Preliminary Five-Year Plan (FY18-22) and Lump Sum Statement (FY17-18)

March 23, 2017

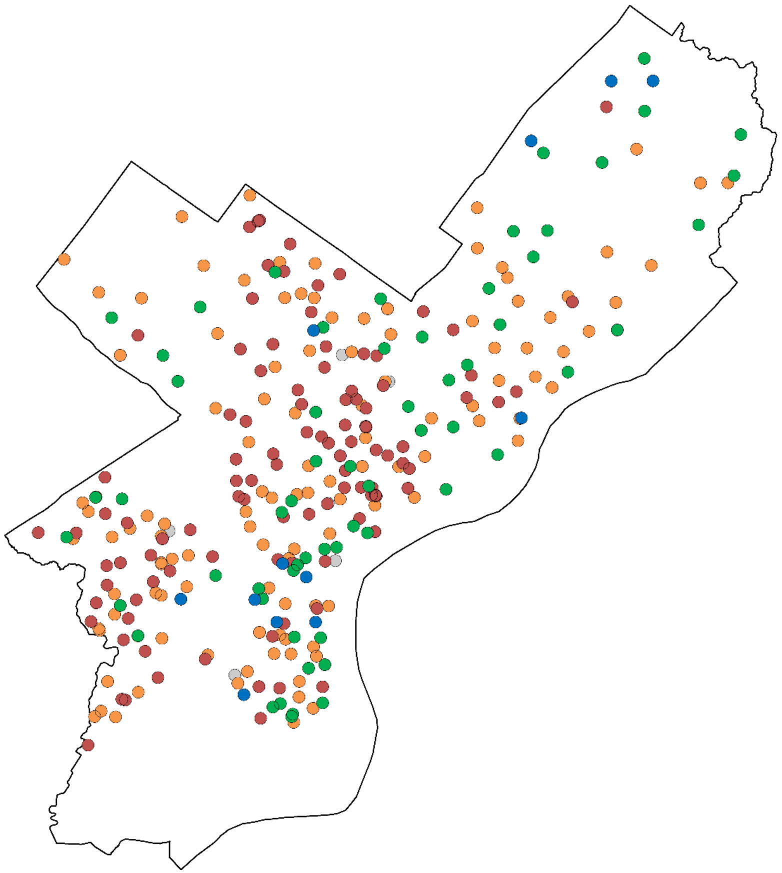
Overview

- Context & Action Plan 3.0 Anchor Goals
- Fiscal Plan Goals and Assumptions
- Preliminary Five-Year Plan for FY2018 - 2022
- FY17-18 Lump Sum Statement

District recent history

- Prior to last year, the District had been operating in austerity mode since 2012 and made many difficult and painful decisions in recent years to ensure fiscal stability
  - Closed 24 schools
  - Eliminated non-core programs
  - Laid off 1000s of teachers, nurses, counselors and staff
  - Made substantial central office staffing cuts
- In FY16, the District began a 5-year, $440 million investment program. With another year added (FY22), the value of those investments is now over $526 million
- While the District has continued to implement and build on the investments from last year's five-year plan, we find ourselves one year closer to the fiscal cliff identified in FY16

Where we are today



- We have made investments to improve performance:
  - Additional literacy coaches
  - Additional alternative education seats

- There are accomplishments to celebrate:
  - 174 schools increased in overall SPR score from 2014-15 to 2015 -16 (115 District, 59 Charter)
  - 71 schools went up an overall SPR tier (43 District, 28 Charter)
  - Increased attendance
  - Increase in graduation rate

Action Plan 3.0 – Our bold goals

Anchor Goal 1: 100% of our students will graduate, ready for college and career

Current: 66% graduation rate

5 year milestone: 80% graduation rate

Anchor Goal 2: 100% of 8-year-olds will read on grade level

Current: 30% on grade level at age 8

5 year milestone: 66% on grade level at age 8

Anchor Goal 3: 100% of schools will have great principals and teachers

5 year milestone: Engaged and supported principals and teachers with strong instructional skills

Anchor Goal 4: SDP will have 100% of the funding we need for great schools, and zero deficit

Current: Narrow current fiscal year surplus with projected out-year deficits

5 year milestone: Five-Year balanced budget projections

Five-Year Plan and Lump Sum – 2016 Investments Maintained

The Plan and Lump Sum Statement both maintain and build on an array of investments introduced in FY16 to support the goals of Action Plan 3.0. Through FY22, the total value of these investments is over $526 million.

Literacy

- Instructional materials refresh for K-8 Math and reading anthologies for all levels
- Additional Children's early literacy specialists
- Investments in District turnaround schools

College and Career Readiness

- IT refresh of all high school classrooms and all high school labs
- Increased funding and opportunity for advanced placement courses, gifted education, and PSAT/SAT testing
- Summer enrichment opportunities

Talent/Workforce Investment

- Supplemental teacher hiring to plan for normal attrition and eliminate system-wide vacancies
- Counselors for every school and nurses in every school/building
- Funding for fair workforce agreements that allow for 21st century learning environments
- Appropriate staffing of Central Office to support schools

Five-Year Plan and Lump Sum – FY17 and FY18 Investments

In addition to the investments introduced in last year's Lump Sum and Five-Year Plan, the following are $98 million in additional investments which were introduced this year or will be introduced in FY18 and are included in the Plan projections through FY22.

- Hydration stations in each school building
- Special education pilot to begin providing internal programs to educate the 1,500 students who are currently served in schools outside of the District, who require a higher level of learning support
- Additional Talent resources to assist in teacher recruitment
- Alternative Education programs and other non-core programs
- Implementation of new middle-college program
- Increased System of Great Schools (SGS) and turnaround school investments

Five-Year Plan and Lump Sum – Example Infrastructure Investments

The District has adopted a Capital investment program designed to not only provide needed repairs and upgrades to our school buildings, but also enhance and support the many programmatic investments being made by the District. These investments will impact 73,291 students at 115 school locations. Some examples include:

Classroom Modernizations - Duckrey, Gideon, Lea, Locke, Meade, Pennell & Stearne

- Seventy Pre-Kindergarten through grade 2 classrooms across seven schools have been selected for classroom modernizations to support the School District's Early Literacy Initiative
- All classrooms will be equipped with new LED lighting, floors, fresh paint, sufficient electrical outlets, and mobile and multi-purpose furniture that allows for collaborative learning

Major Renovation - Dobbins

- Alterations and improvements to: existing CTE classroom spaces, science labs, music suite, fitness room, student restrooms, and locker rooms
- Design and construction of additional program spaces within the existing building footprint, including digital media, computer networking, and biotechnology teaching spaces
- Heating and electrical upgrades consistent with the Americans with Disabilities Act and life-safety improvements (sprinkler and fire alarm systems)

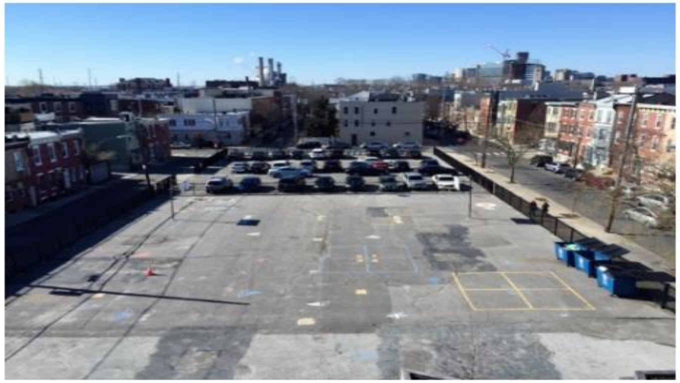
Five-Year Plan and Lump Sum – Example Infrastructure Investments

Site Improvements & Playground- Cramp

Improvements include: synthetic turf field with new painted walking track, basketball hoop, outdoor classroom area, outdoor stage area, new play equipment, trees, and landscaping

Site Improvements & Playground - Chester Arthur

Improvements include: synthetic turf berm with seating amphitheater, multiuse basketball court/painted track/greenwall, outdoor classroom area with boulder seating, and stormwater features



Five-Year Plan – Aiming for Fiscal Stability

- Propose a budget and spending plan which strives for structural balance, while determining investments designed to achieve the mission of achieving equity in educational opportunity for all children

- Utilize reasonable projections for revenues and expenditures, based on:
  - Actual revenues and expenditures
  - Current law
  - Historic trends
  - Most recent City and State budget proposals

- Primary objectives:
  - Identify sufficient revenues to meet the anticipated obligations of the first 24 months
  - Establish baseline financial projections to enable dialogue among all School District funders (City, State, Private) identifying pathways to achieving long-term structural balance

FY17 Significant Fiscal Achievements

- Positive Fund Balance
  - Currently project to end FY17 with a $104 million positive Fund Balance.
  - The third consecutive year with a year end positive fund balance.

- Improved Bond Rating
  - On October 6, 2016, Moody's upgraded the Pennsylvania School District Enhancement Programs to A2 from Baa1 and revised the outlook to stable from negative.
  - On October 7, 2016, Fitch revised the School District's outlook to stable from negative.
  - This change represented the first positive movement by Fitch in the School District's credit outlook since 2010.

- Refunding Savings
  - In November 2016, the District completed a bond refunding which will result in over $100 million in projected present value debt service savings over the next 20 years.

- Extending the Cigarette Tax
  - Due to an amendment to the Fiscal Code contained in Act 85, the City cigarette tax will no longer sunset in FY19 and the District will receive at least $58.0 million annually.

- New Rideshare Funding
  - In FY17, the State implemented a Ridesharing program effective through December 2019, in which the District will receive a portion of revenues. In FY17, the Ridesharing revenues are projected to be approximately $2.0 million.

Preliminary
Five-Year Plan

FY18-22 Key Assumptions

<u>REVENUES</u>

- Local revenue projections consistent with City's Five-Year Plan projection, which assumes no changes in tax rates
- FY18 State Revenues consistent with the Governor's FY18 proposed budget presented on February 7, 2017
- FY19-22 State Revenues grow a nominal 2.5% per year
- Does not include impacts of changes in State Transportation Aid formulas
- State reimbursements related to City Market Valuations are reduced beginning in FY19 (due to City's Actual Value Initiative "AVI" implementation)
  - Total FYP impact: ($284M)
  - Annual budget impacts:
    FY19 ($61M), FY20 ($70M), FY21 ($75M), FY22 ($78M)

FY18-22 Key Assumptions

EXPENDITURES

- Based on historic expenditure and enrollment trends
- Charter School growth is based on recent approvals, renewals, and historic enrollment trends
- Assumes closure of three District-operated schools per year, beginning in FY19, due to enrollment declines
- Capital borrowing every other year starting in FY19
  - FY19 $200M, FY21 $200M

ADJUSTMENTS

- Negative fund balance adjustment of ($83.7M) to reflect annual severance liability
  - See Appendix A for full explanation
- This adjustment has no impact on cash, does not alter the amounts or timing of required payments by the School District, and is for proper accounting presentation on the District’s Financial Statements

Preliminary Five-Year Plan Projections

FY18-FY22 FINANCIAL PLAN
Operating Funds
(in thousands)

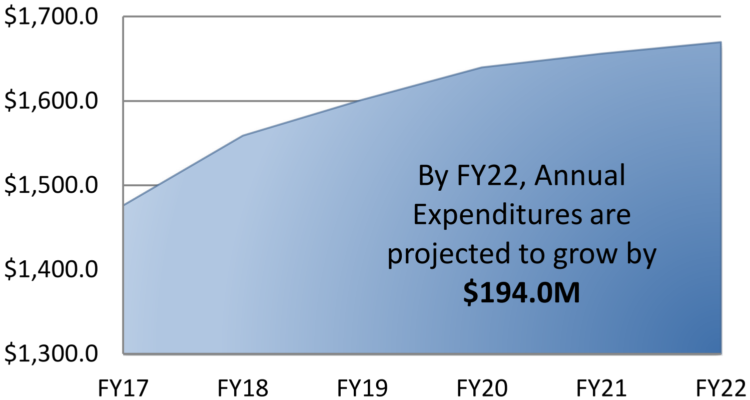
	FY17 Projected	FY18 Projected	FY19 Projected	FY20 Projected	FY21 Projected	FY22 Projected	CAGR FY17 to FY22
REVENUES & OTHER FINANCING SOURCES							
Local Tax Revenues	$1,141,671	$1,162,072	$1,204,864	$1,219,913	$1,256,358	$1,283,632	2.4%
Local Non-Tax Revenues	$131,725	$124,736	$122,808	$122,808	$122,808	$122,808	-1.4%
State Revenues	$1,533,550	$1,567,099	$1,551,213	$1,595,442	$1,632,676	$1,670,417	1.7%
Federal Revenues	$13,054	$16,713	$16,615	$16,516	$16,400	$16,283	4.5%
Other Financing Sources (excluding Refunding)	$1,309	$289	$789	$289	$789	$289	-26.1%
TOTAL REVENUES & OTHER SOURCES (excl. Refunding)	**$2,821,309**	**$2,870,909**	**$2,896,290**	**$2,954,968**	**$3,029,031**	**$3,093,429**	**1.9%**
EXPENDITURES							
District Operated Schools	$1,475,928	$1,558,824	$1,601,501	$1,639,683	$1,656,011	$1,669,902	2.5%
Charter Schools (Incl. Transportation)	$813,956	$896,385	$975,531	$1,052,293	$1,122,936	$1,182,216	7.8%
Other Non-District Operated Schools (Incl. Transportation)	$109,779	$112,009	$112,924	$113,858	$114,812	$115,786	1.1%
Debt Service (excluding Refunding)	$269,265	$271,891	$291,955	$282,283	$286,309	$291,925	1.6%
Administrative Support Operations (Central Offices)	$85,646	$91,886	$93,121	$94,407	$95,343	$96,389	2.4%
Undistributed Budgetary Adjustments	($11,713)	($5,268)	($5,252)	($5,235)	($5,217)	($5,199)	-15.0%
Other Financing Uses (excluding Refunding)	$2,252	$2,252	$2,252	$2,252	$2,252	$2,252	0.0%
TOTAL EXPENDITURES & OTHER USES (excl. Refunding)	**$2,745,113**	**$2,927,978**	**$3,072,033**	**$3,179,543**	**$3,272,447**	**$3,353,271**	**4.1%**
Refunding Revenues and Sources	**$1,306,745**	**$0**	**$0**	**$0**	**$0**	**$0**	
Refunding Expenditures and Uses	**$1,315,876**	**$0**	**$0**	**$0**	**$0**	**$0**	
OPERATING/FUND BALANCE							
Operating Surplus/(Deficit)	**$76,196**	**($57,069)**	**($175,743)**	**($224,575)**	**($243,416)**	**($259,841)**	
Net Impact of Refunding	($9,131)	$0	$0	$0	$0	$0	
Transfers from Reserves	($9,702)	($14,702)	$4,633	($13,321)	($13,321)	($13,321)	
Fund Balance at Beginning of Year - July 1	**$131,228**	**$104,848**	**$33,077**	**($138,033)**	**($375,929)**	**($632,666)**	
Prior Period Adjustment	($83,744)						
Restated Fund Balance at Beginning of Year - July 1	**$47,485**	**$104,848**	**$33,077**	**($138,033)**	**($375,929)**	**($632,666)**	
ENDING FUND BALANCE							
Fund Balance at End of Year - June 30	**$104,848**	**$33,077**	**($138,033)**	**($375,929)**	**($632,666)**	**($905,828)**	
Fund Balance as % of Total Revenues (excl. Refunding)	*3.7%*	*1.2%*	*-4.8%*	*-12.7%*	*-20.9%*	*-29.3%*	

Five-Year Plan Risks

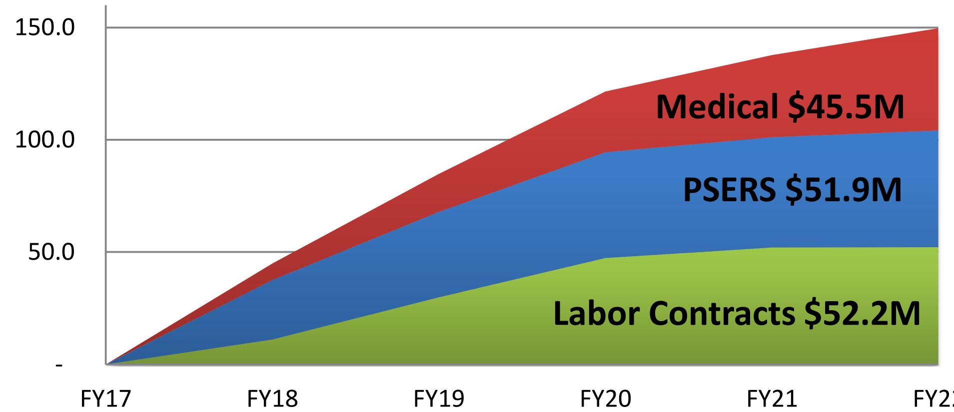
- Changes in federal funding priorities
- FY18 approved State budget does not include additional revenues
- Impact of changes to State Transportation Aid formulas
- Delays in the approval and release of State funds in FY18
  - Increases borrowing costs and uncertainty, making planning and investments more difficult
- Narrow positive Ending Fund Balances
  - Projected FY17 Fund Ending Balance of $104.8M equal to just 3.7 percent of revenues
- Changes to the charter school formula and authorizing authority
- Economic Downturn affecting funding assumptions
- Additional increases in the Public School Employees' Retirement System (PSERS) contribution schedule

Five-Year Plan District-Operated School Cost Drivers

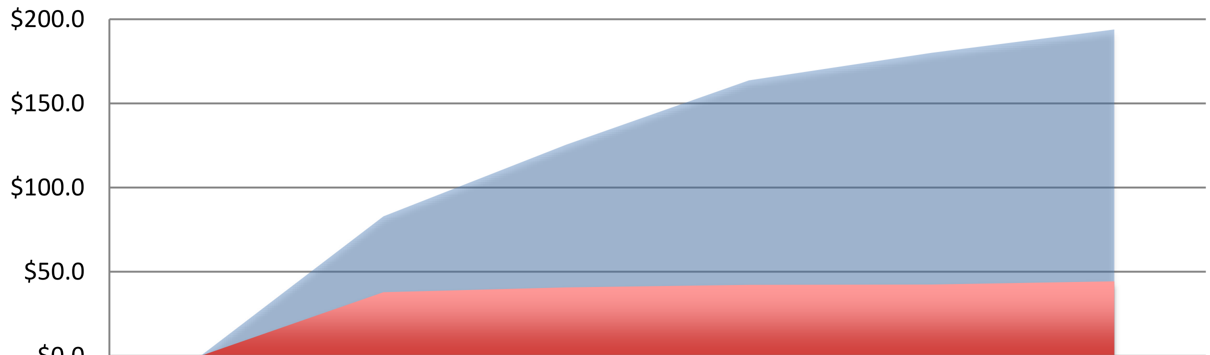
FY17 - FY22 District Operated Schools Projected Expenditure Growth ($M)



District Operated Schools Key Annual Expenditure Drivers: Annual Increase by FY22 ($M)



By FY22, Key Drivers make up **77% of Annual Expenditure Increase**

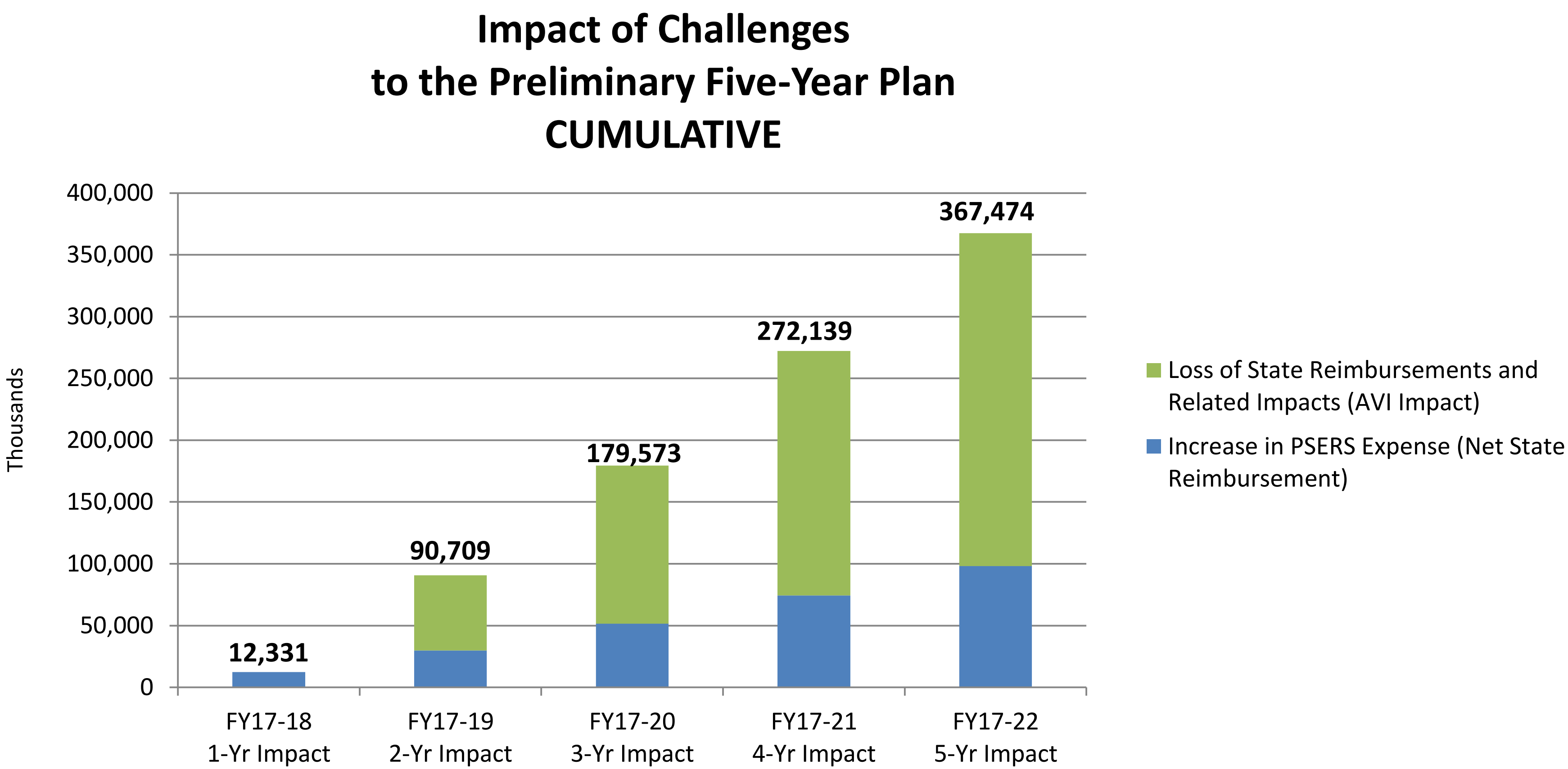


	FY17	FY18	FY19	FY20	FY21	FY22
Change - District Operated Schools (DOS) Expenditures	$0.0	$82.9	$125.6	$163.8	$180.1	$194.0
Change - DOS Excluding Key Expenditure Drivers	$0.0	$37.9	$40.8	$42.3	$42.4	$44.3

Five-Year Plan Challenges

The negative ending fund balance beginning in FY19 is driven in part by:

- Reduction of AVI State reimbursements and related impacts (beginning FY19)
- Scheduled increases in the PSERS rate



Five-Year Plan Strategy: AVI Offset

Though it would not make up for all of the five-year plan challenges, the State could make formula changes to offset the impact of reduced reimbursements related to the City's AVI changes in property values.

This action would help narrow the annual operating deficit, and would nearly cut in half the District's negative ending fund balance in FY19.

	FY17 Projected	FY18 Projected	FY19 Projected	FY20 Projected	FY21 Projected	FY22 Projected
OPERATING/FUND BALANCE						
Operating Surplus/(Deficit)	**$76,196**	**($57,069)**	**($114,801)**	**($157,467)**	**($173,662)**	**($188,273)**
Net Impact of Refunding	($9,131)	$0	$0	$0	$0	$0
Transfers from Reserves	($9,702)	($14,702)	$4,633	($13,321)	($13,321)	($13,321)
Fund Balance at Beginning of Year - July 1	**$131,228**	**$104,848**	**$33,077**	**($77,091)**	**($247,878)**	**($434,860)**
Prior Period Adjustment	($83,744)					
Restated Fund Balance at Beginning of Year - July 1	**$47,485**	**$104,848**	**$33,077**	**($77,091)**	**($247,878)**	**($434,860)**
ENDING FUND BALANCE						
Fund Balance at End of Year - June 30	**$104,848**	**$33,077**	**($77,091)**	**($247,878)**	**($434,860)**	**($636,454)**
Fund Balance as % of Total Revenues (excl. Refunding)	*3.7%*	*1.2%*	*-2.6%*	*-8.2%*	*-14.1%*	*-20.1%*

Lump Sum

Lump Sum Statement

(in thousands)

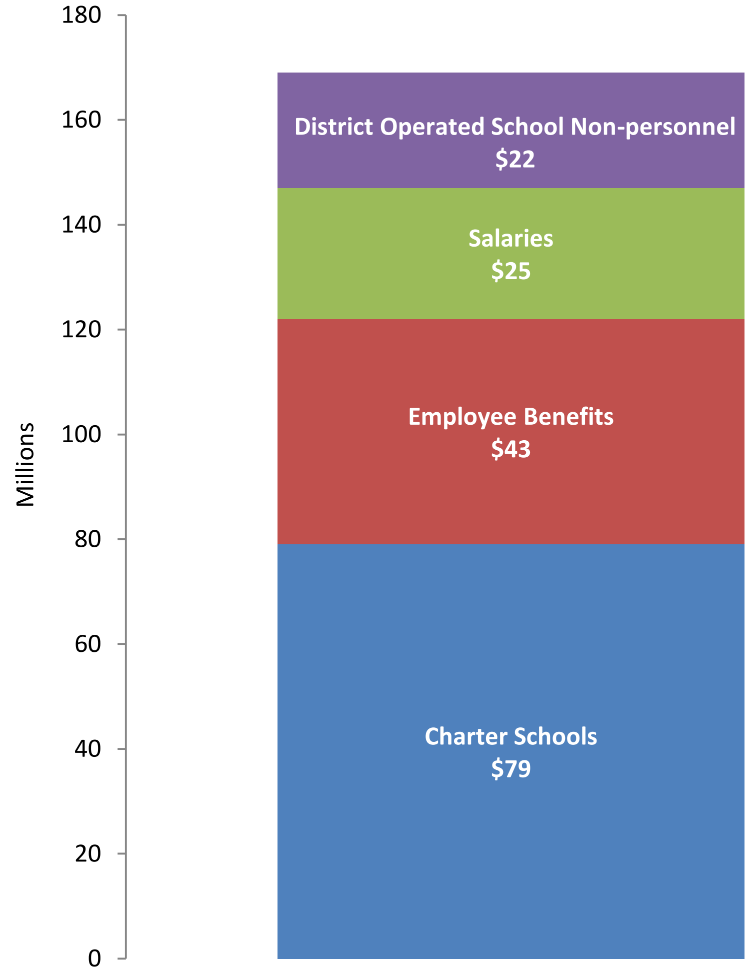
	FY16 Actual	FY17 Projected	FY18 Proposed
REVENUES & OTHER FINANCING SOURCES			
Local Tax Revenues	$1,120,731	$1,141,671	$1,162,072
Local Non-Tax Revenues	$143,556	$131,725	$124,736
State Revenues	$1,443,194	$1,533,550	$1,567,099
Federal Revenues	$11,387	$13,054	$16,713
Other Financing Sources (excluding Refunding)	$6,691	$1,309	$289
TOTAL REVENUES & OTHER SOURCES (excl. Refunding)	**$2,725,559**	**$2,821,309**	**$2,870,909**
EXPENDITURES			
District Operated Schools	$1,484,365	$1,475,928	$1,558,824
Charter Schools (Incl. Transportation)	$744,818	$813,956	$896,385
Other Non-District Operated Schools (Incl. Transportation)	$107,813	$109,779	$112,009
Debt Service (excluding Refunding)	$260,604	$269,265	$271,891
Administrative Support Operations (Central Offices)	$75,317	$85,646	$91,886
Undistributed Budgetary Adjustments	($8,534)	($11,713)	($5,268)
Other Financing Uses (excluding Refunding)	$1,662	$2,252	$2,252
TOTAL EXPENDITURES & OTHER USES (excl. Refunding)	**$2,666,046**	**$2,745,113**	**$2,927,978**
Refunding Revenues and Sources	**$349,960**	**$1,306,745**	**$0**
Refunding Expenditures and Uses	**$349,731**	**$1,315,876**	**$0**
OPERATING/FUND BALANCE			
Operating Surplus/(Deficit)	**$59,513**	**$76,196**	**($57,069)**
Net Impact of Refunding	$229	($9,131)	$0
Transfers from Reserves	($16,562)	($9,702)	($14,702)
Fund Balance at Beginning of Year - July 1	**$88,048**	**$131,228**	**$104,848**
Prior Period Adjustment	$0	($83,744)	$0
Restated Fund Balance at Beginning of Year - July 1	**$88,048**	**$47,485**	**$104,848**
ENDING FUND BALANCE			
Fund Balance at End of Year - June 30	**$131,228**	**$104,848**	**$33,077**
Fund Balance as % of Total Revenues (excl. Refunding)	*4.8%*	*3.7%*	*1.2%*

Why are Expenditures and Revenues increasing from FY17 – FY18?

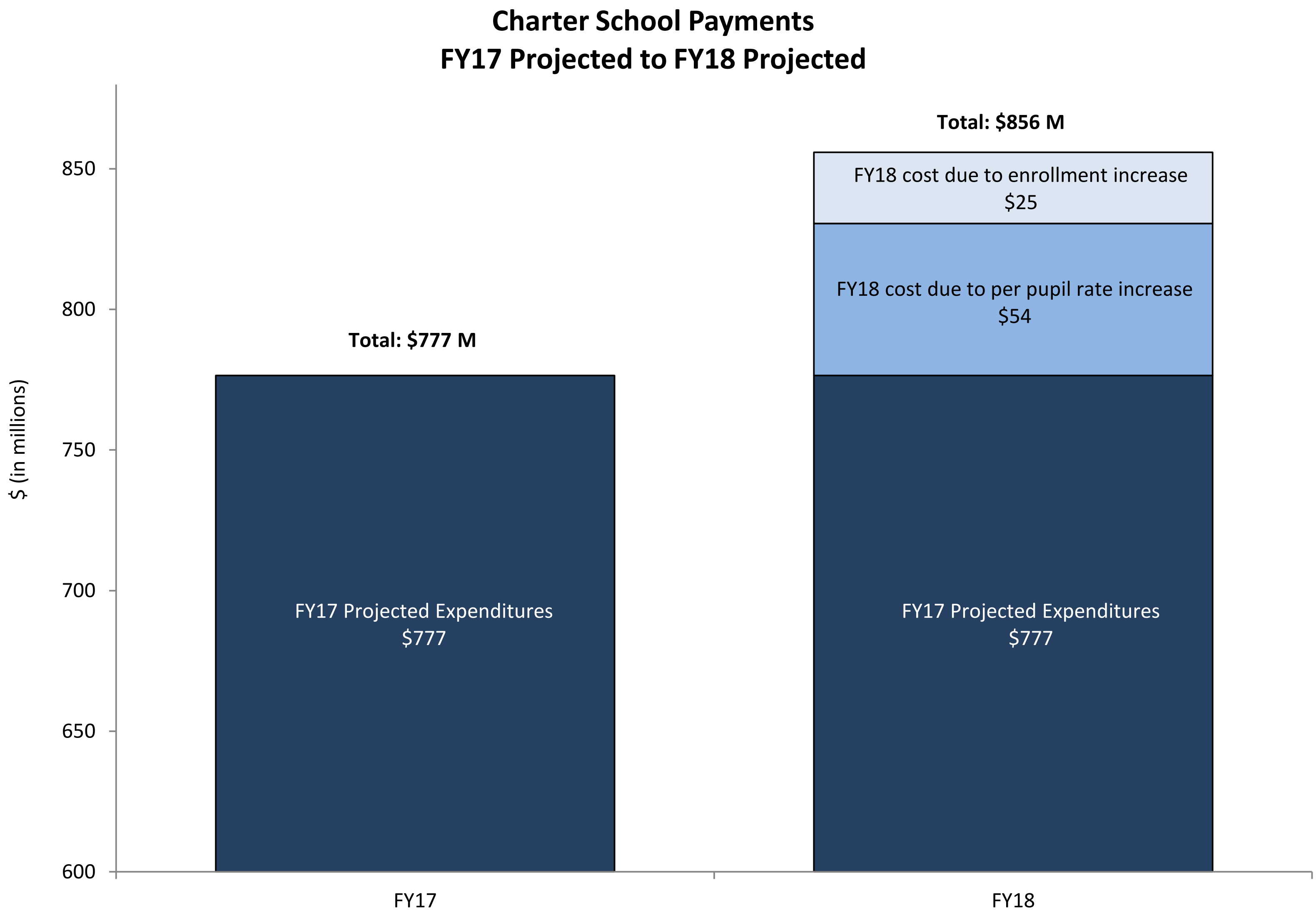
- Four major expenditure areas are driving growth from FY17 to FY18:
  - Increase of $79M for payments to charter schools
  - Increase of $43M for employee benefits
  - Increase of $25M for salaries
  - Increase of $22M in other District Operated Schools Non-personnel

- Baseline revenue increases between FY17 and FY18 are primarily due to:
  - Increase of $27M in basic education and special education funding included in the Governor's FY18 proposed budget
  - Increase of $20M in real estate tax revenues
  - Increase of $19M due to higher retirement reimbursements

Major Expenditure Increases from FY17 to FY18



Between FY17 and FY18, charter expenditures are projected to increase by $79M. The change is due primarily to a projected increase in per pupil cost rates.



Next Steps

Timeline

- **March 13-31:** Principals complete school budgets
- **April 20:** SRC Budget Hearing
- **May 10:** City Council Hearing
- **May 25:** SRC Budget Vote
- **June**: City Adoption of Tax Measures for School District
- **June:** State Budget Adoption

Appendix A:
FY18-22 Key Assumptions - Reflection of Accrual Liability

- In 1982, the School District agreed to new labor contracts with the PFT and the Association of School Administrators which included the transition of certain payments to employees from a 10 month work/10 month pay schedule (10 pay 10) to a 10 month work/12 month pay schedule (10 pay 12).

- This action resulted in a Fiscal Year 1983 year-end presentation whereby the School District recognized a one-time salary expense reduction and established a long-term severance liability equal to the summer salaries of 10 pay 12 employees. The liability as of June 30, 1983 was estimated at $74.3 million. As a long-term severance liability, it did not decrease fund balance.

- In the audit issued for Fiscal Year 1983, the audited financial statement footnotes of the School District identified this liability as a long-term severance payable. The City Controller Audit Opinion Report recited that the District complied with Generally Accepted Accounting Principles (GAAP).

- In every audit since 1983, the School District has disclosed the annual severance liability in an Obligations footnote and has also included it in the Statement of Net Position, and the City Controller has issued an opinion that the School District's financial statements are fairly stated in all material respects.

FY18-22 Key Assumptions - Reflection of Accrual Liability (cont)

- During the past few months, as we conducted our annual review of finances, questions arose as to whether or not this presentation of the liability was consistent with current Generally Accepted Accounting Principles (GAAP) and the modified accrual basis of accounting. The School District consulted with outside GAAP/GASB experts and considered presentation of this information by similar K-12 school districts.

- These experts advised the District that in order to conform with GAAP standards, the School District should make a one-time adjustment to prior year fund balance at the end of FY17, which would accurately reflect the accrual liability as of June 2016.

- This adjustment does not alter the amounts or timing of the required payments by the School District to the 10 pay 12 employees.

- The projected FY17 budget reflects an Adjustment of Prior Year Fund balance in the amount of $83.7 million.