

LaGrange School District 105

**Strategic Financial Planning
(using StratPlan Model)**

Spring 2018

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Strategic Planning Update

LaGrange 105

Spring 2018

Recent History and Future Mystery

LaGrange 105's history over the last decade had been characterized by the two-fold thrust of effectively phasing in the 2005 operating rate referendum to solidify operating balances, and implementing long-anticipated facilities improvement projects that had been deferred during lean times.

StratPlan was enlisted to help facilitate longer range strategic planning, beginning in 2006, with periodic updates since then. Those studies investigated the ability to ensure long-range operational stability and evaluated the ability to accommodate unforeseen expense escalations as the environment unfolded.

Initial upgrade projects were undertaken and planning was begun for a comprehensive package eventually costing about \$30 million. Just as those plans were being solidified, however, the dynamic changes in the economy in late 2008 and early 2009 raised potential questions about the viability of those plans, or at least the need to reassess them in the context of the changing landscape.

An update to previous studies was therefore conducted in the spring of 2009 to evaluate the outlook for the future in that dramatically different economic climate, investigating various scenarios of timing and scope, and the ability to complete those plans was reaffirmed. In recent years, StratPlan has again been periodically enlisted to evaluate the future outlook, in the context of a continually evolving economy.

As the economy appears to have stabilized somewhat, the longer term focus has now shifted to the more conventional concerns of balancing the ongoing budgets while maximizing educational efficiency.

LaGrange 105 has done an outstanding job in recent years of controlling expenses and underrunning budgets, and establishing a solid financial foundation. The ongoing budget focus now centers on the ability to continue that discipline and the potential to apply the success of that discipline to reduce debt obligations. There continues, however, to be ongoing concerns about the potential escalation of benefits and pension obligations emanating from Springfield, and now about any fallout effects from the recent SB1947 legislation as the details are finalized.

Financial Parameters

Background

To calibrate the StratPlan model for LaGrange 105, a decade of actual financial data (via audits and "AFR" data) along with the current budget were analyzed in detail. That analysis provides factors that uniquely reflect both the revenue and expense patterns within the district, and allows investigations of the trends that they represent in order to subsequently forecast the financial health of the district over a 10-year financial horizon. District 105 is thus uniquely modeled in this StratPlan development and almost any permutation or combination of circumstances can be projected into the future.

Variables

The overall basis for this study incorporates previous financial data, reflects completed construction projects and the finalized financing obligations, and includes the current operating budget with the following considerations and future assumptions:

GENERAL ASSUMPTIONS:

- | | |
|------------|---|
| CPI | * an inflation rate slowly returning from recent lows to more historical averages of about 2.5%. |
| EAVs | * recovering from below historical averages during the recent slowdowns |
| | * New construction increasing to historical averages of about \$7 million/yr |
| | * Reassessments returning to the historical triennial Cook sawtooth pattern after recent devaluations, reverting to a more typical historical pattern of 2.0%, 10.0%, -2.0%, 2.0%, 10.0%, -2%, etc. |
| | * No new TIF additions |
| Enrollment | * actual for 2017-18, with a relatively flat enrollment picture going forward. |

REVENUE ASSUMPTIONS:

- | | |
|--------------|--|
| Tax Patterns | * maximum tax rate as limited by PTELL (tax cap) with |
| | * \$350k/yr PTAB protests/refunds |
| | * 99% collection rate on the levy |
| CPPRT | * increasing at CPI/inflation levels |
| Federal | * escalating from current levels at CPI/inflation |
| State | * With the passage of the recent SB1947, GSA and Categoricals are being reconfigured. Initial commitments from Springfield have increased only slightly if any and are now assumed to increase from these levels only with CPI/inflation |
| | (Details, however, are still being developed in Springfield at this writing) |
| Fees/Misc | * current levels and increasing modestly over time with inflation |

EXPENSE ASSUMPTIONS:

Future Salary/Benefits – the current contract is now expiring but a 2-year extension is being considered as an option until details of state support are finalized. That would reflect

- * salaries - 3% for 2 years and then 0.7% over CPI patterns in the next contract
- * benefits increasing at 7.0% indefinitely, after a projected high of 10% in FY19, reflecting concern over potential pension reform and TRS escalations from Springfield, and ongoing health/med escalations, etc.

The most significant expense concern involves the continuing escalation (and the uncertainty) surrounding benefit costs on several fronts.

- Springfield has for awhile been mulling shifting its TRS financial obligations to the local districts. Various proposals would progressively force local districts to begin funding additional amounts into the state's TRS fund every year. It is unclear if those proposals have died with other recent legislation.
- Overall medical benefit costs have continued to rise and are estimated to continue that escalation in the 5-8% range.

Given the uncertainty (in the levels, if not the direction) of these costs, an ongoing middle-of-the-road escalation is estimated at 7% in total for the combination of these effects.

Special Ed escalations

- * "payments to others" (Special Ed) increasing at 2.5% for 3 years then 5% annually

Average class size

- * essentially steady in the 19-21 average range with minor fluctuations in enrollment

Miscellaneous costs

- * increasing with CPI/inflation

The combination of Salaries and Benefits and Special Ed continuously increasing faster than the CPI are projected to create an important compounding effect on expenses and cash flows that are higher than anticipated in previous studies.

PROJECT WORK:

Major Project Work	* none anticipated (since major completions in FY11-12)
Ongoing Project Work	* ongoing background project work at \$300k/yr
Life Safety Projects	* any ongoing requirements to be completed as part of miscellaneous capital work in O&M

DEBT RETIREMENT:

- * as required to meet remaining obligations on current debt certificates of \$23 million over a remaining 13 year retirement period. The possibility of applying any available surplus to reducing future debt obligations, and/or renegotiating outstanding debt, has been under investigation.

Current Base Case

Basis

The *Current Base Case* is developed using historical revenue and expense data (via "AFRs") along with current budget data, and develops factors and drivers that accurately represent the district's current status and near term future. There is a high degree of correlation and confidence level that the district is in fact very accurately modeled. This case projects the current environment and expectations into the future in order to develop and better understand emerging issues.

In particular, this base case is built upon the assumptions outlined in the previous section. It reflects operation in a relatively stabilized overall economy with a solid financial foundation, but with uncertainty in two areas:

- Various new school legislation is still being considered in Springfield and the fallout from SB1947 is still being clarified.
- Secondly, current estimates for FY18 suggest slightly higher expenses than in previous years. This study conservatively projects that continuing cash flow trend into the future.

Significant Issues

Future Focus

After nearly a decade of concentrating first on the phase-in of referendum revenue, then on completing comprehensive capital and renovation projects, and then worrying about the effects of the overall economic malaise, the long term focus is now shifting to the more conventional issues of balancing the budget and enhancing educational quality – but with continuing concerns about both recent legislation and potential Springfield actions.

Revenue and Tax Patterns

Revenue for LaGrange is overwhelmingly dependent (80-90%) on local tax sources - primarily local property taxes.

- The tax cap law (PTELL) limits any increases in tax revenue to the Government's Consumer Price Index (CPI). In recent years, the official CPI has generally fluctuated in the 2-3% range, with occasional excursions as high as 4.1% and as low as 0.1%. The CPIs for the current tax year is established at 2.1% and is now forecast to return to more historical levels of about 2.5% in the base case – but with speculation about more increasing inflation over time. Future increases in tax revenue are then generally limited within that general range.
- Added to that revenue baseline, there has historically been a modest amount of new construction and tear-down/rebuilds, generally providing another 1-2% of additions to the tax base on average. Although the recent economy slowed most construction to a near standstill, it does appear to be recovering, and this base case assumes that will slowly recover to modest levels, eventually averaging about 1% in the future – about \$7 million/yr. in new EAV.

- Any changing revenue patterns will also depend on the actual effects of the revised state aid formulae (with details still emerging from Springfield) and any practical fallout of the underlying SB1947.

Expense Control

Just as the local tax base is the overwhelming source of district revenue, employment costs are the dominant factor on the expense side of the ledger at about 80% of operating costs. Other fixed overhead costs such as utilities and maintenance are a smaller piece of the pie and generally less controllable in any case. Future salary and benefit increases are the overwhelming factor driving the expense side of the ledger.

Salaries – As noted above, since revenue increases will be essentially determined by the CPI, expense increases must also fall within that same general range. With salaries and benefits constituting 80% of expenses, and with future benefit costs being somewhat of a “wild card,” it is important to limit salary increases to near the CPI.

Benefits – Benefits have fluctuated in recent years and may continue to be a wild card. After a recent moderation and a projected 10% next year, they are assumed to resume increasing at historical rates in the 5-8% range.

There is some advantage to perhaps a reasonable 2-year extension of the current expiring contract until the effects of the new state aid formula and legislation clarify. That would extend salary increases to 3%, with an assumed escalation of 7% in benefits. Thereafter the base case assumes salaries will be limited to no more than 0.7% over CPI with benefits continuing with 7% increases.

Escalations in salaries and benefits and in Special Ed costs, if they do increase above the CPI outlined in the previous section, may begin to nibble at LaGrange’s otherwise healthy fund balances.

Enrollment – Enrollment has fluctuated modestly in recent years and is projected to continue to do so. As a practical matter, however, this is not likely to be a significant financial factor. *Average* class sizes in the district are generally low – about 19-20 or so on average. Any modest changes in enrollment would not be a significant problem if incremental students are simply sprinkled into or out of existing classrooms.

Balancing the Budget

The important strategic goal is of course to keep the two sides of the financial ledger in reasonable long-term balance. In a simplistic view, that means keeping primary expenses (80% of which are salaries and benefits) in line with primary revenues (80-90% of which are local tax dollars). The significant strategic considerations are then as follows:

Revenue. In LaGrange's case there is essentially no control over the revenue side of the books. Given the PTELL formulas, the district will likely continue to be at the mercy of the local and national economies as they evolve. Historically revenues have grown in an average range of about 2-3% from the CPI plus perhaps 1% from growth in the local tax base. Both of those are projected to continue in the near term. As noted, future variations in future state revenue are not well defined at this time. Initial commitments from Springfield, however, have increased modestly and are assumed to now increase from these levels with CPI/inflation

Expense. A contract extension would likely retain some stability until the state uncertainties are clarified. It is critical, however, to restrain those expenses within the general CPI range to balance the budget.

There is, however, considerable *potential* leverage on the expense side of the ledger *if needed* - in two key employment areas:

- The first is to restrain salary and benefit increases to within the emerging CPI- i.e. at a cost of living level that will also match projected revenues. Any restraint in the benefits area could have an important compounding effect in the future.
- The second would be to constrain overall employment costs by increasing class size – and thereby reducing staff and support costs. LaGrange has enviably low class sizes that might provide some flexibility if needed by selectively consolidating sections where possible. That would likely involve separate studies.

Overall, now that the hectic pace of construction, modernization and reorganization has in fact abated and if contractual negotiations can be extended, the district could settle into a more “normal” pattern of operation until the situation in Springfield and the general economy clarifies.

Other Factors

Many other factors that need to be managed can of course affect ongoing operations, but the above issues are the critical *strategic* factors that will have the greatest effect on long-term planning and financial stability for District 105. Other factors are generally smaller, of less strategic importance, or are obscured by the larger effects of the CPI/EAV combinations on revenue, and by the results of periodic contract negotiations and ongoing benefit escalations on expenses.

The subsequent set of charts illustrates the overall picture for District 105 over the next decade under these base case assumptions.

Potential Future Strategy and Issues

Set Aside

If the budget discipline in recent years has in fact been institutionalized, and if current fund balances can be sustained, District 105 has embraced an option to set-aside available funds to minimize future debt obligations. That process has been investigated in previous studies and is also updated here in a subsequent section, particularly in light of changing cash flows and fund balances.

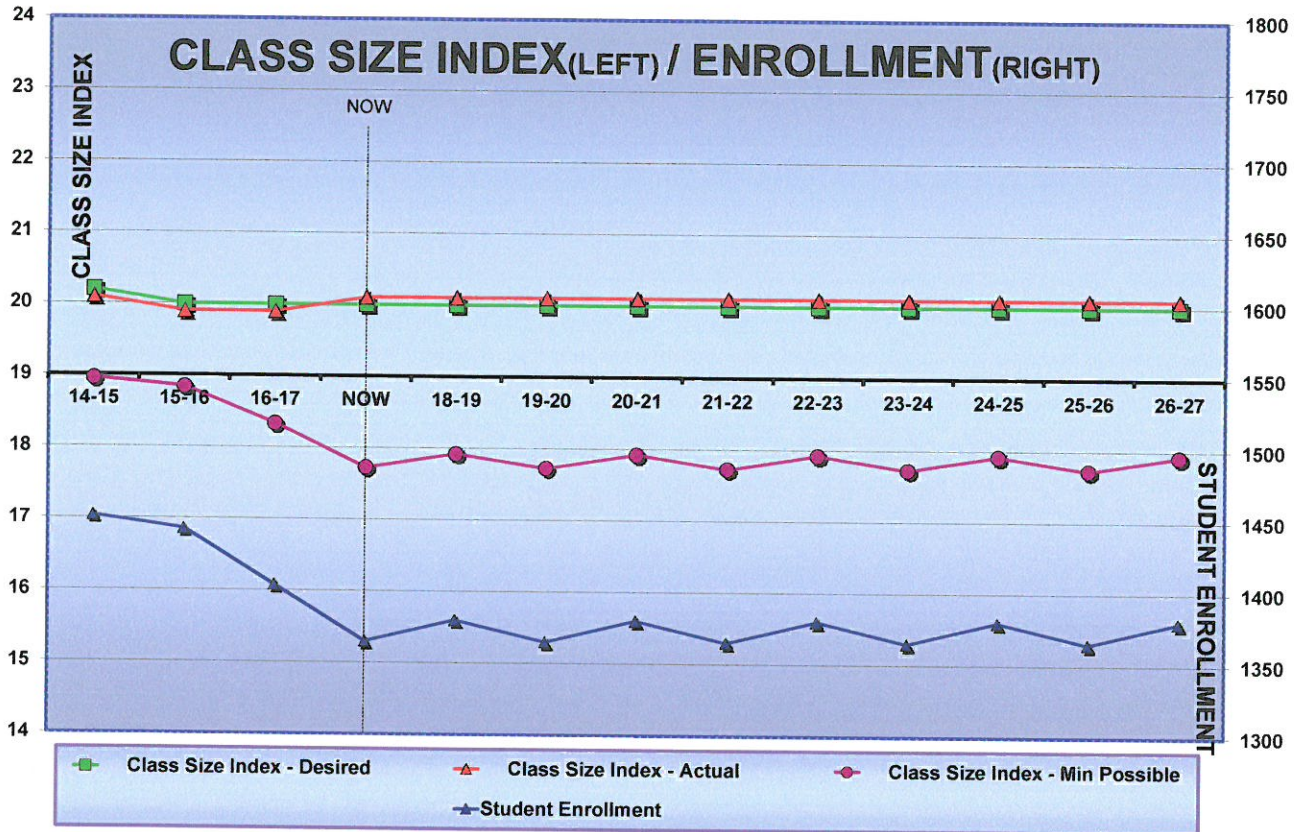
Tax Freeze

There are continuing whispers in Springfield about imposing a property tax freeze even after SB1947. That situation is also investigated in a subsequent section.

SB1947

There are also ongoing concerns about some of the eventual fallout from SB1947 as it is fully implemented. That is the subject of separate potential study.

Spring 2018 Base Case



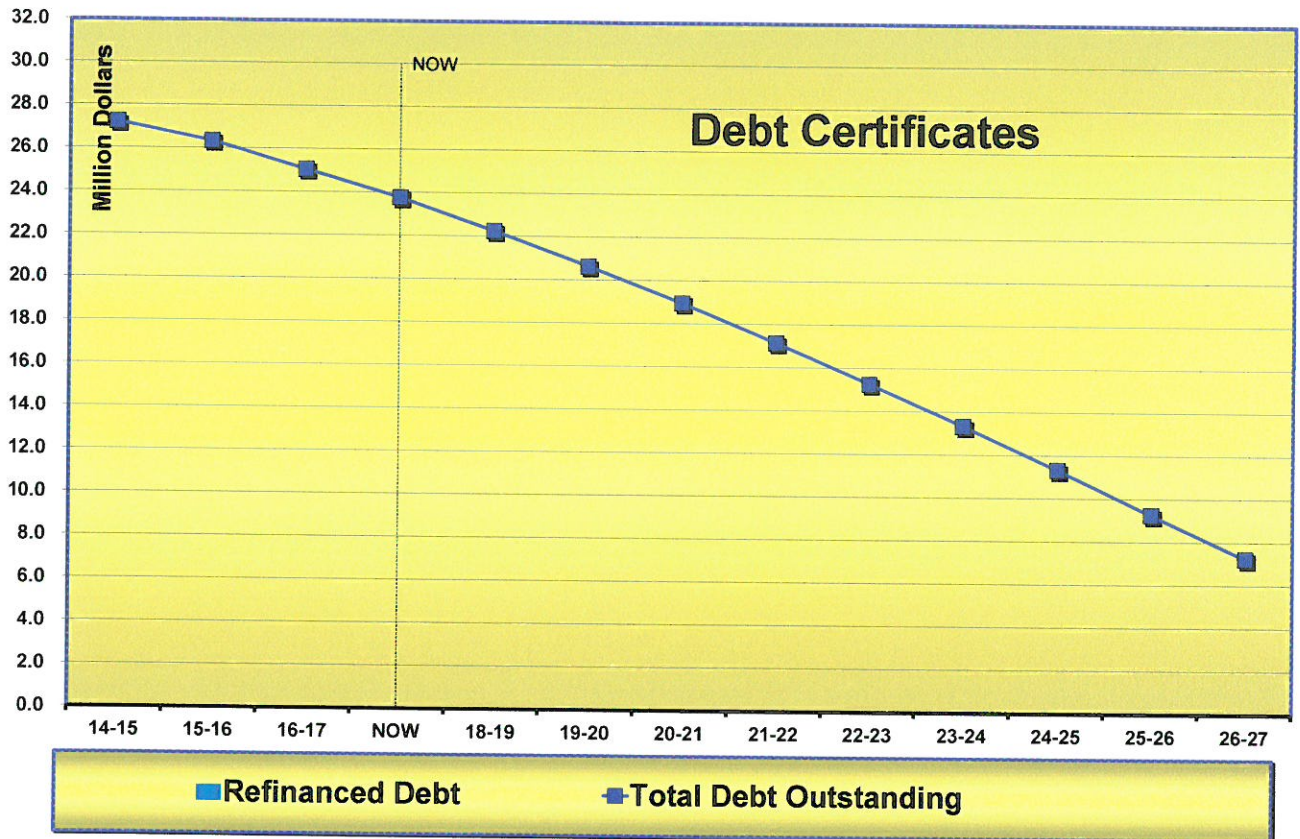
Projected enrollment (blue) is reflected on the right-hand scale. Only very modest fluctuations are forecast.

Class sizes currently **average** in an enviably low range of 19-20 (red-left scale) and that is also used as a nominal long range target (green-left scale). Based on physical capacity, the minimum average class size possible would be in the 18-19 range (maroon-left scale).

Average class sizes can of course be deceptive, recognizing a general desire for smaller class sizes in the lower grades, some variation at the middle school level, and general variations between schools.

As a practical matter, however, changing enrollments should not be a significant problem. Classroom populations are conveniently low (recognizing the caveats about averages), and simply sprinkling additional children into or out of existing classrooms should not have any significant financial or educational effect. There is considerable room to accommodate any reasonable changes in enrollment.

Spring 2018 Base Case



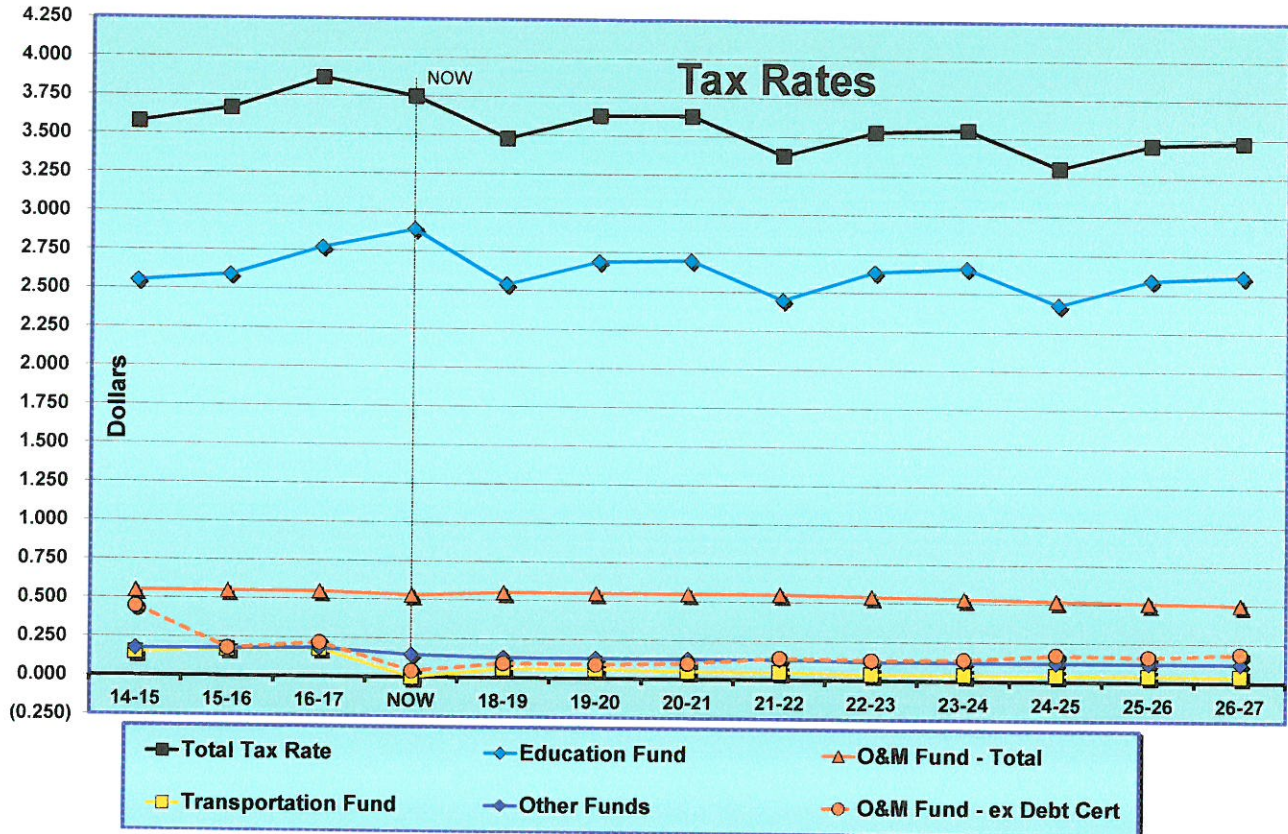
After the completion of the capital program and the finalization of the debt certificate structure, outstanding debt is now at about \$23 million. That is scheduled to be retired over a remaining 13 year period, accelerating slowly as the EAV tax base tends to expand. Total debt service (principal and interest) is currently about \$2.8 million/yr, and should remain in that general range.

Part of the interest payments are offset by a "Build America" federal subsidy, currently at about \$400-450k/yr.

Debt payments are in practice actually being made from the O&M fund and its ongoing annual levy and by dedicating most of CPPRT revenue to the O&M Fund.

A subsequent case investigates setting aside available operating funds to reduce future interest/debt service payments.

Spring 2018 Base Case



Tax rate patterns are reflected in this chart. The Total Tax Rate (black) is composed of all of the component pieces below it, and is "capped" by the PTELL tax cap process.

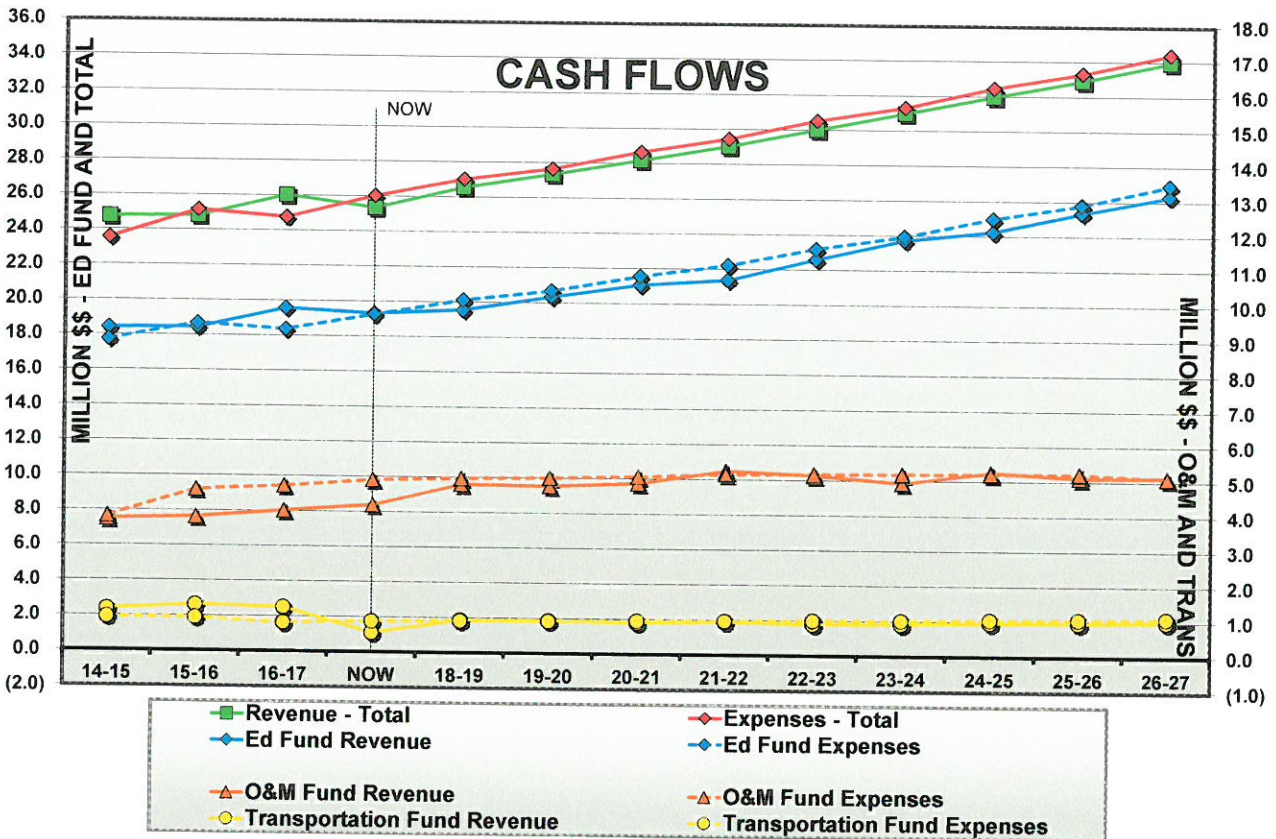
Fund Balances for the smaller funds are held relatively constant by levying the requisite tax rates to keep them solvent, while any variations and tax cap effects are taken in the larger (turquoise) Ed Fund. As a result the Ed Fund rate closely mirrors the capped operating rate pattern.

LaGrange's debt service requirements are paid from funds generated by the (orange) O&M fund levy. The levy rate for O&M is expected to be at the legal limit of \$0.55 (solid orange), with about \$0.20-0.25 of it (dashed orange) devoted to ongoing O&M, with the balance being applied to payments on the outstanding debt certificates.

It is important to note that the recent apparent rise in total tax rate does **not** imply a similar rise in the tax levy or revenue, but is rather a function of EAV reassessments. The tax cap limits total levy increases to the percentage increase in the CPI - generally in the 1-3% range recently. As the EAV tax **base** has fallen, however, the tax **rate** has therefore increased in inverse proportion in order to generate the required tax dollars.

The subsequent jagged appearance of the Total (black) Tax Rate (and mirrored by Ed) is the result of the tri-ennial reassessment process by the county. As EAVs are reassessed upward, tax rates drop and vice versa, but a line-of-sight average suggests a very slowly declining average tax rate overall.

Spring 2018 Base Case



Cash flows for the major funds and totals are illustrated here.

Cash flows for O&M (solid orange revenue and dashed orange expenses - smaller right-hand scale) and for Transportation (solid yellow revenue and dashed yellow expenses - smaller right-hand scale) are held relatively steady. Tax rates in the model for the smaller funds are generally levied to meet ongoing expense obligations and deviations are taken in the larger (turquoise) Ed Fund.

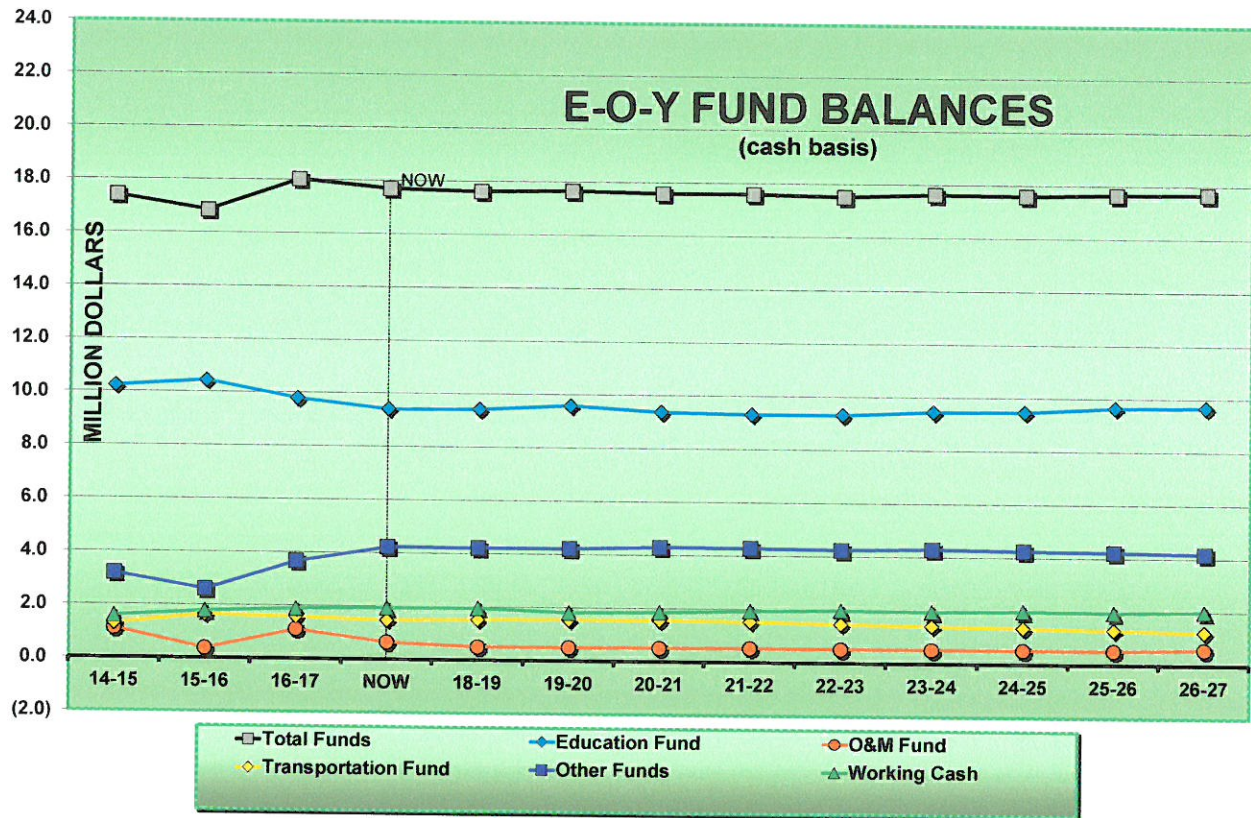
The (turquoise) Ed Fund shows a very slight ongoing deficit - greater than in previous studies. This is primarily due to assumed salary increases that slightly exceed the CPI (assumed to average about 3.2% vs a 2.5% CPI). The small deficit also includes the projected ongoing 7% increase in **total** benefit costs (intended to reflect ongoing increases in medical premiums plus a contingency for any increases imposed by Springfield).

Overall cash flows are projected settle into a very stable range as Total Revenues (green -left scale) essentially cover Total Expenses (red - left scale) in the long term.

There is also very good news on the horizon. The (red) Total Expense and (dashed orange) O&M Expense both include about \$2.5M of ongoing debt service. Those expire 3 years off the right side of this chart and by about 2030, a potential surplus of several million dollars begins to emerge. In the meantime, balances are very stable permit the flexibility to watch and await developments on the horizon in the economy and in Springfield.

(Note that the O&M and Total cash flows here do include ongoing debt payments)

Spring 2018 Base Case



EAVs, tax rates, and cash flows result in these all important E-O-Y (end-of-year) Fund Balances.

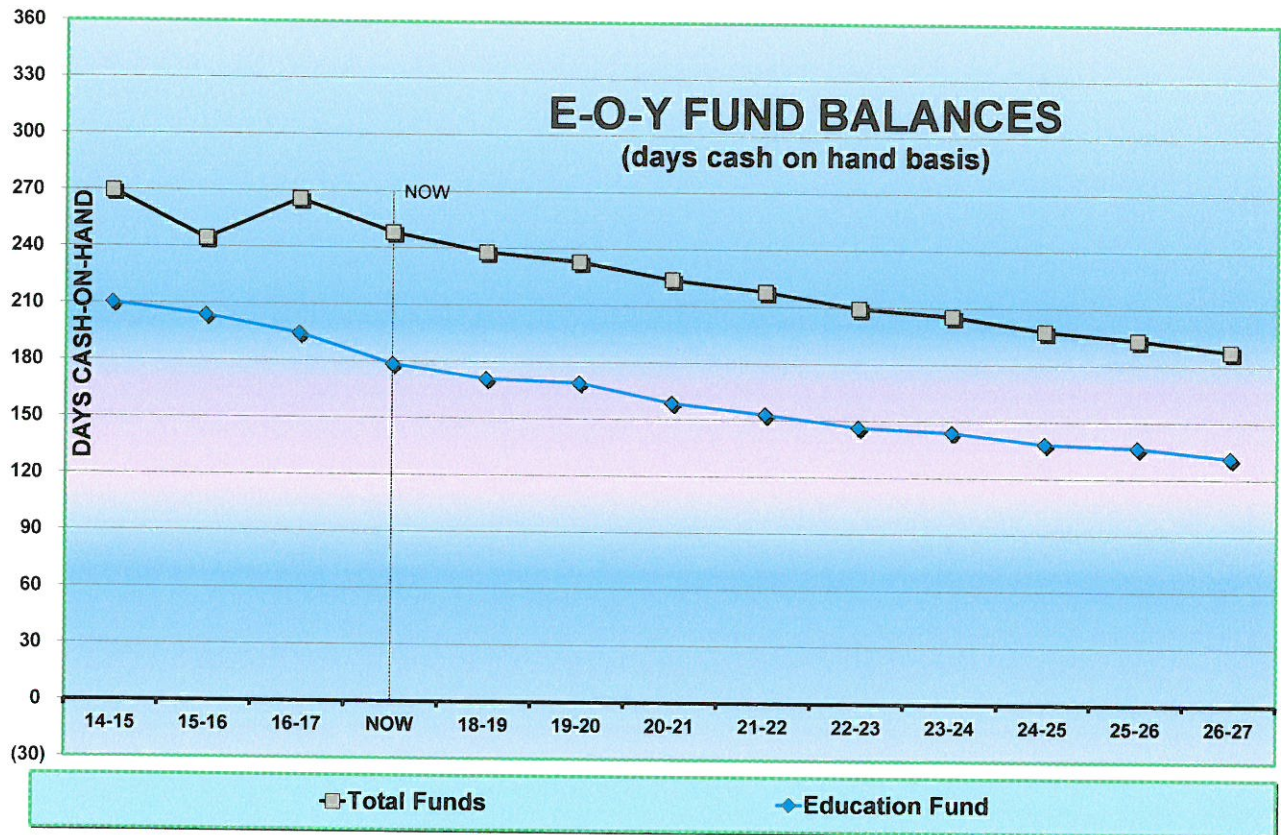
The smaller funds are all anchored with relatively solid fund balances as levies are assessed to meet their general obligations. The (blue) Other Funds primarily includes funds being held to meet ongoing debt payments. The larger Ed Fund usually absorbs any larger fluctuations.

Previous projections had suggested modest improvement in cash flows and fund balances. These projections, however, now include annual salary increases exceeding the CPI by about 0.7%, and an ongoing (and compounding) 7% annual increase in overall benefit obligations. These projections have now flattened somewhat as a result, but they remain remarkably stable.

Overall, as the previous cash flow chart would also suggest, Total Fund Balances (black) are expected to remain very stable while debt certificates are being paid from operating funds, and then begin a steady increase off the right side of this chart by about 2030 once debt is retired. In the meantime, there is considerable flexibility to adjust individual pieces somewhat by annual adjustments within the capped levy process as appropriate.

As a result of thoughtful strategic planning in recent years, the district has established a solid set of fund balances as an operating base. The district can now afford to watch and await developments on the horizon in the economy, in Springfield, and in particular on the local negotiating front. The following "Days-Cash" chart illustrates the available cushion better.

Spring 2018 Base Case

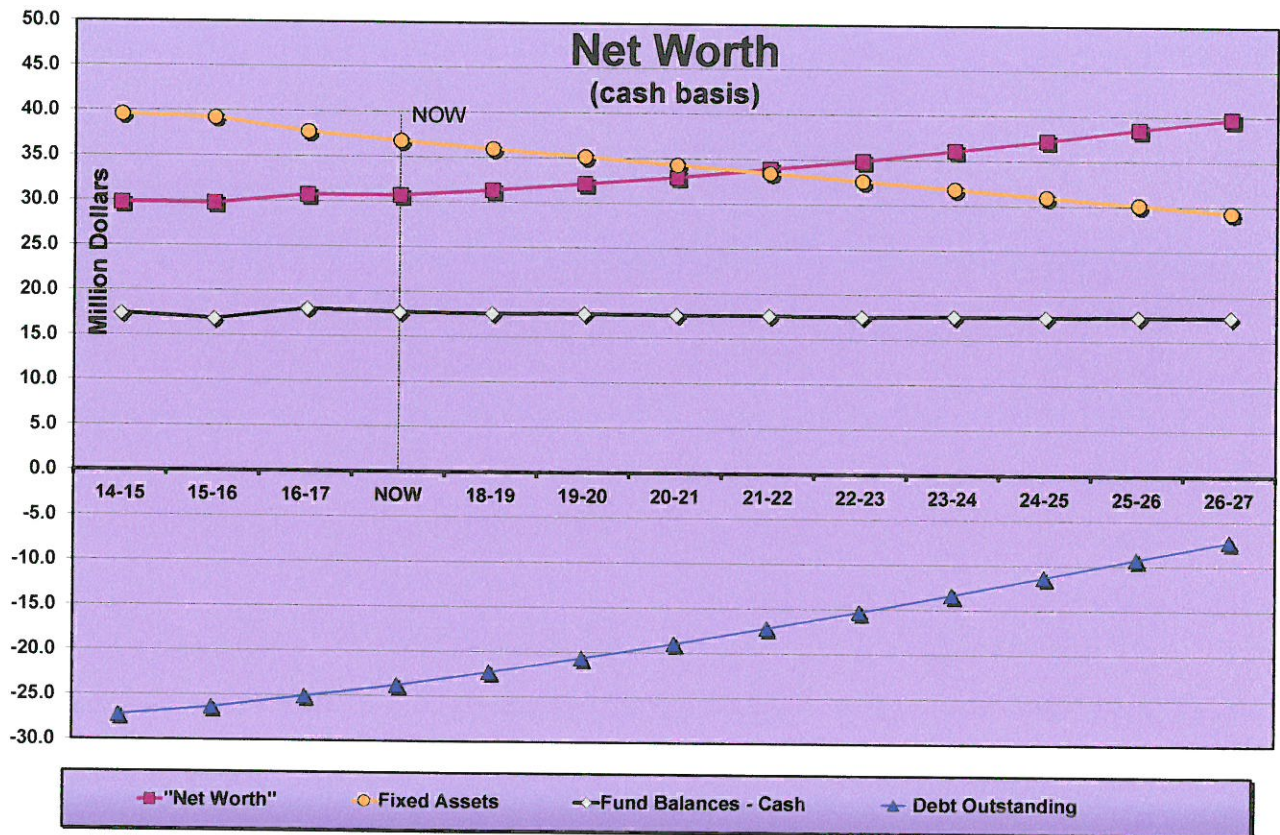


An alternative way to look at fund balances is on a "days-cash-on-hand" basis. As future fund balances were changing on the previous chart, so were expense obligations. This chart normalizes those effects and looks at how many days expenses can be paid without new cash infusions. Since tax receipts generally arrive in two major dispersements from the county, most districts target for a 3-6 month range in total (shaded rose color).

LaGrange has recently been comfortably above that nominal 3-6 month level in total and is projected to gradually slide into that range over the next decade. As noted previously, that can be expected to turn around dramatically a few years off the right side of this chart.

While the Ed Fund is also shown for reference, it is the total balance that is the key metric. Internal transfers or levy adjustments can generally be arranged in the interim without effecting total balances. In particular, the (black) Total Fund includes about a \$2 million balance in the Working Cash Fund that can be used to support The Ed Fund or others.

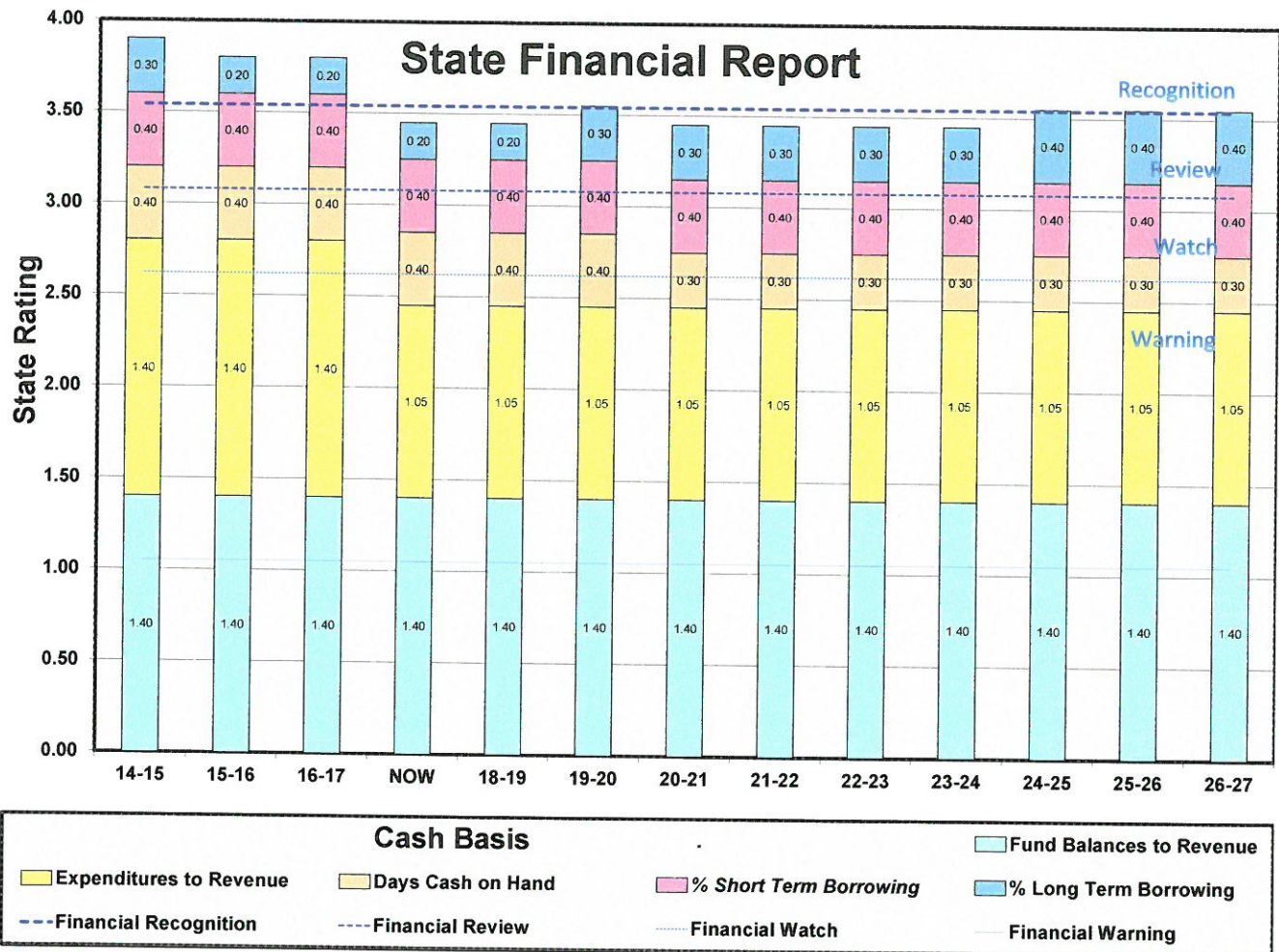
Spring 2018 Base Case



Although public entities are not strictly analogous to private industry, Net Worth is still a reasonable metric to assess general stewardship. In its simplest form Net Worth (maroon) is the sum of Fixed Assets (orange) plus Cash Balances (black) less Debt (blue).

Net Worth (maroon) increases modestly as declining debt tends to offset the slow depreciation of the major new fixed assets.

Spring 2018 Base Case



The state of Illinois of course has its own financial report card for school districts. The five parameters it measures result in a numerical rating from 0 to 4.

LaGrange's ratings remain in or near the top "recognition" category, limited only by the projection of very slight "overspending" (yellow) emerging in the near-term to support increasing payments on the debt certificates.

Sensitivities

A wide range of sensitivities was investigated in previous studies. The major *strategic* factors in LaGrange's future now is the ability to manage salary and particularly benefit escalations, with enrollment increases probably a fading concern. With the implementation of full-day kindergarten in place other educational options may now be considered. Other factors have also been accurately modeled, but generally have a smaller impact and can either be accommodated in ongoing operations or may even be masked by the larger issues.

Previous studies had suggested several possible long range scenarios, including that of accelerated debt reduction and expense control in different combinations. While that is still a long range option, it is clouded by the possibility of fallout from SB1947 or the possibility of a tax freeze being imposed by Springfield.

Useful Rules of Thumb

There are a variety of approximate relationships that can be used for “what-if” discussions of sensitivities. All are dependent to a degree on where and in which case they are applied and upon the timing, because of varying EAVs, CPIs, tax rates, and other factors. All can (and should) be verified in detail within the StratPlan model if they are under active consideration. Nonetheless, they are useful for “back of the envelope” type discussions. Some useful approximate rules of thumb – cast in the context of tax rate for comparison - are:

	<u>is roughly equivalent to</u>
• each 2.5% salary escalation (i.e. @ ~CPI)	7 cent tax rate
• each 7% benefit escalation (i.e. current assumption)	4 cent tax rate
• each 5% change in level of state/federal funding	2 cent tax rate
• each \$200k in ongoing expenses or revenue	3 cent tax rate
• each \$10 million in new EAV	4 cent tax rate
• each class size increment of +/-1	5 cent tax rate
• 2-year property tax freeze	14 cent tax rate

Or, when considering tax rates, referenda, tax cap, or tax freeze consequences,

each 14 cent tax rate increment is roughly equivalent to:

- 5% employment costs – salaries/benefits
- Class size increment of +/- 3
- \$1.1 million/yr tax revenue

Addendums to Current Base Case

\$5 million Set-Aside

Two-year Tax Freeze

SB1947 (separate study)

Strategic Set-Asides

The Strategy

To fund the needed repairs and upgrades of aging physical buildings in the last decade, LaGrange was able to secure needed “debt certificates” to complete the upgrades and modernize the district facilities.

Initial debt was about \$27M and payments were structured to be made from available operating cash instead of any tax levy for bonded debt. Payments (for principle and interest) were initially about \$1.6M/yr but with gradually escalating amounts that are now about \$2.8M/yr and scheduled to be in that range before eventual retirement in 2030.

Interest rates in these remaining years are in the range of 5-6% and contribute to the higher payment obligations. The structure of the loans allows a potential refinancing or restructuring in 2020-21. With the potential availability of “extra” cash, previous studies had explored the possible strategic option to refinance the loans when they become callable, to both pay down some of the debt early and save interest payments in addition.

LaGrange’s board has authorized the set-aside of \$5M of operating funds to be used to eventually pay down the debt as part of that potential refinancing when the debt becomes callable in 2020-21. That does not change the total amount of cash in the district’s bank account in the short term, but rather reallocates \$5M (primarily from the Ed Fund) to be set-aside in a separate fund to await the refinancing option.

If/when that option is exercised in 2020-21, operating funds *will* be reduced by \$5M. Outstanding debt will be reduced by that \$5M, but with the balance refinanced at hopefully lower interest rates. The savings are estimated to be in the \$2-3M range overall from a combination of the hoped-for lower rates on the remainder of the balances being refinanced, and the savings of 5-6% on the \$5M that have been eliminated. Overall savings will be subject to the actual timing and interest rates if/when the program is executed.

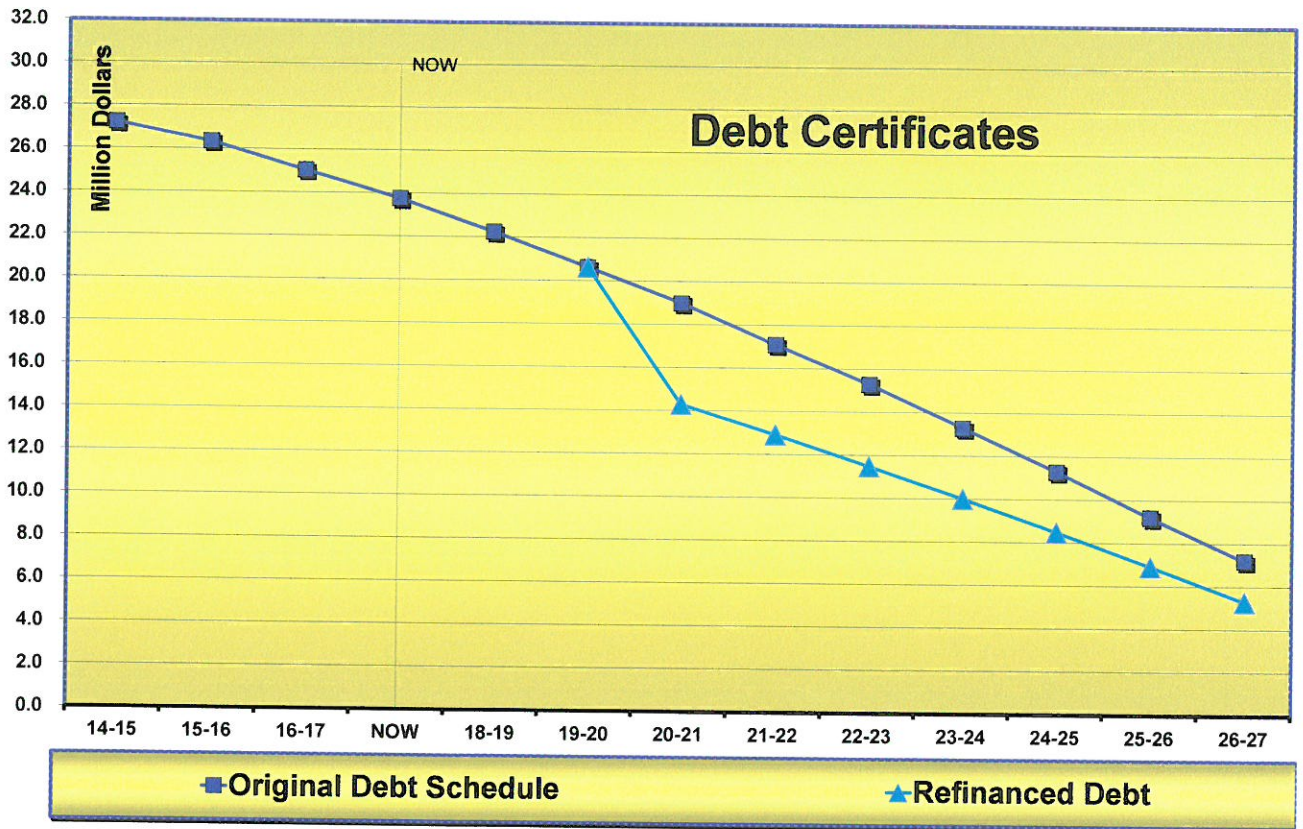
Total operating “days-cash-on-hand will drop from the current 6-9 month range into the 3-6 month range and stabilize there. Thereafter, cash flows and fund balances will actually outpace projections in the Current Base Case by approximately the amount of the interest savings that will have accrued.

As it stands, a nominal \$5M has been set aside, with the ability to scale back or abandon the strategy if necessary, but with the upside of expanding it if the opportunity does present itself – with no irreversible obligations in the meantime.

The debt will eventually be retired in 2030 in any case, but with lower operating balances being traded in the near term for interest savings and higher fund balances in the longer term if the strategy is implemented.

The following set of charts illustrates the potential results of this strategy.

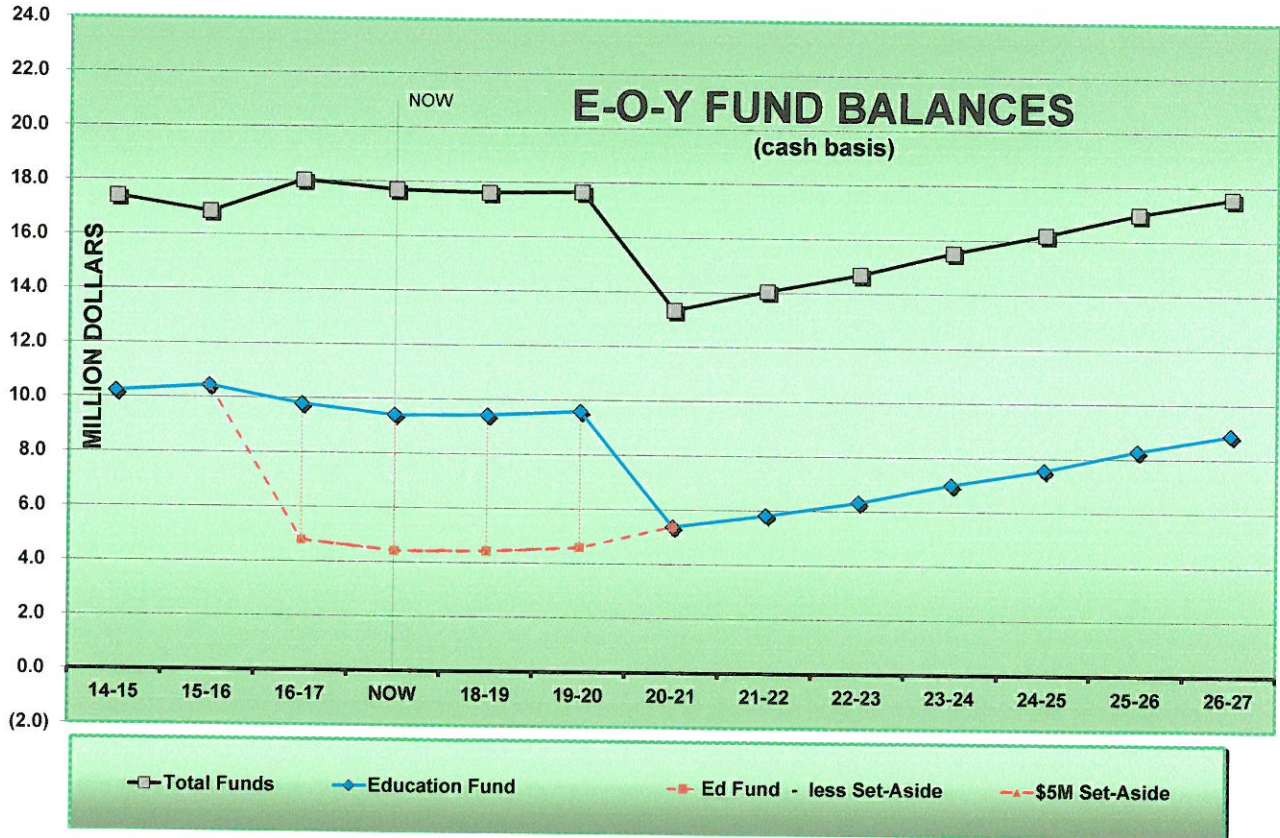
Strategic Set-Asides



Current bonds are callable in the 2021 time frame. If the \$5M "set-aside" is applied to reduce debt and refinance the remaining balances in 2021, the Original Debt Schedule (dark blue) would then be converted to a refinanced schedule (turquoise). Debt would still be scheduled to be retired by 2030 but payments would now be lower - and at a lower interest rate.

The savings from lower interest payments would be partially offset by then lower "Build America" federal subsidy payments, but with a net positive savings overall.

Strategic Set-Asides

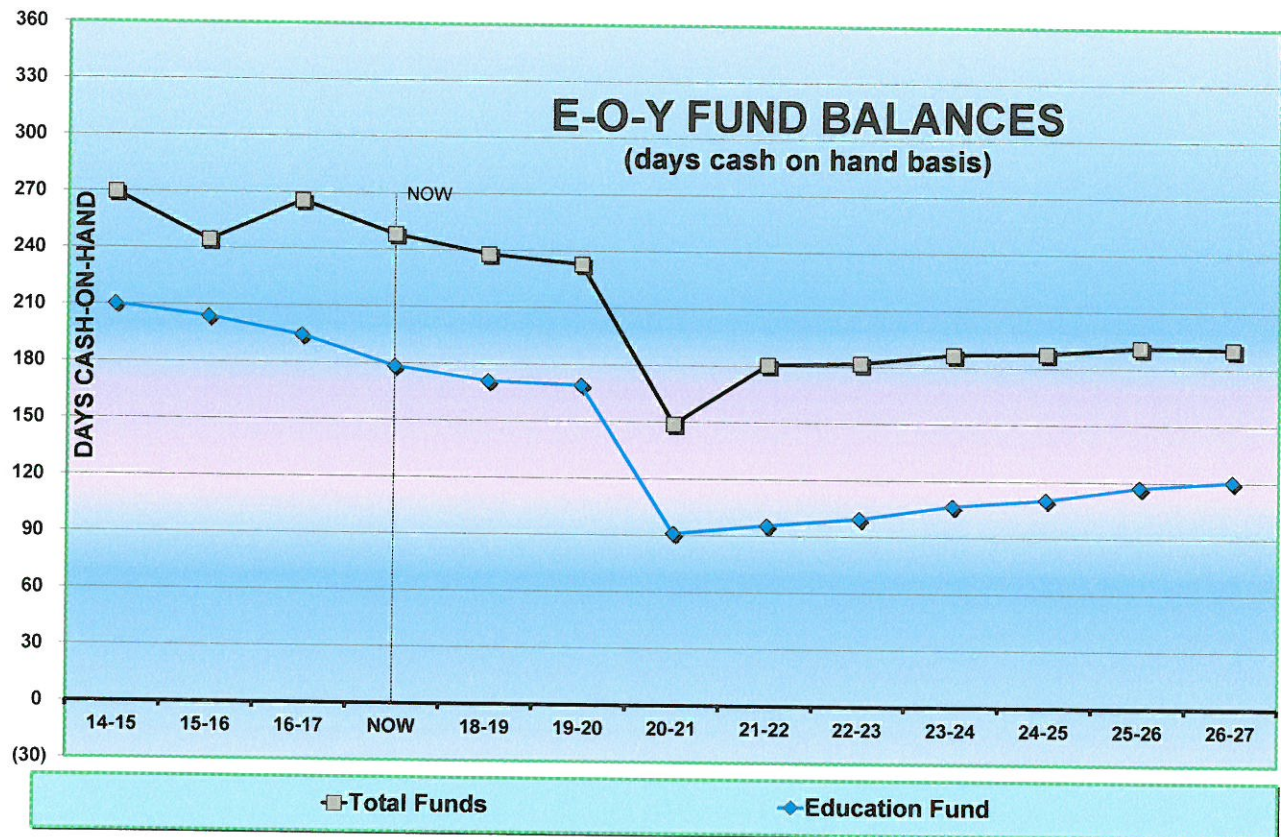


The District has previously earmarked \$5 million in fund balances (primarily in the Ed Fund) to be set aside for potential debt reduction and refinancing. Available Ed Fund balances (turquoise) would then be reduced by that \$5 million, as illustrated in (red), until the payments are actually made as anticipated in 2021. Total Fund Balances (black) and actual Ed Fund Balances (turquoise) would then both drop by that amount. Balances would then recover steadily as a result of the now lower required debt payments.

At the conclusion of the program when debt is actually retired in 2030 (off the right side of the chart), balances are actually higher than in the base case, by approximately the amount of interest savings accumulated over the retirement period.

Different amounts of set-asides are also possible and have been discussed with bond experts. Details of all of these will depend upon eventual timing and the rates in effect at the time, but the picture is expected to be essentially as reflected here.

Strategic Set-Asides



After the \$5 million "set-aside" payment is applied to debt reduction, days-cash-on-hand drops accordingly for both the Ed Fund and Total Funds. Both fall into what is generally considered the target 3-6 month (rose-colored) range, and then begin a very modest recovery.

Compare this to page 13 in the base case which showed slight declines. There is a very modest recovery here compared to the base case and continuing until the 2030 debt retirement - by approximately the amount of interest savings that have been accumulated over the decade.

In addition, as noted in the Current Base Case, a few years off the right side of the chart in 2030, a \$1.5 million surplus can be expected to emerge when debt payments are concluded, and a steady rebuilding of fund balances actually escalates.

A Tax Freeze

There apparently continue to be rumors in Springfield about imposing a local tax freeze of some sort even after the passage of SB1947. The version heard most frequently is a two-year freeze on local property taxes.

This is usually proposed as a tax protection of sorts for taxpayers, but in fact there is already an effective system in place. The Property Tax Extension Limitation Law (“PTELL”) limits any tax increases to the CPI – a reasonable approach that allows local districts to keep up with their ongoing inflationary costs, but no more. A freeze of course would eliminate that ability.

While the details of any proposed tax freeze are somewhat speculative, this example illustrates the effects if a two year tax freeze is imposed for FY20 and FY21. Property tax revenue is held constant for two years except for that generated by new property.

In practice that would reset the tax cap lower after two years by about 14 cents and result in a lower levy by about \$1 million/yr. Tax increases would then be allowed but from that lower tax cap starting point. While a \$1 million shortfall may be livable in any given year, the consequences of this proposal are likely to be long-lived. Under PTELL, a tax freeze will likely reset the tax cap at that **permanently** lower base levy. If it is implemented that way, that would result in a **permanent reduction of \$1 million/yr** less revenue. That is the projected proposal that is modeled here.

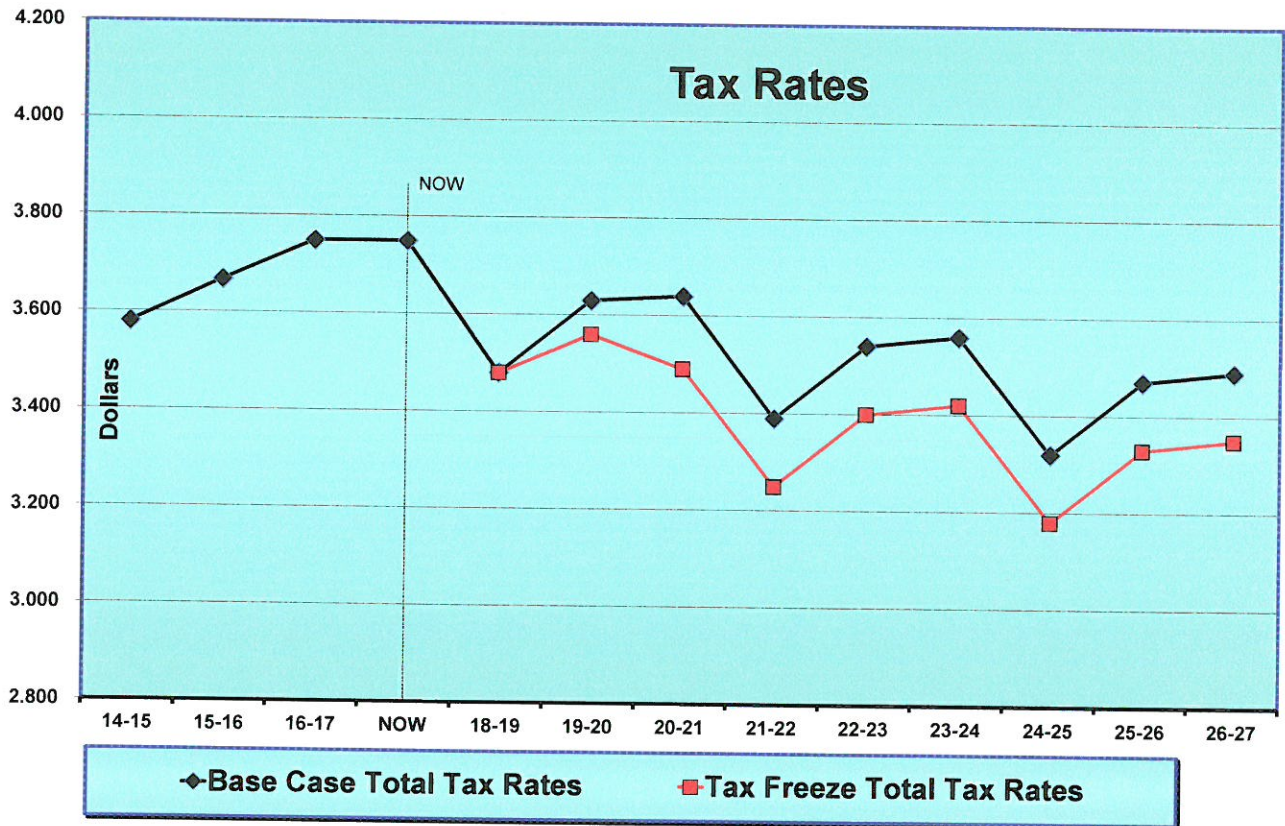
There is a simple way to view this as a first approximation. With an expected CPI of about 2.5%, a two year freeze would prohibit a normal 5% increase over that two year period. State another way that would create a 5% deficit in the normally expected tax revenue. In LaGrange’s case, a 5% shortfall in an expected \$22 million tax levy would be over \$1 million/yr.

That kind of permanent loss could be devastating for LaGrange, and for most other districts. The effects are illustrated on the following charts. The only way to recoup that kind of loss may be an eventual referendum to reset a livable tax rate.

Recognize, however, that this is currently only a best guess (albeit a possibly worst case scenario) at how such a program would be imposed.

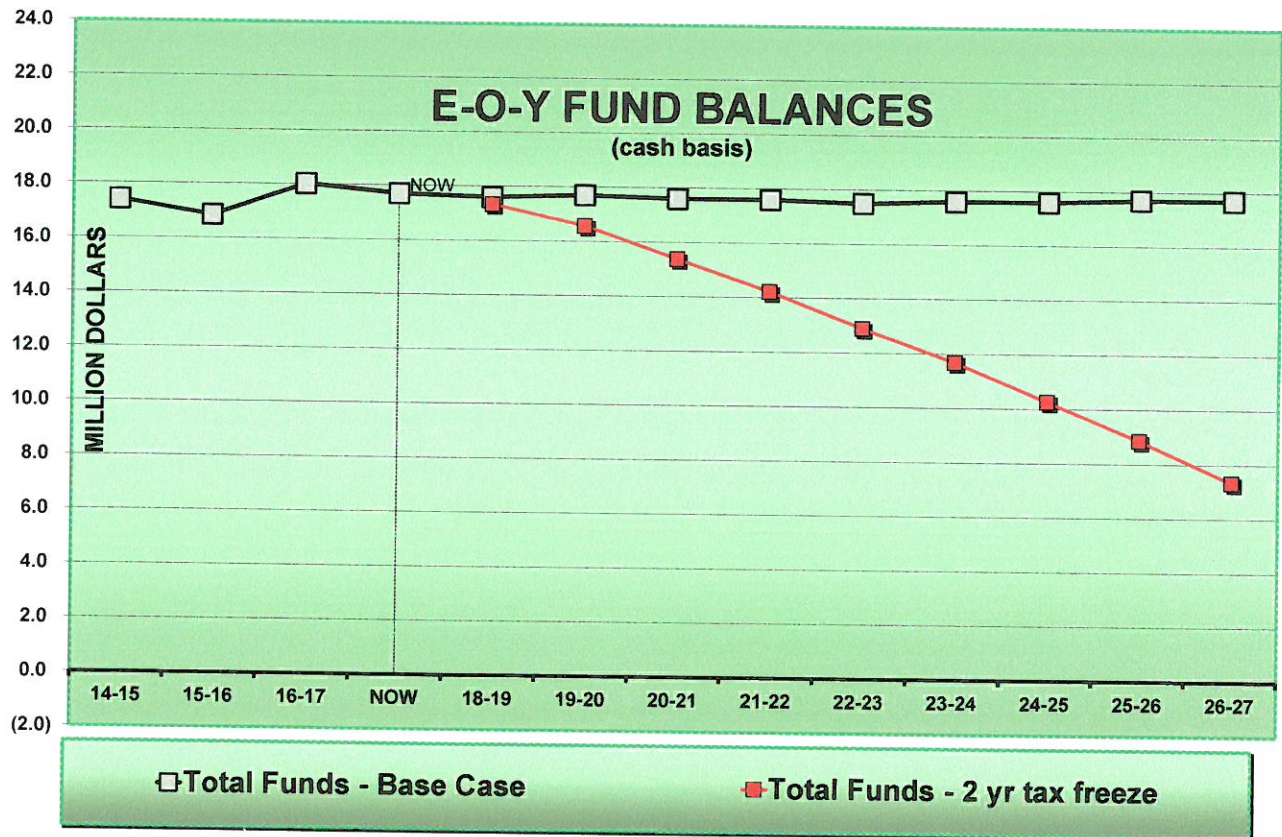
(There is also a cynical view in some circles that this is a thinly-veiled attempt by Springfield to further shift its funding obligations. Springfield poses as the white knight protecting the local taxpayers by imposing a freeze. Ultimately local districts, rather than Springfield, are then cast as the villain as they are forced to ask for tax increases to recover lost revenue?)

Two-year Tax Freeze



The practical effect of how a tax freeze may actually be implemented extends beyond the actual two year time frame. In addition to the two year freeze, it will likely reset the tax cap maximum at the ending 2 year level. Increases may then be allowed, but then from the new lower tax cap rate. That translates to about a 14 cent permanent reduction in this example.

Two-year Tax Freeze

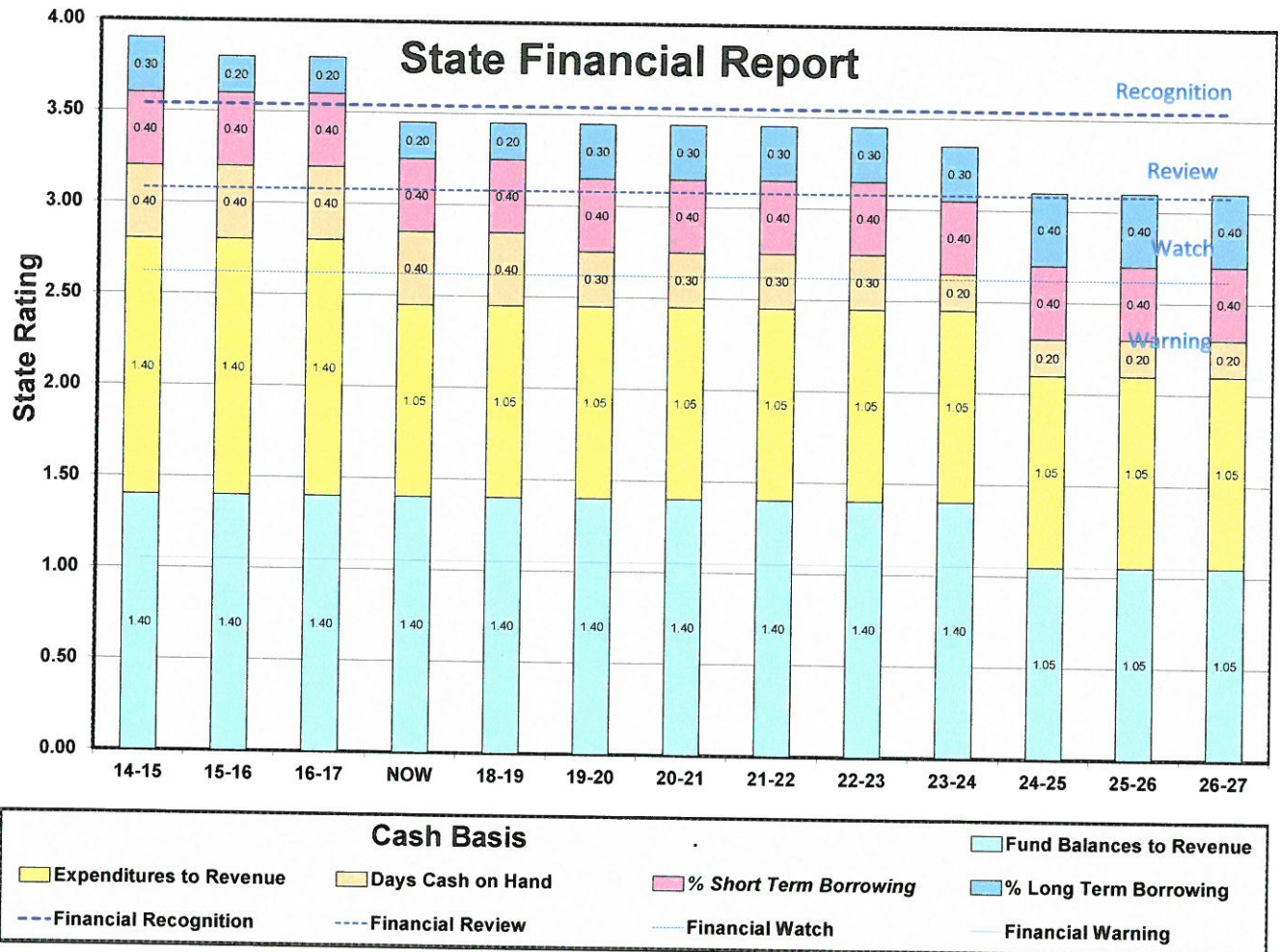


This chart illustrates the effects of a two year tax freeze in FY20 and FY21. Tax *revenue* is held constant for those two years except for that generated by new property.

The practical effect is that the tax cap is permanently reset by about 14 cents lower, resulting in a permanently lower levy of about \$1.1 million/yr. The black line repeats the stable fund balance projections from the base case while the red line demonstrates the effects of that annual loss in revenue. That steady slide would likely be devastating and non-recoverable without a referendum to reinstate the lost revenue.

The next chart in fact reflects how the state report card itself would then "grade" the results of such a program.

Two-year Tax Freeze



The state of Illinois of course has its own financial report card for school districts. The five parameters it measures result in a numerical rating from 0 to 4.

LaGrange's ratings would remain acceptable in the near term as its starting fund balances are healthy enough to absorb the cash flow deficit for a few years. Eventually, however, ratings would drop as fund balances evaporate (light blue) and cash flow deficits (yellow) continue or accelerate. The rating decline could be expected to continue in future years off the right side of this chart.