Key Measures of Financial Health for School Leaders to Understand and Track

ISFIS, Inc.
Iowa School Finance Information Services

Unspent Authorized Budget

Unspent Authorized Budget (UAB, also called "Unspent Balance") is the most important indicator of the financial health of the district. Failure to manage your district's UAB, resulting in a negative UAB at the end of the fiscal year, can lead to enforced workout plans, enhanced scrutiny, up to and including the takeover and/or dissolution of your district by the state board of education.

What is UAB?
It is the amount of unused district General Fund capacity to spend on behalf of students, or spending authority, left over at the end of the fiscal year that is carried over into the next fiscal year. Since spending authority is generated on a per pupil basis as set by the legislature, districts are limited in their capacity to increase their UAB.

UAB can accumulate over several years, but spend down very quickly if districts do not adjust expenditures to align with current spending authority. For example, declining enrollment reduces spending authority. Failure to adjust in that scenario can quickly and substantially reduce your UAB. Districts are urged to consider UAB as one-time funding and are cautioned against obligating it for ongoing expenditures, such as employee contracts and salary increases, absent a plan for sustainability.

How does a district increase its UAB?
School districts have little ability to increase spending authority since the legislature determines the per pupil spending authority. Enrollment is multiplied by the regular program district cost per pupil to determine the district's regular program budget. Beyond that, a school district may

- Impose an Instructional Support Levy (ISL). An ISL can be used to increase a district's budget by up to as much as 10% of the regular program district cost. 324 out of 325 districts in Iowa use the ISL.
- Pursue every avenue of claiming additional Modified Supplemental amount (spending authority) for on-time funding for enrollment growth.
- Fully claim a Budget Guarantee during enrollment declines that outpace SSA increases.
- Maximize additional Modified Supplemental amounts for Dropout Prevention, English-Learner Authority, Special Education Deficit, or an additional request related to unique or unusual circumstances.
- Receive Grants or Federal funding. These sources of funds are considered as Miscellaneous Income and create dollar-for-dollar spending authority when the funds are received.
- Increase enrollment. School funding is on a per-student basis. More students increase your General Fund revenues. This could be an increase in resident students or an increase in students open-enrolled from a neighboring district. This could also be a decline in open enrollment out of the district.
- Reduce General Fund expenses. Unfortunately, because most sources of revenue are tightly controlled, this is where the districts have the most latitude. Note: Cutting special education expenses does not increase your UAB.

How do I manage UAB? What is a good target?
School boards can set goals or parameters around Unspent Budget Authority targets to clarify their level of comfort with a specific range of Unspent Budget Authority. There is no general "rule of thumb" because all districts have unique circumstances. However, spending more than your UAB (i.e., "going negative") will cause a review by the School Budget Review Committee (SBRC), including a district workout plan to come into compliance, which requires expenditure reductions.

UAB is the same as cash in the bank, right?
No. UAB is your spending authority limit. Even if you have more cash available in the bank than your UAB, you cannot spend beyond your UAB limit without consequences.

Why doesn't cutting special education expenses increase my UAB?
Special education expenditures that exceed revenues generated by special education weighting create spending authority that is annually granted to districts by the SBRC. Similarly, reducing special education expenditures below the revenues generated by the weighting does not increase the district's spending authority. Cuts to special education staff and expenditures do not "free up" spending authority or save General Fund spending authority for other purposes. A school district's unspent budget authority is not affected by special education expenditures; however, its solvency ratio is impacted because excess expenditures are not funded by the state.

Are there other funds that can impact my UAB?
Yes. English Learner weighting generates funding for services to students whose primary language is not English. If EL expenditures exceed the funds generated by the weighting, the district can request additional MSA from the SBRC for excess expenditures while students are eligible in the program and for services provided for students beyond the 5 years of eligibility. Districts should also pay attention to dropout prevention funds. Any carry forward in Dropout Prevention is automatically subtracted from a district's DOP spending authority that they would otherwise be able to generate in the next fiscal year.

Solvency Ratio

Solvency Ratio measures the relationship of fund balance to revenues as a percentage for the fiscal year. In short, it is how much cash you have related to the amount of annual revenues. Here is how ISFIS calculates a district's solvency ratio:

Unassigned General Fund Balance *PLUS* Assigned General Fund Balance
DIVIDED BY
Total General Fund Revenues *LESS* AEA Flow-Through

Explained another way, a district's solvency ratio is a snapshot point-in-time measure of the percentage of revenue remaining, assuming the district closed its doors on June 30 of the fiscal year, after gathering all the year's revenues and paying all the year's obligations. The concept of Solvency Ratio was generated years ago as a consideration by bond rating agencies as a good indication of a district's ability to pay for bonds. The irony of this concept, based on Iowa school finance law, is that districts can't automatically spend cash on hand without the spending authority to back it.

How does a district change its solvency ratio?
A district can impact its solvency ratio by increasing revenues, reducing expenditures, or a combination of both. A district may choose to generate additional revenues through the use of the Cash Reserve Levy if they have not reached the statutory limit of 20% cash reserve relative to two prior years' General Fund expenditures.

What is a reasonable solvency ratio target?
Recommended ranges have typically been somewhere between 5 and 15 percent (with the lower range considered "good" and the higher range considered "excellent"); however, school boards should consider local reasons and comfort levels based on acceptable levels of risk that could justify a deviation from the recommended range.

Districts with a history of comparatively high solvency ratios should consider whether local experiences compel a continued higher solvency ratio trend and, if so, at what expense? What cash might be required for cash flow purposes until property taxes and state funding are received in the Fall? Districts must consider competing issues. Do we need to spend more on learning opportunities for students? Do we need to lower the level of taxation for district residents? In other words, is our high solvency ratio indicative of inadequate educational opportunities, taxation that is too high, cash flow needs, or are we satisfied with the current positions in all of these areas?

If I have a high solvency ratio, I can spend it regardless of my UAB, right?
No. The solvency ratio only relates to the relative fund balance of a district, and therefore is not indicative of the district's spending authority position. Many districts have experienced a negative solvency ratio for a number of years without any sanction from the Iowa Department of Education or State Board of Education, while a negative UAB will draw immediate review from the SBRC.

Enrollment Trends

The Iowa school foundation formula is driven by student enrollment. Both increasing and decreasing enrollment will impact a school district's spending authority and need for expenditures. District leaders should consider short-term and long-term enrollment trends and contemplate scenarios for adjusting staffing and expenditures along the way. Trends in open enrollment (both in and out of the district) also directly impact the district's revenues and expenditures and should be carefully analyzed and trended forward to anticipate the financial impact. In recent years, Education Savings Accounts (ESAs) for private school students may have impacted public school enrollment. Public schools do receive some categorical funding for every resident private school student attending a private school through an ESA. In many cases of districts encountering financial hardship, local leaders have looked back to discover that staff reductions were not made along the way as enrollment declines continued over a number of years.

Number of Staff/Staffing Ratios

Staff salary and benefits are the largest expenditure of a school district's General Fund. District leaders should anticipate a staffing ratio that results in personnel costs around 75 to 85 percent of the planned district budget. Even small increases in salary or benefits costs combined with declining enrollment will compound very quickly if staffing ratios are not maintained, as staff costs creep up to over 75-85 percent. Districts should evaluate the trend in salary and benefit costs as a percentage of the General Fund annually.

Building Level Staff/Staffing Ratios

One way to detect expected staffing cost increases in advance is to carefully consider staff cost trends at the building level. Typically, elementary school staff costs are slightly less per pupil than the average cost per pupil. At the high school, staffing costs are typically slightly higher per pupil. Deviations from this pattern can help identify differences, such as variations in seniority or degree status among staff in a particular building. Understanding building-level staffing costs and anticipating sensible staffing ratios can inform district leaders and help in long-term planning. Maintaining a healthy overall staffing ratio over time is less disruptive than staff reductions made after the district is experiencing economic hardship. It may also help inform districts whether an early retirement plan may be utilized to reduce such expenditures or if natural attrition will deliver the expected staff ratio relative to the number of students anticipated to be enrolled.

New Money / New Spending Authority

School districts typically learn how much new spending authority they will receive for the next fiscal year based on the October 1 enrollment headcount, when the legislature sets the state cost per pupil percentage of growth for the next school year (known as State Supplementary Aid or SSA). The Iowa Code requires the legislature to set the SSA rate within 30 days of the release of the Governor's budget recommendation (typically required by often not completed by mid-February). This report has been historically referred to as the "New Money" report, although it isn't money (cash or revenue), but instead measures the change in spending authority. ISFIS has titled this report the "New Authority Report," and it can be found on the ISFIS Subscriber Website at www.IowaSchoolFinance.com. With the 101% budget adjustment in place (also known as Budget Guarantee), districts with declining enrollment must look one year beyond this notice of new spending authority to realize the impact of an enrollment decline. Historical looks at new spending authority and carrying forward trend lines for long-term planning can go a long way towards helping school leaders plan for revenue and expenditure changes down the road.

Four Key School Finance Ideas for Iowa School Leaders to Keep in Mind

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1. Iowa school finance is based on the number of students in the district. The total amount of money a district has is determined primarily by the number of students enrolled. Except for a few specific tax levies dedicated to specific purposes, the state prohibits districts from levying as much local money as they might otherwise want to fund the school district.

2. The district's tax rate is primarily set by the school foundation formula. There are only limited steps a school board can take to increase or decrease the property tax rate.

3. Certain funds have to be spent on certain things. Each tax levy has a limited purpose and the General Fund is for everything else. Although it may not make sense that the district has enough money to pave a parking lot or buy computers but not enough money to hire teachers (or vice versa), that's how the state law works.

4. Schools are a labor-intensive business, with about 80 percent of a district's General Fund made up of staff salary and benefit costs.