

# Flint Community Schools: Fiscal and Service Solvency

## MSU Extension White Paper

*By Samantha Zinnes, Law Fellow*

*Eric Scorsone, Director*

*Mary Schulz, Associate Director*

*Center for Local Government Finance and Policy*

*Michigan State University Extension*

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## I. Introduction

Flint Community Schools faces a significant financial challenge that goes back to the end of the Great Recession in 2010 and 2011. Since 2011, Flint School District has run an operating deficit of nearly \$67 million. During the past nine years, the school district has only managed to successfully run an operating surplus once. During those same years, the school district has used one-time monies of over \$53 million to try and plug the budget gap. As of June 30, 2019, the school district had an overall net negative fund balance (or savings) of \$2.5 million. A negative fund balance is not allowed under state law and has triggered a series of required reporting and state oversight once again.

After accounting for one-time fixes and other transitory flows, the school district is estimated to run an on average structural deficit of \$8 million. This structural deficit does not necessarily mean that the district would be spending enough to properly provide an education to the students of Flint.

An adequacy study is designed to estimate what amount of funding per student would be needed to ensure an appropriate education for each child across many different types of school districts.

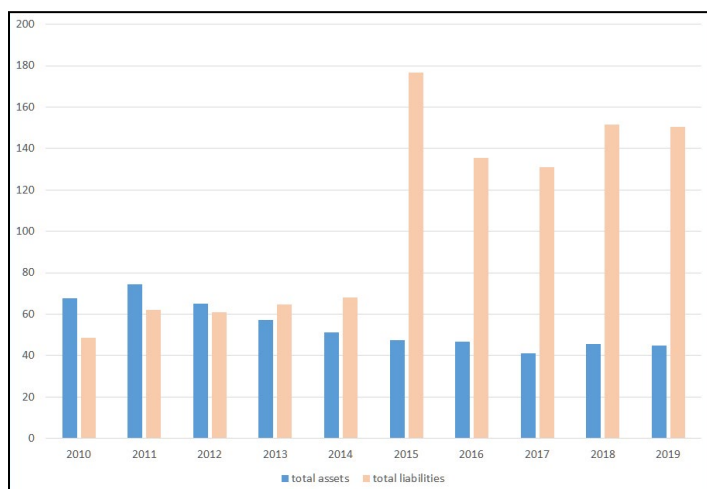
## II. More Detailed Look: Financial Situation of Flint Community Schools

In 2012, Flint School District had an unrestricted net position of -\$11 million. By FY 2015, this negative net position had declined to a negative -\$150 million. A significant part of that, -\$123 million, was due to new reporting requirements for the school teacher pension system. At that point in 2015, Flint’s non-pension long-term debt had remained stable at about \$21 million with an additional \$7 million of long-term debt also due in the next fiscal year.

The school district was unable to fully meet its ongoing expenditure commitments with ongoing revenues. From 2011 through 2018, the school district ran a cumulative deficit of over \$50 million. This \$50 million was ultimately covered by “borrowing” via nonpayment of unemployment compensation and teacher pension obligations. Later, these obligations were refinanced to a lower interest rate and longer maturity. However, in doing so, these short-term liabilities were simply converted into long-term liabilities.

The 2018 net position of Flint School District remained at about -\$150 million. However, long-term debt continued to climb as nearly \$27 million in long-term due later was owed and \$4.5 million in long-term due in the next year was also owed. By FY 2018, therefore, the school district had accumulated an additional debt of more than \$10 million since 2015 above and beyond the new reporting requirements for pension and retiree health care liabilities.

**Figure 1. Flint School District assets and liabilities**

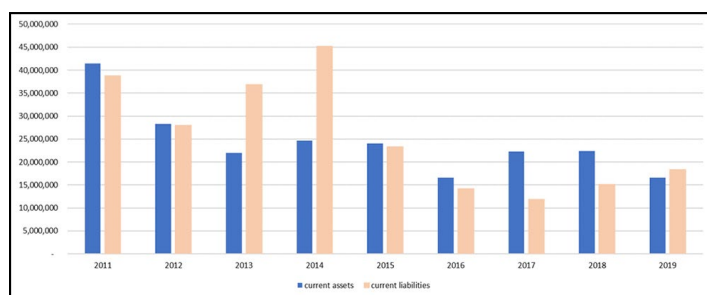


Flint school district’s assets and liabilities are key financial tools in which to examine the district since 2011. The school district’s liabilities have greatly increased since 2015 due to an accounting rule change. In 2015, the Government Accounting Standards

Board (GASB) determined that local governments must report long-term pension liabilities on their balance sheet and not just in a footnote. The liability existed prior to 2015 but it was not reported in the formal balance sheet. The conclusion we can draw is that liabilities have outstripped assets for at least this entire time period going back to 2011.

A short-term view is also helpful in examining the district. In this case, we can look at current assets and current liabilities.

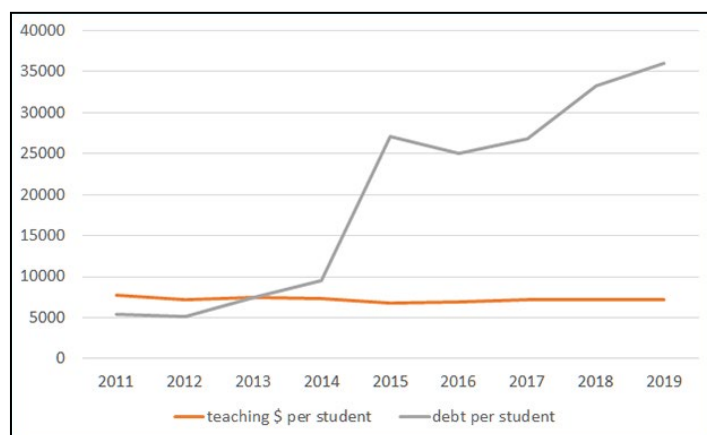
**Figure 2. Flint School District current assets and liabilities (2011-2019)**



Here, we see that current liabilities exceed current assets in some years but not all years. These numbers are not impacted by the GASB changes from 2015. There was a period of time, from 2016-2018, where the school district did in fact show a positive current ratio. The current ratio is current assets divided by current liabilities. However, those calculations reversed in 2019 and the prior period positive ratios are more due to a change in the status of some debt amounts rather than a true change in the financial picture.

A final view relates the school district’s debt to its spending on students. At this time, the school district’s debt has exceeded

**Figure 3. Debt per student and instruction spending per student (2011-2019)**



over \$35,000 per student. This debt includes the general obligation debt and the pension and retiree health care debt. At the same time, spending on students in classrooms has been flat at about \$7,500 per student. A growing share of the school district budget has had to go to make good on debt and pension payments.

**Figure 4. Flint School District net financial asset ratio (2011-2019)**



In this case, the net financial asset ratio is negative and a larger negative over time. This implies the school district was destroying or using up its assets faster than it was growing them. Net assets and net financial assets represent the slack or discretionary resources a school district has to maintain flexibility and a resource cushion for it to function over time. In Figure 3, capital assets are removed from the calculation. It is possible the government could sell some assets and improve its overall financial position.

The overall financial story of the Flint School District was one of foregoing payments in the period 2009-2012, leading to a major buildup of general debt including unemployment insurance and pension payments. The school district remains committed to repaying over \$20 million in debt, which places a major debt overhang on the district. The district’s real options to address this problem are either a debt forgiveness plan, which seems unlikely, or to free up monies through structural changes to continue to make these debt payments and free up more money for the classroom. As we will see, the reality is that Flint School District needs more funding to meet its real needs in order to meet the educational needs of the district’s school children.

### Enhanced Deficit Elimination Plan (EDEP)

Flint School District had to file an Enhanced Deficit Elimination Plan (EDEP) this year. As previously discussed, Michigan local units cannot have a negative fund balance. “Districts that incur a general fund deficit projecting to last five years or more are under treasury oversight and thereby required to develop an approved Enhanced Deficit Elimination Plan (EDEP).”<sup>1</sup> Flint School District incurred a substantial general fund deficit. The district’s EDEP seems to show there are 20 vacant buildings that can be moved on, thus generating savings in general maintenance and insurance, Rehmann accounting fees and other audit/legal counsel fees are being reduced, bus times may increase due to savings from route reductions, and that almost \$1 million will be saved from 11 high salaried positions being reduced.

<sup>1</sup> Office of School Review and Fiscal Accountability, Michigan Department of Treasury, at [https://www.michigan.gov/treasury/0,4679,7-121-1751\\_51556\\_74806-373681--,00.html](https://www.michigan.gov/treasury/0,4679,7-121-1751_51556_74806-373681--,00.html).

## III. Service Solvency, Educational Adequacy and the Law

Service solvency<sup>2</sup> has been defined as the condition whereby a government has or does not have “the ability to provide services at the level and quality that are required for the health, safety and welfare of the community and that the citizens desire and expect.”<sup>3</sup> “Level” may refer to a more quantitative description related to, for example, items such as the number of students per teacher. “Quality” refers to perhaps the quality and certification of teachers or the outcomes achieved by students as measured by standardized tests. This definition is problematic because it is unclear whether it refers to inputs, outputs or outcomes. Under this definition, how should we measure “service solvency”? Should we measure the number of teachers, the quality of those teachers or the outcomes achieved by students under those teachers?

This definition tends to be used when talking about the wants and desires of citizens, but only using those desires to measure service solvency is also problematic. Every citizen will have a different idea regarding what level and quality of education is needed. Further, many other stakeholders, including the state government and the federal government, will want to have a say in any policy changes relating to certain issues such as service solvency as well as quantity and/or quality. Government stakeholders have legal standing to dictate the nature of policy changes for these types of issues and can also influence the discussions surrounding potential changes to current law and practice.

When a government unit provides electricity to residents, it is providing a service, and, for some services, there are established ways to determine whether those government-provided services are adequate. A school district is not a typical governmental organization. Education is not a typical service. And while there are some metrics, like testing and student assessments, that can be used to measure whether public schools are producing educated children, some learning is harder to measure in the classroom. Even so, the care and quality of that learning and the environment in which it is permitted to grow is vitally important to determining whether a school district is fulfilling its obligation to educate students.

As previously discussed, determining whether the City of Flint is service solvent or insolvent involves figuring out whether the

2 There is a potential problem with using the word “solvency” in this context. Solvency is typically defined as an adjective as “being able to pay all legal debts” or alternatively as “that dissolves or can be dissolved”. The phrase “service solvency” places emphasis on the financial aspects of service provision rather than the nature of those services and the inherent rights to those services by those being served. “Solvent,” as a noun, can refer to “liquid substance” or “something that provides a solution.” In this case, however, it is clearly more of an adjective to modify the word “service.”

3 <https://icma.org/sites/default/files/I01456.pdf>

government can perform the services necessary to provide for the health, safety and protection of its citizens. That said, when talking about Flint Community Schools and the school district, the conversation is not just about whether the schools can provide adequate services in terms of fiscal health, not like how we discuss how many police officers are patrolling or how many potholes need to be fixed. Instead, this conversation involves whether schools and the school district are providing Flint’s children with the education and skills necessary to be successful in life.

It does not sound quite right to describe “educating children” as a “service” in the same way we talk about the service of providing water or electricity to residents. Reasons for this might be because of the importance of education as well as the emotions that tend to come up when discussing education policy and schools. This is especially true when a school district is in fiscal distress and/or the children are not receiving a viable education. While there is some available data to measure and assess the academic abilities of students (standardized or assessment tests), knowing what is actually happening in the schools, common issues and what is being done to address those issues by the district is very valuable and can tell us a lot about the direction the school district is headed in for the foreseeable future.

### Current Education Policy Trends

There is no federal fundamental right to a public education. It is mandatory that children attend school, even if the school provides “education” in name only, but there is no fundamental right to a publicly-provided minimum level of education. In “Brown v. Board of Education,” the Supreme Court rejected the “separate but equal” doctrine and, instead, held that segregation was inherently unequal and that all children have a fundamental right to equal access to public education;<sup>4</sup> this applies to every

4 Jane K. Babin, Adequate Special Education: Do California Schools Meet the Test?, 37 San Diego L. Rev. 211, 237 (2000):

“The Supreme Court’s decision in Brown v. Board of Education heralded the beginning of modern reform in general education. In rejecting the ‘separate but equal’ doctrine announced in Plessy v. Ferguson, the Court dismissed arguments that the Fourteenth Amendment should be interpreted in light of the circumstances surrounding its adoption. Specifically, ‘education of Negroes was almost nonexistent’ in the late nineteenth century, much as education of the disabled was virtually nonexistent in the mid-twentieth century. The Brown Court held that the educational segregation of children, solely on the basis of race, was indeed an unconstitutional denial of Equal Protection because ‘separate educational facilities are inherently unequal.’”

U.S. state via the 14th Amendment.<sup>5</sup> Right to equal access means<sup>6</sup> that, if a government decides to provide free public education and opens schools, it must make that education and those schools accessible to all children; but access is not the same thing as adequate and there is no fundamental right to even a minimally adequate education. As long as all students are treated equally, with all students getting a good education or all students getting a bad education, then the fundamental right to equal access to education is basically satisfied.

Every state constitution contains language requiring the state to create and support a public education system. In Michigan, this language is found in Article VIII § 2 of the Constitution and mandates that Michigan must have a system of free public schools (elementary and secondary) as defined by law. All states provide free public education and school is compulsory for children. That said, just because a child is required to go to school does not mean that child is getting an education.<sup>7</sup> A compulsory but inadequate education fulfills the constitutional requirement of a government providing equal access and compliance with the mandatory aspect requiring children to attend school is covered by the compulsory nature of attendance. The adequacy of the education provided does not impact the state's ability to comply with the law. Instead, education can mean the child simply showing up at school, remaining for the day, but not being taught much of anything. It is the difference between equality and equity. Whereas some schools have more resources and can therefore provide a higher level of services and programs, there are schools that have barely any resources that can provide the bare minimum amount of materials needed.

In recent years, education policy activists and others have worked on getting courts to definitively say that there is a “fundamental right” to a public education, specifically they argue for a fundamental right to a “minimally adequate education.”<sup>8</sup>

5 Under the 14th Amendment of the U.S. Constitution:

“All persons born or naturalized in the United States, and subject to the jurisdiction thereof, are citizens of the United States and of the State wherein they reside. No State shall make or enforce any law which shall abridge the privileges or immunities of citizens of the United States; nor shall any State deprive any person of life, liberty, or property, without due process of law; nor deny to any person within its jurisdiction the equal protection of the laws.” U.S.Const. amend. XIV, § 1.

6 The *Brown v. Board of Education* decision “established a right to equal access to education under the United States Constitution. Yet in describing education as ‘perhaps the most important function of state and local governments,’ and further limiting the right to equal opportunity in education to circumstances where ‘the State has undertaken to provide it,’ the Supreme Court foretold of the limits it would subsequently impose on that right.” Jane K. Babin, *Adequate Special Education: Do California Schools Meet the Test?* 37 *San Diego L. Rev.* 211, 236 (2000).

7 Education, meaning learning traditional school subjects, taking tests, going to class, etc. Normal things that happen (or are meant to or expected to happen) in a school.

8 From Michigan Attorney General Dana Nessel’s Amicus Brief, *Brief of Amicus Curiae Michigan Attorney General Dana Nessel in Support of Plaintiffs-Appellants, in Support of Reversal*, June 7, 2019, at [https://www.michigan.gov/documents/ag/151.GaryB.AG\\_Amicus\\_Brief\\_657252\\_7.pdf](https://www.michigan.gov/documents/ag/151.GaryB.AG_Amicus_Brief_657252_7.pdf)

Right now, all children must attend school and, per “*Brown v. Board of Education*,” all children have a fundamental right to equal access to an education. However, an inadequate but compulsory education counts as an education. Therefore, those wanting a fundamental right to a minimally adequate education recognized in court argue in favor of establishing legal standards be put in place to uphold the fundamental right; and, in order for a court to permit a government’s non-compliance with those standards, the government action must be reviewed using strict judicial scrutiny, just like the court would with any other fundamental right violation.

Judges are, generally-speaking, hesitant to attach the label of “fundamental right” to a government provided service, meaning something the government has to actually do as opposed to limiting a government’s actions. That is to say, judges tend not to like creating new “positive” rights as opposed to “negative” rights.

The recent Detroit “right to literacy” case saw plaintiffs arguing that there was a right to literacy and education, and not just a right but a “fundamental right.” Labeling a right as “fundamental” is meant to not only emphasize its importance, but also when a case involves fundamental rights, it signals specific legal tests must be applied. When a government fails to act (or not act) in a constitutional way that advances a fundamental right, courts apply strict scrutiny (the highest level of judicial scrutiny). Strict judicial scrutiny results in a judge deeming a government action or law unconstitutional unless the government proves the law was narrowly tailored and the least restrictive means to achieve a compelling government interest; furthermore, the burden of proof is on the government.

Also, a government cannot claim that it failed to conform to a fundamental right due to lack of funds. This defense does not hold up in court. Whereas a lack of funds is a credible defense in other areas where a government is sued, this defense is not valid when it is a fundamental right that is being denied.

## What is Happening in Flint Community Schools?

In trying to make a positive impact on the schools’ ability to fulfill its purpose, there are common sense, albeit expensive, actions schools can take. If service solvency is about determining whether a government is capable of providing for the health, welfare and safety of its residents—is it capable of fulfilling its purpose as a government—then these softer elements are important as they help schools fulfill their function as well.

The learning that takes place in schools is a service that is not always quantifiable. However, we don’t always need to use traditional measurements; some things are just common sense, like having less tension and yelling in classrooms will improve the learning taking place. Flint School District’s superintendent hired a non-profit organization to help train and educate

teachers and other faculty on how to interact with children who are uncooperative, confrontational, scared, etc., such that problems can actually get resolved as opposed to escalating and resulting in classroom disruption and punishment.

Superintendent Derek Lopez and his staff told us about some of the changes made to hopefully improve the learning environment and academic achievement of students. Some of the changes already introduced are smaller class sizes, more funding to special education programs, not shuffling students to different teachers after the year starts, and renegotiating teacher contracts. These changes have already been made and some cost a lot of money. The increase in special education programming hit the budget hardest, according to the administration.

It is important to understand and acknowledge that these types of things can take time and the rewards of such improvements or reforms might not manifest immediately. While these types of actions may not show visible positive results until further into the future, one of the main goals of school is to produce functioning members of society and to help them learn necessary skills to survive adulthood; we don't know what a child will do or not do as an adult until they are actually an adult and producing something and engaging with the world around them in an independent manner. These things take time, and regular and long-term funding sources are needed to support such changes. It takes money to do these things; if the school district needs more money, what does it do if none can be found? In that case, should drastic action be considered, such as restructuring the district?

As previously stated, Michigan local governments cannot run a general fund deficit. Flint School District ran up a substantial operating deficit last year and must therefore create an Enhanced Deficit Elimination Plan to show what it plans to do to eliminate this deficit. The School District proposed the possibility of closing multiple schools in November 2019 as a way of cutting cost, thereby reducing the district's deficit. However, when brought to Flint residents, this proposal was very unpopular and there was significant pushback. Other school districts, such as Benton Harbor, experienced similar reactions when they proposed school closures. Consequently, Flint school district needed to come up with different ways of eliminating the deficit and lowering debt.

Instead of closing schools, another way to eliminate the deficit and decrease debt is to increase revenue. Recently, Flint School District announced it will "ask voters in March to approve a 25-year \$30 million bond to pay off legacy debts and provide funds for this year's budget."<sup>9</sup> According to Lopez, levying this tax will "help us reduce our debt and deficit in a rapid time and...help us with our infrastructure."<sup>10</sup> The March 2020 ballot will also have language that renews the district's sinking fund bond.<sup>11</sup>

<sup>9</sup> Flint Schools to Borrow \$30 Million, Levy New Tax to Settle Deficit," Citizen Research Council of Michigan, Jan. 10, 2020, at <https://crcmich.org/flint-schools-to-borrow-30-million-levy-new-tax-to-settle-deficit>

<sup>10</sup> Keefer, Winter, "Flint school board votes to get bond proposals on March ballot," Dec. 12, 2019. at [www.mlive.com/news/flint/2019/12/flint-school-board-votes-to-get-bond-proposals-on-march-ballot.html](http://www.mlive.com/news/flint/2019/12/flint-school-board-votes-to-get-bond-proposals-on-march-ballot.html)

<sup>11</sup> Keefer, Winter, "Flint school board votes to get bond proposals on March ballot," Dec. 12, 2019. at [www.mlive.com/news/flint/2019/12/flint-school-board-votes-to-get-bond-proposals-on-march-ballot.html](http://www.mlive.com/news/flint/2019/12/flint-school-board-votes-to-get-bond-proposals-on-march-ballot.html)

## IV. Conclusion and Moving Forward

The ability of Flint Public Schools to meet adequacy standards is severely constrained and it seems unlikely this will change under the current policy structure. The school district had a large negative general fund balance last year, which is not permitted in Michigan. As a result, the district is now under review by the Michigan Department of Treasury. In the past, the school district has issued debt in order to have a positive general fund balance. However, after years of repaying some debt with other debt, Flint School District has built up a substantial amount of debt, and the district is unable to restructure to meet its ongoing operating revenue.

The school finance system is quite detrimental to Flint School District in terms of special education funding, per pupil funding losses and school of choice, and charter unregulated options. Flint needs to comply with mandated needs and research determined funding levels to meet adequacy standards. However, it is unable to do this under the current funding model and, if that model does not change, Flint School District will continue to fall short in this area.

## V. Appendix

### Fiscal and Service Solvency Framework

Fiscal solvency is the concept that a local government can pay its bills as they come due both in the short and long term. In the short term, we refer to the idea of cash and budget solvency. Cash solvency is the idea that a government can pay bills in the next few months to a one year timeframe. Budget solvency implies a one- to three-year timeframe and again the question of whether a government can meet its financial obligations.

Service solvency is the concept that a local government can provide the critical public services that are needed to protect public health, safety and welfare. In the case of a school district government, this would mean the provision of an adequate education to students. Every state constitution contains language requiring the state to create and support a public education system. In Michigan, this language is found in Article VIII § 2 of the Constitution and mandates that Michigan must have a system of free public schools (elementary and secondary) as defined by law.

Fiscal and service solvency are closely interrelated. There are several scenarios we can consider in understanding this

interrelationship. A government that is running out of access to financial resources may be unable to adequately protect the public or provide needed resources. Being fiscally solvent does not necessarily imply that services are being adequately provided. A government may be forced to pay out significant sums of money to meet fixed commitments and even legal obligations from the past. These legacy obligations may undercut the ability to provide current services or maintain and invest in infrastructure.

**Table 1: Fiscal and Service Solvency Interrelationship**

	<b>Fiscally solvent</b>	<b>Fiscally insolvent</b>
<b>Service solvent</b>	Fiscally solvent/ service solvent	Fiscally insolvent/ service solvent
<b>Service insolvent</b>	Fiscally solvent/service insolvent	Fiscally insolvent/ service insolvent