Bond Accountability
Commission 2, Inc.

Issue 14

Locally Funded Initiative Update 2

July 20, 2011

Introduction

The BAC's Program Progress Update 18 in January 2011 and Issue 14 / *Locally Funded Initiative* in March 2011 noted a sharp increase in the rate of the Cleveland Metropolitan School District's spending of Issue 14 money that is not matched by the state.

As this report will show, the trend continues, so it may be helpful to explain the causes and effects of such spending.

First, what is the Locally Funded Initiative? This is a term that the District uses to describe construction, repair and maintenance projects that are not co-funded by the Ohio School Facilities Commission (OSFC).

The OSFC pays 68 percent of most costs of the District's construction/renovation program, essentially paying slightly more than two dollars for every dollar the District spends. However, the OSFC will not co-fund certain items, such as athletic facilities and auditoriums, and it will not co-fund building features that it considers to be unnecessary, such as certain sloped-roof styles, curved walls, and ornamental fences. It also will not co-fund work on schools that are not part of the Master Plan, which is governed by building needs that are determined by enrollment forecasts. It is this latter spending for repairs that is of most concern and the focus of this report.

Question of Priorities

Such expenditures may be necessary – for example, if a roof is leaking it must be fixed to prevent water damage to the interior of a school as well as a distraction to learning -- but the BAC has noted the trend of increasing LFI expenditures because such spending quickly diminishes the limited pool of money available for fully renovating or building schools.

The impact is a matter of simple math: Without considering interest payments, one dollar of LFI spending produces one dollar's worth of work; one dollar spent in the co-funded construction program produces slightly more than three dollars' worth of work. Most taxpayers would presumably prefer to see their Issue 14 contribution leveraged at three dollars for one -- unless their child happens to be attending one of the non-Master Plan schools where the roof is leaking.

That is the dilemma facing the District's capital projects staff. As the pool of $335 million approved by voters in May 2001 is drained (the last $55 million of the authorized bonds were issued last September and will cover only Segments 5 and 6 of nine construction phases), and with no guarantee that voters will authorize more bond issues, those responsible for making sure that the schools are in acceptable condition are left with little choice but to make sure that those schools not in the funded replacement pipeline are fortified for at least the near future. That means spending unmatched LFI local tax money, even at the cost of possibly building some new schools in Segment 7.

This summer alone, the District plans to spend about $10 million on LFI repairs and improvements. If matched by the OSFC, that would be abut enough money to build two more schools like Segment 4's Harvey Rice.

The list of items included in this summer's projects is instructive: ceiling repairs; packing and moving furniture and equipment to accommodate the move of students and teachers from closed schools; roof replacements; heating and cooling system repairs; repair and replacement of security cameras; lighting replacement; sewer and waterline repairs; restroom fixture repairs; window replacements; pavement and concrete maintenance and repair; desk replacement; painting; plastering; and much more. While one could argue that packing and moving should more properly an operational, rather than Issue 14, expense, most of the items are routine, similar to what the owner of an aging home might face.

Insufficient maintenance budget

The routine nature of much of the LFI expenses points to the ultimate cause of having to spend Issue 14 money on things other than new or fully renovated schools: The District lacks a comprehensive operations maintenance plan and budget designed to keep its buildings in optimal working order -- and thus to prevent very expensive problems, such as recently occurred at the Kentucky K-8 due to a leaking roof, that occur as a result of failure to perform routine maintenance. An analogy would be waiting to re-shingle your home's roof until rainwater has caved in your kitchen ceiling.

The District's operational budget for purchased repairs and maintenance services is only $2.03 million for Fiscal 2012, which began this past July 1. It has been about the same in recent past years. That pales in comparison to the LFI money that the District plans to spend this summer alone.

It is worth noting that District's last major round of capital bond spending, in the late 1980s and early 1990s, was exhausted on addressing long-overdue repairs and still left District facilities wanting. The partial collapse of East High School's gym roof less than 10 years later illustrated the conditions plaguing Cleveland's schools and gave rise to the $335 million Issue 14 bond authorization in 2001.

Pay now, or pay much more later

So what's wrong with spending Issue 14 money on needed repairs? Not a thing, especially if your child is attending Kentucky and the roof is threatening to collapse. But this report is intended to highlight the costs of a strategy of using capital bond issue money to address such problems on an ad hoc basis.

First, as noted above, every LFI dollar spent for repairs takes three dollars from construction of brand new schools that are better lit, heated and cooled and generally more comfortable and suited to today's technologies – and are not likely to require major repairs for years.

Second, reliance on bond issues to repair or replace problems after they occur generally costs more long term than using an adequate operational budget to routinely perform preventive maintenance. Which is better, to bear the expense of regular oil changes on your old car, or to let it go and eventually have to pay for a new engine or buy another car?

Third, capital bond money is borrowed money. The taxpayers have to pay interest on that borrowed money. As an example, the District's financial advisers once estimated that the debt service on a never-executed issue of $57 million in bonds in 2009 would total more than $106 million by the time the bonds were retired in 2034. So the taxpayers end up paying almost two dollars for one dollar worth of repairs. (In a few cases, the District has issued short-term notes, rather than bonds, and paid off the interest with current tax receipts.)

It makes financial sense to borrow long term to build a school that will last for decades. But it makes much less sense to pay interest for as many as 25 years on a roof re-surfacing with a 10-year guarantee.

It's nothing new for a financially struggling urban school district to put building maintenance at the bottom of its budgetary priority list. Because which is more important, teachers and books or paint and roof patches? (The architect for the Chicago schools renovation program once told the BAC that the program called for installation of virtually indestructible terrazzo floors because history had shown that the Chicago district was unlikely to spend enough to maintain anything less robust.)

That's why the OSFC requires that districts participating in its co-funded school construction program create comprehensive maintenance plans for their newly built schools and dedicate proceeds of at least a half-mill continuing levy to funding that maintenance. The District has complied with this requirement (In addition to the bonds, Issue 14 included a half-mill levy.), but the maintenance plan's authors acknowledge that the levy, even with matching funds from the state, is woefully inadequate to pay for execution of the plans.

Setting a new course

The Cleveland District faces gargantuan financial problems. The interim chief executive officer and the Board of Education recently undertook operational cost-cutting measures designed to get the District through the next two fiscal years without additional tax money. After that, more budget cuts are inevitable unless voters approve a request for additional operating money in the meantime.

Likewise, the end is in sight for Issue 14 proceeds. When that money is gone, the construction and renovation program will stop, unfinished, and the District will no longer have that pool of money to tap the next time one of its schools springs a leak. Issue 14 was never big enough to fund the construction program envisioned in 2001, not even to fund the reduced construction program resulting from the District's declining enrollment. So a request to voters for a successor to Issue 14 is very possible.

Both an operating levy request and a bond-authorization request include possibilities for addressing the perennial problem of how to keep the District's schools in good working order. Either could include a companion continuing levy earmarked solely for system-wide building maintenance and set at a rate sufficient to pay for routine work that will reduce the likelihood of catastrophic repair bills later. In the long run, it would be less expensive for taxpayers.

Planning ahead

The BAC would like to have an idea of the District's plan for LFI spending over the next two or three years, because without such a budget it will be impossible to independently assess the District's need for additional bond authorization to complete the construction program while keeping up with ordinary repairs. Unfortunately, more than two years after the BAC first asked for such an LFI budget, it still has not seen one.

In any case, establishment of a comprehensive maintenance plan with estimated annual costs would be a good first step toward ending the cycle of budget-deferred maintenance and consequent expensive repair crises.

Last January, the Administration reported that it was working on a comprehensive report detailing LFI expenditures. A report of sufficient detail would allow the BAC to assess whether expenses were for the purposes specified in Issue 14: "renovating, rehabilitating, constructing, furnishing, equipping and otherwise improving school facilities and acquiring and improving their sites." For instance, is mowing grass properly an Issue 14 capital expense, or should it be charged to an operations account?

About 10 days ago, the BAC received an itemized listing of LFI expenditures, dated Jan. 31, 2011. The list does not give the purpose for every expense and does not give the dates of the expenses, but it is a start.

A rising trend

LFI spending includes costs for features of the co-funded construction projects that the OSFC does not cover, such as ornamental fences, brick veneer upgrades, sloped roofs, auditoriums and the like, as well as property purchases. It also includes ordinary repairs and upgrades of buildings that are not part of the co-funded Master Plan. Part of a marked boost in LFI spending in 2010 was for upgrades and alterations done in implementing the District's Academic Transformation Plan.

As an update, LFI payments in the first half of 2011 totaled about $6.08 million. Some $3.99 million in encumbrances remain. Among the leaders in LFI payments at schools in the first half, according to the District Finance Department, were:

East Tech High, $1,362,096.51
Whitney Young High, $564,614.72
Garret Morgan High, $254,136.40
Glenville High, $234,813.15
Washington Park High, $320,253.41
Ginn Academy at Margaret Spellacy, $231,661.04

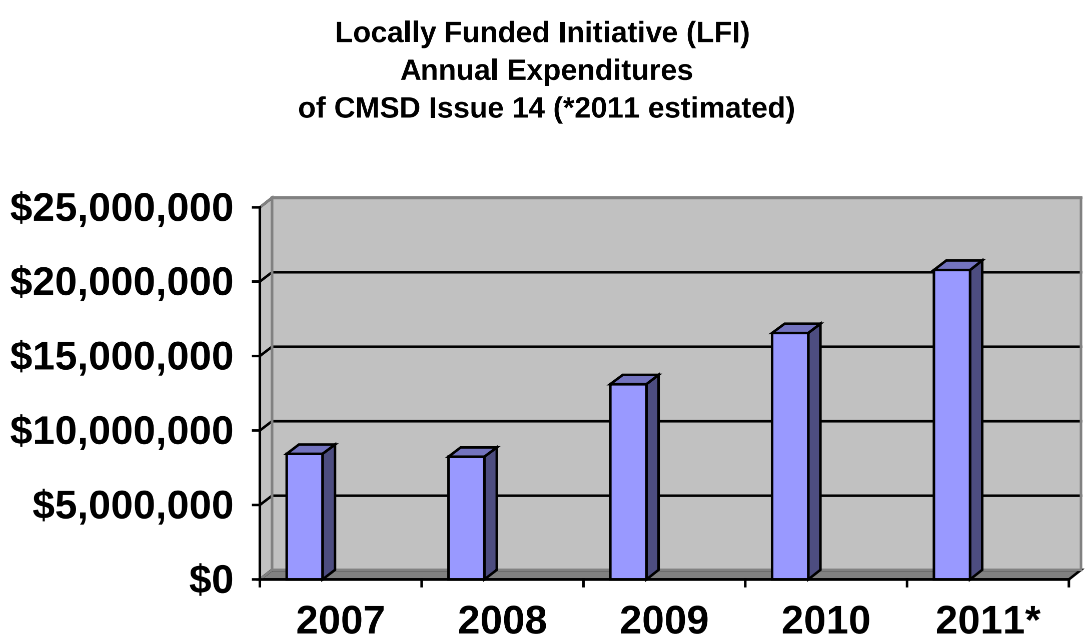
Kentucky K-8, $97,703.15
Valley View, $174,994.00
Douglas MacArthur, $97,703.15
Euclid Park, $290,253.59
Andon Grdina, $149,997.37.

The latter two involved LFI expenses incurred in the construction of new schools. The rest were for repairs or improvements to existing, non-Master Plan schools. Much of the LFI expenses above may have been incurred in 2010, but the bills were paid in 2011.

The Finance Department has reported that Issue 14 LFI spending as of June 30, 2011, totaled $74.67 million. LFI spending amounted to $8.2 million in calendar-year 2008, $13.1 million in 2009, and $16.6 million in 2010.

The District is executing another summer LFI program of repairs, modifications to prepare buildings that will receive students from closed schools, and fulfill Academic Transformation Plan provisions for the start of the 2012 school year. The projected cost in Issue 14 funds is about $10.02 million. The summer program was authorized by the Board of Education on May 24, 2011. (See a complete list of the summer projects below.)

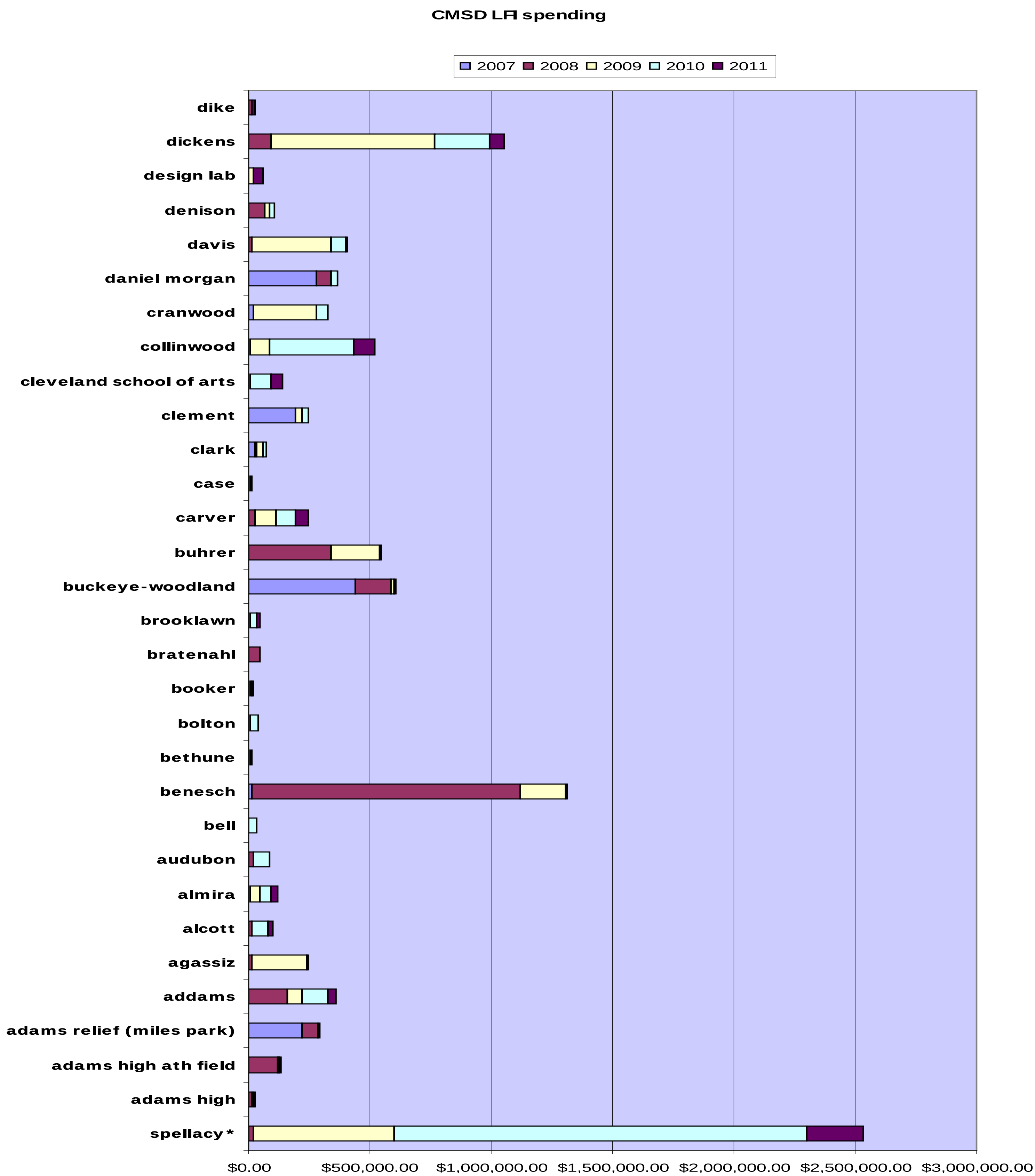
Taken together, the **$10.02 million** in summer work, the **$6.08 million** already expended this year, **$3.99 million** in pending LFI encumbrances, and an estimated **$0.77 million** more in miscellaneous costs, including for District capital projects staff, legal counsel and other administrative expenses, result in an **expected LFI total for 2011 of about $20.79 million**, not counting any further LFI expenses incurred this year as part of construction/demolition/land acquisition for Segments 4, 5 and 6. The chart below illustrates the trend:

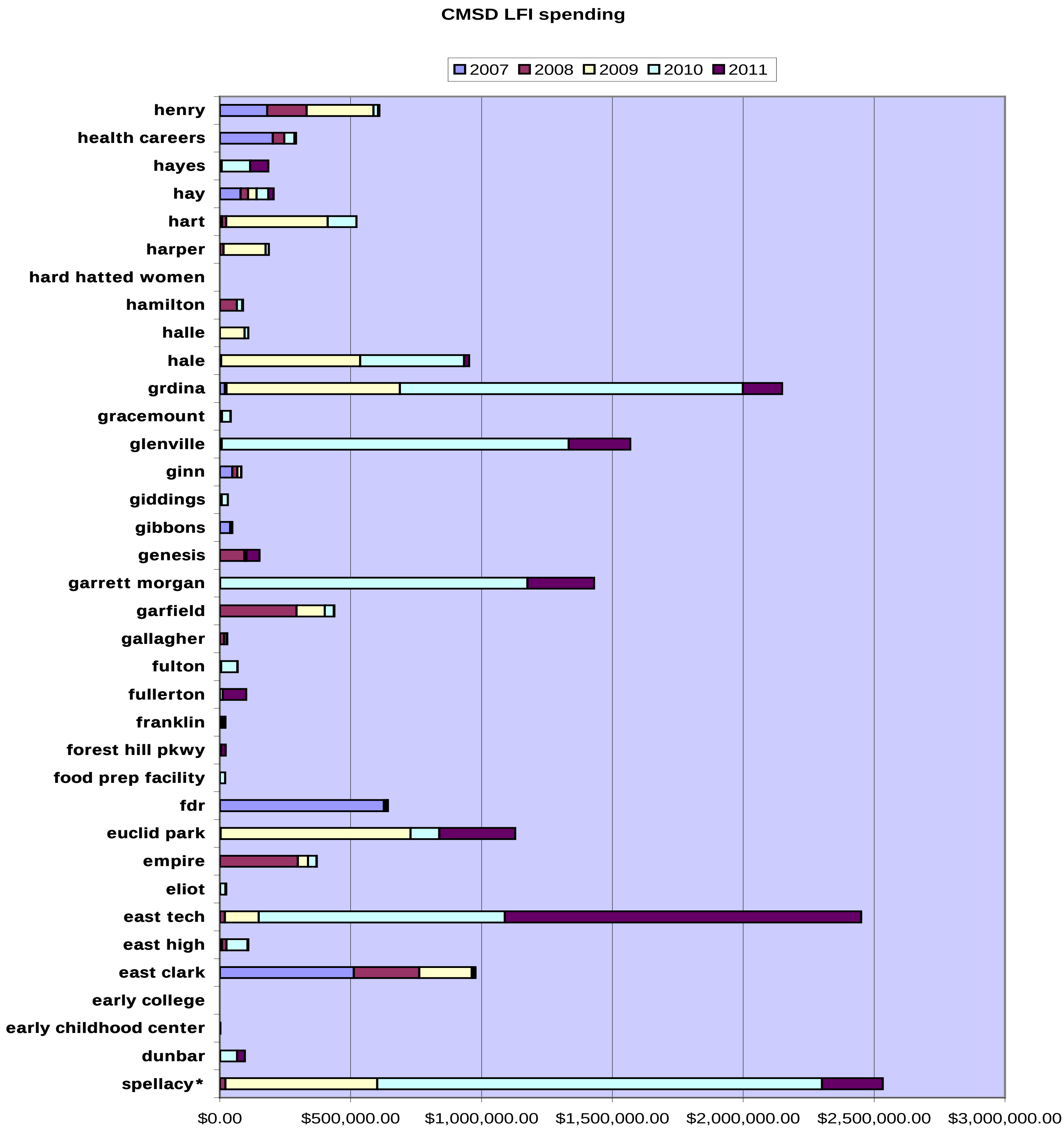


The following charts illustrate Issue LFI spending in calendar years 2007 to June 30, 2011 for selected District facilities.

(* The District Finance Department has separate listings for Ginn Academy and Margaret Spellacy, but the listed Spellacy expenses for at least the last two years clearly are for the Ginn Academy. The line for Margaret Spellacy is repeated on the charts to provide the proper comparative range).

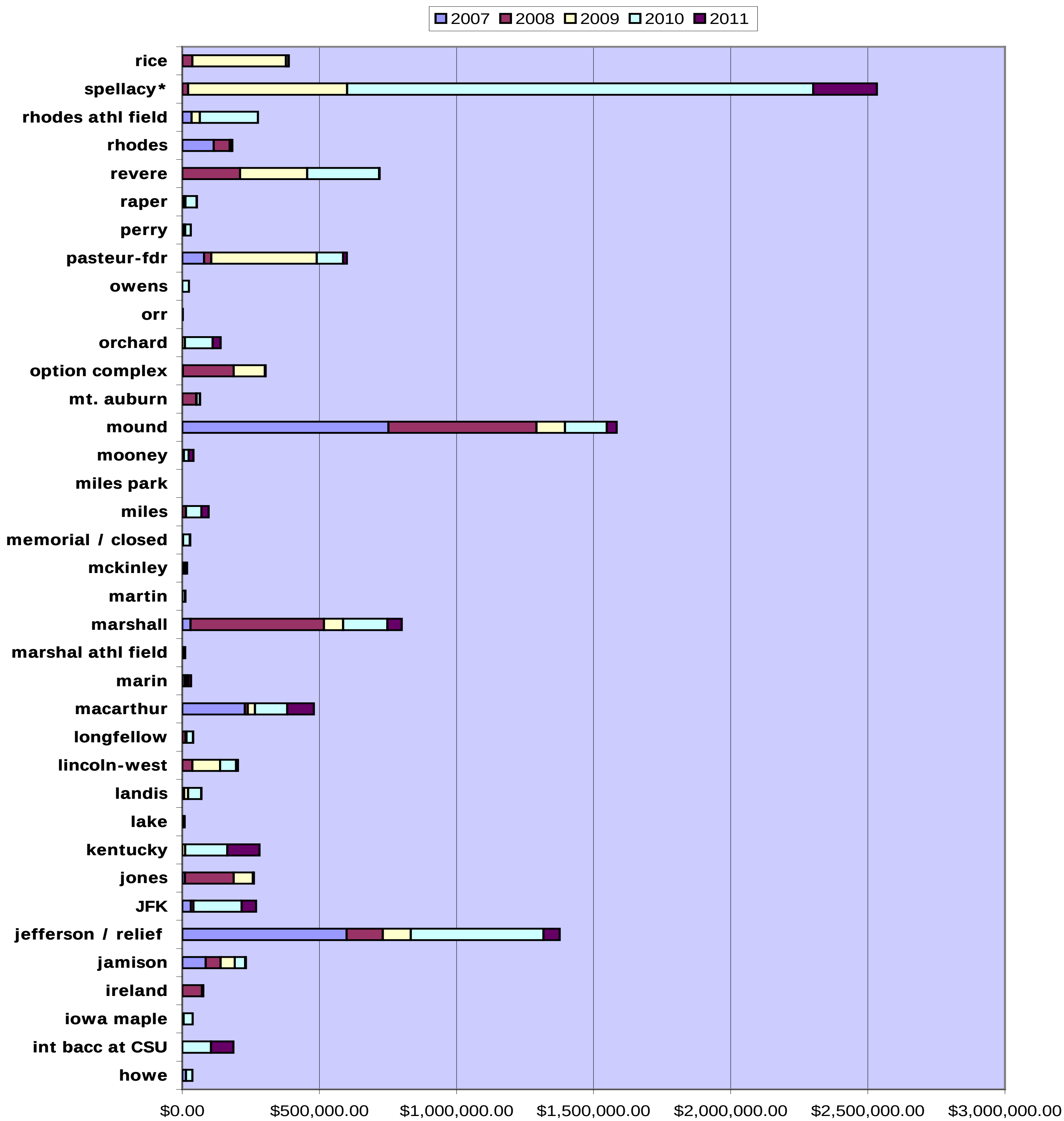
Contact the BAC: You may reach the Bond Accountability Commission at bondaccountability@hotmail.com, or call (440) 781-8654.

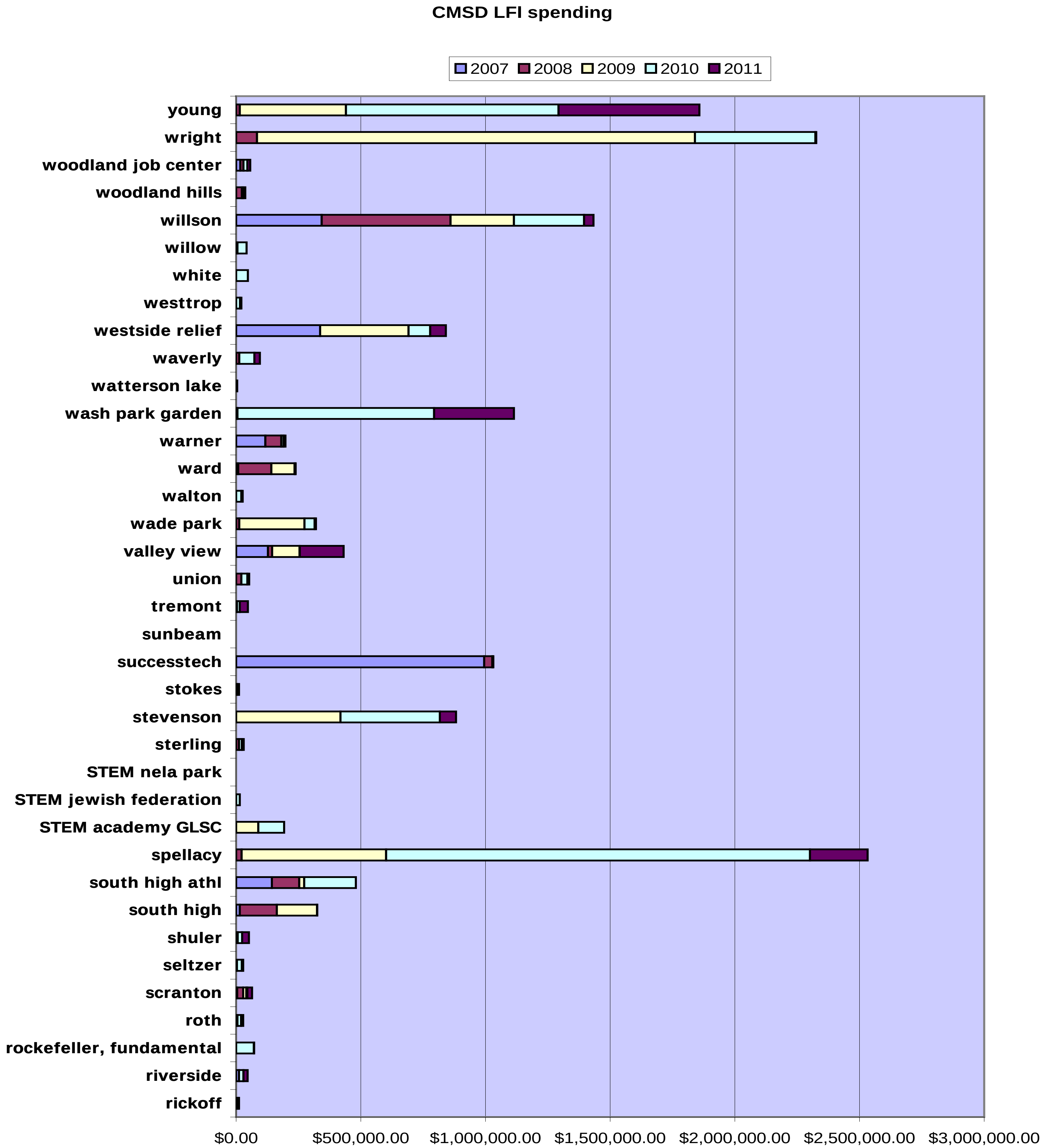

CMSD LFI spending
2007
2008
2009
2010
2011
dike
dickens
design lab
denison
davis
daniel morgan
cranwood
collinwood
cleveland school of arts
clement
clark
case
carver
buhrer
buckeye-woodland
brooklawn
bratenahl
booker
bolton
bethune
benesch
bell
audubon
almira
alcott
agassiz
addams
adams relief (miles park)
adams high ath field
adams high
spellacy*
$0.00
$500,000.00
$1,000,000.00
$1,500,000.00
$2,000,000.00
$2,500,000.00
$3,000,000.00



CMSD LFI spending
2007
2008
2009
2010
2011
henry
health careers
hayes
hay
hart
harper
hard hatted women
hamilton
halle
hale
grdina
gracemount
glenville
ginn
giddings
gibbons
genesis
garrett morgan
garfield
gallagher
fulton
fullerton
franklin
forest hill pkwy
food prep facility
fdr
euclid park
empire
eliot
east tech
east high
east clark
early college
early childhood center
dunbar
spellacy*
$0.00
$500,000.00
$1,000,000.00
$1,500,000.00
$2,000,000.00
$2,500,000.00
$3,000,000.00

CMSD LFI spending




CMSD LFI spending
2007
2008
2009
2010
2011
young
wright
woodland job center
woodland hills
willson
willow
white
westtrop
westside relief
waverly
watterson lake
wash park garden
warner
ward
walton
wade park
valley view
union
tremont
sunbeam
successtech
stokes
stevenson
sterling
STEM nela park
STEM jewish federation
STEM academy GLSC
spellacy
south high athl
south high
shuler
seltzer
scranton
roth
rockefeller, fundamental
riverside
rickoff
$0.00
$500,000.00
$1,000,000.00
$1,500,000.00
$2,000,000.00
$2,500,000.00
$3,000,000.00