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Can Our Community “Afford” this Bond Issue for Our School? Proposed Factors for Determining Affordability of School Building Projects

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Proposed Factors for Determining Affordability of School Building Projects

Each year various Indiana communities are asked to fund millions upon millions of dollars for public school building projects. In 2005, the most recent reported year, the Department of Local Government Finance, the state agency authorized to approve or disapprove school corporation proposals to construct new schools or to remodel existing schools, approved \$1.3 billion in school construction projects.¹ In that same year payments by Indiana taxpayers on construction debt consumed more than \$777 million in property tax revenue.²

Recently the Fort Wayne Community Schools (FWCS) attempted to add another \$500 million to the public debt.³ The taxpayers remonstrated and soundly defeated the proposed building project by more than a three to one margin.⁴ Although the margin of defeat was unusual, it was not unusual that a school district would lose a remonstrance. Less than 50% of the remonstrances in Indiana are won by taxpayers.⁵ Other than the large amount asked for by FWCS, there was nothing unusual about the debate concerning the building program or the results of the remonstrance.

The remonstrators clamored throughout the petition process that the community couldn't afford the half billion dollar building program. Just as vociferously, the supporters of the building program retorted that the community could afford it and that it was past time for the renovation of many of the buildings. As usual, both sides exhibited a tendency to use emotional rhetoric with scant supporting evidence of affordability. In other words, the debate was long on opinion and short on facts.

Bond Ratings and Rating Criteria. In 2005 the three bond rating agencies, Standard & Poor Corporation, Moody's Investors Service, and Fitch IBCA rated \$144.6 billion in general obligation bonds and \$264.5 billion in revenue debt.⁶ In assigning a rating, the agencies assess a school district's ability to pay the principal and interest on debt by evaluating its economic base, financial condition and practices, certain debt factors, governance and planning, and whether the state has an oversight of local government's issuance of debt and financial management practices.⁷ Hildreth & Miller (2002) stated that bond rating agencies typically will look at four main factors in assessing the credit quality of the school district which issues debt: (1) the economic base; (2) financial results; (3) debt levels; and (4) management capability.⁸ These four factors do not necessarily have equal weight.

A bond rating is an opinion of the creditworthiness of the school district with regard to specific bond issue. A rating evaluates a government entity's strength or weakness on factors that bear on the school district's ability and willingness to make timely principal and interest payments on the debt.⁹ The lower the bond ratings the higher the interest cost.

Standard and Poor bases an issuer's rating for long-term debt on three basic factors: (1) the likelihood of the government entity's meeting its financial commitment under the debt contract; (2) the nature and provisions of the debt contract, i.e. the security pledged and other protections afforded to investors; and (3) protections available to investors under laws that authorize and limit local debt and/or provide for its repayment.¹⁰

A debt rating also takes into account credit support, if any, from bond insurance or other forms of financial guarantee for debt. Bond insurance guarantees to investors debt service payments and is now widely used in the debt market by school districts. Bond insurance raises a rating of the issuer to the triple-A rating of the insurance company.¹¹

According to Vogt (2004), ratings of general obligation bonds of local government entities are based on an assessment of the issuer's general creditworthiness. He classifies the criteria for rating general obligation bonds into four categories:

1. *Local and regional economy conditions* - Size, wealth, growth or change, diversity, stability, infrastructure and facilities, and policies related to sustainable growth or progress.
2. *Condition of local government finances* - Growth or change in revenues and spending, fund balance and reserves, budget practices, accounting and financial reporting, tax and revenue administration, investment practices, and other factors.
3. *The amount of debt burden* - Net debt per capita and as a percentage of tax or market valuation of real property, annual debt service on net debt in relation to general fund and other governmental fund spending, net debt in relation to personal income, pay-down pace for long-term net debt, and net debt of overlapping and underlying jurisdictions.
4. *Governance and planning considerations* - Coherence in local governmental structure, ability of local elected officials to work together and reach decisions, management, and multiyear planning.¹²

School building corporation lease ratings are based on the essentiality of the school building financed with the lease and pledged to secure the debt. The more essential the building is, the less likely is the school district lessee to stop making payments on the debt and risk loss of the building.¹³

The Question of Affordability. FWCS was assured by its financial consultants that it would not incur any excessive interest premium costs with the proposed bond issue. The consultants advised that there would be no penalty exacted by the market because of the size of the massive bond issue. Proponents used this as a marker of whether the community could afford the bond issue. The fact of whether the bond market will extract a higher premium interest cost with the school district's bond issue may indeed be one small indicator as to whether the community can afford it.

However, this particular criterion is not especially helpful in determining community affordability for two reasons. First, it only looks at the probability of repayment of the principal plus interest *from the perspective of the purchasers of the bonds*. It does not deal directly with the issue of whether the community can afford it. Secondly, Indiana has a statute that guarantees the payment of the bond issue if the school district defaults.¹⁴ This statute requires the state treasurer to make the principal and interest payments that were not paid but due on the bonds, and to reduce the school district's revenues that it receives from the state, in order to pay for the bond payments in default. Thus, the bondholders are guaranteed by statute that they will be paid, reducing their risk to near zero. Therefore, there is no need for the bond market to extract a premium from a school district that might not be able to afford a particular bond issue. It is possible to have a situation that the bondholders get paid, but the school district has insufficient funds to make payroll for its teachers. Certainly, in that event it would appear the community could not afford the bond issue. Indiana school boards and taxpayers have been lulled into a false sense of security by this statute, thinking that if the bond market does not add a premium to the interest cost that the community can afford it.

The supporters in the FWCS case were buttressed with the argument that the Yellow Ribbon Panel¹⁵ looked at the needs of FWCS and the ability of the FWCS to fund the project and concluded that the needs existed for a half-billion dollar building project and proclaimed that the community could afford assumption of a half-billion dollar debt load.

There was nothing unusual about a school board appointing a group of interested lay citizens to make a recommendation to the school board on the need for a building program and whether the community can afford it. But that is precisely the problem that exists throughout Indiana – that this is a common practice. Such panels are almost always appointed by the schools' administration and the school board with the unstated criteria that most of the panel is likely to support a building project. Such panels are normally anything but unbiased and neutral. Many community members are smart enough to realize that such bodies are simply the alter ego of the superintendent and school board and do not provide unbiased advice.

However, the purpose of this paper is not to bash citizen advisory committees. This paper is intended to deal with the issue of affordability of school district bond issues. Communities need more than just seat-of-the-pant guesses as to whether a particular community can afford a proposed bond issue. But seldom, if ever, does the conversation and debate surrounding a proposed bond issue elevate beyond opinions, misstatements of fact, and misrepresentations. Simply put, debates surrounding proposed Indiana school corporation bond issues are long on rhetoric and short on the facts.

The FWCS case study is just one recent example of the lack of facts concerning the issue of affordability. The Yellow Ribbon panel failed to report any factors or guidelines that they used to determine whether the Fort Wayne community could afford a half-billion dollar bond issue. It was simply the personal judgment of some members of the panel that the community could afford the proposed bond issue – a judgment

unsupported by any publicly revealed facts or data. But this is not unusual. This is standard operating procedure by so-called citizen advisory groups. But it does not have to be this way. There are quantitative data and measurements available to use in determining whether a community can afford a particular bond issue.

Affordability from the School District's Perspective. There is a growing concern among state policy makers that unrestrained debt may exceed politically acceptable or financially sustainable levels of debt.¹⁶ Affordability is one important and widely accepted element of state and local debt policy. However, in Indiana there is no general use of well-established measure of affordability and no clear standard for making normative judgments about what amount of debt is affordable for a specific school district.¹⁷ Brecher, Richwerger, and Van Wagner (2003) define "affordability" as keeping the cost of debt in line with a jurisdiction's economic and fiscal base. They argue that to qualify as an affordable bond issue, the repayment of debt (1) should not cause a government unit's tax rate to increase to uncompetitive levels in order to cover the debt service, and (2) should not require cutbacks in other public services that similarly cause the government unit to become uncompetitive with other areas.¹⁸ Thus, they would compare other governmental units to determine if the debt is "too much." They also argue that affordability should be assessed as a relationship between the amount of debt and the resources available for repayment. They present six analytic steps to assess affordability:

1. Identify the amount of relevant long-term debt.
2. Adjust the amount of long-term debt to include unfunded pension liabilities.
3. Identify the resources available to repay the debt.
4. Adjust the resources available to account for the division of responsibilities between the state and local government units.
5. Examine the distribution of the ratio of adjusted debt to adjusted resources in order to identify a point that is sufficiently "out of line" with most governmental units' practices that it constitutes the beginning of a danger zone.
6. Adjust the danger zone threshold to provide a safety margin for an economic downturn.¹⁹

There are a few informal guidelines that have been used by some Indiana school boards when determining whether the school district's taxpayers can afford a bond issue. Some financial consultants have advised school boards that the school corporation's debt as a percentage of assessed valuation of taxable real property should be generally be under 15% in growing communities. For static communities who are not growing, the ratio should generally be in the 10%-12% range. For communities who are in decline, the percentage varies based upon the individual demographic and economic factors in the community, but it is usually suggested that the debt ratio to assessed valuation be kept under 10%.²⁰

One can also look at the guidelines used by the Indiana Department of Local Government (the "Department"). Indiana school corporations must obtain Department

approval before they incur bond indebtedness or enter into a lease agreement for financing a school building project.²¹ Before the Department makes a determination on a building project's financing, the Department may, and almost always does so, seek the recommendation of the School Property Tax Control Board (the "Control Board").²² The Control Board, when requested by the Department, will hold a hearing on the requested financing and make a recommendation to the Department. The Department may approve, disapprove, or modify the recommendation regarding a proposed bond issue or lease rental agreement.²³

The Indiana General Assembly described in statute what factors the Department and Control Board are to use in their determination of whether to approve or disapprove a school building construction project. These factors are:

1. The current and proposed square footage of school building space per student.
2. Enrollment patterns within the school corporation.
3. The age and condition of the current school facilities.
4. The cost per square foot of the school building construction project.
5. The effect that completion of the school building construction project would have on the school corporation's tax rate.
6. Any other pertinent matter.²⁴

Note the absence of any express factor dealing specifically with the issue of community affordability. The Department and Control Board do state in their published guidelines that they "will also consider any other pending or potential debt service issues by other political subdivisions within the school district and the impact of those debt issues on the total tax rate" and that "(I)f the tax rate for a district is already overly burdensome, a project may be rejected with instructions to find a more cost-efficient alternative to addressing the school's needs."²⁵ The Department also states in its guidelines that "(A) school's annual financial performance report will also be considered in reviewing the district's overall financial condition and ability to fund long term operating costs."²⁶ Finally, the Department informs citizens in its guidelines that it will consider, among other things, "the support or resistance of the community."²⁷ The Department concludes its guidelines by stating: "(T)his guidance is not an exhaustive list of factors that will be examined and considered by the Department and Control Board."²⁸

Although the above guidance from the Department may be helpful in dealing with the issue of community affordability, it does not go far enough in describing the factors it will consider in making a determination that the project and its bond issue will be "overly burdensome." School Facility Guidelines²⁹ adopted by the Indiana State Board of Education use such vague phrases as "economically efficient system of school facilities;" "maximize the cost benefit;" "study...impact of the proposed building project;" "local community interest;" "effect on the community as a whole;" economic interest of the community;" and "ability to fund the project." None of these vague guidelines are especially helpful in determining the affordability of a specific bond issue.

In fact, there are no criteria specified precisely to answer this question. Thus, there is a need for further guidelines. The good news is that there are guidelines available. A search of other municipalities' and states' guidelines reveals some possibilities that could be added to the Department's and the State Board of Education's guidelines.

The creation of debt by a school district places an obligation on its taxpayers to repay the principal and interest on the bonds from property taxes. One measure of a community's wealth is its assessed valuation of its property. Thus, conventional debt studies usually include an indicator measuring debt as a proportion of the value of the property tax base. Another usual indicator is debt per capita. However, these indicators may not reveal the vulnerability of a community that is not economically diverse.

Hildreth and Miller (2002) argue that economic factors should be more closely connected to debt factors in assessing the vulnerability to a downgrade in bond rating. They argue for a broader analytical approach that measures and incorporates economic analysis as well as comparison with other localities as to whether a community can afford a certain debt level. They suggest an analysis of the economic base include its diversity. To not analyze the economic base of a community could lead to fiscal distress for the local government entity issuing the bonds, as well as the community itself.

There are several types of economic diversity that can be measured in a community.³⁰ Fundamental diversity of a large metropolitan area is one type. A community with many employers and a good mix of different types of industry and businesses will be looked upon favorably. The second type of diversity is where the local economy appears to be diverse, but is not in reality, as it is dependent, not on a single employer, but on a single core industry. An example is where the largest employers are all car manufacturers and their many suppliers. Property classifications are a third type of diversity. Property can be residential, commercial, industrial, offices, rental/residential, farmland, lots, or vacant buildings.

The financial condition of individual taxpayers and businesses affect the school corporation's borrowing capacity. Without a viable local economy, there is no real security for the debt, other than the Indiana statute, because there is an insufficient tax base to repay the debt. (Hildreth & Miller, 2002).

Moody's analysts have used the diversification of the economic base in determining their bond ratings.³¹ One important factor they use is the number of businesses and industrial concerns in the community. The larger the number the more diverse the community is. A common approach in measuring the economic base of a community is to measure the value of real estate owned by the top ten taxpayers as a percentage of the community's total assessed valuation. Thus, a community with say 90% of its assessed valuation in the hands of the top 10 property owners is more vulnerable to a downturn than one with only 10% of the assessed value held by the top ten property owners. Another way to measure diversification of the economic base is to compare all the firms in a particular industry to all the other industries in the community. If say 90% of the assessed value is in one industry, even though it may be spread around in many different companies, that community is more vulnerable than a community with only

10% of the assessed value in the largest and dominate industry. In summary, the revenue variables are less important than the base from which the revenues are taken (Hildreth & Miller, 2002).

Conventional debt affordability studies usually focus on debt levels and not economic concentration of business and industry. Hildreth and Miller (2002) argue that both debt levels and economic concentration are important factors in determining debt affordability of local communities.

Outstanding debt per capita and debt as a percentage of the tax value of property are two factors that can be considered in evaluating affordability. Another way of measuring affordability of debt levels is to compare the debt levels and concentration of business and industry with other communities of similar demographics, size, and wealth. National norms can also be used as a measure. Medians are particularly helpful to assess debt affordability. *Moody's Medians* can be used to provide measure four key local government debt levels: (1) net debt per capita for the single government entity; (2) combined net debt per capita for all the government entities in the taxing jurisdiction; (3) net debt to property tax value for the single jurisdiction; (4) and combined net debt to property tax value for all the government entities in the taxing jurisdiction. Groves and Valente (1994) propose that if net debt as a percentage of taxable value of property is greater than or equal to 20 percent over the past year or 50 percent over the amount four years earlier, the community cannot afford the bond issue.³²

In North Carolina, the Local Government Commission uses these criteria in deciding whether a local government unit can sell a general obligation bond: (1) the adequacy of the bond amount; (2) the bond's effect on the property tax rate; and (3) whether the bond can be marketed at a reasonable interest rate.³³

Predicting Fiscal Distress. An additional measure of community affordability of proposed debt is to determine the likelihood that the school might become a financially distressed school corporation.³⁴ It is not just the school district that should be the focus of concern as to the possibility that the proposed bond issue would jeopardize the financial health of the school district, but the entire community should also be the focus as well. The entire economic health of the community is at risk if only one governmental entity undertakes action that creates fiscal distress for the entire community.

The Advisory Commission on Intergovernmental Relations (ACIR) conducted one of the early studies that examined the fiscal health of local government entities. The ACIR identified six early warning signs of possible distress for local government entities which are:

1. an operating fund revenue to expenditure imbalance in which current expenses significantly exceed current revenues in at least one fiscal period;
2. a consistent pattern of current expenses exceeding current revenues by small amounts for several years;

3. an excess of current operating liabilities over current assets;
4. short-term operating loans outstanding at the conclusion of a fiscal year;
5. a high and rising rate of property tax delinquency; and
6. a sudden and substantial decrease in assessed values for unexpected reasons.³⁵

Kloha, Weissert, and Kleine (2005) offer a 10-point scale that predicts local government financial problems before they become serious. The scale uses nine indicators:

1. *population change* over two-year periods, with a benchmark standard of showing no population loss;
2. *real taxable value growth* (inflation-adjusted) over two-year periods, with a benchmark standard of showing any positive growth;
3. *large real taxable decrease of less than -0.04 in real growth* over a two-year period (more than one standard deviation below the average two-year growth rate for cities and villages);
4. *general fund expenditures as a percentage of current year's taxable value*, with a benchmark standard set at one-half standard deviation from the average of the type of governmental units compared;
5. *general fund operating deficit in the current year* with the benchmark standard set at one percent or less deficit;
6. *general fund operating deficit over the past two years*, with the benchmark standard set at no operating deficit;
7. *general fund balance as a proportion of general fund revenues*, with the benchmark standard set at one-half deviation below the average for the type of governmental units compared;
8. *negative balance in the current or previous year in either the general, special, capital, or debt service funds*, with the benchmark standard set at no negative balance in any of the four funds in either year;
9. *general long-term debt as a percentage of taxable value* with a benchmark standard of one deviation from the average debt-to-taxable value ratio of the type of government units compared.

In order to predict the impact of a school bond issue, and whether the issue will lead to financial distress, a study of the school district's financial condition is necessary. The most widely held concept of good financial condition is the ability of an organization to timely meet its financial obligations. If the organization can pay its obligations without incurring significant financial hardship it may be presumed that the organization is in sound financial condition.³⁶

Wang, Dennis, and Yuan Sen (2007)³⁷ developed and tested a measure of financial conditions of state governments. Their study used four dimensions of solvency associated with the concept of financial condition:

1. Cash solvency;

2. budgetary solvency;
3. long-run solvency; and
4. service-level solvency.

To measure cash solvency, they used three indicators: (1) the *cash ratio* (cash + cash equivalents + investments / current liabilities); (2) the *quick ratio* (cash + cash equivalents + investments + receivables / current liabilities); and (3) the *current ratio* (current assets / current liabilities).

To measure budget solvency, they used these two indicators: (1) the *operating ratio* (total revenues / total expenses); and (2) *surplus or deficit per capita* (total surpluses or deficits / population).

To measure long-term solvency, they used these three indicators: (1) *net asset ratio* (restricted and unrestricted net assets / total assets); (2) *long-term liability ratio* (long-term non-current liabilities / total assets); and (3) *long-term liability per capita* (long-term non-current liabilities / population).

To measure service solvency, they used two indicators: (1) *revenue per capita* (total revenues / population); and (2) *expenses per capita* (total expenses / population).

Measuring and Determining Debt Capacity. Denison, Hackbart & Moody (2006) define debt capacity as a state's ability to sustain debt in the long run (however they fail to define "the long run"). They suggest that in this context, it is the amount of debt that a state can afford.³⁸ They recant a variety of ways debt capacity can be measured for states as set out by various scholars. These measurements include: whether the debt places unacceptable or undue burdens on state services and the state's budget; debt per capita; total debt outstanding; debt relative to current revenues; debt ratios, limits, and burdens of similar governments; and debt service as a percent of current revenues.³⁹

The Government Finance Officers Association recommends that state and local government issuers of bonds analyze their debt capacities before they issue bonds.⁴⁰ Galgano (2001) informs that the same factors that bond rating agencies use when they evaluate a government entity's ability to repay its debt should be used as factors that local governments use to evaluate their own debt capacity. These factors measure demographic, wealth, and management factors, and include these indices:

1. *Ratio of total debt to fair market value of taxable property* (debt burden) which helps assess government entity's wealth;
2. *Ratio of total GO debt divided by the government entity's population base* (debt per capita), and if too high, may suggest that the entity may not be willing or able to pay debt service in future;
3. *Debt per capita divided by average personal income* (debt to income), which reflects the individual taxpayer's ability to pay taxes to service the debt;

4. *Debt service divided by general fund expenditures* (debt service as a percentage of general fund expenditures), which reveals the amount of expenditures used to pay debt service and shows budget flexibility;
5. *Top five taxpayers should not account for more than 25 percent of the tax base, and the largest taxpayer should not account for more than 10 percent* (tax base diversity), which diversity will allow the debt to be paid even if one or more of the largest employers fails to pay its taxes;
6. *Market value divided by population* (market value per capita), which can indicate the wealth of the community;
7. *Growth patterns of tax base* (historic rate of tax base growth), which can help indicate what the debt burden might be in the future;
8. *History of tax collections* (tax collections), which can help measure the citizens' ability to pay the debt service; and
9. *General fund ending balance divided by expenditures* (financial obligations), which indicates the government entity's ability and willingness to live within its means, and can also indicate the sufficiency of its reserves.⁴¹

The Institute of Government at the University of North Carolina at Chapel Hill has published local debt capacity guidelines.⁴² Determining how much debt a school district can afford to issue is an important step in the district's capital projects planning and overall fiscal management. A school district's debt capacity can be measured by assessing the school district's financial resources and revenues that will be available to pay the debt service on all its bond issues. This can be started by looking, according to Vogt (2004), at the government unit's current financial position, its prospects, and key debt ratios. Vogt argues that there are numerous ratios available for measuring local debt burden, but the most frequently used are: (1) net debt per capita; (2) net debt as a percentage of taxable or market valuation; and (3) annual debt service on net debt as a percentage of general fund revenues or spending, including any other operating funds that pay for government services, if any. Vogt defines net debt as debt that is paid from general revenues or taxes. This includes debt for holding corporation leases. It also can be described as the bonds, capital lease obligations, and other debt that is not self-supporting or self-liquidating and which must be paid from general revenues and taxes.

Vogt (2004) also states that there are other ratios for assessing net debt. He asserts that median family income, personal income, or per capita income for a community can measure a community's wealth and therefore ultimately the ability of citizens to pay debt service on net debt and support other local government spending. However, income data are not available for many medium and small jurisdictions.

The National Advisory Council on State and Local Budgeting recommends that a governmental entity should adopt a policy that sets forth the maximum amount of debt that should be outstanding at any one time.⁴³ This suggests that school districts would be well served by adopting a policy setting out the maximum amount of debt service that the school board would be willing to accept at any given time.

Examples of Debt Affordability Policies by Local Government. Mecklenburg County, North Carolina, adopted a debt policy concerning debt affordability, among other policy matters.⁴⁴ The adopted policy sets forth that the County will use an objective, analytical approach to determine the amount of debt to be considered for authorization and issuance. The county compares what it calls generally accepted standards of affordability to the current County values. These standards include:

1. *Debt per capita* – which measures the burden of debt placed on the size of the population supporting the debt and, according to the County, is widely used by analysts as a measure of an issuers’ ability to repay debt. The county set a range of \$3,500 to \$3,600 for the ceiling for debt per capita.
2. *Debt as percentage of assessed valuation* – this ratio measures debt level against the property tax base which generates the tax revenues that are the main source of debt repayment. The County targeted the ratio at 3.3% with a ceiling of 4.0%.
3. *Debt service as percentage of operational budget* – this ratio reflects the County’s budgetary flexibility to change spending and respond to economic downturns. The County targeted a ratio at 14% with a ceiling of 16%.
4. *Ten-year payout ratio* – a faster payout is considered to be a positive credit attribute according to the County. The County policy set a floor for its ten-year payment of 64.0%.
5. *Unreserved/undesignated general fund balance* – a cash balance in the general fund (operating fund) is always advisable for any organization to pay for emergency or unplanned expenditures. The County set a target range of unreserved general fund balance to general fund expenses at 12% to 14% and the target for undesignated fund balance at 8% of budgeted expenses.

Montgomery County, Maryland established a fiscal policy and set out its criteria for determining debt capacity for the County.⁴⁵ Maryland County declared its goal as to maintain its AAA rating and adopted the following guidelines to be used in deciding how much additional County general obligation debt may be issued in a six year period:

1. *Total debt*, both existing and proposed, should be kept at *about 1.5% of full market value of taxable real property* in the County.
2. *Required annual debt service expenditures* should be kept at *about 10% of the County’s total general fund operating budget*.
3. *Total debt outstanding* and annual amounts issued, when adjusted for inflation, should *not cause real debt per capita to rise significantly*.
4. The *rate of repayment* of bond principal should be kept at existing high levels and in the *60-75% range* during any ten-year period.

5. Total debt outstanding and annual amounts proposed should not cause the *ratio of per capita debt to per capita income* to rise significantly above its current level of about 3.5%.⁴⁶

Allegany County, Maryland, adopted a policy regarding affordability of debt.⁴⁷ The County stated that debt affordability can be determined by examining and deciding the maximum amount of debt that can be borrowed by the County. Two overall constraints were adopted by the County, to wit: (1) that the amount of debt per person will not exceed \$585, and (2) that the debt service payments should be kept at the current level of \$5 million per year as adjusted for inflation for the general fund. The County also adopted the use of three ratios to use in the determination of affordability of debt:

1. General fund debt service divided by general fund revenue shall not exceed 11.70%.
2. General fund debt service divided by general fund expenditures shall not exceed 13.50%.
3. Debt divided by the full property value shall not exceed 3.15%.

The Los Angeles Unified School District has also adopted a debt policy.⁴⁸ An overall limit on the total outstanding debt (the principal portion only) was set at 2.5% of the assessed valuation of the taxable property of the District (with tax and revenue anticipation notes and lease payment obligations in support of certificates of participation generally excluded). The policy sets forth four debt burden ratios that the District will consider in developing its debt issuance plans:

1. *Ratio of outstanding debt to assessed value* – the ratio is to be calculated for both direct debt (G.O.s) and combined direct debt (G.O.s and COPs) or overall debt burden, where G.O.s are general obligation bonds and COPs are certificates of participations.
2. *Ratio of outstanding debt per capita* – This computes outstanding debt divided by the population residing in the District. Ratios are required for both direct debt per capita and overall debt per capita.
3. *Ratio of annual lease debt service to general funds expenditures* – For this computation, annual lease debt service expenditures are divided by general funds (i.e. general and debt service funds) expenditures (excluding interfund transfers).
4. *Proportion of fixed-rate and variable-rate COPs issues* – The District must keep its variable rate exposure, to the extent not hedged or swapped to fixed rate, at or below 20% of the total principal of outstanding COPs or \$100 million, whichever is less.⁴⁹

The District policy also states that the determination of how much indebtedness the District should incur will be based on the impact of planned debt issuances on the long-term affordability of all outstanding debt. The affordability of the incurrence of debt is to be determined by calculating various debt ratios which would result after issuance of

the debt and analyzing the trends over time. The District's debt factors and its debt burden ratios are set forth in tables 1 and 2 below:

Table 1
Debt Factors

Debt Factor	Target	Ceiling
COP Debt Service Limit (gross)	2.0% of General Funds Expenses	2.5% of General Funds Expenses
COP Gross Debt Service Cap	\$105 Million	\$105 Million

Table 2
Debt Burden Ratios

Debt Burden Ratio	Benchmark
Direct Debt to Assessed Value	(1) Moody's Median for Aa Rated School Districts with Student Population Above 200,000 (2) Standard & Poor's Mean for AA Rated School Districts with Student Population Above 150,000
Overall Debt to Assessed Value	(1) Moody's Median for Aa Rated School Districts with Student Population Above 200,000 (2) Standard & Poor's Mean for AA Rated School Districts with Student Population Above 150,000
Direct Debt Per Capita	(1) Standard & poor's Median for AA Rated School Districts with Student Population Above 150,000 (2) Standard & poor's Mean for AA Rated School Districts with Student Population Above 150,000
Overall Debt Per Capita	(1) Standard & Poor's Median for AA Rated School Districts with Student Population Above 150,000 (2) Standard & Poor's Mean for AA Rated School Districts with Student Population Above 150,000

“Direct Debt” includes all debt that is repaid from the general fund or from any tax revenues deposited into special funds not supporting revenue bonds. “Overall Debt” includes any debt that is paid from general tax revenues and special assessments by residents in the District. This includes debt issued by other agencies whose taxing boundaries overlap the District, but excludes revenue bonds.

A final example of a debt affordability policy is Texas. That state conducted a debt affordability study.⁵⁰ This was the first debt affordability study for the state of Texas which had traditionally used a decentralized approach to debt authorization and issuance. The study provided policymakers with a broad perspective on Texas's debt position and will serve as a tool for evaluating the fiscal impact of bond financing options. The Texas study proclaimed a number of benefits and goals of using a debt affordability study:

1. Provides a big-picture view of the state's debt position;

2. Matches available debt funding with prioritized capital needs, by providing a tool to integrate debt management in the capital planning process;
3. Establishes a systemic approach to debt management;
4. Helps centralize debt management and authorization decisions;
5. Helps assess the effect of individual or a group of new debt authorizations on the state's debt burden;
6. Evaluates the effect of fluctuating revenues on the state's ability to meet existing debt service obligations and to issue new debt;
7. Ensures sufficient cash balances and reserves;
8. Protects and enhances the state's bond rating and outlook;
9. Helps achieve the lowest cost financing for taxpayers; and
10. Assists in maximizing resources for debt financing.⁵¹

The Texas study defined debt affordability as an integrated approach that helps analyze and manage state debt by factoring in historical debt use, financial and economic resources of the state, and long-term goals for capital needs. The debt affordability study presents the state's current debt burden with an overview of the state's historical and current debt. The authors of the study affirmed that one key component of debt affordability is determining the state's additional debt capacity, which they said was to be measured in terms of annual debt service capacity.⁵² To determine debt affordability, Texas used five key ratios:

1. *Not self-supporting debt service as a percentage of unrestricted revenues* - This ratio helps determine additional debt service capacity for not self-supporting debt. The study used a guideline of a two percent target and a three percent cap. The Texas constitution prevents debt issuance to no more than five percent of unrestricted general revenue funds.
2. *Not self-supporting debt to personal income* - The capability of the state's populace to absorb the financial debt is determined by the ratio. Standard & Poor's considers a ratio of 0 percent to 3 percent to be a low debt burden. Texas calculates that at current and projected debt and personal income levels, over a five-year period this ratio ranges from a high of 0.34 percent in fiscal year 2007 to a low of 0.19 percent in fiscal year 2011. When compared to a peer group of the ten most populous states Texas has the lowest debt to personal income ratio.
3. *Not self-supporting debt per capita* - This ratio also serves an important role in rating a state's bond issues by the bond rating agencies. Under \$1,000 of state debt per capita is considered low by Standard & Poor's. Over a five year period, Texas calculates a range for this ratio of \$119.24 in fiscal year 2007 to \$80.33 in fiscal year 2011. Texas has the lowest debt per capita in the ten-state peer group. However, the report states that Texas's low state debt burden is due to having a higher local government debt burden. Thus, state elected officials can manipulate the state into appearing to be a low debt burden state by simply passing on the debt

burden to local governments and requiring them to issue bonds for needs that some states do on a statewide basis.

4. *Rate of debt to retirement* – This ratio highlights the state’s progress on retiring debt in a timely fashion. The rapidity at which long-term debt obligations are repaid measures the extent to which repayments create capacity for future debt issuance. For a 20-year bond, the bond rating agencies expect that 25 percent of the bond will be retired at five years and that 50 percent of the bond principal will be paid off by 10 years. This is considered the average ratio by the bond rating agencies. Texas’s current rate of retirement for not self-supporting debt is a 78.29 percent principal payout in a ten year period, which is a high rate of retirement.
5. *Not self-supporting debt service as a percentage of budgeted general revenue* – This ratio shows how much of budgeted (or expended for complete fiscal years) general revenues are dedicated to long-term debt financing. This is a reflection of the state’s financial flexibility. This ratio is similar to the first ratio, but is more restricted because the pool of available general revenue in this ratio is limited to budgeted general revenue, which is generally less than all unrestricted general revenue that is available for debt service. The higher the percentage of the budget reserved for debt service, the less financial flexibility the state has for responding to economic slowdowns, unexpected expenses, or changes in budget priorities for operation or fixed capital outlay expenditures. Since fiscal year 1996, Texas has had a not self-supporting debt service commitment of less than 1.5 percent of expended general revenues.⁵³

Analysis and Recommendation for Adoption of Affordability Guidelines. So what does all of the above mean? As evidenced above, Indiana has few meaningful guidelines on the issue of the affordability of a school district’s debt. The state of Indiana has essentially passed off the burden to determine local affordability of school bond issues to the local school boards and their taxpayers. What isn’t found is a meaningful use by any level of government, state or local, of quantitative measures to help determine affordability of school district bond issues. State guidelines in Indiana such as “the effect...the project would have on the school corporation’s tax rate”; and “if the tax rate for a district is already overly burdensome”; and “the support or resistance of the community” are wholly inadequate measures to determine whether a community can afford a particular bond issue. It is important for the analysis of affordability to go far beyond just glancing at tax rates and letters in support or against the issuance of proposed debt. A more thorough and precise quantitative analysis will help taxpayers make better informed judgments about the affordability of school bond issues.

Affordability in Indiana has largely been equated to whether it is financially feasible for the *school district* to issue its bonds. The current guidelines are not adequate to measure whether the *citizens* of a community can afford a bond issue. The current guidelines tend to look at the affordability from only the school district perspective. But what about individual homeowners of the community? What about the retiree who lives on social security alone and is trying to hold onto his or her house in old age? What about

the factory worker who just became unemployed when his factory closed its doors and who is rapidly falling behind on his or her mortgage payments? What about the white collar worker who has lost his or her job to a company located in a foreign country and is struggling not only to pay the house payments but to feed the children? What about the professional worker who is laid off from a high salary job and who can only find work in a retail store at barely above minimum wage? What about the renters who can barely afford the monthly rent payment but will be facing higher rent payments as landlords recoup their higher property taxes as a result of the issuance of more and more debt by a school district? Where are their measures, guidelines, and ratios of affordability? Who is looking out for the poor, the disabled, the aged, and the families who are economically deprived? None of the guidelines set forth above appear to be concerned with the affordability of school district debt on these disadvantaged groups in society. The state of Indiana has no public measures of the personal and economic impact of school district debt on these groups of people.

This glaring flaw in Indiana's system for financing long-term debt for school districts may have contributed to the proliferation of school bond issues. According to the Indiana Governor's office, last year one-quarter of all property tax payments went to debt. Seventy-five percent were for school district obligations. Property taxes dedicated to debt are increasing eight percent annually.⁵⁴

What this writer suggests is a tripartite measurement of affordability of school district debt. This measurement can also be used in determining affordability of other debt issued by other local government units.

The first group of measurements of affordability needs to concern the school district itself. The *school district affordability index* should be used to measure internal affordability of the school district when it proposes to issue its bonds. If the school district defaults on its long-term debt, the state will step in and deduct general fund revenue from the school district. This can result in severe cutbacks in educational services and cause substantial turmoil and disruption in the community. The economic impact would ripple through the community as school workers are laid off and have little or no money to spend in the community.

A second group of measurements can be termed the *community affordability index*. This index measures whether the community as a whole can afford the bond issue. Perhaps the school district will not become financially distressed by issuing the bonds, but if the overall tax rate in the community, including overlapping tax rates of all taxing units in the community, becomes excessive - disastrous community and business economic effects can result. Businesses and families may flee the community for communities with less burdensome tax rates.

The final group of measurements can be termed *individual and family affordability index*. This index may be used to measure the human impact on individuals and families in the community who may not be as economically advantaged as others, and who are often overlooked by school boards who propose bond issues. This might be

called the individual and family “misery index.” Burdensome property tax payments will jeopardize the American dream of home ownership for homeowners who are in the lower economic range and are marginally hanging on to their homes on a month to month and paycheck to paycheck basis. The needs of this group are seldom the discussion of school boards. School boards, understandably so, focus on the needs of the school district. The loss of homes by this group because of the burdensome tax rates is the silent cost of school district bond issues.

Various measurements, guidelines, and ratios that may be used in determining affordability of proposed school district debt are presented below. This recommendation can be used to determine affordability of school district bond issues in relation to each of the three above referenced groups. What this paper will not attempt to do is to set specific standards for each recommended measurement, guideline, and ratio. The setting of standards, limits, and caps is a political decision and is best left for elected officials after informed discussion by the electorate. However, by adopting quantitative criteria for use by government officials in calculating debt affordability, the citizens can better judge whether proposed debt is in reality affordable for the school district, the community, and its less fortunate residents. The citizens will also be better prepared with data to hold government officials accountable to carry out their responsibility to issue government debt only when affordable. The recommendations are set forth below in tables 3, 4, and 5.

Table 4
School District Affordability Index

Index Item	Description
Cash Ratio	Cash + cash equivalents + investments / current liabilities
Quick Ratio	Cash + cash equivalents + investments + receivables / current liabilities
Current Ratio	Current assets / current liabilities
Operating Ratio	Total revenue / total expenses
Surplus or Deficit Per Capita Ratio	Total surpluses or deficits / population
Net Asset Ratio	Restricted and unrestricted net assets / total assets
Long-term Liability Ratio	Long-term non-current liabilities / total assets
Long-term Liability Per Capita Ratio	Long-term non current liabilities / population
Revenue Per Capita Ratio	Total revenues / population
Expenses Per Capita Ratio	Total expenses / population
Total Debt Outstanding	Sum of all debt for school district
Debt Service to Expense Ratio	Debt service payments / general fund expenditures
Debt Service to Revenue Ratio	Debt service payments / general fund revenue
Expense to Assessed Value Ratio	General fund expenses / assessed value of all real estate
GF Balance to GF Revenue Ratio	General Fund balance / General Fund total revenue
Ten-year Payout Ratio	Rate of repayment of bond principal over ten year period
Current Operating Liabilities	Whether there is an excess of current operating liabilities over current assets
Substantial General Fund Deficit	Whether current expenses exceed current revenues by substantial amount in at least one fiscal period during past three years
Pattern of General Fund Deficit	Whether there has been a consistent pattern of current expenses exceeding current revenues by small amounts for several years
Unfunded Liability	Whether there are any unfunded liabilities

Services Cutback	Whether repayment of debt causes cutback in school district services resulting in school district becoming uncompetitive
Bond Interest Rate	Whether the bond issue can be marketed at a reasonable interest rate
Overall Financial Condition	Whether the school district's annual financial report shows overall financial condition and ability to fund long-term operating costs and the debt
Controlled School Corporation	Whether the school district is a controlled school district

**Table 4
Community Affordability Index**

Index Item	Description
Net Long-term School District Debt Per Capita Ratio	Total long-term school district debt / population in school district
Net Long-term Community Debt Per Capita Ratio	Total long-term debt of school district and overlapping jurisdictions / population in school district
Net Long-term Debt to Personal Income Ratio	Net long-term debt / median household net income before taxes
Per Capita School District Net Long-term Debt to Per Capita Income Ratio	Per Capita net long-term school district debt / per capita income of school district residents
Per Capita Community Long-term Debt to Per Capita Income Ratio	Total net long-term debt of school district and overlapping jurisdictions / per capita income of school district residents
School District Tax Rate	Whether school district tax rate is burdensome
Net Long-term School District Debt to AV Ratio	Net long-term school district debt / total assessed valuation of all real estate in school district
Net Long-term Community Debt to AV Ratio	Net long-term debt of school district and overlapping jurisdictions / total assessed valuation of all real estate in school district
Decrease in AV	Whether the assessed valuation of the school district has decreased during any of the past five years
Inflation Adjusted Decrease in AV	Whether the inflation adjusted assessed valuation of the school district has decreased during any of the past five years
Population Change Percentage	The percentage increase or decrease of the population of the school district during the past five years
Percent of Tax Collections	The percent of property tax bills paid during past three years
Top Five Taxpayers to AV Ratio	The taxable value of the real estate owned by the top five property taxpayers / total school district assessed valuation
Top Ten Taxpayers to AV Ratio	The taxable value of the real estate owned by the top ten property taxpayers / total school district assessed valuation
Top Twenty-Five Taxpayers to AV Ratio	The taxable value of the real estate owned by the top twenty-five property taxpayers / total school district assessed valuation
Percent of AV In One Industry	The percent of the school district's total assessed valuation that is in one type of industry
Percent of AV From Largest Taxpayer	Percent of total assessed valuation of school district that the district's largest taxpayer holds

**Table 5
Individual and Family Affordability Index**

Index Item	Description
Number of Personal Bankruptcies	Number of individual or family bankruptcies during

	each of last three years
Personal Bankruptcies to Population Ratio	Number of personal bankruptcies during each of last three years / number of school district residents
Number of Residential Tax Delinquencies	Number of individual or families who have current outstanding property tax delinquencies on their personal residences
Amount of Residential Tax Delinquencies	Total dollar amount of current individual or families with property tax delinquencies on their personal residences
Residential Tax Delinquencies to AV Ratio	Total dollar amount of residential individual or family owned property tax delinquencies during each of last three years to total school district assessed valuation
Median Household Income	Median household income of all families residing in school district
Residential Foreclosures to Number of Residences Ratio	Number and percent of single family residential foreclosures during each of last three years / total number of single family residential units in school district
People Living in Poverty to Population Ratio	Number and percent of individuals living at or below federal poverty level / total population in school district
Children Living in Poverty to Population Ratio	Number and percent of children living at or below federal poverty level / total population in school district
Single Parent Households to Population Ratio	Number and percent of single parent households / total population in school district
Disabled People to Population Ratio	Number and percent of disabled people / total population in school district
People Over Age 65 to Population Ratio	Number and percent of people over age 65 / total population in school district
Free and Reduced Lunch to Population Ratio	Number of children on free or reduced lunch / total population in school district

Commentary and Recommendations for Further Research. It should be understood that the above tripartite set of criteria is not a magic formula for determining affordability. The author does not represent that it is the only set of criteria that can be developed to measure affordability. It is but one example of a possible set of quantitative criteria that can be developed to help Indiana's school districts, local tax boards, state tax boards, and taxpayers make informed judgments on the affordability of school bond issues.

Neither is this tripartite set of criteria a complete formula for determining affordability of school district debt. It is a mere skeleton outline of the criteria. Flesh needs to be added to the skeleton by inserting specific standards, limits, and caps into each index item. For example, policymakers need to decide what debt percentage of assessed valuation of taxable property is appropriate? What should the standard be? Should it be different for growing communities (e.g. 15%) than declining communities (e.g. under 10%)? Another example is the tax base diversity of the community. Should the top five taxpayers account for no more than 25% of the tax base? Should the largest taxpayer account for no more than 10% of the tax base? Much is left to be answered from

the above set of basic criteria. The answers are policy decisions that need to be made by elected officials.

Reliable data may be lacking for some of the index items. Meaningful measurements of the index items need to be developed for measuring the affordability of school district bond issues. Especially helpful would be statewide medians, means, and standard deviations for all Indiana school districts for these index items. Statewide statistics as well as statistics by size, wealth, and demographics of similar school districts would be beneficial. Moody's medians and Standard and Poor's means can be used as a national or regional comparison of school districts. What is important to understand is that statistics without any meaningful comparisons will not be sufficiently informative to help policy-makers and taxpayers make sound decisions on affordability of school districts' debt.

The collecting of useful data, the calculation of data, and the dissemination of meaningful data for determining affordability of bond issues is not being done locally by school boards. First of all, they don't have the expertise or staff to do so. Secondly, they would be under the burden of voluntary compliance with their requests for data from other schools, and would not likely find many school districts with the willingness to spend the time to collect the data. Thus, if the use of meaningful data and comparisons in determining affordability is to become a reality, the state must take the lead and undertake the project of collecting the data, analyzing the data, and distributing the data to school districts and their taxpayers. Transparency of the data is the key to meaningful decision-making.

Much more research needs to be done and many questions arise. Will the quantitative data be understood by school boards and the citizens, or is it too complicated to provide meaningful dialogue on the issue of affordability of school district debt? What do school boards and taxpayers believe to be appropriate standards, limits, and caps?

A question arises as to the impact of the recent movement in Indiana to a market value assessed valuation of real property pursuant to the 1997 Indiana Tax Court decision.⁵⁵ Indiana's Constitution provides in Article 13 Section 1 in part that

“No political or municipal corporation in this State shall ever become indebted, in any manner or for any purpose, to an amount, in the aggregate, exceeding two per centum on the value of the taxable property within such corporation....”

Because the move toward a market valuation system of property taxation resulted in roughly tripling the taxable assessed valuation of real property in school districts throughout the state, does this mean that Indiana taxpayers can afford three times the taxes than before implementation of the new system? It appears that under the new system the debt allowed under Article 13 Section 1 has about tripled. This emphasizes the need for affordability criteria.

If this was not enough flexibility to issue local debt, Indiana courts have held that future annual lease rental payments made to school building corporations by school corporations pursuant to a lease do not violate the two percent debt limitation, even where the total rental for the term exceeds the school corporation's debt limit, when the annual lease rental installments do not increase the debt beyond the limit, even though the lease includes an option to purchase.⁵⁶ Thus, by all practical accounts, the two percent constitutional debt limit has been reduced to a fiction. All a school corporation has to do is to form one or more public or private school building corporations pursuant to Indiana statute⁵⁷ and it can issue as much debt as the Department of Local Government Finance and the taxpayers will let it issue, notwithstanding the two percent limit of the Indiana Constitution. The statute permitting local school districts to avoid the constitutional debt limitation is a sham and is yet another illustration of the necessity for the establishment of affordability criteria.

The debate in Indiana should also include a vigorous discussion on the issue of equity. Is the current system where the Indiana General Assembly essentially delegates to local school districts and their taxpayers the decisions to renovate, build new schools, and issue long-term debt instruments a fair and equitable way of making building program decisions? Is it a system that rewards wealthy communities and penalizes poor communities? Has this delegation of authority by the state led to inequities throughout the state? Does the present system of financing school construction and technology allow some schools to put million dollar artificial grass on their football fields while others play on barren grass and mud? Do some children go to dark, dingy, non air conditioned schools fifty to seventy-five years old or more, and others go to brand new shining, architecturally pleasing, state-of-the-art fully air conditioned schools? Do some teachers have all the computers and software, LCD projectors, and smart-boards, that they ever dreamed of, and do other teachers not have access to this technology?

Is this the best way to construct the school facilities needed for the education of the state's children? Do children of wealthy parents who can afford to move to growing and wealthy school districts that continually build new facilities and buy all the new technology desired, benefit at the expense of middle class and economically deprived children who cannot afford to move to the wealthy districts?

A more basic issue is whether Indiana really needs \$100 million dollar high schools and other schools costing tens of millions of dollars. Are Indiana public school districts building dinosaurs that may not even be needed a decade or so from now? Are there less expensive ways to house children while they learn, and if so, can they be just as efficient in providing a sound learning environment? What impact can distance learning have on the need for new construction or expensive remodeling? Can charter schools, some of whom operate in storefronts, malls, offices, and other buildings, take some of the demand off the table for building new schools and remodeling old schools? Could Indiana taxpayers save tens or even hundreds of millions of dollars by the state's leaders thinking out of the box and developing new, creative, innovative, and less expensive ways to provide the necessary learning environments for Indiana's school children?

Yet another question for further research concerns the efforts of school boards to decrease the need for building programs. Have school districts done everything possible to diminish the need for proposed building projects, or at least to reduce the cost by making new buildings or renovations smaller? Some school districts have proposed building projects that include additions to buildings for more kindergarten classrooms while they have empty classrooms in other buildings, and while dozens upon dozens of classrooms in community churches go unused during the week.

Will the new county tax adjustment boards serve as effective fiscal watchdogs to control local government spending and debt?⁵⁸ Early returns are not encouraging.⁵⁹ Without any meaningful quantitative criteria for determining debt affordability these county tax adjustment boards will be reduced to yet one more level of meaningless government, or worse yet, will make unwise property tax decisions based on inadequate data.

Finally, the last question and area of further needed research is whether Indiana's way of financing school construction and technology violates the Indiana Constitution. Article 8 Section 1 provides in part:

“...it shall be the duty of the General Assembly to...provide, by law, for a general and uniform system of Common Schools, wherein tuition shall be without charge, and equally open to all.”⁶⁰

Whether the Indiana General Assembly is meeting its Constitutional obligation to provide a general *and uniform* system of public schools in Indiana is open for debate. The reason is that the Indiana Supreme Court has not definitely ruled that a system that provides potentially a wide disparity in school facilities, equipment, and technology to Indiana's school children fulfills the Constitutional mandate. This is particularly questionable when one considers that the capital projects fund has been expanded to include not only school building and renovation expenses, but also now can be used for:

1. purchasing, leasing, repairing, or maintaining equipment;⁶¹
2. construction, repair, replacement, remodeling, or maintaining sports facilities (up to five percent of property capital projects fund tax revenues in the calendar year);⁶²
3. purchase, lease, upgrade, maintain, or repair computer hardware, software, wiring and computer networks, communication access systems used to connect with computer networks or electronic gateways, computer maintenance employees, conduct nonrecurring in-service technology training of school employees, to acquire any equipment or services necessary to implement the technology preparation curriculum, to participate in a program to provide educational technologies, including computers in the homes of students, the 4R's technology program, or any other program under the educational technology program described in statute,⁶³ or to obtain any combination of equipment or services described above;⁶⁴

4. purchase land, buildings, building materials, and equipment for vocational building trades classes;⁶⁵
5. leasing or renting existing real estate;⁶⁶
6. salaries and fringe benefits for certain categories (an exhaustive list) of maintenance employees under certain conditions;⁶⁷
7. energy savings contracts;⁶⁸
8. carry out the school district's plan for improving indoor air quality;⁶⁹
9. utility services;⁷⁰
10. property or casualty insurance premiums under certain conditions;⁷¹
11. transfer money to other funds,⁷² specially for implementation of the district's technology preparation task force,⁷³ for the repair and replacement fund,⁷⁴ for the district's health services and liability self-insurance fund with certain limitations;⁷⁵ and
12. advances for the school district's educational technology program.⁷⁶

The debt service fund also has been expanded to include items other than payment of interest and principal on school district debt. School districts can pay unreimbursed costs of textbooks for the district's students who were eligible for free or reduced lunches.⁷⁷ Also, districts have been allowed to issue bonds and establish a separate debt service fund for payment of employee severance and retirement benefits given by the local school board.⁷⁸ Although the statute required the school district to lower its property tax levy for its transportation, school bus replacement, capital projects, art association, or historical society funds in an amount equal to the new debt needed to pay off the retirement and severance bonds, clever superintendents merely upped the levy in one or more of those funds the year before the district sought approval for its retirement or severance bonds, and then only to "drop" the fund in an amount equal to the debt service payment the first year of paying for the bonds.

What all of this means is that through the years the Indiana General Assembly has transferred more and more of a district's normal operating costs to the local property tax levy. The wealthy districts have been funding more and more salaries, fringe benefits such as health insurance, retirement, and severance benefits, and technology costs through their local property tax levies. This raises the inevitable question: Has this half-hazard financing scheme created a public school system that is not uniform under the Indiana Constitution? Are the state's wealthy children enjoying educational privileges provided by the State of Indiana that the state does not provide to the middle class children and children of poverty? Only the Indiana Supreme Court can provide that state with the answer.

The Governor of Indiana has stated that between 1984 and 2006, property taxes for school debt service and capital projects have increased over 8% per year.⁷⁹ The Governor has also stated that between those same years, local spending funded by property taxes increased from \$1.1 billion dollars to \$7.9 billion dollars, averaging 6.1% per year. Given all of the above ways the Indiana General Assembly has added to the local taxpayers' burden, is it any wonder there is a property tax crisis throughout Indiana?

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- ¹ 2005 *Indiana School Construction Annual Report*, (2006). Indiana Department of Local Government Finance. Retrieved 9-26-07 from <http://www.in.gov/dlgf/boards/school/construction.html>.
- ² *Id.*
- ³ Fort Wayne Community Schools, School Board Minutes 2-26-07.
- ⁴ The vote was 26,700 against the building program and 7,566 for the building program. See Fort Wayne Journal Gazette, July 21, 2007 for a report on the remonstrance.
- ⁵ E-mail communication from Dr. John Ellis, Executive Director, Indiana Public School Superintendents, dated September 25, 2007. The Associated Press reported that since 1995 opponents have forced 94 building projects into a remonstrance, and that remonstrators won in 42 cases and the school districts won in 52 cases. See Fort Wayne News Sentinel, November 5, 2007 at p. 3L.
- ⁶ The Bond Market Association, Bond Markets.com; available from: <http://www.bondmarkets.com/story.asp?id=2296>; accessed 2 February 2006.
- ⁷ Coe, Charles K. (Fall 2007). Preventing local government fiscal crises: The North Carolina approach. *Public Budgeting & Finance Vol. 27 Issue 3*, pp. 39-49.
- ⁸ Hildreth, W.B. & Miller, G.J. (Winter 2002). Debt and the local economy: Problems in benchmarking local government debt affordability. *Public Budgeting & Finance* 22(4), 99-113.
- ⁹ Vogt, A. John (2004). *Capital budgeting and finance: A guide for local governments*. International City/County Management Association. Washington, D.C. at p. 130.
- ¹⁰ Standard and Poor's Corporation, *Public finance criteria 2000* (New York: S&P, 2000), 21. As quoted in Vogt 2004 at 130.
- ¹¹ Vogt, A. John (2004), *supra* at p. 131.
- ¹² Vogt, A. John (2004), *supra* at p. 131.
- ¹³ Vogt, A. John (2004), *supra* at p. 131.
- ¹⁴ I.C. 20-48-1-11.
- ¹⁵ The Yellow Ribbon Panel was a group of about 24 Fort Wayne community members hand-picked by the FWCS administration and school board to make recommendations concerning the building needs of FWCS.
- ¹⁶ Denison, D.V., Hackbart, M., & Moody, M. (Winter 2006). State debt limits: How many are enough? *Public Budgeting & Finance*, 26(4), 22-39.
- ¹⁷ Brecher, C., Richwerger, K., & Van Wagner, M. (Winter 2003). An approach to measuring the affordability of state debt. *Public Budgeting & Finance*, 23(4), 65-85.
- ¹⁸ *Id.*
- ¹⁹ *Id.*
- ²⁰ Conversation with Rod Wilson, Senior Vice President, City Securities Corporation, Fort Wayne, Indiana, July 1, 2007.
- ²¹ See I.C. 20-46-7-8.
- ²² See I.C. 6-1.1-19-4.1.
- ²³ See I.C. 6-1.1-19-4.1.
- ²⁴ See I.C. 20-46-7-11.
- ²⁵ *Guidance for Review of School Building Project Financing (2005) at page 11*. Indiana Department of Local Government Finance. Retrieved from <http://www.in.gov/dlgf/boards/school/construction.html> on September 27, 2007.
- ²⁶ *Id.* at pages 11-12.
- ²⁷ *Id.* at page 12.
- ²⁸ *Id.* at page 12.
- ²⁹ The School Facility Guidelines have not been adopted as administrative regulations by the agency and have not been included in the Indiana Administrative Code. However the "Guidelines" were adopted by the Indiana State Board of Education on January 10, 2002 and can be found at <http://www.doe.state.in.us/stateboard/constguide.html>.
- ³⁰ Loviscek, A.L., & Crowley, F.D. (1988). Analyzing changes in municipal bond retains: A different perspective. *Urban Studies* 25: 124-132.
- ³¹ Loviscek, A.L., & Crowley, F.D. (February 1990). What is in a municipal credit rating? *The Financial Review*, 25(1), 25-53.
- ³² Groves, S. M., & Valente, M.G. (1994). *Evaluating financial condition: A handbook for local government*. Washington, D.C.: International City/County Management Association.

- ³³ Coe, C. K. (Fall 2007). Preventing local government fiscal crises: The North Carolina approach. *Public Budgeting & Finance* 27(3), 39-49.
- ³⁴ See I.C. 20-45-6-1 et seq. for a description of a financially distressed school district which will be subject to certain controls by the Department of Local Government Finance.
- ³⁵ Advisory Commission on Intergovernmental Relations (ACIR). (1973). *City financial emergencies: The intergovernmental dimension*. Washington, D.C.: U.S. Government Printing Office.
- ³⁶ Wang, X.H., Dennis, L., & Yuan Sen, J. T. (2007). Measuring financial condition: A study of U.S. states. *Public Budgeting & Finance*. 27(2), 1-21.
- ³⁷ Id.
- ³⁸ See Bahl, R. W., & Duncombe, W.D. (1933). State and local debt burdens in the 1980s: A study in contrast. *Public Administration Review* 53, 31-49. (As cited in Denison, Hackbart, & Moody, 2006).
- ³⁹ Miranda, R., & Picur, R. (2000). *Benchmarking and measuring debt capacity*. Chicago: Government Finance Officers Association. (As cited in Denison, Hackbart, & Moody 2006).
- ⁴⁰ Galgano, T. (2001). Improving municipal debt efficiency. *American City & County*, 116(12), p. 6.
- ⁴¹ Id.
- ⁴² Vogt, A. J. (2004), *supra*.
- ⁴³ National Advisory Council on State and Local Budgeting, *Recommended budget practices: A framework for improved state and local government budgeting*. Chicago: Government Finance Officers Association, at 19. As quoted in Vogt (2004) at 139.
- ⁴⁴ www.charneck.org
- ⁴⁵ Retrieved October 2, 2007 from <http://bonds.montgomerycountymd.gov/fiscal.htm>.
- ⁴⁶ Id.
- ⁴⁷ Adopted May 10, 2007 by Allegany County Finance Department, retrieved on September 15, 2007 from <http://www.gov.allconet.org/finance/finance.html>.
- ⁴⁸ Office of the Chief Financial Officer, Los Angeles Unified School District Policy Debt Management Policy, April 2007, retrieved on September 1, 2007 from http://notebook.lausd.net/pls/ptl/docs/PAGE/CA_LAUSD/LAUSDNET/OFFICES/CFO_HOME/CFO_TREASURY/CFO_POLICIES/DEBT%20POLICY%202006-07%20V1%20CLEAN.PDF.
- ⁴⁹ Id.
- ⁵⁰ *Debt Affordability Study (February 16, 2007)*. Legislative Budget Board. Austin: TX. Retrieved on August 20, 2007 from www.lbb.state.tx.us/Other_Pubs/Debt_Affordability_Study_0207.pdf.
- ⁵¹ Id. at p. 1.
- ⁵² Id. at p. 1
- ⁵³ Id. at p. 1.
- ⁵⁴ Associated Press (2007). *School officials fight proposal*. Fort Wayne News Sentinel, November 5, 2007 at p. 3L.
- ⁵⁵ *Town of St. John, et al. v. State Board of Tax Commissioners*, Case No. 49T10-9309-TA-00070, slip op. at 55 (Ind. Tax Ct. Dec. 22, 1997).
- ⁵⁶ See *Hively v. School City of Nappanee*, 202 Ind. 28 (1929), 169 N.E. 51, reh'g denied, 202 Ind. 36, 171 N.E. 381 (1930); and *Teperich v. North Judson San Pierre High School Building Corp.*, 257 Ind. 516 (1971), 275 N.E.2d 814, *cert. denied*, 407 U.S. 921, 92 S.Ct. 2462, 32 L.Ed.2d 806 (1972).
- ⁵⁷ See I.C. 20-47-2-1 et seq. and I.C. 20-47-3-1 et seq.
- ⁵⁸ See I.C. 6-1.1-29-1 et seq. which establishes a county board of tax adjustment in each county. This statute gives broad powers to the boards to review and approve capital projects to be financed with bonds by each political subdivision in the county.
- ⁵⁹ An example of the struggles of at least one such board is chronicled in an article entitled "Tax board tosses in towel; changes urged." *Fort Wayne Journal Gazette*, October 27, 2007.
- ⁶⁰ Constitution of the State of Indiana, Approved in Convention at Indianapolis, February 10, 1851, and adopted by the electorate, effective November 1, 1851, as amended through 2006, Article 8 Section 1.
- ⁶¹ I.C. 20-40-8-11.
- ⁶² I.C. 20-40-8-12.
- ⁶³ See I.C. 20-20-13 for the description.
- ⁶⁴ I.C. 20-40-8-13.
- ⁶⁵ I.C. 20-40-8-14.
- ⁶⁶ I.C. 20-40-8-15.

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- ⁶⁷ I.C. 20-40-8-16.
- ⁶⁸ I.C. 20-40-8-17. See I.C. 36-1-12.5 for energy savings contracts.
- ⁶⁹ I.C. 20-40-8-18. See I.C. 16-41-37.5 for indoor air quality plans.
- ⁷⁰ I.C. 20-40-8-19.
- ⁷¹ I.C. 20-40-8-19.
- ⁷² I.C. 20-40-8-20.
- ⁷³ See I.C. 20-20-10-5 for the technology preparation task force.
- ⁷⁴ See I.C. 20-40-11-3 for the repair and replacement fund.
- ⁷⁵ See I.C. 20-40-12-6 for the self-insurance fund.
- ⁷⁶ See I.C. 20-49-4-22 for the educational technology program.
- ⁷⁷ I.C. 20-40-9-7.
- ⁷⁸ I.C. 20-48-1-2.
- ⁷⁹ See Access Indiana web site, www.in.gov.