



## POLICY BRIEF

### Explaining School Fund Balances:

### Are PA Schools, with \$4.7 Billion in Reserve Funds, Really Flush? An Update

DAVID W. DAVARE

JULY 2016

Temple University’s Center on Regional Politics (CORP), Penn State’s College of Education, the University of Pittsburgh’s Center for Metropolitan Studies, and the Pennsylvania Policy Forum (a group of faculty and researchers at 18 public and private colleges and universities) formed a consortium to support state legislators, local officials, and education policymakers in a review of options for improving public school finance. CORP has been periodically publishing policy briefs, papers, and studies to support the consortium’s mission. This is the third annual analysis on school fund balances.

Tax increases and an unprecedented 9-month state budget impasse called attention to the \$4.7 billion in reserve funds accumulated by the state’s 500 school districts, 67 vocational/technical schools (AVTS/CTC), and 178 charter schools. The total fund balance has increased by about \$400 million since 2012-13 (\$4.3 billion). This may suggest to some that these funds are being hoarded by school officials who raise taxes or cut programs unnecessarily or exaggerate their need for additional state aid. For example, a recent Philadelphia Daily News editorial called the idea of stockpiling revenues, especially for those districts running deficits, “galling.”<sup>1</sup>

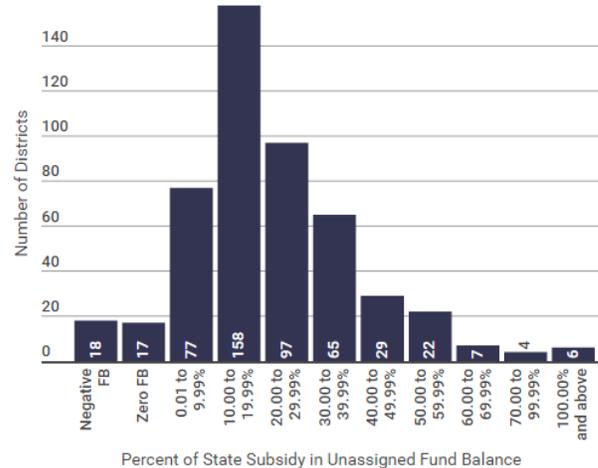
In 2014-15, only six districts had a fund balance equal to or greater than their state subsidy. As shown in Figure 1, there were 461 districts with fund balances that were less than half of the state subsidy. The delay in state payments to school districts forced districts to rely on the available fund balance to continue district operations. Indeed, the Pennsylvania Association of School Business Officials (PAS-BO) estimated that school districts collectively borrowed about \$1 billion to cover their expenses during FY 2016. Presumably, if their unassigned balances were sufficient to avoid short-term borrowing and interest costs, they would have adopted that strategy.

Here are the (admittedly dry) accounting facts.

Fund balance is the accounting term for the difference between total assets and total liabilities. A fund balance is

Figure 1

Distribution of Districts by Percent of State Subsidy in Unassigned Fund Balance, 2014-15



Source: PA Department of Education

not all cash. In school accounting, as required by the Pennsylvania Department of Education, assets include money to be received in the 60 days after the close of the fiscal year. Liabilities include only current liabilities and not long-term liabilities such as debt payment or pensions. Fund balance generally increases when a district’s revenue exceeds its expenditures in a given year. The fund balance declines when the expenditures exceed revenues in a given year.

1. Philadelphia Daily News. 2016. “Cloudy, Chance of Crisis.” Editorial. July 6.

According to the Accounting Manual for school districts, districts must comply with the Governmental Accounting Standards Board (GASB) statements on accounting for local governmental entities. GASB issued Statement 54, which divides fund balance into four parts:

- **Restricted** – funds limited by external parties or legislation, e.g. debt covenants
- **Committed** – funds limited by board policy or board action, e.g. planned construction
- **Assigned** – funds intended for a particular purpose such as special revenue funds
- **Unassigned** – funds that are available for consumption or not limited in any manner

Just as an individual or family should maintain a savings account for unforeseen expenses or emergencies, school districts should also have funds in reserve to pay for emergency repairs or cover unexpected interruptions in revenues - such as a layoff at a major factory which suddenly affects tax collections. The fund balance can also be used to offset year-to-year variations in local or state cash flow, such as a delay in subsidy payment from the state. In addition, fund balances enable districts to generate investment income which, in turn, helps to keep tax rates lower.

A November 1990 research bulletin by the Government Finance Officers Association (GFOA) recommended that an unassigned fund balance be retained to guard against an economic downturn. It also advised that a fund balance is necessary to meet emergency situations, which could include: uninsured loss, major repairs to heating systems, and replacement of damaged educational equipment prior to scheduled change. In 2002, GFOA established a best practice for minimum fund balance of 5% of total expenditures for large governments. In October 2009 the GFOA revised its best practice in light of GASB Statement 54 to

suggest that an appropriate minimum fund balance could be as low as 5% or as high as 15%. The GFOA did not provide a maximum suggested fund.<sup>2</sup>

Having a positive fund balance benefits the school district when issuing debt. Credit ratings of school districts and other public entities can be affected directly by the level of their fund balances; those with little or no money in reserve are considered to be higher risk, and their ratings - along with their cost of borrowing - suffer accordingly.

In Pennsylvania, fund balances in the 1990s covered school districts when the state failed to make school subsidy payments in a timely manner. This has occurred four times since 1992. More recently, fund balances have allowed some districts to maintain services or minimize service cuts or tax increases during the economic downturn when real estate and earned income tax revenues declined. Beginning in 2010, the state froze funding for repair/renovation/construction subsidies, which leaves total construction costs to the individual districts. This means that districts either need to set aside funds for repair/renovation/construction or raise taxes for individual projects. The set aside is referred to as an assigned fund balance. Additionally, districts have set aside funds to try to minimize or phase in tax increases in individual years to cover pension payment increases mandated by the Public School Employees' Retirement System, which operates as a state entity. The budget impasse for the 2015-16 school year resulted in districts relying on the fund balance as a way to meet obligations until state subsidies were available.

**Table 1 - Fund Balance by Type of School, 2014-15**

	Number	Committed	Assigned	Unassigned	Total
<b>School District</b>	500	\$1,618,067,094	\$930,064,515	\$1,805,245,670	\$4,353,377,279
<b>Percent of Total</b>		37.2%	21.4%	41.5%	
<b>AVTS/CTC</b>	67	\$16,679,267	\$19,897,385	\$19,388,953	\$55,965,605
<b>Percent of Total</b>		29.8%	35.6%	34.6%	
<b>Charter School</b>	178	\$92,795,224	\$40,098,913	\$140,213,810	\$273,107,947
<b>Percent of Total</b>		34.0%	14.7%	51.3%	
<b>Total</b>	745	\$1,727,541,585	\$990,060,813	\$1,964,848,433	\$4,682,450,831
<b>Percent of Total</b>		36.9%	21.1%	42.0%	

Source: PA Department of Education, web page, Expenditure Detail - SDs: 1995-96 to 2000-01 | 2001-02 to 2014-15 (Excel), accessed June 2, 2016. <http://www.education.pa.gov/Teachers%20-%20Administrators/School%20Finances/Finances/AFR%20Data%20Summary/Pages/AFR-Data-Detailed-.asp#.VICLXeQepOd>.

2. Gauthier, Stephen J. 2009. "GFOA Updates Best Practice on Fund Balance." *Government Finance Review* 25(6): 67-68.

**Table 2 - Unassigned Fund Balance as a Percent of Total Expenditures, 2014-15**

	Fund Balance as Percent
School District Total	6.6%
AVTS/CTC Total	3.4%
Charter School Total	8.1%
Total	6.6%

Source: PA Department of Education, web page, General Fund Balance: 1996-97 to 2014-15 (Excel), accessed June 2, 2016. <http://www.education.pa.gov/Teachers%20-%20Administrators/School%20Finances/Finances/AFR%20Data%20Summary/Pages/AFR-Data-Detailed-.aspx#.VICLXeQepOd>.

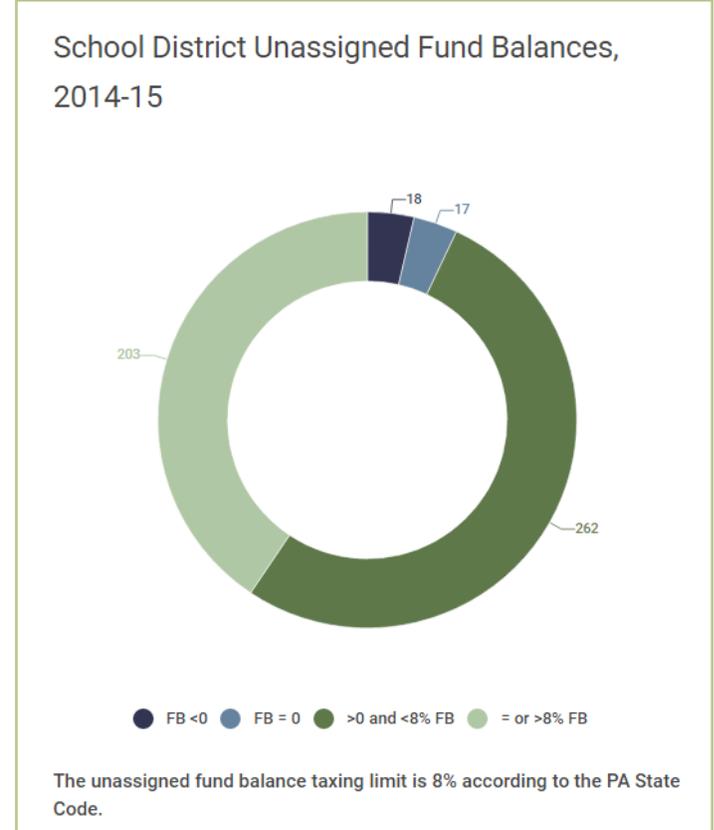
The size of a fund balance is dictated by the local circumstances of a school district. For example, a higher fund balance may be appropriate when the local economy and tax base are weak and the district budget either relies heavily on state and federal sources of funding, which can change or be delayed without notice, or when the district is carrying a sizeable debt burden. There are, of course, many other legitimate reasons to hold funds in reserve. School officials may build a fund balance over time, with the intention of using the money for a renovation project or another one-time expenditure, instead of borrowing and repaying a bank with interest.

The financial industry suggests that a government unassigned fund balance should be between 5% and 10% of total operating expenditures and GFOA suggests minimums between 5% and 15%. (A 5% unassigned balance would cover a district's operating costs for about two and a half weeks.) Indeed, Moody's cited the Commonwealth of Pennsylvania's depletion of its reserves as one factor in recently downgrading its bond rating. Simultaneously, Moody's downgraded the Commonwealth's intercept program, which serves as a credit enhancement for school district debt. The Pennsylvania School Code (24 PS §6-688) limits the amount of unassigned fund balance to 8% for a district whose expenditures exceed \$20 million if it is going to raise taxes. Table 1 shows the dollar value of fund balances for the 2014-15 school year.

Table 2 shows unassigned fund balance as a percent of total expenditure by type of school, and the distribution for school districts is shown in Figure 3. As shown in Table 2, the average unassigned fund balance for school districts is 6.6% or below the School Code limitation. Vocational/technical schools are also below the school code at 3.4%. Charter schools have an 8.1% fund balance. In fairness to the charter schools, they operate as not-for-profits, which have a different limitation for fund balance. The American Society of Association Executives (ASAE) along with the finance industry recommends a fund balance for not-for-

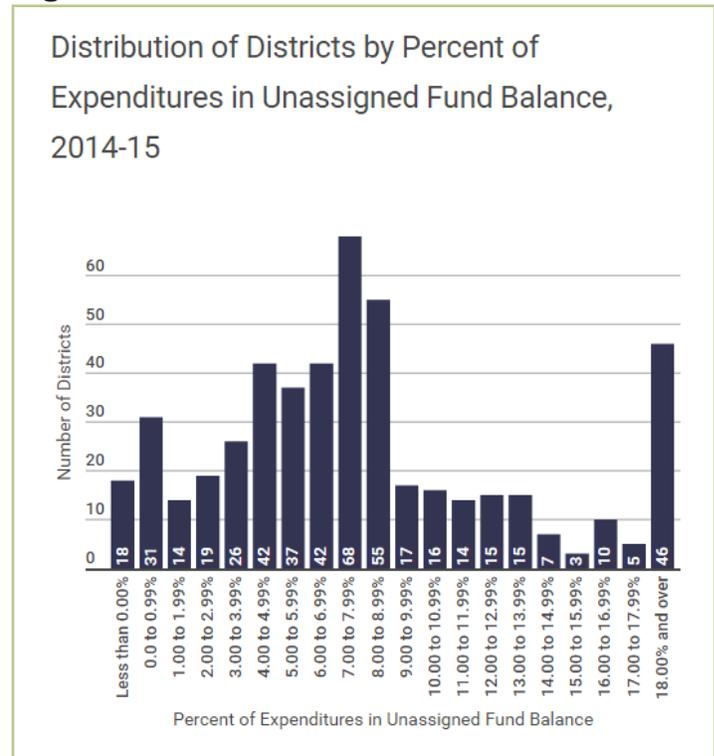
profits of 50% or about six months of operating expenditures. While the total unassigned fund balance is below the school code limit, individual districts and schools will vary.

**Figure 2**



Source: PA Department of Education

**Figure 3**



Source: PA Department of Education

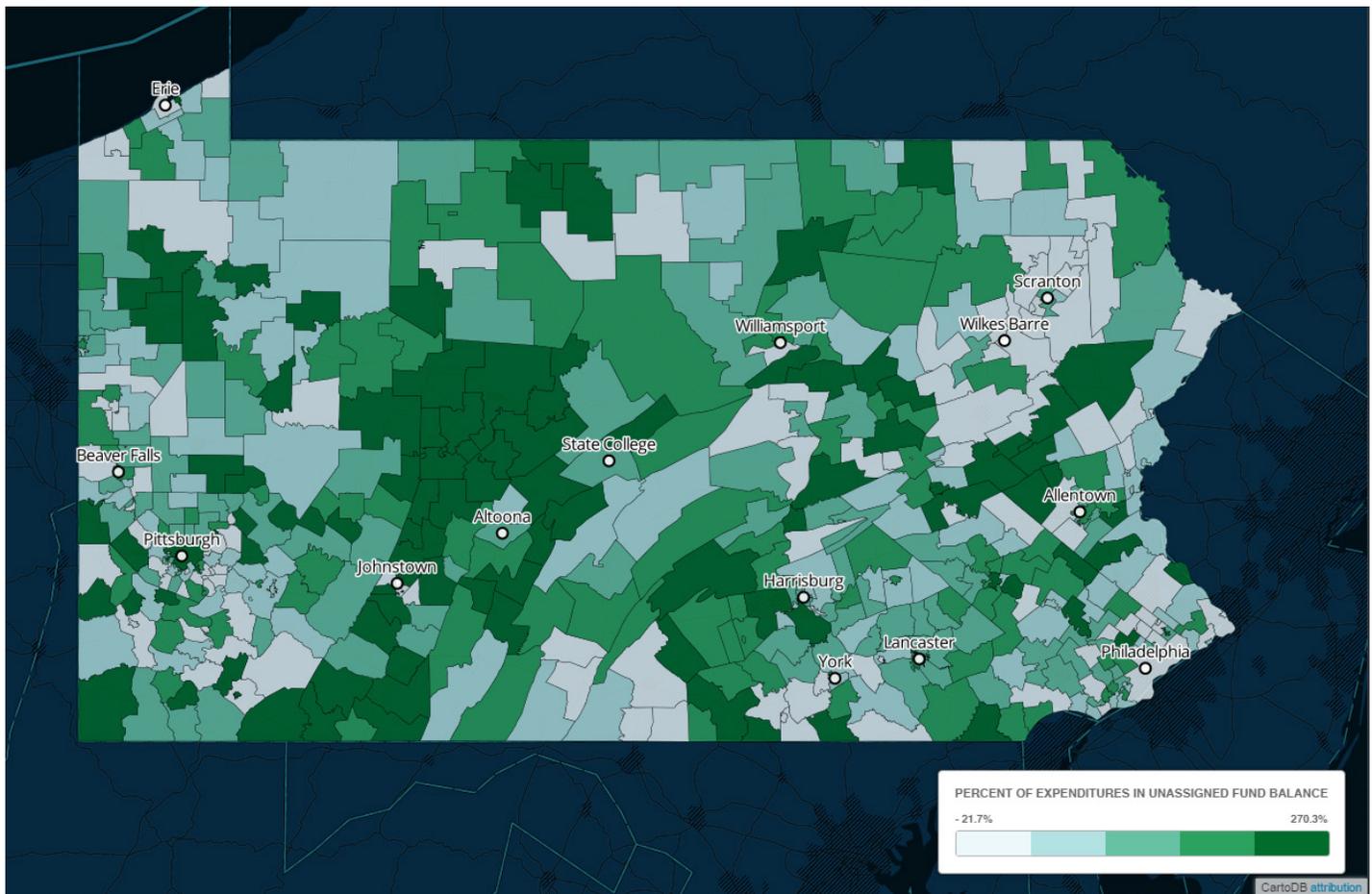
Figure 2 shows that among individual school districts, 17 districts have an unassigned fund balance of zero, and another 18 have an unassigned negative fund balance. Among the vocational schools, 31 have a zero unassigned fund balance and one has a negative fund balance. There are 29 charter schools with negative unassigned fund balances and 16 with zero unassigned fund balances.

If the district is going to use a fund balance, it should proceed with caution. The assigned fund balances, if they contain federal funds, bond proceeds, or funds in the debt service fund, must be used for their assigned purposes. Committed fund balances should be used first for the purposes for which they were committed. The unassigned fund balance should be used for one-time expenditures. (A map of PA school districts' unassigned fund balances as percent of expenditures is in Figure 4.) Fund balances, like an individual's savings account, are one-time revenues and when used need to be replenished with board approval.

The fund balance is an important financial tool for school districts and needs to be considered individually by the districts as they look at their future needs and the changing economic climate. However, they should follow the financial industry recommendation of maintaining a minimum of 5% for an unassigned fund balance. Given these facts, it seems fair to say that the distribution of fund balances is a rough indication of the unequal resources available to schools under Pennsylvania's system of public education finance. But the amount of fund balances is not an indication that school districts collectively -- and even individual districts -- are irresponsibly hoarding a pot of gold that could be used to avoid tough decisions on how to meet the financial challenges facing our public schools.

*David W. Davare is director of research for the Pennsylvania Economy League's Central Division and an advisor to the University Consortium to Improve Public School Finance and Promote Economic Growth*

**Figure 4 - PA School Districts' Percent of Expenditures in Unassigned Fund Balance, 2014-15**



\* Find an interactive map of all PA districts according to the percent of expenditures in the unassigned fund balance at: [temple.edu/corp/fundbalancesupdate/](http://temple.edu/corp/fundbalancesupdate/).

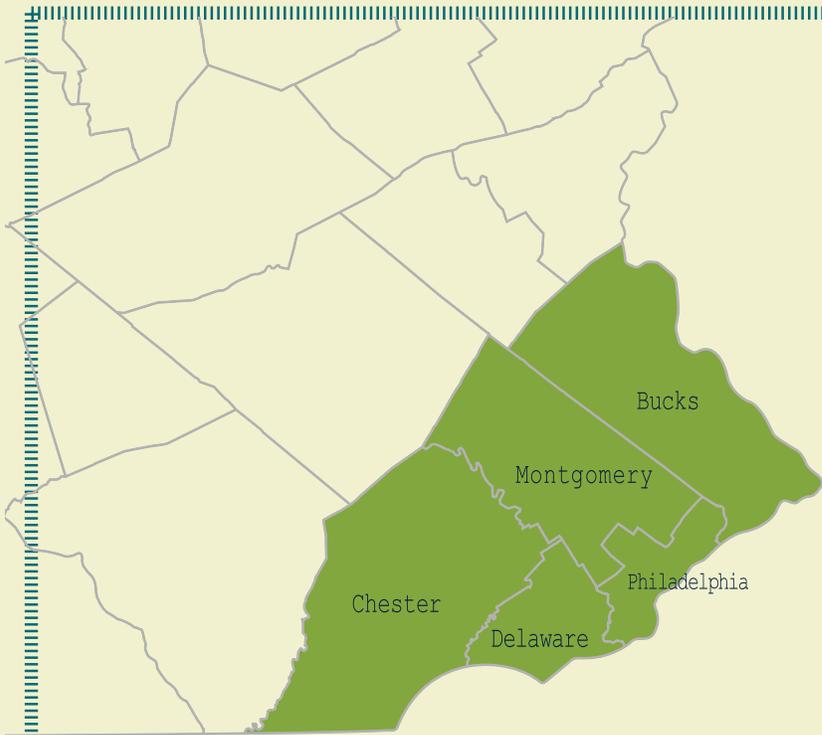
\* Data by House and Senate district are also available at the above address.





**Center on Regional Politics**  
 1114 W. Polett Walk (022-02)  
 840 Anderson Hall  
 Philadelphia, PA 19122-6090  
 corp@temple.edu  
 www.temple.edu/corp  
 @TempleCORP  
 215-204-1600

NONPROFIT ORG.  
 US POSTAGE  
**PAID**  
 PHILADELPHIA, PA  
 PERMIT NO. 1044



# Center on Regional Politics

## POLICY BRIEF

**Explaining School Fund Balances:**  
 Are PA Schools, with \$4.7 Billion in Reserve Funds,  
 Really Flush?  
 An Update

DAVID W. DAVARE

JULY 2016

**Center on Regional Politics - Staff**

Joseph P. McLaughlin, Jr. - Director  
 Kelly D. Colvin - Associate Director  
 Michelle J. Atherton - Senior Policy Writer and Publications Editor

Meghan E. Rubado - Graduate Assistant