, including funds established to account for American Recovery and Reinvestment Act of 2009 (ARRA) funding.

District administration initially projected an operating funds deficit of \$8.5 million at June 30, 2011, prior to budgetary reductions (see Appendix B). In addition, district administration projected a cash flow shortfall of \$15.7 million would exist by November 2010, if budgetary reductions were not approved. Also, the combined year-end balance of the General and Teachers Funds would have been less than 3 percent of the prior fiscal year expenditures and the district would have been classified as financially stressed as defined by Section 161.520, RSMo.

As a result of these concerns and to stabilize the district's financial condition and balance its budget, the Board approved approximately \$68.8 million in expenditure reductions for the year ended June 30, 2011. These reductions included approximately \$55.5 million from district operating funds, \$11.2 million in ARRA funding,² and \$2.1 million in child nutrition services. The reductions will be achieved through various cost saving measures, primarily the "right-sizing" of the district which was approved by the Board in March 2010.

Based on the budgetary projections for the year ended June 30, 2011, the projected combined balance of the General and Teachers Funds will be more than \$25 million at June 30, 2011, or approximately 9 percent of expenditures for the year ended June 30, 2010.

¹ Revenues, expenditures and fund balances as of June 28, 2010, are per the district's initial year-end financial statement and subject to change as accruals and other year-end entries are booked.

² ARRA funding was distributed to public school districts for the year ended June 30, 2010, and will be to a lesser extent for the year ended June 30, 2011; however, the district is uncertain if these funds will be available after the year ended June 30, 2011.



Kansas City 33 School District Financial Position

While the district has made progress toward improving its financial position, the Board must continue to closely monitor the budget for the year ended June 30, 2011. Additional budgetary reductions may be necessary to compensate for additional decreases in state funding as the state attempts to balance its own budget for the year ended June 30, 2011. In addition, the district projects state funding will continue to decrease through the year ended June 30, 2013.

Factors leading to financial difficulty

Several factors have contributed to the decline in the district's financial position, including but not limited to, decreased funding from the state, declining student population, declining property valuations, and increased enrollment in charter schools in the Kansas City area. Between the years ended June 30, 2006 and 2010, district enrollment declined by approximately 8,000 students, including approximately 2,000 students annexed to the Independence School District in the year ended June 30, 2008. During this same period, charter school enrollment increased by approximately 2,000 students. In addition, the state basic formula funding was changed, to be phased-in over a 7 year period beginning in 2007. State basic formula revenues decreased over \$26.6 million between the years ended June 30, 2007 and 2009, and are projected by the district to decrease an additional \$50 million through the year ended June 30, 2013 (see Appendix C).

In contrast, between 2005 and 2009, the district's average current expenditures per average daily attendant were approximately \$4,700, or 54 percent more than the statewide average (see Appendix D). In addition, during this same timeframe the district's student to teacher and administrator ratios were significantly lower than the statewide averages. For the year ended June 30, 2009, the district's student to classroom teacher ratio of 14 to 1 was the lowest in the state for similarly sized school districts. Also, according to data collected by the National Center for Educational Statistics, the district's year ended June 30, 2008, student to teacher ratio was one of the lowest of any similarly sized district, with similar demographics, of any nearby state.

Right-sizing

School closings were proposed by the district's administration to the Board every year since June 2006 with minimal action taken, all while the district's enrollment continued to decline. Maintaining underutilized schools caused a financial burden to the district. As a result, right-sizing of the district was considered critical by the current district management.

Facilities

On March 10, 2010, the Board approved a plan to close, mothball, or reconstitute over 50 percent of district facilities. This plan was updated May 26, 2010, with the district planning to close or reconstitute 29 of its 61 facilities, including 26 schools. The estimated utility cost savings alone from the closed buildings is projected to be approximately \$2.6 million.



Kansas City 33 School District Financial Position

In June 2006, a facilities utilization study found district buildings were aging and deteriorating, district schools were operating at less than 70 percent of designed capacity, and student enrollment was declining. The study concluded the desired level of building utilization was 85 to 90 percent occupancy.

The district updated this study in 2010, and the current findings were very similar to those noted for 2006; district buildings were aging and deteriorating, district schools were operating at less than 50 percent of designed capacity, and student enrollment was declining. During the year ended June 30, 2010, the district operated approximately 60 educational sites with a capacity of over 34,000 seats. Less than 50 percent of these seats were occupied.

Staffing

To further reduce the district's budgeted expenditures, district administration proposed eliminating approximately 900 full-time equivalent (FTE) positions.

The district estimates a savings to the operating funds of approximately \$46.1 million through the elimination of approximately 745 FTE positions. An additional 113 FTE positions and salary expense of \$6.2 million will be eliminated as a result of decreases in ARRA funding. The remaining cuts in FTE positions will be in the area of child nutrition services. These cuts in FTE positions will be achieved through the following processes:

1. Approximately 80 employee contracts were not renewed for performance and several FTE positions were lost due to attrition. According to the Interim Director of Human Resources, the reorganization of the district has called for these positions to remain unfilled and to be removed from the system, duties to be collapsed or combined into other positions, or responsibilities otherwise shifted within the organization.
2. The Board approved a \$20,000 early retirement incentive for certified employees. The district received 234 applications, of which 215 employees were eligible for the program. The total liability to the district for this incentive will be \$4,300,000. Funding for this early retirement incentive program was previously set aside, or reserved, by the district.
3. The Board approved a \$10,000 early retirement incentive for classified employees. The district received 71 applications, of which 60 employees were eligible for the program. The total liability to the district for this additional early retirement incentive will be \$600,000. Funding for this early retirement incentive program was previously set aside, or reserved, by the district.



Kansas City 33 School District
Financial Position

4. Additional terminations or layoffs necessary to adequately decrease the FTE positions in accordance with budget projections for the year ended June 30, 2011, will be handled through a Reduction of Force (RIF). This process is required by state law, has been authorized by the Board, and is currently in process as of July 2010.

Upon the elimination of these FTE positions, district management estimates the student to classroom teacher ratio will exceed 20 to 1 for the year ended June 30, 2011, a significant increase from the 2009 ratio of 14 to 1.

Contracts

Finally, district administration proposed cancelling and/or renegotiating various district contracts to reduce the district's expenditures. The district is in the process of reviewing vendor contracts. As a result, cost savings are expected as these contracts are cancelled and/or renegotiated, vendors are consolidated, goods and services are rebid, state contracts are identified and utilized, services are moved in-house, etc.

Future issues

The budget for the year ended June 30, 2011, assumes certain events, activities, revenues, and costs. As changes continue to be made at the district, the actual results will differ from these projections. In addition, further cuts in state funding could occur. As such, it is imperative the Board continue monitoring the budget and cash flow projections and make reductions in expenditures as necessary to maintain a balanced budget and carry the district into the year ended June 30, 2012, and beyond.

The State Auditor's office is still in the process of auditing district operations, including its financial position, and any findings and recommendations will be included in a subsequent report.

Kansas City 33 School District

Organization and Statistical Information

The Kansas City 33 School District was organized in 1867. By the 1970s, the district had grown to one of the largest in the state.

In 1977, the district and a group of parents filed a racial segregation suit in federal court against the state and federal agencies, with the intent to ultimately desegregate Kansas City schools. In 1984, the court ruled the district was also liable for the segregation. In 1985, a federal judge took partial control of the district and ordered the state and district to build new schools, integrate classrooms, and bring student test scores up to national norms. By 1999, when the state stopped making desegregation payments to the district, nearly \$2 billion had been spent on new schools, facilities, and equipment; busing students in an attempt to desegregate schools; and increased teacher and administrator salaries, etc.

In 1999, the district was stripped of its accreditation by the state, which was subsequently restored to provisional accreditation in April 2002. In 2003, the federal court relinquished its control over the district.

Today, the district encompasses approximately 68 square miles within the City of Kansas City, Missouri, and serves a population of approximately 239,000 citizens. With a total average daily attendance of 16,573 students in school year 2009-2010 and total budgeted operating expenditures historically exceeding \$300 million per year, the district operates as one of the larger public school systems in the State of Missouri. As of June 30, 2010, the district employed 3,482 individuals, including 1,678 teachers and certified personnel.

The nine-member Board of Education is responsible for setting district policy to ensure efficient operations, overseeing the Superintendent of Schools, and adopting an annual budget and its supporting tax rate. Board members are elected by the voters of the city and serve without compensation. Three new members were elected to the Board in April 2010, with the remaining six members having served on the Board since at least 2008. Members of the Board at June 30, 2010, were:

- Airick Leonard West, President and Member At-Large
- Derek Richey, Vice President and Representative of Sub-District 2
- Arthur Benson, Representative of Sub-District 1
- Duane B. Kelly, Representative of Sub-District 3
- Joseph Jackson, Representative of Sub-District 4
- Ray Wilson, Representative of Sub-District 5
- Marilyn Simmons, Representative of Sub-District 6
- Crispin Rea, Member At-Large
- Kyleen Carroll, Member At-Large



Kansas City 33 School District Organization and Statistical Information

On April 30, 2009, the Board approved the hiring of Dr. John William Covington as the district's fourth Superintendent since July 2006. Dr. Covington's employment began July 1, 2009. Subsequently, the district has updated its strategic plan; approved the "right-sizing" process to close/reconstitute several schools and other costs centers; drafted a comprehensive transformation plan, including a 5-year capital improvement plan; and adopted a balanced budget for the year ended June 30, 2011. In addition, the district plans to establish a repurposing committee to explore innovative ways to transform unused properties into community assets.

Appendix A

Kansas City 33 School District
 Comparative Statement of Revenues, Expenditures, and Changes in
 Fund Balance - Operating Funds

	Year Ended June 30,			
	Unaudited 2010 *	2009	2008	2007
BEGINNING FUND BALANCE	\$ 57,260,601	54,768,175	78,493,471	86,527,702
REVENUES				
Local	163,260,409	177,737,164	187,651,597	183,526,714
County	2,541,154	4,209,103	4,025,235	3,433,163
State	49,974,940	81,104,407	101,827,817	109,458,491
Federal	51,054,927	39,279,771	31,032,680	37,349,243
Tuition	2,948,946	13,274	4,341	76,881
Total Revenues	<u>269,780,376</u>	<u>302,343,719</u>	<u>324,541,670</u>	<u>333,844,492</u>
EXPENDITURES				
Administration	19,804,560	25,593,541	23,984,587	27,345,569
Instruction	127,183,916	159,430,441	174,895,836	177,412,969
Support services	48,649,361	60,292,858	55,888,317	52,270,401
Operation of facilities	40,034,432	41,286,297	44,484,620	39,363,329
Pupil transportation	15,295,931	17,210,741	18,703,194	22,133,487
Community and adult services	9,300,580	8,553,042	11,578,108	6,138,910
Capital outlay	0	0	108,296	171,347
Debt service - principal	12,738,579	0	0	414,000
Total Expenditures	<u>273,007,359</u>	<u>312,366,920</u>	<u>329,642,958</u>	<u>325,250,012</u>
REVENUES OVER (UNDER) EXPENDITURES	<u>(3,226,983)</u>	<u>(10,023,201)</u>	<u>(5,101,288)</u>	<u>8,594,480</u>
OTHER FINANCING SOURCES (USES)				
Capital leases	0	0	0	1,527,387
Sale of capital assets	0	0	864,347	100
Tranfers in	2,704,652	18,170,479 **	15,737,733	16,461,368
Transfers out	(6,127,232)	(5,654,852)	(35,226,088)	(34,617,566)
Total Other Financing Sources (Uses)	<u>(3,422,580)</u>	<u>12,515,627</u>	<u>(18,624,008)</u>	<u>(16,628,711)</u>
ENDING FUND BALANCE	\$ <u>50,611,038</u>	<u>57,260,601</u>	<u>54,768,175</u>	<u>78,493,471</u>
RESERVED	1,699,559	5,871,353	5,491,216	2,708,486
UNRESERVED -				
Designated	516,728	7,741,641	4,040,546	2,394,166
Undesignated:				
General Fund	33,923,471	37,701,384	35,593,416	57,919,018
Capital Projects - Operating	14,471,280	5,946,223	9,642,997	15,471,801
TOTAL FUND BALANCE	\$ <u>50,611,038</u>	<u>57,260,601</u>	<u>54,768,175</u>	<u>78,493,471</u>

Source: District accounting records and Comprehensive Annual Financial Reports

* Revenues, expenditures and fund balances as of June 28, 2010, are subject to change as accruals and other year-end entries are booked.

** The district closed its internal service funds and transferred \$17,170,479 to its General Fund during the year ended June 30, 2009. These internal service funds were primarily used to account for and finance the district's insured and un-insured risk of loss (e.g. workers' compensation).

Appendix B

Kansas City School District
 Comparative Budget Summary for the Year Ended June 30, 2011 -
 Original Projected vs. Actual Adopted - All Budgeted Funds

	Original Projected	Actual Adopted	Variance
BEGINNING FUND BALANCE \$	40,189,966	33,026,500	(7,163,466)
REVENUES			
Local	158,024,840	159,916,234	1,891,394
County	3,906,829	3,611,720	(295,109)
State	44,337,729	36,627,838	(7,709,891)
Federal *	51,091,947	44,926,278	(6,165,669)
Tuition	5,209	5,209	-
Total Revenues	257,366,554	245,087,279	(12,279,275)
EXPENDITURES			
Administration	19,182,618	6,052,562	(13,130,056)
Instruction	139,566,407	124,047,175	(15,519,232)
Support services	64,881,809	50,958,810	(13,922,999)
Operation of facilities	39,239,678	33,047,862	(6,191,816)
Pupil transportation	15,995,384	15,891,519	(103,865)
Community and adult services	9,974,026	4,747,008	(5,227,018)
Debt service	12,966,405	12,949,254	(17,151)
Total Expenditures	301,806,327	247,694,190	(54,112,137)
REVENUES OVER (UNDER) EXPENDITURES	(44,439,773)	(2,606,911)	41,832,862
OTHER FINANCING SOURCES (USES)			
Net fund transfers	2,500,000	3,075,157	575,157
ENDING FUND BALANCE	(1,749,807)	33,494,746	35,244,553
Less: Restricted Fund Balances			
Capital Projects - Operating	(3,964,430)	(8,403,155)	(4,438,725)
Federal Grants	(2,741,641)	0	2,741,641
General Fund Balance \$	(8,455,878)	25,091,591	33,547,469

Source: District budget documents and Right-Sizing plan

* The actual adopted budget for the year ended June 30, 2011, included \$3,450,964 in American Recovery and Reinvestment Act of 2009 (ARRA) funding. No ARRA funding was included in the district's original projections (ARRA funding for the year ended June 30, 2010, was approximately \$14.68 million).

Appendix C

Kansas City 33 School District
Comparative Statement of State Basic Formula Funding

	Year Ended June 30,						
	2007	2008	2009 *	2010 ** Estimated	2011 Estimated	2012 Estimated	2013 Estimated
Enrollment							
Kansas City 33 School District (KCSD)	24,449	22,479	18,178	17,275	15,609	15,609	15,609
Kansas City Charter School Districts	6,962	7,159	7,925	8,503	***	***	***
Weighted Average Daily Attendance (WADA)							
Kansas City 33 School District (KCSD)	31,235.5073	29,573.1882	26,359.5912	25,573.4451	20,993.7989	20,680.3000	18,658.9500
Kansas City Charter School Districts ***	7,154.2493	8,071.6078	9,381.4686	10,564.8167	12,075.2593	12,075.2593	12,075.2593
a State Basic Formula payment	\$ 147,231,751	148,569,742	145,048,580	146,660,551	134,204,760	132,932,470	124,729,189
b Less Charter School portion of State Basic Formula	(27,437,857)	(31,855,577)	(38,072,981)	(42,875,384)	(49,005,244)	(49,005,240)	(49,005,240)
c Less Charter School portion of local revenue	(22,414,264)	(26,579,805)	(36,156,179)	(41,921,193)	(51,329,845)	(50,907,307)	(55,279,984)
Less State Appropriation Reduction of 4 percent	0	0	0	0	(3,407,980)	0	0
State Basic Formula payment to KCSD	\$ 97,379,630	90,134,360	70,819,420	61,863,974	30,461,691	33,019,923	20,443,965

Source: District WADA and KCSD/Charter Local Education Agency formula calculations

* Independence Annexation was effective July 1, 2008.

** Updated enrollment numbers as of October 13, 2009.

*** Per a KCSD representative, Kansas City Charter School District enrollment was not available at the time the district performed these calculations, so the Kansas City Charter School District estimated WADA for the year ended June 30, 2011, was calculated based on prior year average increases.

a Total State Basic Formula payment based on KCSD and Kansas City Charter School Districts' combined WADA.

b Based on Kansas City Charter School Districts' percentage of the total WADA.

c Local tax levy is \$4.95 per \$100 of assessed valuation. Amount is net of local revenue needed to retire KCSD debt.

Appendix D

Kansas City 33 School District
Selected Department of Elementary and Secondary Education Core Data

Comparative Statement of Average Expenditures per Average Daily Attendant

	Year Ended June 30,									
	2009		2008		2007		2006		2005	
	KCSD	Statewide	KCSD	Statewide	KCSD	Statewide	KCSD	Statewide	KCSD	Statewide
Average Daily Attendance (ADA)	17,371	845,909	21,142	851,104	23,090	858,101	31,135	858,338	31,001	850,038
Total expenditures	\$371,898,763	\$11,071,361,932	\$377,991,840	\$10,813,004,411	\$379,778,852	\$10,046,897,221	\$431,362,127	\$9,246,815,784	\$417,292,295	\$8,806,183,464
Total current expenditures *	\$301,266,027	\$8,124,097,976	\$320,120,712	\$7,947,205,825	\$321,223,065	\$7,449,867,620	\$364,362,233	\$7,050,924,520	\$355,294,611	\$6,604,885,197
Current expenditures per ADA	\$17,343	\$9,604	\$15,141	\$9,338	\$13,912	\$8,682	\$11,703	\$8,215	\$11,461	\$7,770

* Current expenditures as defined by the Department of Elementary and Secondary Education do not include Capital Projects - Operating Fund expenditures or non-instructional/support expenditures (i.e. community and adult services expenditures) included in Appendix A.

Comparative Statement of Student to Staff Ratios

	Year Ended June 30,									
	2009		2008		2007		2006		2005	
	KCSD	Statewide	KCSD	Statewide	KCSD	Statewide	KCSD	Statewide	KCSD	Statewide
Students per teacher	10	13	11	13	12	13	12	13	12	14
Students per classroom teacher	14	17	15	18	17	18	17	19	17	19
Students per administrator	118	187	140	189	149	197	149	203	145	204

Source: Department of Elementary and Secondary Education (DESE) core data as submitted by Missouri Public Schools as of November 2, 2009