HANDOUT E2

Research Report

Fiscal Distress

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Prepared for

THE HOUSE INTERIM COMMITTEE ON EDUCATION AND
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2019-2020 Adequacy Study

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INTRODUCTION

The Arkansas Fiscal Assessment and Accountability Program, or fiscal distress, is the state program used to identify and correct school districts that are struggling to maintain fiscal stability. Under state statute, the Division of Elementary and Secondary Education (DESE) identifies districts in fiscal distress; the State Board of Education (SBOE) approves or denies the identification and classifies school districts as being in fiscal distress. DESE, the Commissioner of Education, and SBOE have authority to take corrective actions in districts identified and classified in fiscal distress.

Fiscal distress is one of two remaining distress programs. The other is facilities distress (the third distress program, academic distress, is now known as Level 5 Intensive Support). Arkansas Code § 10-3-2102 requires the House and Senate Committees on Education to evaluate the entire spectrum of public education to determine whether students receive equal opportunity for an adequate education. As one part of that responsibility, the law requires the Committees to review the fiscal and facilities distress programs. Facilities distress was presented as part of the report on the Facilities Partnership Program and Facilities Distress in October 2019. This report is presented to fulfill the requirement that the Committees review the fiscal distress program.

According to DESE, open-enrollment charter school financial issues are handled through the Charter Authorizing Panel, which has the authority to place charters on probation for fiscal issues. Charters are not handled through the fiscal distress program and will not be discussed in this report.

HISTORY OF THE PROGRAM

Fiscal distress was created by Act 915 of 1995. The original program contained three phases: districts that did not file improvement plans with DESE (then the Department of Education), did not implement the district improvement plans according to DESE regulations, or failed to follow DESE recommendations moved into higher phases. In Phase III, DESE had the ability to replace a district's superintendent, act as the district's school board, or annex the district to another district.

Act 1467 of 2003 modified the fiscal distress program and eliminated the three phases that existed in the original program. Under Act 1467 of 2003, districts could remain in fiscal distress for two consecutive years. In 2013, Act 600 extended the amount of time a district could remain in distress from two years to five years.

Act 929 of 2019 broadened the focus of the Fiscal Assessment and Accountability Program. Prior to Act 929 of 2019, the goal of the program was to identify, assess, and address school districts in fiscal distress. Act 929 of 2019 seeks to create a new program to improve public school districts' finances through reviewing financial management practices of all public school districts, identifying and addressing districts in fiscal distress, and providing continuous support to districts returned to local control after being removed from the fiscal distress classification. Act 929 of 2019 will be discussed in more detail later in the report.

Fiscal Distress	Districts
Number of Districts in Distress	77
Districts in Distress Remaining (not consolidated or annexed)	56
Districts in Distress Consolidated or Annexed	21
Districts in Distress Twice	11

Since the beginning of the program in 1995, 77 districts have been classified in fiscal distress. Of those 77 districts, only 56 still exist. Twenty-one districts have been consolidated or annexed to other districts. Most of the consolidations and annexations were due to Act 60 of 2004, which requires consolidation or annexation of districts whose average daily membership (a calculation representing student count) falls below 350 for two consecutive school years. Many of the consolidations occurred in 2004; however, a few districts were consolidated or annexed under Act 60 of 2004 much later. In addition, a few districts were consolidated or annexed for other reasons.

Following Act 1467 of 2003, 59 districts have been classified in fiscal distress. Of those districts, 47 still exist. Of those 47 districts, 11 districts have been classified in distress twice following Act 1467 of 2003, including Dollarway, Earle, and Lee County, three districts currently in distress.

FISCAL DISTRESS PROCESS

The fiscal distress process includes early warning, identification, classification, sanctions and corrective actions, and removal. Each of these steps is discussed in greater detail below.

EARLY WARNING

Act 798 of 2009 created fiscal distress early warning. Early warning requires DESE to monitor districts for signs of fiscal problems and notify districts with more than two non-material violations in one year. Under DESE rules, a nonmaterial violation is something that does not directly jeopardize the fiscal integrity of a school district but has the potential to put the school district in fiscal distress. Each year, DESE is required to report to school district superintendents if DESE is aware that the school district has experienced two or more nonmaterial indicators of fiscal distress that DESE believes could put the district at risk without intervention. Similarly, superintendents are required to report to DESE if the superintendent is aware that the district has experienced two or more nonmaterial indicators of fiscal distress that, without intervention, could put the school district at risk of fiscal distress.

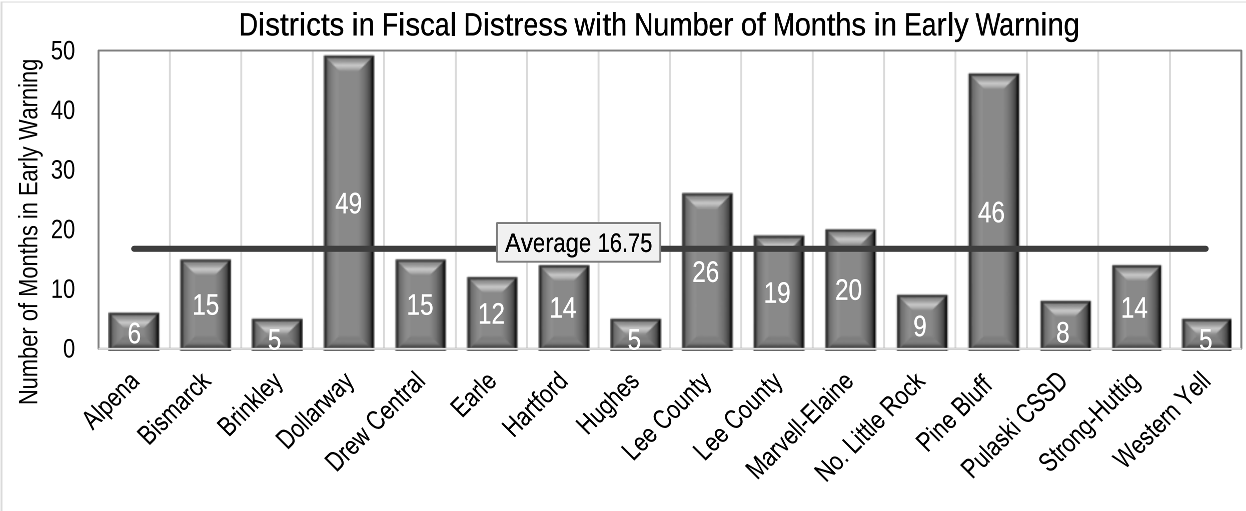
To help identify potential problems, DESE provides an early intervention checklist to school districts. A copy of the checklist is attached in the Appendix. This tool helps districts identify issues that could lead to a fiscal distress classification if left unaddressed. Districts are not required to complete the checklist. According to DESE, DESE reviews three years of districts' unrestricted fund balances, audits, and average daily membership records. If DESE has concerns about a district after the review, DESE sends the district the checklist.

A district may move into or out of early intervention in any given school year. The districts currently in early warning are Cleveland County, Clinton, Huntsville, and Pangburn.

Early Warning	Districts
Total Districts in Early Warning	36
Districts in Early Warning Twice	5
Districts in Fiscal Distress at some point prior to being placed in Early Warning	18
Districts that moved from Early Warning to Fiscal Distress	15
Districts that moved from Early Warning to Fiscal Distress Twice	1
Districts in Early Warning that were not moved to Fiscal Distress	21

Since the beginning of early warning in 2009, 36 districts have been classified in early warning. Five districts (Augusta, Deer/Mt. Judea, Dollarway, Lee County, and Mountain Pine) have been classified in early warning twice.

Of the 36 districts in early warning, 18 were classified in fiscal distress at some point prior to being placed in early warning. That number includes Deer/Mt. Judea (the Mt. Judea School District was previously classified in fiscal distress before it merged with the Deer School District) and Forrest City (the Forrest City School District was classified as being in fiscal distress on December 14, 2009, shortly after early intervention took effect).

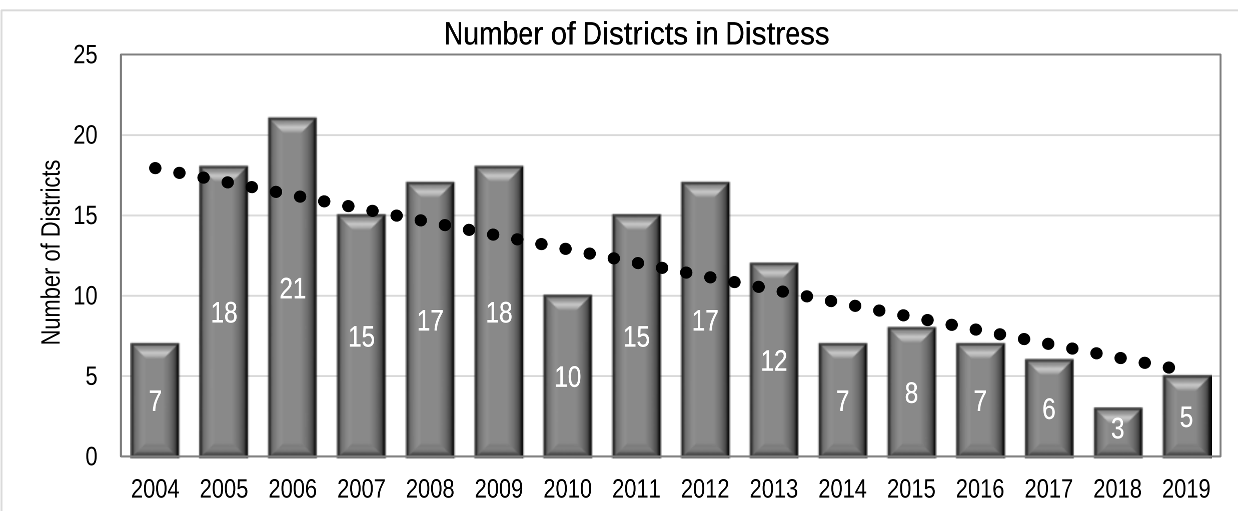


Of the 36 districts in early warning since 2009, 15 of those districts were classified in fiscal distress after being identified in early warning (Lee County moved from early warning to fiscal distress twice). In other words, for about 42% of districts, early warning did not prevent them from moving to full fiscal distress. The early warning program appears to have prevented the remaining 58% of districts from moving to fiscal distress. Eight of the 15 districts were previously in fiscal distress prior to the existence of early warning.

Of the 21 districts in early warning that have not been moved to fiscal distress, four are currently in early intervention (Cleveland County, Clinton, Huntsville, and Pangburn). Of those 21 districts, three have been classified in early warning twice (Augusta, Deer/Mt. Judea, and Mountain Pine). Ten of the 21 were previously in distress (counting Mt. Judea and Forrest City).

For districts that moved from early warning to a fiscal distress classification, the average time in early warning was 16.75 months.

The table below shows the number of districts that have been in fiscal distress at any point during each calendar year from 2004 to 2019. The table starts with 2004 because it is the first full year after the changes to fiscal distress enacted under Act 1467 of 2003.



While the number of districts in fiscal distress increased from 2010 to 2012 (after the adoption of early warning in 2009), the number of districts in distress during the calendar year has mostly declined since 2012. The table shows that the number of total districts in distress generally has declined since the adoption of the early warning program.

IDENTIFICATION AND CLASSIFICATION

Arkansas Code § 6-20-1904 lists the indicators of fiscal distress. DESE may identify a district in distress if the district has any of the indicators. The indicators include:

- Declining balance determined to jeopardize the fiscal integrity of the district
- An act or violation determined to jeopardize the fiscal integrity of the district
- Any other fiscal condition of a school district deemed to have a detrimental negative impact on the continuation of educational services by the district

Such acts, violations, and conditions include:

- Material failure to maintain school facilities, provide timely and accurate financial reports to specific state agencies, meet minimum teacher salaries, comply with state purchasing, bid agreements, or audit requirements
- Material violation of local, state, or federal fire, health, safety, or construction codes
- Material default on any school district debt obligation
- Material discrepancy between budgeted and actual expenditures
- Insufficient funds to cover payroll, salary, employment benefits, or legal tax obligations

Once DESE has identified a district in distress, DESE is required to notify the district in writing. Once the district receives the notification from DESE, the district has 30 days to appeal to the SBOE. SBOE must hear the appeal within 60 days after receiving the appeal from the district. If the district chooses not to appeal, SBOE must still vote to classify the district in distress. While DESE *identifies* districts in distress, only SBOE may vote to *classify* the district in distress.

Most districts do not appeal. SBOE has classified districts as being in distress 73 times since Act 1467 of 2003; only ten districts appealed during that time, and only one appeal was successful. Districts that DESE has identified as being in fiscal distress are prohibited from incurring additional debt without written approval from DESE.

POSSIBLE SANCTIONS AND CORRECTIVE ACTIONS

Once a district is classified in fiscal distress, a district has certain responsibilities. A district in fiscal distress must:

- File an improvement plan with DESE that includes specific ways to correct fiscal deficiencies
- Allow on-site technical evaluations and other assistance conducted by members of the DESE Fiscal Services and Support Unit
- Adhere to recommendations from DESE to improve staffing and fiscal policy practices
- Report the reason for fiscal distress to the newspaper
- Obtain written permission from DESE before incurring additional debt

After a district is classified in fiscal distress, DESE and the State Board may take actions in the district, including:

- Removing and replacing the superintendent
- Suspending or removing the local school board
- Requiring fiscal training for the district staff or local board
- Monitoring the fiscal operations and accounts of the district
- Petitioning to the SBOE to annex, consolidate, or reconstitute the district
- Imposing additional reporting requirements on the district
- Taking any other action allowed by law that is deemed necessary to assist a school district in removing the classification of fiscal distress

Since the inception of fiscal distress in 1995, nine districts have been in state takeover for fiscal distress. Helena-West Helena has been in state takeover for fiscal distress twice. It is important to note that districts in fiscal distress may have been in state takeover for another reason; for example, Lee County has never been in state takeover for fiscal distress, but is currently under state takeover for being in probationary status for accreditation violations.

The average amount of time districts are in fiscal distress depends somewhat on the timing of when the district was in distress. Act 915 of 1995 did not contain a limit on the amount of time a district could remain in fiscal distress. From 2003 until 2013, the time limit on fiscal distress was two consecutive years, unless the district was unable to be removed from fiscal distress due to conditions beyond its control. Act 600 of 2013 extended that time limit to five years, unless the district is unable to be removed from fiscal distress due to conditions beyond its control. The average amount of time districts spend in distress is therefore different depending on when the district was classified and removed.

For all districts classified as in fiscal distress after Act 1467 of 2003, the average time in fiscal distress was 20.2 months. For districts classified after the passage of Act 600 of 2013, the average time in fiscal distress was two years. The average amount of time increased slightly after the amount of time each district could remain in distress was increased to five years; however, the average amount of time in distress was still under the two-year timeframe that existed prior to Act 600 of 2013.

REMOVAL

To be removed from fiscal distress, a school district must demonstrate that all causes of fiscal distress have been corrected.

SBOE must vote to remove a district from distress. If a school district is not removed from fiscal distress within five years, the SBOE is required to annex, consolidate, or reconstitute the district. However, if the district is unable to be removed from fiscal distress due to conditions beyond its control, the law allows the SBOE to grant additional time. Arkansas Code § 6-20-1908 does not specify what conditions qualify as “beyond the school district’s control.”

Currently, none of the school districts in fiscal distress are nearing the five-year mark. Of the districts currently in fiscal distress, Dollarway was the earliest district classified in April 2016.

Districts returned to local control or removed from fiscal distress must comply with all monitoring and reporting requirements from DESE and SBOE, cannot incur additional debt without written approval from DESE, and must use Arkansas Legislative Audit to conduct an annual audit.

If a district’s board of directors has been removed, the Commissioner may return administration of the school district to the previous board of directors or a newly elected board of directors. DESE must first certify that the district has corrected all issues that led to the classification of fiscal distress and that the school district has not experienced any additional indicators of fiscal distress. The SBOE must also determine that the district has corrected all issues that caused the classification of fiscal distress.

ACT 929 OF 2019

Act 929 of 2019 mirrors the changes Act 930 of 2017 made to the academic distress program (now known as Level 5 Intensive Support).

The purpose of Act 929, according to Arkansas Code § 6-20-1902, is to improve Arkansas public school districts’ financial practice and use of resources by enabling DESE to review financial management practices of school districts, establishing a program by which DESE can identify and address public school districts in any phase of fiscal distress, including early indicators of fiscal distress, and creating a system for providing fiscal support and monitoring to school districts that were once in fiscal distress. According to testimony in the House and Senate Education Committees during the Regular Session of 2019, in late 2015 or early 2016 DESE changed the name of the unit handling fiscal distress from the Fiscal Distress Unit to the Fiscal Services and Support Unit. The unit began providing support to districts prior to a classification of fiscal distress. According to the testimony, the Fiscal Services and Support Unit is already providing many of the services mandated in the bill; the purpose of the bill is to expand the outreach to all districts. In addition, the bill provides support for districts exiting fiscal distress so that those districts would not fall into old spending practices and habits.

While Act 929 of 2019 mirrors Act 930 of 2017, Act 930 of 2017 allows for the waiver of certain statutes that are not allowed under Act 929 of 2019. Act 929 of 2019 allows the Commissioner to waive application of Arkansas law and corresponding SBOE rules with certain exceptions, including the Teacher Fair Dismissal Act of 1983 and the Public School Employee Fair Hearing Act. Act 930 of 2017 allows the SBOE to waive the application of those two acts.

Act 929 requires DESE to implement a system for reviewing the financial management practices of public school districts to determine the support needed in the districts. The system shall consider a school district's use of resources, financial accountability, and personnel systems and benefits management. Testimony indicated that this requirement was added to try to create situations where the best financial management practices could be in place.

In addition, Act 929 sets out requirements for general business managers. A general business manager must meet the minimum requirements established in DESE rules. The DESE rules must ensure minimum qualifications to support the implementation of best financial management practices for districts.

Act 929 also repealed the process for the SBOE to return a public school district to local control. Act 929 did not change the requirement that a school district may not remain in fiscal distress after the end of the fifth school year following the district's classification, unless the state board grants additional time due to external forces beyond the control of the district that prevented the district from removing itself from fiscal distress. This is similar to the requirements for districts in need of Level 5--Intensive support. If a district does not meet the criteria for exiting Level 5—Intensive support within 5 years after the assumption of authority, then the SBOE must annex, consolidate, or reconstitute the district. Under Act 930 of 2017, there is no provision to grant additional time.

EARLY WARNING

Under the early warning system, DESE is required to report to school district superintendents if DESE is aware that the school district has experienced two or more nonmaterial indicators of fiscal distress that DESE believes could put the district at risk without intervention. Superintendents are required to report the same information about their districts to DESE. Act 929 changed the required date for DESE and superintendents to report from August 31 to November 1. Act 929 also adds that the indicators of distress may be indicators listed in the statute or in DESE rules. Act 929 requires that if a district is determined to be experiencing fiscal distress at a nonmaterial level, the district must comply with all requirements of the state board in rules (including review of budget, reporting, and hiring and termination of staff), and receive written approval from DESE before incurring debt. Prior to Act 929, DESE could identify a district in early warning, but had no authority to require the district to comply with DESE recommendations.

Finally, Act 929 allows DESE to request that Arkansas Legislative Audit conduct an annual audit of a public school district determined to be experiencing fiscal distress at a nonmaterial level. According to testimony at the Senate Education Committee, an original draft of the bill that became Act 929 required that Legislative Audit conduct the annual audits of public school districts determined to be experiencing fiscal distress at a nonmaterial level. The bill was changed prior to introduction in committee at Legislative Audit's request. Legislative Audit had expressed concerns about staffing and whether its staff would be sufficient to conduct the increased number of audits. Legislative Audit does not conduct all school district audits. Under DESE rules, school districts must be audited annually. Under certain circumstances, districts may request that Legislative Audit conduct the audit, but otherwise, the school district board must select a private auditor.

IDENTIFICATION AND CLASSIFICATION

Act 929 of 2019 adds two violations for identifying and classifying a district in fiscal distress:

- Material failure to comply with Arkansas Code § 6-20-1913, which concerns the minimum qualifications for a general business manager
- Material failure to comply with reporting, debt approval, or other requirements placed on a public school district that has been returned to local control

Act 929 changes the date of notification; DESE must now provide required notice prior to June 30 (rather than March 30). However, DESE may identify a school district as being in fiscal distress at any time after June 30 if DESE discovers that a fiscal condition of the school district negatively impacts the continuation of educational services by the district.

POSSIBLE SANCTIONS AND CORRECTIVE ACTIONS

Act 929 added the following sanctions and corrective actions:

- Authorize an individual appointed to the school district to remove, replace, reassign, or suspend public school district personnel in accordance with state law
- Suspend on a temporary basis some or all of the powers and duties granted to the current public school district board of directors but allow the board of directors to continue to operate under the direction and approval of the Commissioner (SBOE defines the powers of the board of directors in this situation)
- Require reassignment of some or all of the staff of the district
- Require reorganization, closure, or dissolution of one or more of the district's schools

REMOVAL

Act 929 requires that the district must not have experienced any additional indicators of fiscal distress.

Act 929 imposes requirements for districts returned to local control or removed from fiscal distress, as well as requirements for DESE in those districts. DESE must monitor the fiscal operations of the district for three years, provide support to the district, and may impose reporting requirements on the district.

DISTRICTS CURRENTLY IN DISTRESS

Five districts are currently classified in fiscal distress: Dollarway, Earle, Pine Bluff, Marvell-Elaine, and Lee County. The five districts are discussed below, in the order they were classified as being in fiscal distress.

DOLLARWAY

DESE identified Dollarway as a district in fiscal distress on March 7, 2016. On April 14, 2016, the State Board classified the district as being in fiscal distress. The district was placed in state takeover in December 2015 for academic distress; that classification was changed to being a district in need of Level 5 support on July 13, 2017, to comply with Act 930 of 2017. SBOE removed the district's school board, reassigned the superintendent to her previous position as a School Improvement Specialist, and appointed a new superintendent.

DESE identified the Dollarway School District as being in fiscal distress due to declining balances and material audit findings. DESE noted at the State Board meeting when Dollarway was classified that the audit findings were some of the worst examples they had seen. Audit findings included overpayments to staff members, unauthorized payments on district credit cards, improper and untimely recording of receipts in APSCN, failure to reconcile gate admission fees for athletic events, failure to reconcile the district's operating bank account, failure to timely deposit checks, failure to document payroll liabilities, employees working without contracts, employee contracts that did not match the salary schedule, and numerous recording errors. Recordings errors included failure to maintain receipt books, receipt ranges not indicated on deposit slips, posting errors to incorrect accounts, and receipt numbers not indicated on deposit slips.

Dollarway did not contest the fiscal distress classification.

Dollarway was also previously on the early warning intervention list twice, beginning in February 2011 and March 2012.

In Dollarway, DESE has assisted in making transparent policies and procedures, building capacity in federal program funding, and providing support to the superintendent.

EARLE

DESE identified the Earle School District as being in early warning on October 19, 2016, based on the district's early intervention checklist completed in July 2016. DESE identified Earle as a district in fiscal distress on August 31, 2017, based on an audit released June 30, 2017; the State Board classified Earle as a district in distress on October 12, 2017. The district did not appeal.

DESE identified Earle as a district in distress based on material audit exceptions or violations and an act or violation determined to jeopardize the fiscal integrity of the district. DESE's identification letter noted that this included failure to fully develop and implement adequate corrective actions for previously identified audit findings and deficiencies. Some of the items in the audit released June 30, 2017, included internal control weaknesses, purchase of gift cards without documentation, credit card purchases without documentation and approval (including hotels, supplies, meals, cell phone, vacuum cleaner, computer, and other items), overpayments to staff, payments to staff not consistent with the salary schedule, National School Lunch categorical funds used to pay ineligible salaries, travel reimbursements made without approval or documentation, bank fees related to insufficient funds, salary increases made without required Board approval, and fund balances being at a deficit in violation of Arkansas statutes.

The Commissioner exercised his power to place the district in state takeover on November 6, 2017, removing and replacing the district's superintendent and removing the district's school board. The district remains in fiscal distress and under state control. In addition, the State Board classified the district as being in need of Level 5 support for academic distress, at the request of the district and DESE.

Earle has been identified as being in fiscal distress three previous times and actually classified as being in fiscal distress two previous times. Earle was classified in fiscal distress in 1996 and 1997 under the first version of the fiscal distress program. DESE identified Earle as being in fiscal distress in 2004, but Earle appealed. The State Board granted the appeal on June 14, 2004, and the district was not classified as being in fiscal distress. Finally, the State Board classified Earle as a district in fiscal distress on May 16, 2011; the State Board removed the district from fiscal distress on April 9, 2012.

In the most recent fiscal distress classification of Earle, DESE has assisted in establishing appropriate processes for requisitions, minimizing new debt, becoming current with bills, training staff, and maintaining the day-to-day finances of the district.

PINE BLUFF

Pine Bluff was originally classified in fiscal distress on December 2, 1998, under the original fiscal distress statute. Pine Bluff was removed from fiscal distress on May 8, 2000.

DESE placed Pine Bluff in early warning on November 7, 2014.

On August 8, 2018, DESE identified Pine Bluff as a district in fiscal distress. The State Board of Education classified Pine Bluff as being in fiscal distress on September 13, 2018. The State Board also voted at that time to place the district in state takeover, removing the district's school board and superintendent and giving the Commissioner the authority of the board, the authority to appoint a new superintendent, and the authority to take other actions he deems appropriate. The district did not appeal the fiscal distress classification.

The reasons DESE identified the district as being in fiscal distress included declining fund balances (from approximately $6 million to approximately $3 million between June 2016 and August 2018), projections that the district would be in the red financially at the end of the school year, IRS penalties, late submissions to teacher retirement, two reports to the IRS not filed in 2017, and reductions in funding due to decreasing enrollment.

The district was in early intervention prior to DESE identifying the district as being in fiscal distress; however, the district did not adopt all of the DESE recommendations made during early intervention. At the time the district was in early warning, DESE did not have the authority to require districts to take suggestions made during early intervention. DESE indicated that this was one reason for identifying the district as being in fiscal distress; once the district is classified, DESE can require the district to follow DESE recommendations.

DESE indicated at the State Board meeting that the district's declining enrollment would not have put the district in danger of being in fiscal distress if the declining enrollment were the only factor. The district increased salaries, added positions, made non-necessary expenditures, and incurred significant expenses in maintaining safe, warm, and dry facilities. DESE indicated that the district could have managed its declining enrollment in a way that would not have put it in danger of being in fiscal distress. At the time of classification, the district was spending into fund balances each month to meet its monthly expenditures.

On Thursday, November 8, 2018, the State Board classified Pine Bluff as a district in need of Level 5 Intensive Support.

Changes in Pine Bluff include a staff reduction-in-force, identifying unused and underutilized buildings and putting those up for sale, creating a fiscal distress plan, and using fiscal year 2019 numbers to create a budget for fiscal year 2020.

MARVELL-ELAINE

DESE identified the Marvell-Elaine School District in fiscal distress on January 29, 2019. The district did not appeal the fiscal distress identification. The State Board of Education classified the district in distress on April 11, 2019.

DESE testimony at the SBOE meeting indicated that there were two reasons for identification. The first reason was a declining fund balance determined to jeopardize the fiscal integrity of the district. The district's fund balances have declined $1.6 million since 2016. The other condition was the conduct of the district's business manager, which was deemed to have a detrimental negative impact on the continuation of educational services by the school district. Between July 1, 2014, and December 31, 2018, the district's business manager issued 90 unauthorized checks to herself totaling $471,666. The business manager's employment with the district was terminated on January 17, 2019. Furthermore, the district was assessed a penalty for failing to make timely tax deposits.

The district is sending complete bank statements to DESE so DESE can monitor those statements. The statements are emailed to eliminate the possibility of alterations to the statements. The district is currently relying on outside services to conduct payroll and debt requests. Finally, the district requested Level 4 academic support. The Public School Accountability Office is working with the district to provide that support.

LEE COUNTY

DESE identified Lee County as a district in early warning on March 14, 2012. DESE identified Lee County as a district in fiscal distress on March 28, 2014. On April 10, 2014, Lee County was placed under state takeover for academic distress; the State Board of Education opted to remove the school board but not the superintendent. The State Board classified the district in fiscal distress on May 8, 2014; the district did not appeal. The district was identified as being in fiscal distress for declining fund balances between 2012 and 2013 (from $2.6 million in unrestricted fund balances in 2012 to $239,000 in 2013). When DESE investigated, it determined that the fund balances in 2012 were actually much lower; the district's bookkeeper was making entries into accounts and reversing them, inflating the balances.

The State Board voted to remove the district from academic distress on February 12, 2015; DESE indicated that the district had met the requirements to be removed from academic distress. The State Board voted to remove the district from state takeover pending the training and election of the school board on March 12, 2015, based on the district's having addressed its academic distress and accreditation issues. The SBOE noted that the district would continue to be in fiscal distress and receive support from DESE. The district returned to local control on September 1, 2015. The State Board voted to remove the district from fiscal distress on September 14, 2017.

On October 10, 2017, DESE identified Lee County School District as being in early intervention. DESE identified the district as being in fiscal distress on April 1, 2019. DESE's reasons for identifying the district were a declining fund balance determined to jeopardize the fiscal integrity of the school district and material state or federal audit exceptions or violations. Some of the audit exceptions or violations include general ledger cash balance understated by $69,770 (repeat finding), bank reconciliation $2,811 less then general ledger balance (repeat finding), significant corrections to cash balance and bank reconciliation (repeat finding), failure to make timely and accurate tax deposits (repeat finding), IRS penalties of $54,558, multiple payroll discrepancies (repeat finding), lack of proper controls in place for both employee health insurance benefits and employee retirement benefits, internal control weaknesses, and unallowable Title I expenditures. The State Board voted to classify the district in fiscal distress on May 9, 2019. The district did not appeal. The district was already under state takeover for being in probationary status for accreditation; the State Board placed the district in state takeover on March 25, 2019, removing the superintendent and school board.

Changes in Lee County since the fiscal distress classification include the creation of a fiscal distress plan, creation of a preliminary budget, a new salary schedule, and starting a staff reduction in force.

CHARACTERISTICS OF DISTRICTS IN DISTRESS

This section examines characteristics of districts in distress in the past several years. The table below shows the districts that were in distress at any point in during the school year (August 1 to the following July 31). Since districts may move in and out of distress at any point during a school year, districts in distress in a school year may not have been in distress the entire school year.

District in Distress at Any Point During the School Year (August 1 to July 31)	2013-2014	2014-2015	2015-2016	2016-2017	2017-2018	2018-2019
Helena West Helena	X	X	X			
Hermitage	X					
Alpena	X					
Brinkley	X					
Hartford	X					
Mineral Springs	X	X				
Western Yell County	X					
Hughes	X	X				
Pulaski County	X	X	X			
Hector	X	X	X			
Lee County	X	X	X	X	X	
Guy-Perkins		X	X	X		
Maynard		X	X	X	X	
Yellville-Summit		X	X	X		
Dollarway			X	X	X	X
Earle					X	X
Pine Bluff						X
Lee County						X
Marvell-Elaine						X

POVERTY

This report uses the percentage of students eligible for free and reduced price lunch as a proxy for examining the relationship between fiscal distress and districts' poverty.

The table below classifies districts as low poverty (less than 70% of students eligible for free and reduced price lunch), medium poverty (between 70% and 90% of students eligible for free and reduced price lunch), and high poverty (more than 90% of students eligible for free and reduced price lunch).

All Districts Classified as Low, Medium, or High Poverty						
Poverty	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Low Poverty (<70%)	140	140	123	118	115	116
Medium Poverty (70%-<90%)	89	87	103	109	110	110
High Poverty (90%+)	9	9	8	8	10	9
Districts in Distress at Any Point in the School Year Classified as Low, Medium, or High Poverty						
Poverty	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Low Poverty (<70%)	2	3	1	0	0	0
Medium Poverty (70%-<90%)	7	4	4	4	3	1
High Poverty (90%+)	2	2	3	1	2	4

It is important to note here 2018-19 is the first year in which the number of high poverty districts exceeded the number of medium poverty districts in fiscal distress. Since 2013-14, more medium poverty districts have been in distress than high or low poverty districts until the 2018-19 school year.

AVERAGE DAILY MEMBERSHIP

This report uses the Average Daily Membership (ADM) to examine the relationship between fiscal distress and district size. ADM is a calculation representing the total number of students in a district.

All Districts Classified as Small, Medium, or Large						
District Size	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Small (750 or Less)	83	80	79	81	82	84
Medium (751-5,000)	138	139	140	138	137	135
Large (5,001+)	15	15	16	16	16	16
Districts in Distress at Any Point in the School Year Classified as Small, Medium, or Large						
District Size	**2013-14**	**2014-15**	**2015-16**	**2016-17**	**2017-18**	**2018-19**
Small (750 or Less)	8	6	4	3	3	3
Medium (751-5,000)	2	2	3	2	1	2
Large (5,001+)	1	1	1	0	0	0

This table shows that the number of small districts in distress is consistently higher than the number of medium districts in distress. Similarly, the number of medium districts is consistently higher than the number of large districts in distress.

While the number of small districts in distress is higher than the number of large or medium districts in distress, it is still a small percentage of the total number of small districts. In the 2018-19 school year, only three small districts were classified in fiscal distress at any point during the school year, 3.5% of the total number of small districts that year (84). For 2013-14, the recent year with the highest number of small districts in distress, there were eight small districts classified in fiscal distress, which was 9.6% of the 83 small districts that year. In addition, the two districts that have spent the longest amount of time in fiscal distress since Act 1467 of 2003 are Pulaski County (a large district) and Helena-West Helena (a medium district).

APPENDIX: EARLY WARNING CHECKLIST JULY 2019

Arkansas Department of Education

Fiscal Distress Early Intervention Checklist

Must be returned to Fiscal Services and Support by July 31, 2019

For the 2018-2019 school year, has the district experienced any of the following?

1. Paid penalties, interest, or late fees on tax deposits and/or vendors within the past year?

   Yes_______No________

2. Addressed and corrected all audit findings from the most recent audit?

   Yes_______No________

3. Received a cash flow loan or entered into a Line of Credit agreement in the past **two** years?

   Yes_______No_______

4. A declining balance that could threaten the fiscal integrity of the school district?

   Yes_______No________

5. Capital outlay expenditures paid from the district's balance?

   Yes_______No________

Any act or violation determined to jeopardize the fiscal integrity of a school district, including, but not limited to:

6. Failure to properly maintain school facilities;

   Yes_______No________

7. Violation of local, state, or federal fire, health, or safety code provisions or law;

   Yes_______No________

8. Violation of local, state, or federal construction code provisions or law;

   Yes_______No________

9. State or federal audit exceptions or violations;

   Yes_______No________

10. Failure to provide timely and accurate legally required financial reports to the department, the Division of Legislative Audit, the General Assembly, or the Internal Revenue Service; **Yes___No___**

11. Insufficient funds to cover payroll, salary, employment benefits, or legal tax obligations;

    Yes_______No________

12. Failure to meet legally binding minimum teacher salary schedule obligations;
    Yes_______No________

13. Failure to comply with state law governing purchasing or bid requirements;
    Yes_______No________

14. Default on any school district debt obligation;
    Yes________No________

15. Material discrepancies between budgeted and actual school district expenditures;
    (such as variance of unrestricted fund balance 2018-2019 budget to 2018-2019 actual)
    Yes________No________

16. Failure to comply with audit requirements; or
    Yes________No________

17. Failure to comply with rules concerning general business manager qualifications.
    Yes_______No________

18. Failure to comply with any provision of the Arkansas Code that specifically places a school district in fiscal distress based on non-compliance.

    Yes________No________

19. What is the average number of days between the receipt of the bank statements and reconciliation with APSCN reports?

    __________Days

20. Any other fiscal condition of a school district deemed to have a detrimental negative impact on the continuation of educational services by that school district. **Yes_No________**

21. Has the school district experienced two (2) or more indicators of fiscal distress in one (1) school year that the superintendent deems to be at a nonmaterial level, but that without intervention could place the district in fiscal distress?
    Yes________No________

____
School District

____________________________________ ____________________
Superintendent Signature Date

Please return to:

Arkansas Department of Education
Fiscal Services and Support
Attention – Cindy Smith
Four Capitol Mall, Rm. 105-C
Little Rock, AR 72201
OR
Email: ade.fiscaldistress@arkansas.gov
SUBJECT: Early Intervention Checklist/District Name