The School District of Philadelphia

FY 2015 Budget in Brief

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Introduction

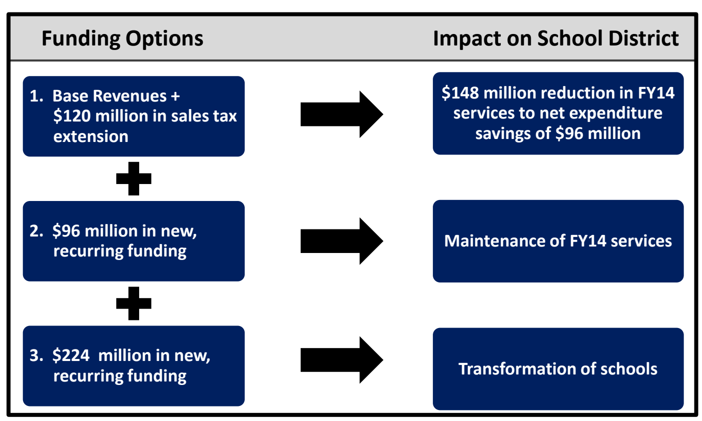
The School District of Philadelphia is guided in each decision it makes by its vision: to deliver on the right of every child in Philadelphia to an excellent public school education and to ensure all children graduate from high school ready to succeed. Though steadfast in this vision, the District has faced unprecedented financial challenges in recent years and, as a result, students, families, and staff have been affected by deep and painful cuts to services and programs. To reverse this trend, the District is seeking additional funding for FY15. In March 2014, the District formally requested $320 million in additional revenues and labor savings in order to operate schools at a level that would adequately serve students and allow for an accelerated transformation of schools. In addition to this requested funding, the District's budget assumes $120 million in new revenues from the authorization of the city's one-percent sales tax. City Council has yet to enact legislation to authorize this tax.

The total funding need for the District is $440 million in FY15, which consists of $120 million in sales tax enactment and $320 million in new request. To maintain a similar level of support for schools and students in FY15 as was available in FY14, a level that is wholly insufficient, the District would require, at minimum, the $120 million from the sales tax enactment and $96.2 million of the newly requested $320 million, totaling $216.2 million in new funding. The remaining $223.8 million of the $320 million requested would fund additional staff and services needed to accelerate the District's transformation of schools.

Whether through new funding or further service reductions, the District is committed to operating within its means. For every dollar not received, the District will need to reduce projected expenditures to align with projected revenues. In the current system, there are few remaining areas to cut that will not materially imperil the District's ability to provide students with an adequate education. Without any additional funding, the District will be forced to cut approximately $148.2 million from FY14 service levels in order to net the $96.2 million in expenditure savings[1] needed to balance the FY15 budget. These cuts would come from schools and administrative supports and would cripple a system already depleted from years of expenditure reductions, including over $140 million in cuts in FY14 alone.

The FY15 reductions would require that **maximum class sizes in the District increase to 37 students in grades 1 through 3, 40 students in grades 4 through 8, and 41 students in high schools**. Additional cuts would include, but are not limited to, **reductions in special education, nurses, school police, alternative education, transportation, facilities, and administrative supports**. These reductions would result in layoffs of over 1,000 staff members.

These cuts will impact the students who are at the highest risk of dropping out, who face the greatest hurdles to opportunity, and for whom an additional investment of time and resources could make the greatest difference. They will hinder superior programs at the District's highest performing schools and further deplete supports desperately needed in the District's lower performing schools. Furthermore, these cuts will reverse the progress made in improving school climate, which includes reducing the number of persistently dangerous schools by 80 percent in the last three years.



There is a collective social responsibility for making high-quality public education available for all students. Now is the time to create a long-term sustainable funding stream for the District.

[1] The $148.2 million in cuts is expected to yield $96.2 million in savings due to employee separation costs. See the "Closing the Gap" section of this document for a detailed explanation of difference between gross and net cuts.

Budget Overview

The District's FY15 lump sum statement includes operating revenues of $2,523.4 million[2] and operating expenditures of $2,814.5 million, resulting in a budget gap of $291.1 million. Additionally, the District is projected to end FY14 with a $28.9 million deficit, which must be paid for in FY15. As a result, there is a total projected gap of $320 million between District revenues and obligations in FY15. The $320 million that the District requested to fill this gap consists of a combination of $150 million in new, recurring revenues from the Commonwealth of Pennsylvania, $75 million in new, recurring revenues from the City of Philadelphia, and $95 million in new, recurring expenditure savings from the District's labor partners. These additional revenues and labor savings would enable the District to:

- Significantly improve early literacy and kindergarten readiness programs through, for example, improved in-classroom supports and summer literacy programs;
- Increase the number of counselors serving District schools by ensuring, at minimum, that each District school has a full-time counselor and that the student-to-counselor ratio decreases, resulting in more personalized services to students;
- Offer a range of extracurricular options for students;
- Support students who demonstrate advanced academic potential through, for example, additional Advanced Placement (AP) programming, SAT preparation opportunities, dual enrollment, and International Baccalaureate programming;
- Provide teachers with opportunities to be observed and receive feedback to help strengthen their effectiveness;
- Replicate high performing schools; and
- Dramatically improve the physical environments of all schools.

It must be noted that while $223.8 million of the requested $320 million is intended to fund District transformation, $96.2 million is required to maintain services at the FY14 level, a level wholly insufficient to meet the needs of Philadelphia's students. With no additional revenues and labor savings, the District would need to reduce expenditures by $96.2 million. Because of separation costs associated with the elimination of positions (discussed in the "Closing the Gap" section of this document), the District will actually need to find $148.2 million worth of additional service reductions in order to realize $96.2 million in savings. Although the goal is for these gap closing measures to affect schools as little as possible, since approximately 61 percent of the budget consists of mandated expenditures, the savings must come largely from the 39 percent of expenditures the District can cut. In short, if funding is not provided, cuts must be made to school budgets and administrative supports.

[2] Projected revenues include $120 million from the sales tax extension.

SCHOOL DISTRICT OF PHILADELPHIA
OPERATING BUDGET
FISCAL YEARS 2013/2014 AND 2014/2015

Amounts in Thousands

	Estimated 2013/2014	**Lump Sum Statement 2014/2015**	**Proposed (without additional funding) 2014/2015**
Revenues	$2,408,527	$2,399,518	$2,399,518
1% Sales Tax		$120,000	$120,000
Other Financing Sources	$65,586	$3,889	$3,889
Total Revenues and Other Financing Sources	**$2,474,113**	**$2,523,407**	**$2,523,407**
Obligations	$2,544,244	$2,812,017	$2,492,017
Other Financing Uses	$2,264	$2,518	$2,518
Total Obligations and Other Financing Uses	**$2,546,508**	**$2,814,535**	**$2,494,535**
Excess (Deficiency) of Revenues and Other Financing Sources Over (Under) Obligations and Other Financing Uses	($72,395)	($291,128)	$28,872
Prior Year Fund Balance (Deficit) July 1	**$39,462**	**($28,872)**	**($28,872)**
Fund Balance Prior to Changes in Reserves	($32,932)	($320,000)	$0
Changes in Reserve	$4,061	$0	$0
Fund Balance (Deficit) June 30	**($28,872)**	**($320,000)**	**$0**
Additional Funding Request		**$320,000**	**$0**
Fund Balance (Deficit) June 30	**($28,872)**	**$0**	**$0**

Notes:

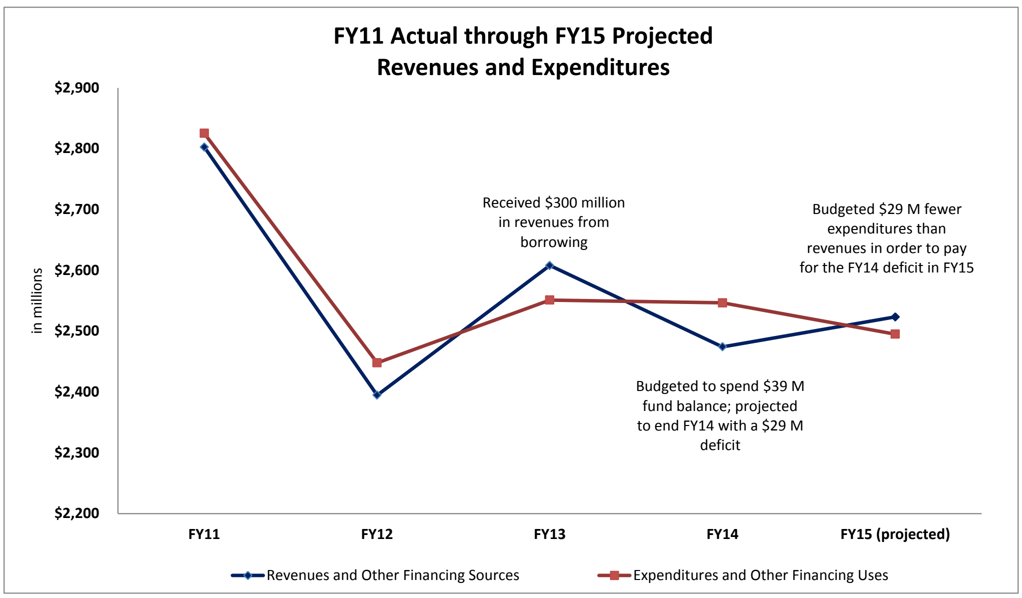
- *The FY14 Estimated Budget projects a $72.4 million funding gap, which is partially filled by $39.5 million in fund balance and $4.0 million in reserves, resulting in a negative $28.9 million projected ending fund balance.*
- *The FY15 Lump Sum Statement, adopted by the SRC on March 27, 2014, includes expenditures that allow the District to accelerate its transformation efforts; however, this increased expenditure level produces a $320 million gap that requires additional funding of $320 million through revenues and labor savings.*
- *The FY15 Proposed Budget includes $96.2 million in gap closing reductions in order to align budgeted revenues with expenditures and account for the FY14 negative ending fund balance. This budget assumes $120 million in revenues from the city's one percent sales tax extension and $39 million in expenditure relief from the state, but not does include any additional funding to maintain FY14 service levels or accelerate the District's transformation.*

How We Got Here

In FY12, the state decreased its revenues to the District for the first time in over 18 years. The lack of a substantial funding increase since then, even with increases in city revenues, has resulted in significant financial challenges for the District. Compounding reduced revenues, the District has been unable to stem the rising costs of many mandated expenditures.

As a result, in FY13, despite significant mid-year reductions, the District borrowed $300 million in order keep schools operating at similar levels to FY12. Understanding it could not continue to borrow funds to operate, in April 2013, the District publicly requested $180 million in additional recurring revenues from the state and city and $133 million in labor concessions to ensure that the District could provide similar service levels again in FY14. Without a promise of additional revenues and labor savings by May 30, 2013, the District adopted an FY14 budget that included dramatic cuts, including nearly 3,800 layoffs,[3] to its already insufficient budget.

Subsequent to the FY14 budget adoption, the District secured an additional $112 million in revenues from the city and state. While this funding allowed for necessary personnel and resources to be restored in schools, it fell $68 million short of the revenues requested and over $200 million short of the resources requested to maintain FY13 service levels. Additionally, $95 million of the $112 million provided by the city and state in FY14 were one-time revenues. Without recurring and growing revenues in FY15, the District will be forced to once again cut significantly from a system already depleted from previous years of reductions.



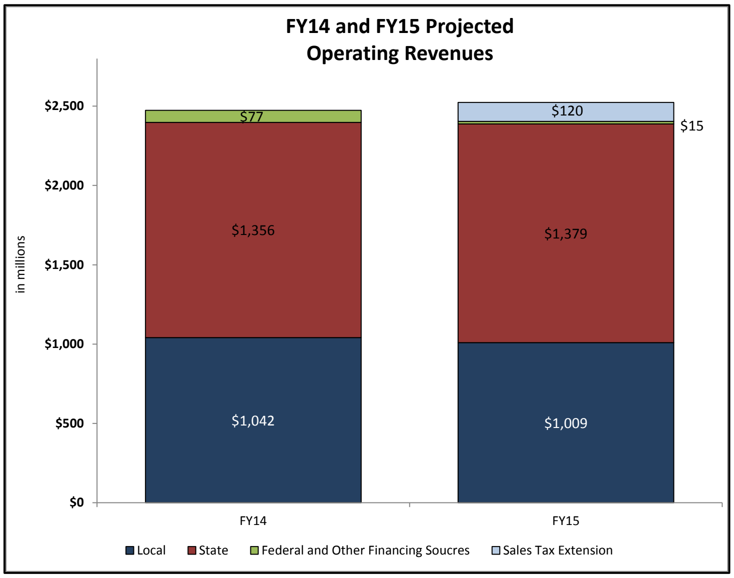
Revenues

Projected revenues, which exclude the District's request for $150 million in revenues from the state and $75 million in revenues from the city, are projected to increase by $49.3 million, or approximately 2.0 percent, from FY14 to FY15. The largest increase is projected in local tax revenues, as the District anticipates $120 million in additional recurring revenues in FY15 from the enactment of the city's one percent sales tax, which is required by statute to be paid to the District.[4] State revenues are projected to grow by $23.4 million from FY14 to FY15, with the sole driver of growth being an increase in Public School Employees'

[3] Includes operating and grants layoffs
[4] Act 52. Article II-B. § 201-B(e)(1)
http://www.legis.state.pa.us/cfdocs/legis/li/uconsCheck.cfm?yr=2013&sessInd=0&act=52

Retirement System (PSERS) reimbursement as a result of the significant rise in the PSERS contribution rate from FY14 to FY15.

Two revenue sources are expected to decrease significantly in FY15 as a result of one-time funding in FY14. Local non-tax revenues are projected to decrease by $46.6 million as the $45 million one-time state funding (passed through to the city and then to the District) expires and other miscellaneous revenues are projected to decrease. Additionally, other financing sources are projected to decrease by $61.7 million due to the elimination of one-time building sales revenue.



A more detailed categorization of the District's revenues is below:

Local Tax Revenues: Local tax revenues are projected to increase by $134.2 million, primarily due to $120 million from the enactment of the city's one-percent sales tax and a $13.6 million increase in real estate tax revenue. The remaining $0.6 million increase is from all other taxes (e.g., business use and occupancy tax, liquor sales tax, school income tax, and public utility realty taxes).

Local Non-Tax Revenues: Local non-tax revenues are projected to decrease by $46.6 million in FY15 due to the elimination of $45 million in one-time state revenue (passed through to the city and then to the District) and reductions in miscellaneous non-tax revenue. Local non-tax revenues primarily consist of the city grant, the Parking Authority contribution, gaming revenue, and stadium agreements. The city grant, projected to remain flat from FY14 to FY15, makes up approximately 69 percent of all local non-tax revenues in FY15.

State Revenues: State revenues are projected to increase by $23.4 million in FY15. However, if the increase in PSERS reimbursement ($23.6 million) is excluded, state revenues are actually expected to decrease by $0.2 million from FY14 to FY15 primarily due to a reduction in debt service revenues. The increase in PSERS reimbursement is provided to pay for a portion of the District's rising, mandated PSERS expenditures in FY15. The largest source of state revenue is the basic education subsidy, which makes up approximately 68 percent of state revenues in FY15. Other large revenue sources include funding for transportation, special education, and reimbursement for PSERS. Growth in the state's basic, transportation, vocational, and special education subsidies are cumulatively projected to increase by less than one percent in FY15 based on the Governor's Proposed Budget.

Federal Revenues: Federal revenues account for less than one percent of FY15 operating revenues. Nearly all of the District's federal revenues (99 percent) are from the federal debt service subsidy, for which revenue is based on the District's debt schedule. Federal revenues are anticipated to remain relatively flat in FY15.

Other Financing Sources: Other financing sources consist of revenues from the sale of property and transfers from other funds. In FY14, anticipated building sales and city funding are projected to yield approximately $61.4 million in revenues. As these are one-time revenues, other financing sources are projected to decrease by over $61 million in FY15 to $3.9 million. Revenues from transfers from other funds are anticipated to remain relatively flat in FY15.

The Governor of Pennsylvania included funding in his proposed budget for a new Ready to Learn Grant, which is expected to provide an additional $29 million to the District. Using these funds, the District intends to seek a waiver to shift $29 million in current expenditures from the operating fund to the grants fund, thereby making available $29 million in the operating budget to cover other expenditures. These savings are addressed in the expenditure section of this document.

Additionally, the Mayor of Philadelphia proposed a tax on cigarettes that, if passed, could generate an estimated $83 million for the School District in FY15. However, the District has not included these revenues in its FY15 projection as legislation for the tax has not yet been introduced in the state legislature.

In addition to its operating revenues, the District also receives grants and food service revenues and borrows capital funds to help support its schools and students. These funds are addressed in more detail later in this document. Considering all funds, revenue growth has been significantly outpaced by the growth of the District's expenditures.

Expenditures

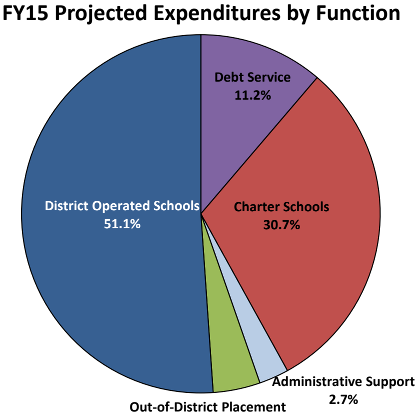
The natural growth of District expenditures, many of which are legally mandated, is projected to continue in FY15. The District has requested additional funding and labor savings in order to expend $2,814.5 million in FY15, a spending level that would enable the District to accelerate its transformation of schools. However, as a part of the District's commitment to spend only within its means, it has also prepared a budget with only $2,494.5 million worth of expenditures for FY15, which is approximately $320 million less than was requested in the lump sum statement and $96.2 million less than FY14 service levels. Based on this projection, in order to balance the budget, the District will need to reduce FY14 services by approximately $148.2 million to net savings of $96.2 million, as separation costs from layoffs are anticipated to cost the District $52.0 million. These cuts and the difference between gross cuts and net savings are further addressed in the "Closing the Gap" section of this document.

This proposed budget is not what the District considers educationally sound. Since FY11, the growth of mandatory expenditures without a corresponding growth in revenues has left District schools with reduced resources and staff.

The expenditure components of the District's FY15 budget are detailed below:

- District Operated Schools: $1,433.2 million
- Charter Schools: $766.7 million
- Debt Service: $280.4 million
- Out of District Placement: $106.0 million
- Administrative Support: $74.5 million
- Undistributed Budgetary Adjustments: -$70.0 million
- Gap Closing Reductions: -$96.2 million

FY15 Projected Expenditures by Function



Note: Undistributed budgetary adjustments and gap closing reductions are distributed for the purpose of the chart

District Operated Schools

The largest portion of District operating funds are expended on District operated schools. Excluding debt service, approximately $1,433.2 million of the District's $2,494.5 million is spent on instruction, support, and operations in schools. Over $900 million of these expenditures are spent on regular and special education instruction. The second largest subset of expenses, approximately $283.2 million, pays for school operations, including facilities, utilities, and transportation for District schools. The remaining $241.4 million is spent on a combination of supports for schools including:

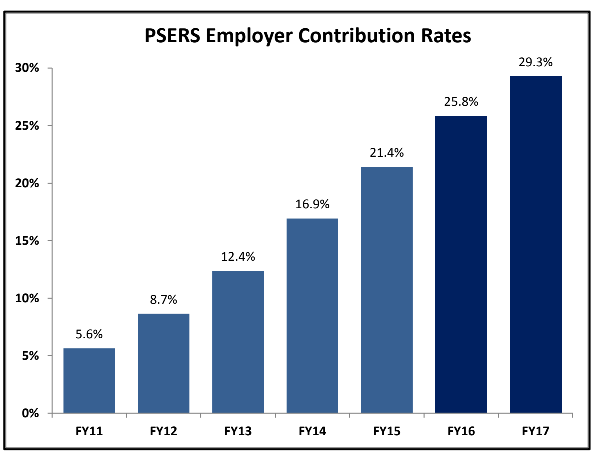
- $63.3 million for nurses, counselors, and psychologists;
- $37.0 million for English Language Learners;
- $34.0 million for school police;
- $28.8 million for alternative education;
- $18.6 million for per diem substitutes;
- $8.7 million for additional supports for promise academies;
- $7.5 million for athletics;
- $7.2 million for itinerant music; and
- $36.4 million for various other supports for schools, such as education technology, professional development, early childhood, summer programs, extra-curricular activities, losses and judgments, and insurance, among others.

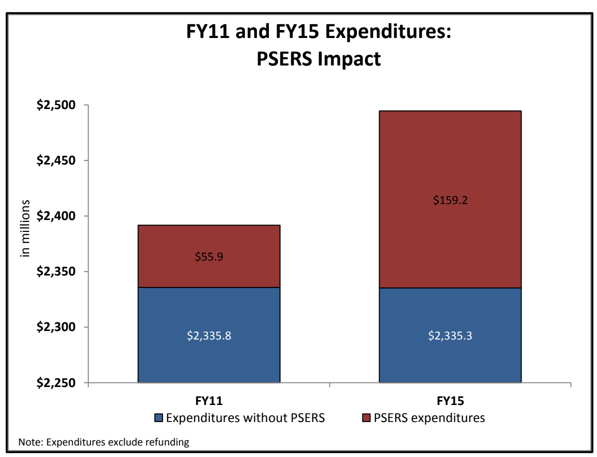
Administrative Support

The District's central office supports students, families, and schools in Philadelphia, including charter and non-District schools. In FY15, it is projected that administrative supports will cost $74.5 million, or 2.7 percent of the District's overall operating budget. In comparison, District of Columba Public Schools (DCPS) spends approximately 5 percent of its budget on central administration.[5] Since FY11, the District has significantly reduced its central office costs, including reductions of over 385 operating fund full-time equivalents (FTEs), equating to a 46.0 percent staff reduction over the last five years.

Rising Cost of Personnel Benefits

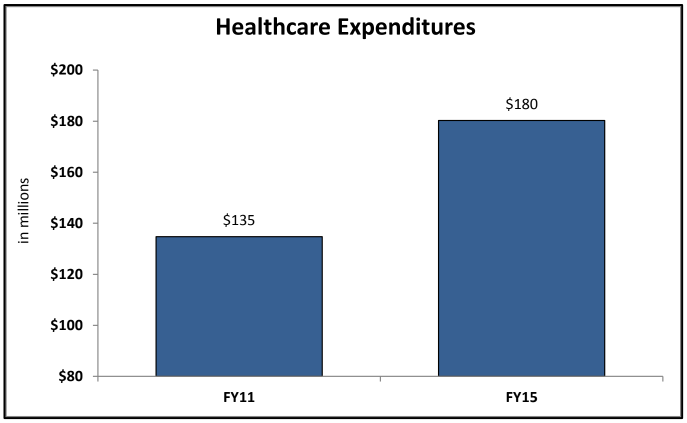
A major cost driver within schools and administration is the rising cost of personnel benefits, namely retirement contributions and medical costs. Retirement contributions are a state mandated expenditure over which the School District has no control. The employer contribution rate for the PSERS, which is set forth in state legislation, has been growing exponentially in recent years, and, as a result, is draining District resources. From FY11 to FY15, the PSERS rate has grown from 5.6 percent to 21.4 percent and is expected to continue to rise significantly in FY16 and FY17. In fact, if PSERS contributions were removed from District expenditures in FY11 and FY15, the District's expenditures in FY15 would be less than in FY11.





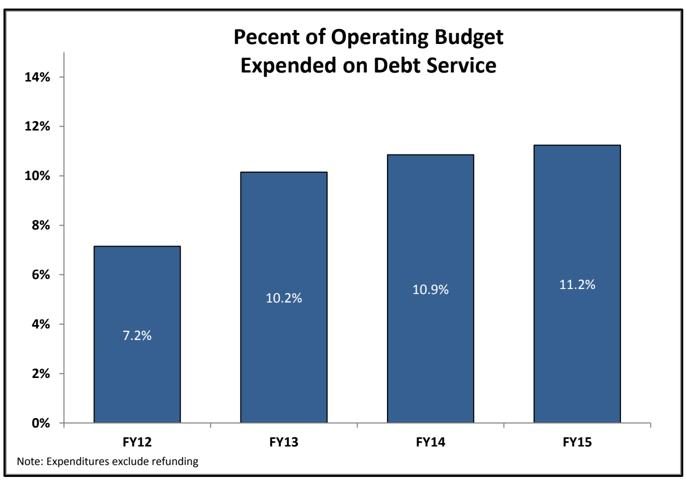
[5] FY13 DCPS Budget Guide; http://dcps.dc.gov/DCPS/Files/downloads/ABOUT%20DCPS/Budget%20-%20Finance/FY13%20documents/DCPS-Budget-Guide_FY2013.pdf

The District's medical, dental, and vision costs have also continued to grow in recent years[6]. Budgeted FY15 medical costs are $45.5 million, or 33.7 percent, higher than FY11 costs. As a result, a growing share of District revenues must be expended on personnel benefits rather than additional services.



Debt Service

Payments for debt service have become an increasingly larger share of the District's overall operating budget in recent years. In FY15, it is projected that the District will spend $280.4 million, or 11.2 percent of its budget, on debt service. This is a significant increase over FY12, when debt service constituted approximately 7.2 percent[7] of the District's operating budget. One reason for this increase is due to the overall decrease of the District's operating budget in recent years; as the overall budget has decreased, the percent of the budget used to pay debt service has increased. As a result, a smaller share of the District's operating budget can be spent directly on District schools. While in the short term, the District has little flexibility with regard to debt service expenditures, in the long run, the District is committed to managing the size of its bond issuance to ensure that a reasonable percentage of District funds is spent on paying debt.



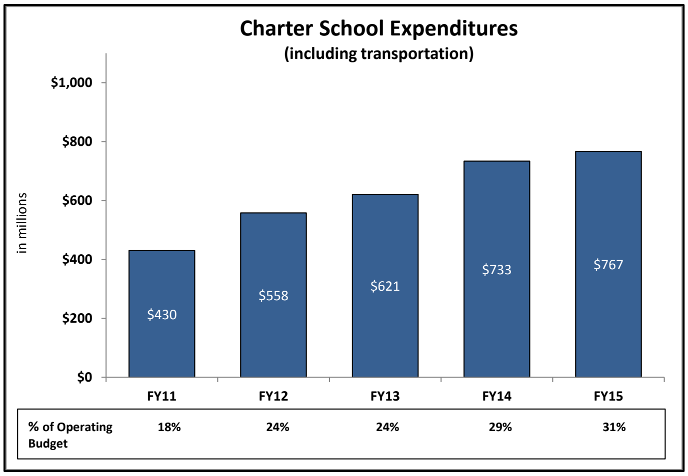
Charter Schools

Payments to charter schools are mandated expenses that have grown exponentially in recent years. In FY11, charter schools constituted approximately 18 percent of the District's operating budget. In FY15, charter schools are projected to be approximately 31 percent of the District's operating budget, costing

[6] The District's new collective bargaining agreement with the Commonwealth Association of School Administrators (CASA), discussed in this document, does include important cost-saving changes to the health care plan and implements employee contributions to health care coverage costs. The District has been seeking similar benefits reforms in its labor negotiations with the Philadelphia Federation of Teachers (PFT), which represents the majority of District employees. Non-represented employees at the District already contribute to their health care coverage.

[7] Expenditures exclude bond refunding costs.

approximately $766.7 million. As a result, a smaller share of the District's operating budget can be spent on District operated schools. In an effort to control these costs and ensure high performing charter schools, the District is taking concrete steps to become a better charter authorizer.



Out-of-District Placement

The District is responsible for paying for educational services for Philadelphia students in institutional settings and other placements outside of Philadelphia. In FY15, it is projected that the District will spend $106.0 million on out-of-district placement, consisting of $84.6 million in payments for educational services and $21.4 million for transportation for these students. Out-of-district placement costs have remained relatively constant in recent years.

Undistributed Budgetary Adjustments

Undistributed budgetary adjustments consist of budget items that affect the entire operating budget but cannot be assigned to a particular departmental budget or set of budgets. These items include:

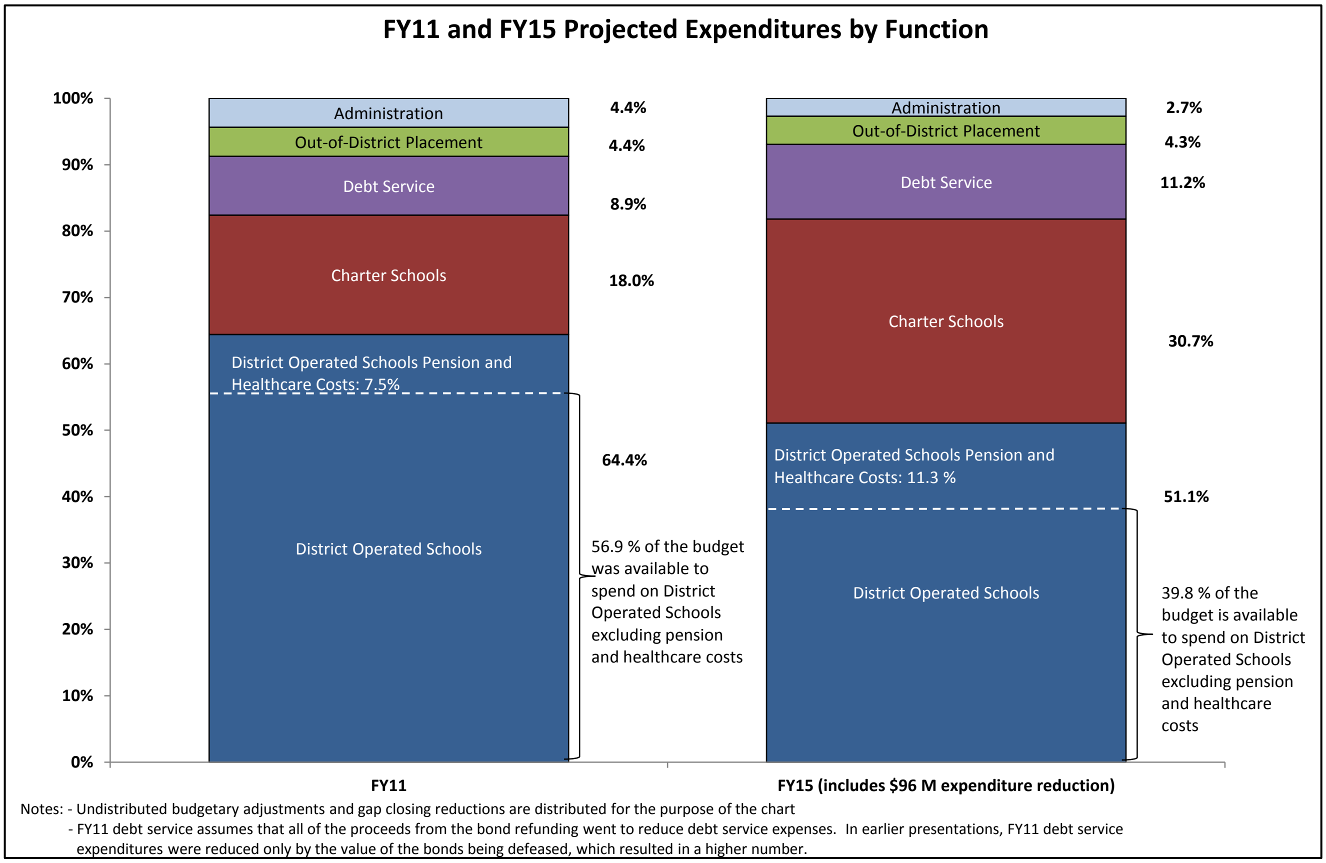
- Personnel costs/savings not associated with a particular department (e.g., benefits provided to retirees or lower separation costs due to the restoration of positions);
- Cancellation of prior year encumbrances (i.e., costs recognized in a prior year that never materialize or cost less than expected);
- Lapsed appropriations (i.e., unspent budgets); and
- Budgetary reserves for unforeseen events (i.e., snow removal).

In FY15, undistributed budgetary adjustments also include $39.0 million in anticipated budget relief from the state and $8 million in savings from the newly ratified collective bargaining agreement with the Commonwealth Association of School Administrators (CASA). Twenty-nine ($29.0) million of the state relief is expected to come from the Ready to Learn Grant that was proposed in the Governor's Budget; the other $10 million is from anticipated pension relief. While the Ready to Learn grant cannot be used as operating revenues, the District intends seek a waiver to shift operating expenditures to the grants funds to be paid for with the Governor's new Ready to Learn Grant.   The $8 million in savings from CASA is a result of the new collective bargaining agreement with principals, assistant principals, and other administrators ,which includes significant salary and healthcare concessions. The District anticipates saving approximately $20 million over the life of the agreement; these savings are vital to the District's effort to maintain and improve services in schools while remaining fiscally responsible.

Gap Closing Reductions

In addition to assuming the $120 million from the enactment of the sales tax ordinance, the FY15 proposed budget requires an additional $96.2 million worth of expenditure savings in order to balance the budget. Due to the separation costs that must be paid in the case of layoffs, the District projects it will need to cut $148.2 million in expenditures to net the $96.2 million needed to close the budget gap. With an already bare-bones budget, these cuts will be devastating to students, families, teachers, and administrators. These gap closing reductions and a deeper explanation of the savings lost to separation costs are detailed below in the "Closing the Gap" section.

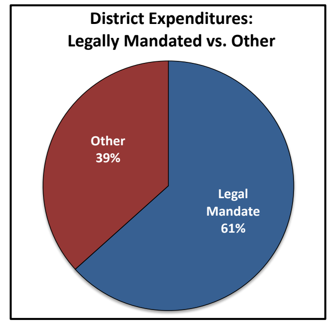
The chart below highlights District expenditures in FY11 compared to District expenditures in FY15, after expenditures have been reduced by $96.2 million.



Closing the Gap

Balancing the budget without additional recurring revenues and labor savings will require cuts that will be immensely damaging to the District's students, families, and schools. This section discusses the impact of reducing expenditures to net $96.2 million in savings to balance the FY15 budget. The District has assumed additional revenues of $120 million from the enactment of the sales tax ordinance in its budget. Given the cuts required to realize $96.2 million in expenditures savings, it is unimaginable what an additional $120 million in reductions would do to District schools and students if one-percent sales tax is not enacted.

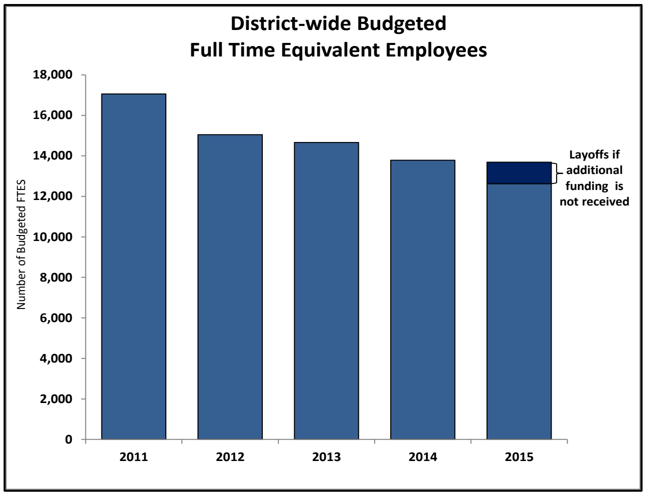
Challenges in Closing the Gap: Why the District Only Has Bad Options

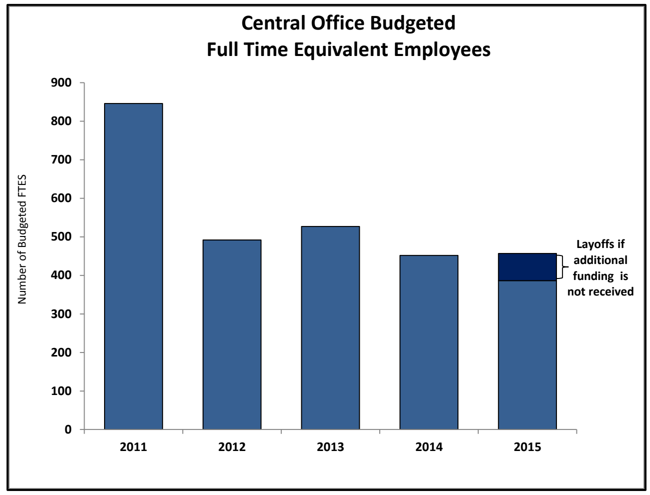


The District has little flexibility regarding what can be cut. Prior to closing the gap, approximately 61 percent of the District's operating budget is spent on legally mandated expenditures. These mandated obligations include: charter school payments, debt service, special education, out-of-district placements, transportation costs for non-district schools, and other essential positions and services. After those payments, only 39 percent, or $1,011.5 million, of the operating budget remains. Therefore, most, if not all, cuts must be taken from the non-mandatory spending areas.

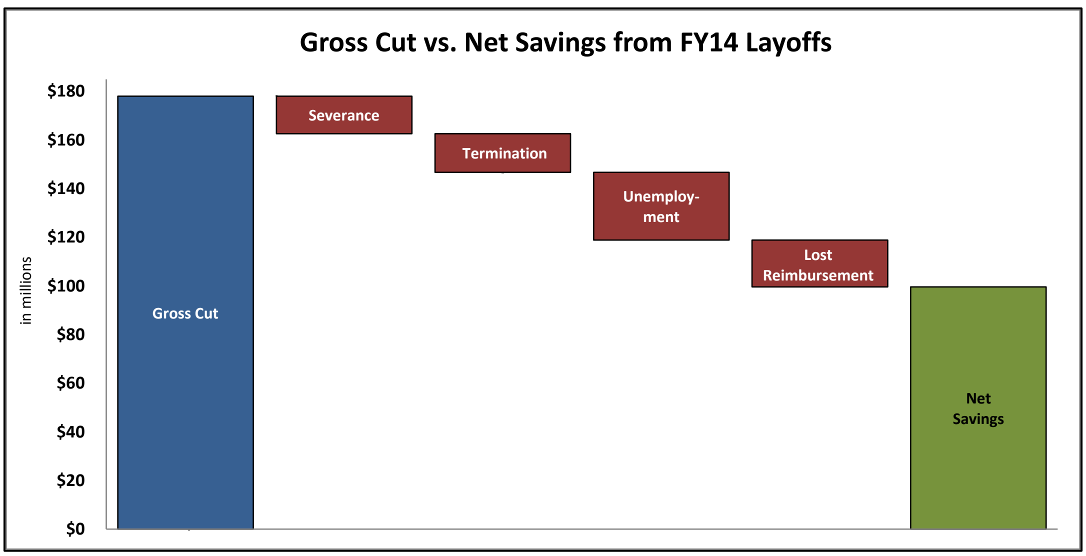
Mandatory Expenditure Area	Required By	Amount
Charter School Payments	PA School Code	$730.1
Debt Service	Local Government Unit Debt Act	$280.4
Special Education	(United States Code) Individuals with Disabilities Education Act; PA School Code; PA Code Title 22	$222.4
Special Education Transportation	(United States Code) Individuals with Disabilities Education Act; PA School Code	$70.8
Out of District Placement	PA School Code	$67.9
Principals	PA School Code	$45.4
English Language Learners	(United States Code) Title VI of The Civil Rights Act	$36.9
Charter School Transportation	PA School Code	$33.1
School Nurses	PA School Code; (United States Code) Individuals with Disabilities Education Act	$21.4
Building Engineers	PA School Code - District of the First Class	$17.7
Psychologists	PA Code Title 22; (United States Code) Individuals with Disabilities Education Act	$15.0
Non Public School Services	Act 89; PA School Code	$13.7
Per Diem Substitute Service	PA School Code	$11.2
Kindergarten	PA School Code	$6.7
Temporary Borrowing	PA School Code	$3.4
Insurance	PA School Code	$2.2
Support Personnel	Section 504 of the Rehabilitation Act of 1973	$1.0
Total		**$1,579.2**

The District has little flexibility regarding where to cut. Over the course of the past five years, schools and central administration have experienced significant budget reductions. In FY14, in order to balance the budget, the District made over $140 million in devastating cuts to schools and administration. While some positions were later restored with one-time funding, the programs and services provided to students in FY14 were drastically reduced compared to historic levels. Additionally, the District's central administration has significantly reduced its staffing and expenditures in recent years. Prior to any further cuts in FY15, the District's central office is projected to have approximately 46 percent fewer full time employees in FY15 than in FY11. If the necessary funding is not provided and the District is forced to implement expenditure reductions, the District as a whole is projected to lose over 1,000 more employees. Since schools and administration have already experienced significant expenditure reductions in prior years, there is simply little room left for additional expenditure cuts without compromising operational viability.





<u>The District has to cut more than the minimum savings amount needed.</u> The District only realizes savings on a portion of employee costs from layoffs. Every time the District lays off an employee, a portion of the expenditures saved must be paid to or for the laid off employee in the form of termination, unemployment, and severance pay. Additionally, the District loses reimbursement from the state for PSERS for each laid off employee, a loss that recurs annually. For example, when the District laid off 3,790 employees in FY14, the gross reduction was $178 million. Offset by approximately $78 million in separation costs and lost reimbursements, the District only realized $100 million in savings, or 56 percent, of the laid off employee's costs.[8]



The proposed budget projects that as much as $71 million of the $96.2 million budget gap will need to come from position reductions. Assuming a separation cost rate similar to the FY14 layoffs, the District would need to reduce staff expenditures by approximately $123 million in order to net $71 million in labor savings, as $52 million would be spent on separation costs and lost reimbursement.[9]

[8] Unemployment, termination, and severance costs are one year costs only. Loss of PSERS reimbursement is a recurring cost.
[9] This assumes $57 million in net instructional cuts, $9 million in net non-instructional cuts, and $5 million in net administrative cuts would come through layoffs.

Proposed Gap Closing Reductions: Choosing Among Bad Options

Many of the cuts needed to balance the budget will be devastating to students, families, and staff. In an effort to do as little harm as possible to instruction, the District's proposed budget includes $37.4 million worth of administrative and non-instructional cuts first, which would yield approximately $27.2 million in savings. However, given the large portion of the District's budget that is spent on mandated expenditures and the hundreds of millions of dollars already cut from the budget in prior years, the District simply has nowhere left to cut other than instruction. Therefore, it is proposed that the remaining $110.8 million in cuts, which is projected to yield approximately $69.0 million in savings, come from classroom instruction. Though not endorsed by the District as educationally sound, the District is committed to realizing $96.2 million in net savings to achieve fiscal balance through the following means:

Savings Area	Gross Savings	Separation Costs	Net Savings
Administrative Cuts	$9.9 million	$3.9 million	$6.0 million
Non-Instructional Cuts	$27.5 million	$6.3 million	$21.2 million
Instructional Cuts	$110.8 million	$41.8 million	$69.0 million
Total	**$148.2 million**	**$51.9 million**	**$96.2 million**

Administrative Cuts: $9.9 million

- *Administrative Support: $9.9 million.* Schools will receive limited information systems and technical support, parent- and community-focused services and activities will be greatly reduced, and functional support for schools (e.g., field trips) will be lessened. The District could also face additional auditing risks and risk of non-compliance with state and federal mandates.

Non-Instructional Cuts: $27.5 million

- *Facilities: $12.0 million*. Fewer staff will be available to maintain the District's continually aging school buildings, meaning greater health and safety risk for students.
- *School Police: $5.4 million.* Funding for school police will be reduced by nearly sixteen percent.
- *School Nurses: $4.3 million.* Funding for school nurses will be reduced by nearly eighteen percent.
- *Transportation: $3.5 million.* Reduced transportation resources will result in increased student travel time as the number and efficiency of routes will be reduced, potentially increasing ride time for students to as long two hours.
- *Space Rental and Losses and Judgments: $2.3 million.* The District will have fewer resources to pay for judgments against the District.

Instructional Cuts: $110.8 million

- *Drastically increased class size: $92.9 million.* The District would need to raise class sizes by seven to eight students per class in grades 1 through 12 in order to layoff enough staff to realize gross expenditures reductions of $92.9 million and net savings of $52.0 million. This action would require layoffs of approximately 810 teachers and would undermine the District's efforts to provide personalized learning experiences for students, drain the District of many talented and dedicated teachers, and strain the physical capacity of school facilities. The proposed class size maximums to realize such savings are detailed below.

Grades	Current Class Size Maximum	Proposed Class Size Maximum	Difference: Additional Students Per Class
1-3	30	37	7
4-8 (Middle)	33	40	7
9-12 (High)	33	41	8
CTE	24	32	8

- *Special Education: $9.1 million.* Special education services will be constrained to providing only basic, legally mandated services, which are inadequate to ensuring sufficient improvement in students' social, emotional, and behavioral health and educational outcomes.

- *Substitute Services: $3.4 million.* Funding for substitute services will be reduced by approximately eighteen percent.
- *Promise Academies: $2.4 million*. The District will further dilute its internal turnaround model. Teachers currently teaching in the District's lowest performing schools will not get the additional support and training necessary to help them improve student performance.
- *Alternative Education: $2.3 million.* Programs that have been successful in helping more students graduate will be cut, decreasing the number of students who can be served through these pathways.
- *Contracts: $0.7 million:* Six schools with challenging safety environments will lose conflict resolution support and a special program for a magnet school will be discontinued.

While necessary to be fiscally responsible, the District in no way endorses any of these gap closing measures as educationally sound. All of these measures are counter to the District's fundamental commitment to provide students with a high quality education. The District reserves the right to adjust its proposed reductions and savings methods prior to the final budget adoption by the SRC.

Risks to the Budget

It is important to note that as devastating as these cuts will be, there are risks associated with some of the budgetary assumptions that have been made. Specifically, additional risks assumed in the FY15 proposed budget but not associated with the proposed gap closing reductions include:

- *Sales tax extension: $120 million*. While the state legislature has enacted legislation allowing for the enactment of the one percent sales tax, City Council has yet to authorize the ordinance implementing the tax in accordance with the statute.
- *Ready to Learn Grant: $29 million.* The Governor proposed the creation of the Ready to Learn Grant, which is projected to provide $29 million to the District. However, the legislature has yet to approve this funding, and even if the legislature passes this legislation, it is not certain that $29 million would be the final amount allotted to the District. Additionally, the District has assumed that it could receive a waiver so this funding can be used to pay for current operating expenditures in FY15; however, restrictions on how this money can be spent could prevent the District from being able to utilize these funds as planned.
- *Pension reform: $10 million.* Pension reform legislation is currently pending in the state legislature. FY15 savings in this area are dependent on the passage of legislation that would provide $10 million worth of savings that can be counted towards the District's operating fund.
- *Zero fund balance.* In order to provide schools with as many resources as revenues could allow, the District fully depleted its fund balance in FY14 and is projected to have a zero fund balance in FY15. Without a positive fund balance, the District has no cushion to balance any potential budgetary shortfall in FY15.

Additional Resources

In addition to the operating budget revenues, the District also receives grant funding to supplement school services, issues debt for capital improvements, and maintains a food services enterprise fund to provide meals to students.

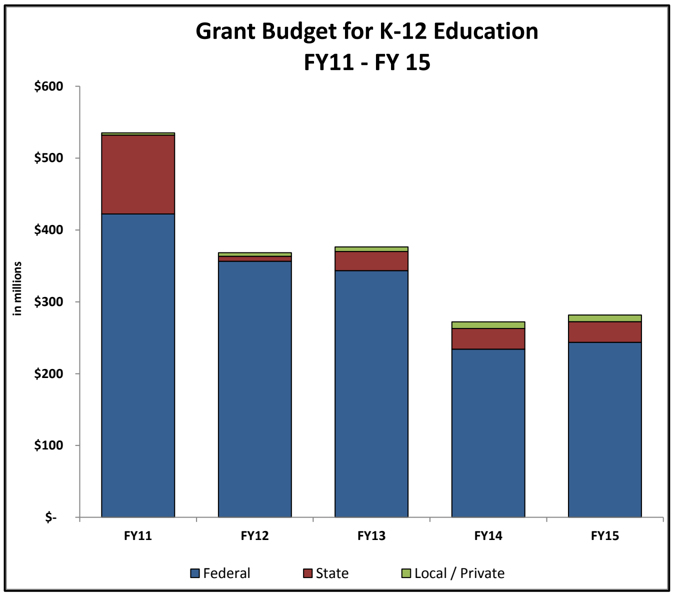
Grant Funds

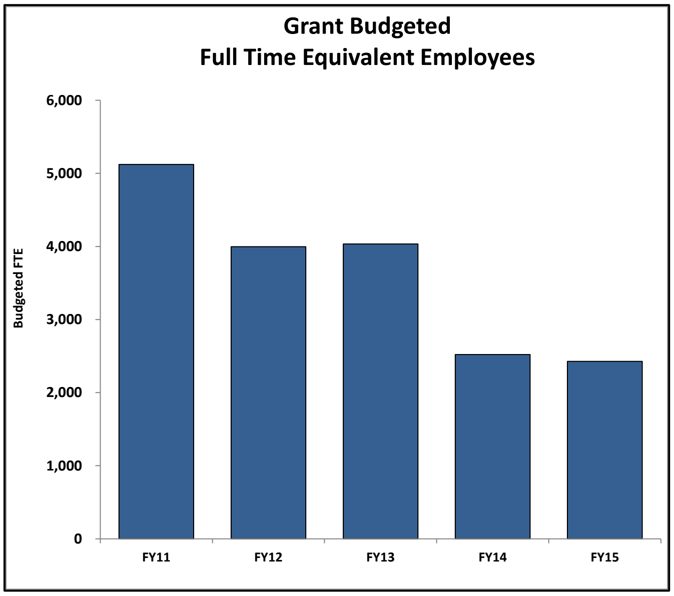
The School District experienced a significant loss of approximately $134 million, or 32.7 percent, in FY14 owing mainly to:

- Title I and School Improvement Stimulus Funds reductions;
- Title II funds reductions;
- Department of Labor Grant expiration; and
- Federal Sequestration Budget reductions.

This drastic reduction has had an adverse impact on schools' abilities to provide supplemental services to students. Specifically, the decline in grant revenues has resulted in the elimination of over 1,000 positions, many of which were in schools and provided direct services to students. The staff reduction in FY14 has compounded the challenges that schools face, owing to a significantly lower operating allocation.

The District's grant revenues for FY15 are estimated to be comparable to those in FY14 and, as a result, schools are unlikely to receive significant support beyond what was provided in FY14.



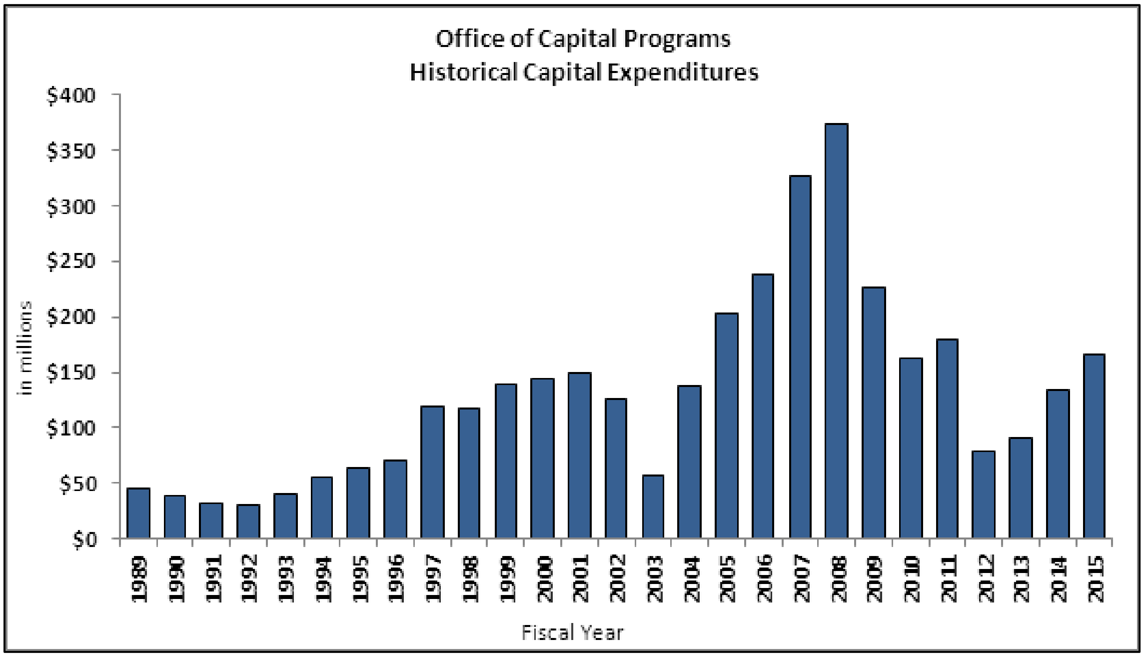


Capital Improvement Program

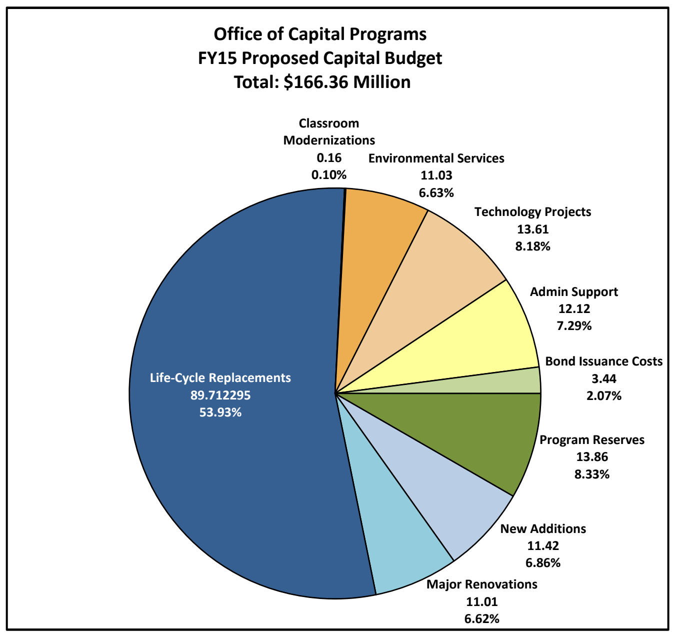
The School District's Capital Improvement Program is a set of projects that build, rebuild, replace, and renovate the District's facilities. Capital projects must have a "useful life" of five years or more. Most capital projects last much longer. The School District's Capital Improvement Program includes the building of new schools and additions, the renovation of existing facilities, and life-cycle replacements for critical building elements like roofs, boilers, and windows. The largest percentage of the capital budget is spent on life-cycle replacements such as boilers, windows, HVAC systems, and building additions.

The School District funds the Capital Improvement Program by selling bonds, which are long-term District debt repayable with interest usually over 30 years. The proceeds from the District's bond sales are the funding source for the Capital Improvement Program. Each year the District adopts a capital budget to reflect that fiscal year's Capital Improvement Plan. The capital budget is used to allocate funds for professional services (i.e. architects, engineers, appraisers, contractors, attorneys), land, equipment, supplies, other items that support the District's capital projects, and for the costs of the projects in the capital budget. The debt service fund in the operating budget is used to make the District's payments of principal and interest associated with the District's bonds.

As recently as the 1990s, the District was spending as little as $40 million annually on repair and reconstruction of its facilities, leading to a deferred maintenance backlog. Despite dramatic increases in the levels of investment in facilities over the past 10 years (see chart below), this backlog has still not been eliminated.



Investment increased dramatically in the past decade, and the District's average annual expenditures from 1989 to 2015 (projected) have been $130.0 million a year. However, this increased expenditure level still remains well below the optimal level of spending the District needs to maintain its facilities as:



- The total estimated value of the District's real property portfolio is currently $7.6 billion (356 buildings), including primary school building, administration, field houses, annexes (little school houses), and garages.
- With an average building age of 67.7 years, the Capital Program Office has estimated the District's optimal annual life cycle replacement costs to be $320 million. This amount has been determined by counting the District's major building components such as roofs, windows, boilers, building envelopes, doors, chillers, elevators, cooling towers, fire alarms, and automatic temperature control systems; evaluating their respective expected life cycles; estimating their respective current replacement costs; and summing up the costs per year per component.
- Life cycle replacement targets for the past several years were:
  - $122.0 million in FY11
  - $33.7 million in FY12
  - $35.3 million in FY13
  - $72.1 million in FY14
  - $89.7 million in FY15 (projected)

The proposed capital budget for FY15 is $166.4 million, and, as of March 2014, will partially fund 38 active construction contracts at 22 locations including:

- Advertisement and award of the Murrell Dobbins addition and major renovation;

- Completion of the West Philadelphia athletic field renovation;
- $89.7 million in life-cycle replacements, comprised of:
  - $14.6 million for boiler and chiller replacements;
  - $33.2 million for structural and façade restorations;
  - $12.1 million for roof replacements;
  - $3.9 million for window replacements; and
  - $25.9 million for electrical systems upgrades and replacements;
- 63 design projects.

Food Services

The District provides school breakfasts and lunches through its food services enterprise fund. A large majority of the $84 million in revenues come from federal grants for free and reduced price meals for students at or below 185 percent of the poverty level. The remaining revenues come from payments from students who are not eligible for subsidy. The District also provides food services to over 20 charter schools on a cost neutral basis to the District; the District receives payments for the services provided to charter schools. The food services fund has been on a multi-year path to eliminate a significant negative fund balance that peaked in FY10. The fund will return to balance in FY15 for the first time in nearly a decade.

The District has been a national leader in providing free lunches to every student in schools with the highest levels of poverty. In recent years, food services has been focused on improving the amount of healthy and fresh food and beverages provided to students in compliance with the SRC and U.S. Department of Agriculture policies. Part of this effort has involved a gradual conversion of more schools to full service cafeterias from satellite food service.

The Need to Invest

Without additional revenues and after consecutive years of deep cuts, there is no way to close the projected budget gap without affecting critical positions and programs, all of which are essential to the functioning of a school system. The lack of sufficient funding puts all of the District's schools in an extremely vulnerable position.

For the District's schools and families, closing the projected budget gap is likely to affect:

- **Class size** owing to the increased likelihood of a shrinking educator workforce.
- **Staff and programs that provide for students' health and safety**, including nurses, counselors, psychologists, school police officers, and anti-bullying and conflict resolution programs.
- **Programs that help build character and keep students engaged**, including music, athletics, and school clubs.
- **School climate and structural stability**, as the District will be further constrained in its ability to meet the cleaning and physical maintenance needs of all its buildings.
- **Career and technical education programs**, as the District must first ensure that students have the resources to meet the state's basic graduation requirements before it can invest in specialized programs.

Budgets are more than numbers and balance sheets; they communicate values, commitments and priorities. Disinvestment in Philadelphia schools is causing real and measurable damage to the District's system of schools and to students' futures. This is not just a matter of stemming disinvestment; it is a matter of necessary reinvestment. The Commonwealth of Pennsylvania, the City of Philadelphia, and the District's labor partners can take the lead in standing up for Philadelphia schools and Philadelphia students by providing a recurring investment of $320 million.