

School District of Philadelphia
Financial Impact Analysis:
Funding, Purchasing Power and Stranded Cost Analyses Outcomes
March 2017

Background and Purpose of this Analysis

- In 2012, an analysis was completed noting that every newly authorized charter seat costs the district \$7,000. This is comprised of two components:
 1. **Migrating Students:** Every student who leaves the district for a charter school costs the district \$5,600, as funding goes with them to the charters, but some fixed costs – *known as stranded costs* – remain at the district.
 2. **New-to-System Students:** Every new student not transferring from the district but attending charters costs the district \$10,400, as the total funding going to the district does not increase for these students, but the district must pay charters for those students.
- Combined, the average impact is \$7,000 per charter student

Question at hand: *What is the financial impact of charter schools on the district, and what opportunities are there to mitigate costs associated with enrollment migration from district-run to charter schools?*

Background and Purpose of this Analysis

In response to the question at hand, the District conducted a three-part analysis using Fiscal Year 2014 data:

1. **Funding Analysis:** *how does public funding available to charter schools compare to district-run schools?*
2. **Purchasing Power:** *what can charter schools afford compared to the District and how do they allocate their dollars compared to the District?*
3. **Stranded Costs:** *what constraints does the District have on its spending flexibility and therefore what are the financial implications of enrollment migration from district to charter schools? What can the District do to mitigate stranded costs (which are costs that cannot be immediately and proportionately reduced when enrollment declines)?*

These three analyses, together, aim to provide a **more detailed understanding** of the implications of future charter authorizations, as well as provide insight into **what the District can do to mitigate the costs of current and future migration of students from district to charter schools.**

Executive Summary

In FY14, charters received slightly less public funding on a per pupil basis; however, charters faced different constraints than the district, allowing them to afford more resources in the classroom.

- ***The analysis sample of charter schools in Philadelphia were funded with public dollars slightly less*** than SDP on a per pupil basis - 2% less on a weighted basis and 4% less on an unweighted basis
- However, Philadelphia ***charter schools had fewer constraints*** on uses of their funding (limited debt, contractual obligations) compared to SDP, and therefore were able to spend more freely and aligned with strategic priorities, including more teachers and technology
- Most notably, because of lower salaries and benefits, **charters were able to afford 3 teachers for the cost of every 2 at the District.** For a school of 400 students, this is the difference between 20 and 30 teachers.
- ***SDP had more constraints*** on uses of funding (including contractual obligations, structural limitations, and resourcing policies). Notably, SDP spent 42% more per teacher on salary and benefits than the sampling of charter schools analyzed.

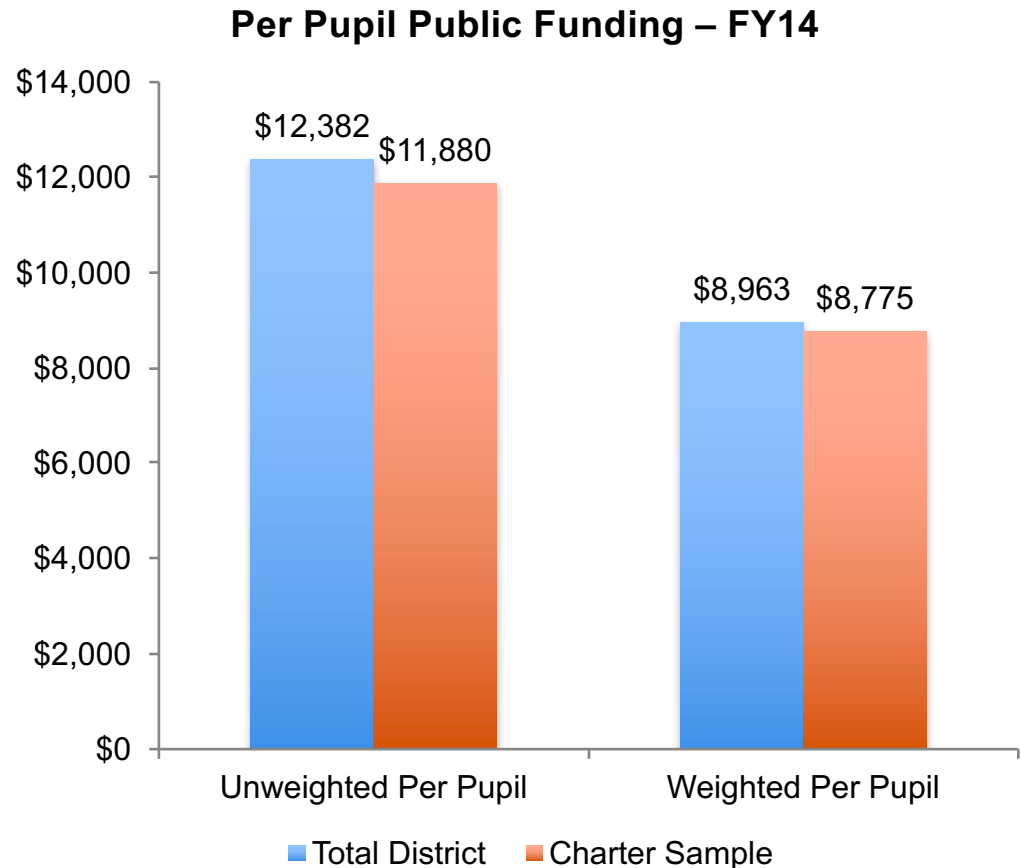
While charter school growth will affect district finances, changes to the current district cost structure could help SDP to plan proactively for and manage such growth

- Due to contractual, structural, and policy constraints, it's ***difficult for SDP to react and reduce its spending*** when students leave district-run schools.
- These constraints at SDP cause ***costs to remain at the District when students leave*** – defined here as “stranded costs.” These costs are estimated to be ***\$4,824 per student migrating*** to a traditional charter school (***or \$461 per student remaining in SDP***). ***If debt service were considered*** a stranded cost, SDP would experience ***stranded cost of \$6,898 per migrating student***.
- However, ***these stranded costs would be reduced by an estimated 65% when a Renaissance charter school is authorized instead of a traditional charter school***. A Renaissance charter school is a turnaround school – where the students remain at the same school, but the operator changes from district to charter. In this case, the enrollment leaves SDP from only one school, not many, and therefore district costs, particularly staffing, are reduced more efficiently.
- Some of the constraints that lead to stranded costs are ***partially controllable*** and can be mitigated with action by SDP, ***albeit via difficult actions such as layoffs, school closures, and/or school turnarounds***.

Analysis Outcomes

In FY14, charter schools were publicly funded just slightly less on a per pupil basis


- Based on the available sample set, charter schools received less public funding that the District on both a weighted and unweighted per pupil basis*
- However, the variance was small – 2% on an unweighted basis and 4% on a weighted basis
- These figures have been adjusted to remove debt service, rent, and special education outplacements



* The analysis was completed two ways: on an unweighted basis, which looks at funding available per average pupil, and on a weighted basis, to account for the varying needs of the student population served by each sector; The funding equity variance reduces on a weighted basis, because the District had a Special Education population with higher needs

However, Charters and Districts spent their resources in very different ways

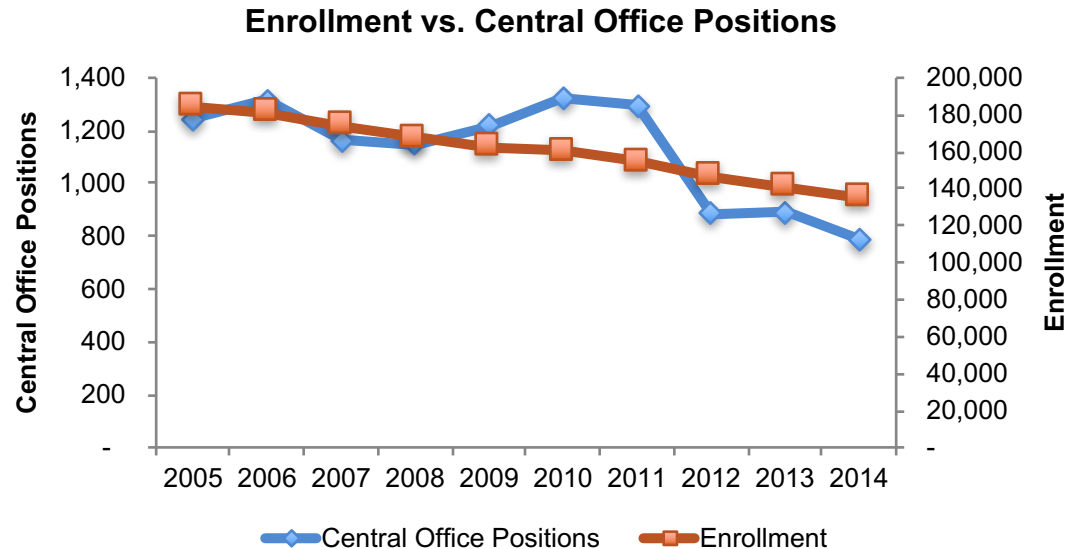
Key Findings:

 Charters spent less than the district on*:	+ Allowing them to spend more on:
<ul style="list-style-type: none">• Facilities & Operations (including maintenance and utilities)• Teacher Salaries (per teacher)• SPED staffing• Staff Benefits• Student Outplacements	<ul style="list-style-type: none">• Decreased class sizes• Instructional Technology• Instructional Materials• Consulting support• Programs and partnerships• Administrative Staffing & support (see next page)

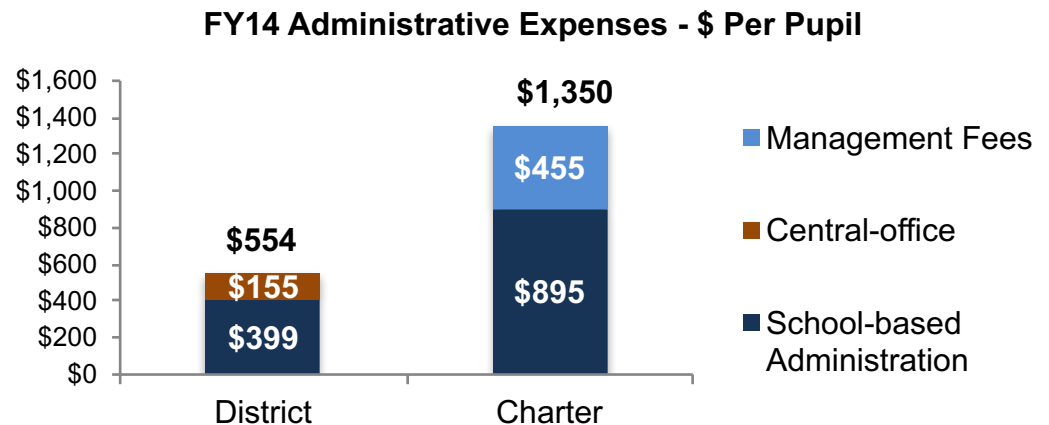
*Because charter payments are adjusted for debt service, in effect, charters contribute to the payment of debt service. Therefore, the district's debt service has been excluded from this analysis.

The District significantly reduced the size of its central office over years of enrollment decline, resulting in significantly lower per pupil administrative costs

- Since 2005, SDP has **reduced central office positions at a deeper rate than enrollment has declined** - cutting 37% of central office positions while enrollment declined 27%*



- Because of this, and from lower school administrative staffing, the **District spends \$796 less per pupil on administrative costs**** in its directly managed schools than the charter schools spend



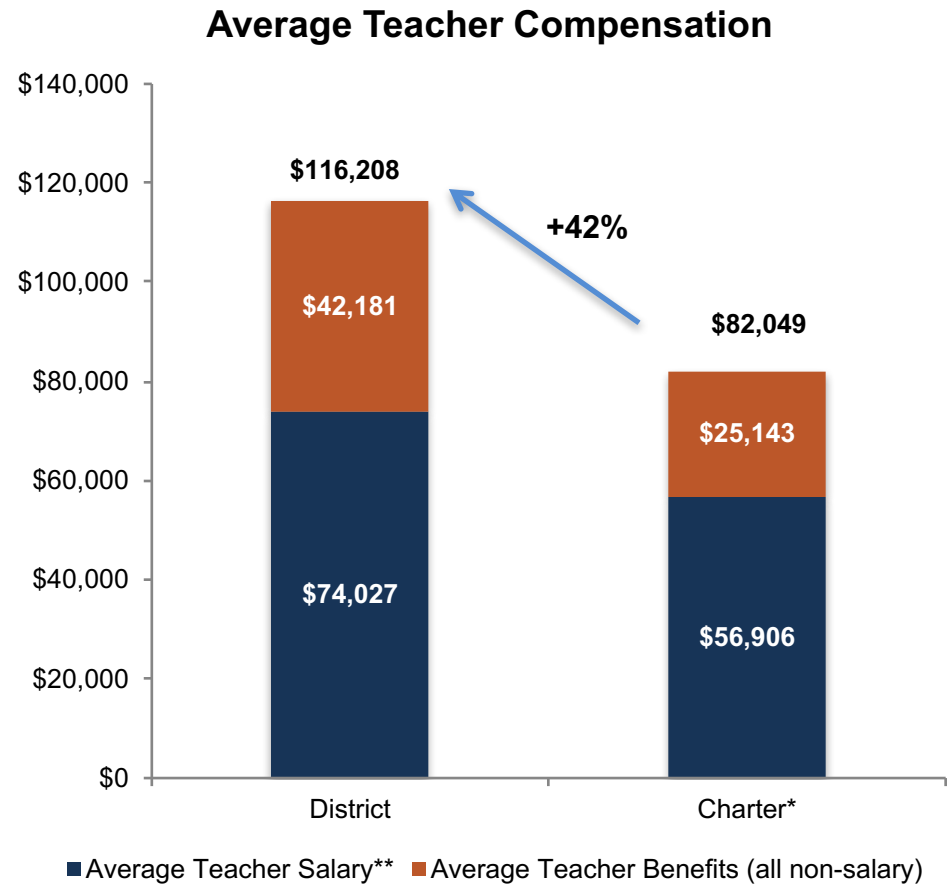
* Data from FY14 CAFR

** Administrative expenses have been defined as school level administration and central office costs

Most notably, because of lower salaries and benefits, charters were able to afford 3 teachers for the cost of every 2 at the District

The District spent 42% more per average teacher in FY14.* Higher average salaries and total benefits at the District, especially Health & Welfare contributions and Pension payments, contribute to this gap. Therefore, charters can afford 3 teachers for the price of 2 at the District.

For a school of 400 students, this is the difference between 20 and 30 teachers.

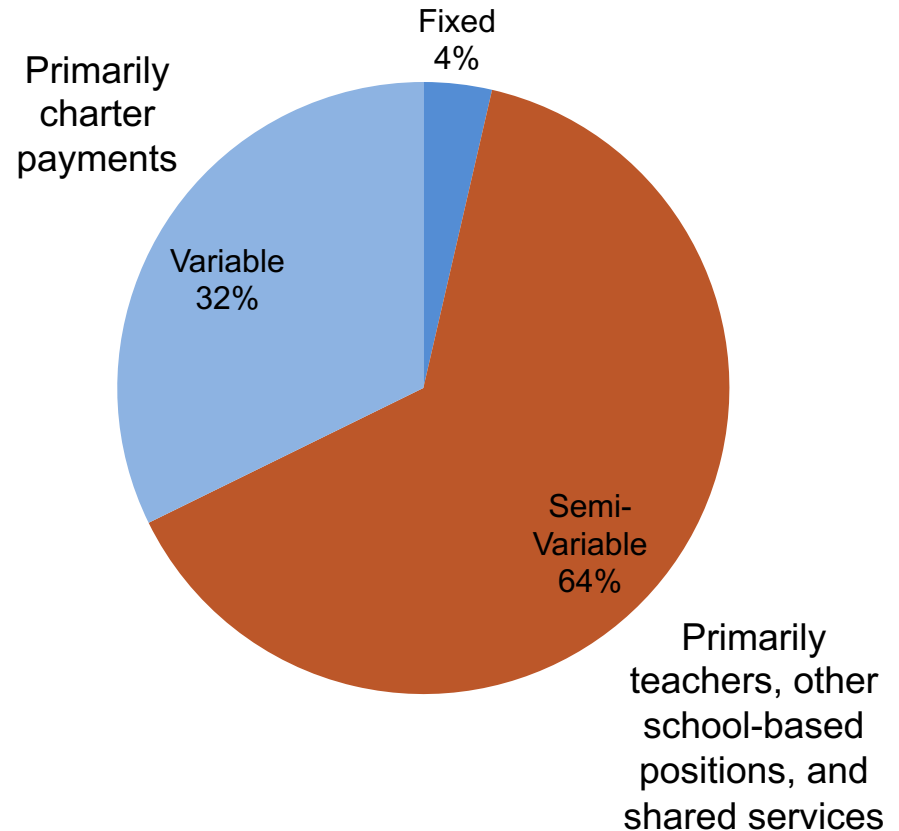


*Based on six charters reporting average teacher salary

** Average is weighted – schools with a higher number of teachers contribute more to the average

The District has more constraints on uses of funding, limiting its flexibility

- Contractual obligations, structural limitations, and staffing policies limit the flexibility of the District's cost structure*
- Because of this, the District has a significant amount of **fixed and semi-variable costs** that cannot proportionately and immediately reduce with an enrollment reduction
 - **4% is fixed** and will not reduce at all with enrollment changes (payments to other LEA's and central office executive leadership)
 - **64% is semi-variable** – it can change but does not reduce proportionately with changes in enrollment (primarily school-based positions, shared services, and supports)



*Because charter payments are adjusted for debt service, in effect, charters contribute to the payment of debt service. Therefore, the district's debt service has been excluded from this analysis.

Therefore, it is difficult for the District to react and adjust its spending when students leave

- As students migrate to charter schools, public funding follows the students, but they leave behind their “share” of fixed and semi-variable costs that do not automatically reduce when they leave – known as “***stranded costs***”
- The District must cover these stranded costs with the funding intended for remaining students, reducing the amount available for each remaining student’s instructional spending
- **As more students migrate, the stranded costs per district pupil continually increase if the District does not take steps to mitigate the costs**

Enrollment shifts from district to charter schools are already financially impacting the District

- Charter authorizations made to date have resulted in an estimated **11,600 students migrating** from district to charter schools over the next eight years. After considering corresponding actions of the District, the District will experience **\$56M of costs annually by 2023 that are “stranded”, or 4.6% of FY15 budget**
 - **This impact excludes debt service.** Because charter schools’ payments are adjusted for debt service, the district effectively withholds revenues to cover debt service out of the general fund. In effect, then, debt service has a guaranteed source of funding. Including debt service would increase stranded costs by approximately \$25M annually.
- This estimate **assumes that the District has not done everything within its control to mitigate costs** – such as closing under-enrolled schools and changing school staff allocation policies – but does **assume reductions of 530 staff** and other expenses (based on existing staffing and allocation policies) resulting from projected enrollment losses
- Each migrating student leaves behind about **\$4,824** in stranded costs – \$56M total – which the district **will incur annually in perpetuity. If debt service were considered a stranded cost, SDP would experience** stranded cost of **\$6,898 per migrating student**
- This equates to about **\$461 per remaining district student** (excluding debt service) of additional cost burden to cover to provide the same level of service

Some of the \$56M of stranded costs are partially controllable and can be mitigated with action by the District

Potential Action	Potential Impact
Reduce fixed cost structures , including closing underutilized schools and sale of buildings	By closing schools that are enrolled at below 50% capacity (based on anticipated enrollment losses from new charter authorizations), the district can reduce an estimated \$33M of the \$56M stranded costs
Consider policy changes that can make costs more variable	Teacher costs are the highest cost in the district. Savings could be realized through establishing more flexible staffing policies to respond to the challenge of uneven enrollment migration across schools and grade levels, allowing for different school schedules or combined grade level classes. Adjusting teacher allocation policies to increase the average student / teacher ratio 10%, the district can reduce cost by \$47M, partially offsetting \$56M stranded costs.
Provide or increase shared services to charters	Doing so will help offset fixed costs in these organizations; impact not quantified and will depend on services provided

In addition to offsetting anticipated stranded costs, **these actions will make the district's cost structure more variable / flexible**. At the same time, these actions can be challenging and painful.

Future charter authorizations will increase stranded costs, but this impact can be minimized

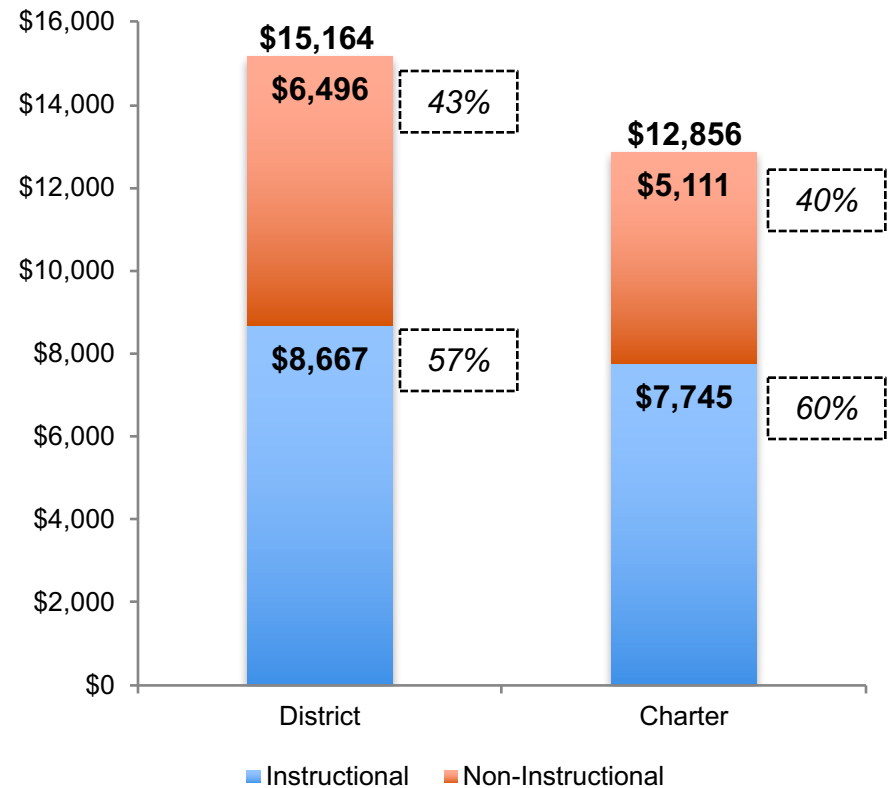
Potential Action	Potential Impact
<p><i>For future authorizations,</i> consider Renaissance charters as opposed to traditional charter openings. Renaissance charters are charter takeovers of existing district schools.</p>	<p>Renaissance charters reduce stranded costs by approximately 65% as compared to traditional charters (from approximately \$5.2M to \$1.8M for every 1,000 students migrating). While both would add to the total stranded costs, Renaissance charters add significantly less.</p>

Supplemental Slides

In FY14, the District spent about \$923 more per pupil on Instruction than the charter school sample

- Items considered Instructional include:
 - Regular Education Salaries
 - Special Education Salaries
 - Other Student Support Salaries
 - Proportionately Allocated Benefits
 - Instructional Materials
 - Information Technology
 - Programs & Student Supports
 - Professional Development
- Charters spend a slightly larger portion of their dollars on Instruction – 60% vs. 57%
- When benefits are not allocated to Instructional Salaries, the District's Instructional spend is about \$212 less than charters
- Eliminating debt service from this analysis, the District's Non-Instructional spend reduces by \$2,046 per pupil; Charters reduce by \$90 per pupil. Instructional spend remains the same.

Instructional vs Non-Instructional Spend Per Pupil



With a migration of 11,600 students, if the district were able to reduce positions proportionately with enrollment reductions, 1,316 positions would be eliminated.

- However, only 530 positions are assumed to be reduced based on current policies and structures, or 40% of proportionate reduction of 1,316 positions.

Position Reductions with 11,600 Student Enrollment Migration from District Schools to Charter Schools

