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DISTRESSED UNIT APPEALS BOARD NON-BINDING REVIEW OF MT. VERNON COMMUNITY SCHOOL CORPORATION'S FINANCIAL CONDITION AND OPERATING PRACTICES

Under IC 5-1-5-2.5(d), certain eligible school corporations may issue refunding bonds to refund a percentage of their outstanding bonds to obtain an annual savings to their debt service funds that can be transferred from those funds to the school corporations' capital projects funds, transportation funds, or school bus replacement funds.

A school corporation that meets the requirements of IC 5-1-5-2.5(d)(3)(B) and issues refunding bonds must report information concerning the refunding to the distressed unit appeals board. The law does not require the board's approval of the eligible school's refunding. However, the board shall make a non-binding review with recommendations regarding the school's financial condition and operating practices.

FACTS

1. On June 15, 2012, the distressed unit appeals board (DUAB) received a petition from the Mt. Vernon Community School Corporation (Mt. Vernon) for a non-binding review regarding the school's financial condition and operating practices.

2. Mt. Vernon issued refunding bonds in June 2012, extending debt payments by ten years through 2036 and incurring additional expenses totaling \$39.37 million. Governing statutes allow certain eligible school corporations, including Mt. Vernon, to issue refunding bonds without DUAB approval.

3. The DUAB scheduled a public hearing for September 20, 2012 to hear testimony from Mt. Vernon regarding their debt restructuring, as well as their financial condition and operating practices. On August 16, 2012, notice of the hearing was sent to Jane Herndon, bond counsel for the school corporation. Notice of the hearing was posted on the DUAB website on September 13, 2012 and outside the meeting room on September 17, 2012.

4. On September 18, 2012, the DUAB received presentation materials from Mt. Vernon for the public hearing.

5. On September 20, 2012, the DUAB conducted a public hearing where it heard testimony from representatives of Mt. Vernon, including Superintendent William J. Riggs and Business Manager

Daniel Kramer. Jane Herndon, Mt. Vernon's bond counsel with Ice Miller LLP, also answered questions from the board regarding the school's debt restructuring.

6. On October 1, 2012, the DUAB sent follow-up questions to Mt. Vernon seeking additional information and clarification on comments made during its presentation at the September 20 hearing.

7. The DUAB scheduled a public hearing for November 8, 2012 to adopt recommendations regarding Mt. Vernon's financial condition and operating practices. On October 10, 2012, notice of the hearing was sent to Superintendent Riggs and Jane Herndon. Notice of the hearing was posted on the DUAB website on October 12, 2012 and at the principal office of the Office of Management and Budget on November 2, 2012.

8. On October 15, 2012, Mt. Vernon responded to the DUAB's October 1 letter.

9. On November 8, 2012, the DUAB conducted a public hearing where it adopted recommendations regarding Mt. Vernon's financial condition and operating practices by a vote of 5-0.

RECOMMENDATIONS

Indiana law authorizes certain eligible school corporations to refund bonds without obtaining DUAB approval. Under this authority, Mt. Vernon refunded a portion of its bonds without going through the petition and remonstrance process requirements and referendum requirements that would otherwise apply. While the debt restructuring may provide some annual operating relief, a critical deficit balance in the general fund remains without a clear course of action for its elimination. Therefore, pursuant to IC 5-1-5-2.5(j), the DUAB conducts this non-binding review and makes the following recommendations to Mt. Vernon.

1. Materials submitted by Mt. Vernon to the DUAB on October 15th indicate that the school corporation is projecting a general fund deficit of $4,779,356 at the end of 2012. Mt. Vernon sought an operating referendum on the November 6, 2012 ballot that would have raised approximately $650,000 per year for three years. However, voters defeated the referendum for a second time (a larger levy was requested in 2010). The referendum failures underscore the urgency of enacting cost savings measures. Mt. Vernon has also indicated it intends to request a state rainy day fund loan from the DUAB for a maximum amount of $3,393,500. The state loan will not resolve the school corporation's general fund deficit. Therefore, the DUAB recommends that Mt. Vernon aggressively pursue further ways to balance its budget while protecting classroom dollars. The documentation of such efforts and expected results will be necessary in the evaluation of any rainy day fund loan application.

2. Materials submitted by Mt. Vernon to the DUAB on October 15th show that the school corporation increased spending (general fund and rainy day fund) by nearly 10% between 2008 and 2011, from $20,986,098 to $22,976,934. These increases occurred almost entirely after the passage of property tax reform. Mt. Vernon has not taken the steps necessary to bring spending in line with revenues, instead delaying decisions and looking primarily to increase revenues rather than decrease spending. It is imperative that Mt. Vernon embrace a much greater sense of urgency with respect to reducing expenditures.

3. Materials submitted by Mt. Vernon to the DUAB on October 15th show that the school corporation's preliminary 2012 average daily membership (ADM) is 3,393.5. This is a decrease from Mt. Vernon's 2011 ADM, which was 3,434. The school corporation stated in its June 15th petition to the DUAB that 2012 ADM was projected to increase. Mt. Vernon's ADM has been decreasing since the 2009-2010 school year. Since ADM carries significant fiscal ramifications, the DUAB recommends that Mt. Vernon reevaluate how it is projecting ADM and enrollment figures to allow for more accurate planning. Clearly, less optimistic assumptions about future ADM levels are required and will necessitate more aggressive actions with respect to cost savings measures.

4. Materials submitted by Mt. Vernon to the DUAB on June 15th show that the school corporation's cash balances have been almost entirely depleted due to spending at a greater level than revenues. Cash balances as of 12/31/2011 were $2.7 million. Expenditures have exceeded revenue since 2009 and are on track to do so again in 2012. The DUAB strongly recommends that Mt. Vernon take steps to operate within the dollars the school corporation is receiving. Achieving structural balance is an important first step in putting Mt. Vernon on a path to fiscal stability.

5. Materials submitted by Mt. Vernon to the DUAB on October 15th show that the school corporation is projected to close CY 2012 with minimal total cash balances (across all funds). Moreover, Mt. Vernon projects total cash balances will be in the red at the close of CY 2013. Pursuing a referendum as well as a rainy day fund loan from the State of Indiana are not sufficient. Again, Mt. Vernon needs to aggressively pursue cost savings measures – both one-time and recurring – to put the school corporation on more solid fiscal footing.

6. Materials submitted by Mt. Vernon to the DUAB on June 15th show that the school corporation continues to have $1 premiums for many of its employees with respect to health, vision, dental, life, and long term disability benefits. The school corporation incurred benefit costs of more than $3.6 million in 2011 for health, dental, vision, life, long term disability, and a 403(b). Mt. Vernon's average annual cost per employee for health care was $13,973 for 2011, or 38% above the state's average annual cost per employee. The DUAB recommends that Mt. Vernon join the

state's health plan to experience immediate and significant savings. Alternatively, Mt. Vernon could join a consortium with other school corporations, but only if the savings would exceed those achieved by joining the state's health plan. In addition to making significant changes to the health care plan, the DUAB recommends Mt. Vernon revisit other benefits to determine if they are absolutely essential, or if they can be scaled back or eliminated to reduce the burden they are placing on the budget. It is clear that Mt. Vernon could easily save in excess of $1 million, or at least half of the amount accrued from the restructuring that has already occurred, by simply bringing benefits in-line with those offered by most other school corporations.

7. Materials submitted by Mt. Vernon to the DUAB on June 15th show that the school corporation froze salaries and eliminated salary increments in 2010, 2011, and 2012. The DUAB recommends that Mt. Vernon continue the working relationship it has with its teachers association so that any necessary future negotiations to amend the salary and increment schedules are successful in addressing the school corporation's financial needs.

8. Materials submitted by Mt. Vernon to the DUAB on October 15th show that the school corporation considered outsourcing custodian services and transportation services but chose instead to eliminate positions and make salary and benefit cuts. The DUAB recommends that Mt. Vernon continue analyzing other services that can be outsourced or delivered under a shared services model with other neighboring school corporations or political subdivisions. Bids should be put out for similar levels of services currently being provided by the school corporation in order to make an appropriate comparison before rejecting any proposals.

9. Materials submitted by Mt. Vernon to the DUAB on October 15th documented the bond yield on the two series of bonds sold as part of the restructuring program. The yield on the 2012 bonds was 4.724%. The yield on the 2012B Bonds, which closed approximately two weeks later and with a shorter final maturity, sold at a bond yield of 5.409%, a significant variance to the first series and market conditions. In addition, the underwriting fee was approximately $100,000 higher than market averages. While it is an additional up-front cost, DUAB recommends Mt. Vernon consider the use of an independent financial advisor for any future financings to ensure the long-term financing costs are as close to market as possible.

Dated this 8th day of November, 2012.

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DISTRESSED UNIT APPEALS BOARD

A M Horst

Adam M. Horst, Chairman