FCMAT

FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM

March 30, 2023

Honorable Joe Stephenshaw, Director
California Department of Finance
1021 O Street, Suite 3110
Sacramento, CA 95814

Honorable Philip Ting, Chair
California State Assembly Committee on Budget
1021 O Street, Suite 8230
Sacramento, CA 95814

Honorable Nancy Skinner, Chair
California State Senate Committee on Budget and Fiscal Review
State Capitol, Room 502
Sacramento, CA 95814

Dear Director Stephenshaw, Chairperson Ting and Committee Members, and Chairperson Skinner and Committee Members:

This letter is submitted for your consideration in accordance with the Fiscal Crisis and Management Assistance Team's (FCMAT's) responsibilities under Assembly Bill (AB) 181 Section 37, which added Section 42163 to the Education Code (EC), regarding the Inglewood Unified School District (district).

Background

In 2018, AB 1840 added EC 42161 to aid in the district's fiscal recovery. The relevant provisions of AB 1840 expired in fiscal year 2021-22. The relevant provisions of AB 181 are considered a modified extension of the basic concepts in the prior legislation. Education Code Section 42163(b) states:

> Beginning with the 2022-23 fiscal year, the annual Budget Act shall include an appropriation for the Inglewood Unified School District, if the district complies with the terms specified in sections (a) and (c), of up to 25 percent of the district's projected operating deficit, as determined by the County Office Fiscal Crisis and Management Assistance Team, with concurrence with the Department of Finance.

The intent of this letter is to provide you with FCMAT's findings regarding the district's achievement of the requirements in EC 42163(a) and (c), as of March 30, 2023.

Education Code Section 42163(a) states:

> By April 1, 2023, the Inglewood Unified School District shall do all of the following:

(1) Meet the requirements for qualified or positive certification for the school district's second interim report pursuant to Article 3 (commencing with Section 42130) of Chapter 6.

(2) Complete comprehensive operational reviews that compare the needs of the school district with similar school districts and provide data and recommendations regarding changes the school district can make to achieve fiscal sustainability.

(3) Undergo an on-time annual independent audit pursuant to Section 41020 that is free of material weaknesses and that includes an unqualified opinion. Furthermore, the audit shall be free from any material internal control findings.

Education Code Section 42163(b) specifies the amount of the additional apportionment available to the district, providing it meets all the requirements specified in sections (a) and (c), and will be addressed later in this letter.

Education Code Section 42163(c) states:

> Disbursement of funds specified in subdivision (b) shall be contingent on the Inglewood Unified School District's completion of activities specified in the prior year Budget Act to improve the school district's fiscal solvency. These activities may include, but are not limited to, all of the following:
>
> (1) Updated comprehensive operational reviews that compare the needs of the school district with similar school districts and provide data and recommendations regarding changes the school district can make to achieve fiscal sustainability, with a progress update on each of the recommendations.
>
> 2. Adoption and implementation of necessary budgetary solutions.
>
> 3. Completion and implementation of multiyear, fiscally solvent budgets and budget plans.
>
> 4. Qualification for positive certification pursuant to Article 3 (commencing with Section 42130) of Chapter 6.
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> 5. Sale or lease of surplus property.
>
> 6. Growth and maintenance of budgetary reserves.
>
> 7. Approval of school district budgets by the Los Angeles County Superintendent of Schools.
>
> 8. Prompt appointment following a competitive process of a permanent, experienced, and highly qualified chief business official for any vacancy of chief business official.

FCMAT Analysis and Findings Regarding EC 42163(a)(1)-(3)

(1) The district's 2022-23 second interim budget, approved by the county administrator on March 15, 2023, indicates a positive certification pursuant to Article 3 (commencing with Section 42130) of Chapter 6. As of the date of this letter, the Los Angeles County Office of Education (LACOE) had not yet finalized its review of or issued its letter regarding, the district's second interim financial report. Preliminary consultation with LACOE indicates an expectation that it will concur with the district's positive certification; however, as of the date of this letter an in-depth review had not been completed to a point where areas of concern could be articulated in a letter to the district. LACOE did confirm the positive

certification of the district's first interim report; however, several areas of concern were noted and addressed in LACOE's letter dated January 17, 2023 (Appendix A). The following is a summary of concerns identified by LACOE in its letter:

- The district included only cost savings and expenditure reductions totaling $3.08 million in the budget year of its multiyear projection (MYP); expenditure reductions identified in the district's updated Fiscal Stabilization Plan (FSP) for the two subsequent fiscal years were not included in the projection.
- The district projects an operating deficit of $4.16 million in its unrestricted general fund in the 2022-23 fiscal year. Deficits are also projected at $3.72 million and $10.82 million, respectively, in the two subsequent fiscal years of the MYP.
- The district's projected 3% reserve for economic uncertainties (REU) in the two subsequent fiscal years of the MYP is based on nonspecific and unallocated expenditure reductions of $2.11 million and $4.07 million, respectively. When these nonspecific reductions are removed from the projection, the projected REU for fiscal years 2023-24 and 2024-25 falls to 1.86 percent and (.51%), respectively.
- LACOE's letter states:

  > The District's 2022-23 First Interim Report reflects declining enrollment of 7,215 for 2022-23, 6,895 for 2023-24 and 6,681 for 2024-25, with projected funded three-year average daily attendance (FADA) of 7,521, 7,129, and 6,335, respectively. The estimated impact on the District's projected FADA reflects a two-year loss totaling 1,186 FADA, representing a 15.77 percent decrease from the District's 2022-23 FADA. The District's FADA is greater than its projected enrollment in 2022-23 and 2023-24 due to the District using an average of the prior three years' ADA to calculate its LCFF entitlement.

  LACOE's letter included the following list of requirements to address these deficiencies:

  - [The district is required to:] ...provide an update on the Board-approved FSP, with the 2022-23 second interim report, due to our office by March 17, 2023. The FSP update must include the implementation status of the planned reductions and alternative options for contingent expenditure reductions and revenue enhancements.
  - We recommend the District monitor the causes for deficit spending in order to prevent further erosion of the fund balance.
  - We are requiring the District update its Board-approved Fiscal Stabilization Plan (FSP), and reflect the identified and implemented cost savings and expenditure reductions in the 2022-23 Second Interim Report and multi-year projections, due to our office by March 17, 2023. The updated FSP should also include identified actions on how the District plans to meet the minimum required REUs if the FSP reductions don't materialize.
  - ...we recommend that the District carefully monitor its enrollment and attendance trends, and adjust financial projections for the current and subsequent fiscal years accordingly to reflect the resulting impact. Staffing needs and facilities planning should also be assessed and adjusted based on the projected rate of decline in enrollment.

The district's 2022-23 second interim budget report (Appendix B) and multiyear projection (MYP) (Appendix C) indicate a favorable shift in its fiscal position compared to 2022-23 first interim. Although on the surface the combination of the unrestricted and restricted resources presented at second interim suggest a degradation of the district's overall fiscal position, evaluating the unrestricted general fund separately from the restricted general fund indicates a favorable change in fiscal position.

Net Increase/(Decreases) in Fund Balance, Combined General Fund

	First Interim MYP		
	2022-23	2023-24	2024-25
Unrestricted	(4,159,472.00)	(3,715,714.00)	(10,822,948.00)
Restricted	40,429,167.00	(31,541,562.00)	(16,294,147.00)
	36,269,695.00	(35,257,276.00)	(27,117,095.00)
	Second Interim MYP		
	2022-23	2023-24	2024-25
Unrestricted	3,650,754.00	1,553,503.33	(7,988,820.13)
Restricted	36,434,522.00	(17,612,436.59)	3,562,639.79
	40,085,276.00	(16,058,933.26)	(4,426,180.34)
Increase/(Decrease)	3,815,581.00	19,198,342.74	22,690,914.66

The district projects that it will eliminate projected deficits in the current and first subsequent fiscal years and reduce the projected deficit in the second subsequent fiscal year. This is reflective of an improved fiscal position in the unrestricted general fund in each fiscal year of the projection compared to that projected at first interim.

Net Increase/(Decrease) in Fund Balance, Unrestricted General Fund MYP

	2022-23	2023-24	2024-25
First Interim	(4,159,472.00)	(3,715,714.00)	(10,822,948.00)
Second Interim	3,650,754.00	1,553,503.33	(7,988,820.13)
Increase/(Decrease)	7,810,226.00	5,269,217.33	2,834,127.87

Adjustments to projected revenues and expenses in the district's restricted general fund presented at second interim are indicative of expending program funds carried over from each prior fiscal year and a balancing of program resources in the second subsequent fiscal year. This is common and expected because program funding is seldom fully exhausted in the current budget year. Carryover funding is commonly spent in the first subsequent fiscal year, resulting in a natural deficit that should be and most commonly is eliminated by a reduction of projected expenditures in the second subsequent fiscal year.

Net Increase/(Decrease) in Fund Balance, Restricted General Fund MYP

	2022-23	2023-24	2024-25
First Interim	40,429,167.00	(31,541,562.00)	(16,294,147.00)
Second Interim	36,434,522.00	(17,612,436.59)	3,562,639.79
Increase/(Decrease)	(3,994,645.00)	13,929,125.41	19,856,786.79

(2) There is no indication that the district completed any new comprehensive operational reviews or evidence that updates to the reviews performed in 2019 have taken place to demonstrate that findings and recommendations have been or are actively being addressed.

(3) The district's 2021-22 independent audit report (Appendix D) was accepted by the district's county administrator on January 11, 2023. The 2021-22 Independent Audit Report Summary of Auditors' Results (page 82) indicates that the type of auditors' report issued was qualified. However, **material weakness(es) in internal control over financial reporting were identified**. Furthermore, the 2021-22 Independent Auditors' Report on Internal Control Over Financial Reporting And On Compliance and Other Matters Based On An Audit of Financial Statements Performed in Accordance With Government Auditing Standards For The Inglewood Unified School District (page 73) cites **identification of deficiencies in internal control that were considered to be material weaknesses** and significant deficiencies. The report goes on to state the following:

> A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, misstatements on a timely basis. A material weakness is a deficiency, or a combination of deficiencies, in internal control, such that there is a reasonable possibility that a material misstatement of the district's financial statements will not be prevented, or detected and corrected on a timely basis. **We consider the deficiencies described in the accompanying schedule of findings and questioned costs as Findings 2022-001 through 2022-004 to be material weaknesses**." [emphasis added]

Details of each finding containing deficiencies in internal control that were considered to be material weakness are found on pages 83-84 and 87 of the audit report attached in Appendix B, and are summarized as follows:

- 2022-001 (repeat audit finding): The district does not maintain adequate source records to support that the district has ownership rights to buildings, land, and land improvements, or that the balances reported as assets reflect historical costs. The district's increases and decreases to capital assets for the 2021-22 fiscal year could not be substantiated because the district did not maintain schedules of construction projects in progress. The district did not maintain adequate records to calculate depreciation of fixed assets. The district has for several years lacked controls to ensure accurate records of additions, disposals and deprecation.
- 2022-002 (partial repeat audit finding): The district failed to reconcile its payroll accounts, which has resulted in the district not recording other post-employment benefits (OPEB) in its year-end financials. In addition, $4,372,129 in accounts payable liabilities could not be substantiated and needed to be written off. As a result, the district's year-end liabilities are subject to misstatement.
- 2022-003 (partial repeat audit finding): The district lacks oversight of its associated student body (ASB) accounts. The district is unable to determine if all ASB accounts have been properly reported, creating a risk that ASB accounts could be misstated and that misstatement could remain undetected. The lack of internal controls and oversight by the district office could lead to loss or misappropriation of ASB assets.

- 2022-004 (partial repeat audit finding): The district was unable to provide documents to verify some entitlement and grant allocations. In addition, $1,759,9231 in invalid receivables that were rolled over from the prior fiscal year were identified and could not be substantiated. As a result, the district's year-end assets are subject to misstatement.

The district's auditors presented the report at the board's January 11, 2023 meeting and spoke about their report on the audit of financial statements. The number of audit findings increased from eight in fiscal year 2020-21 to 17 in fiscal year 2021-22, seven of which were repeated or partially repeated findings from fiscal year 2020-21.

a. The auditor issued a qualified opinion on the district's financial statements. The auditor cited an inability to obtain sufficient audit evidence to support the amounts at which the capital assets and related accumulated depreciation are reported in the district's financial statements. Because the district's accounting records were inadequate and certain supporting documents were not available, the qualified opinion was assigned.

b. The auditor issued an unmodified opinion (clean opinion) regarding compliance for federal programs and internal controls over compliance because there were no significant deficiencies or material weaknesses related to federal compliance.

c. The auditor issued a qualified opinion on the district's compliance with state programs and **internal controls over compliance**. The auditor cited findings in the following areas:

    i. Attendance

    ii. Instructional Time

    iii. School Accountability Report Cards

    iv. Expanded Learning Opportunities (ELO) Grant

    v. Immunizations

    vi. Mode of Instruction (Charter School)

    vii. Independent Study Ratio (District and Charter School)

Findings

The district did not meet the requirements listed in EC 42163(a)(2) or (3). The district's 2021-22 independent audit was not free from material weaknesses, and it cites material internal control findings. Furthermore, there is no indication that the district completed any new comprehensive operational reviews that compare its needs with those of similar school districts and provide data and recommendations regarding changes the district can make to achieve fiscal sustainability.

FCMAT Analysis and Findings Regarding Activities Defined in EC 42163(c)

Because the district did not meet the requirements listed in subdivision (a) of EC 42163, FCMAT and the county administrator mutually agreed that further efforts to confirm compliance with the requirements defined in EC 42163(c) would place an unnecessary burden on district staff.

Conclusion

Education Code Section 42163(b) provides for an additional apportionment of state funds to assist the district in achieving fiscal solvency "...if the school district **complies with the terms specified in subdivisions (a) and (c)...**" [emphasis added]

Although the district met the requirements for qualified or positive certification for its second interim report, there is no indication that the district completed any new comprehensive operational reviews or any updates to address the recommendations made in those prepared in 2019. Furthermore, although the district's 2021-22 independent audit includes an unqualified opinion, it was **not** free of material weaknesses, nor was it free of any material internal control findings.

FCMAT's evaluation of conditions and criteria outlined in EC 42163(a) confirm that the Inglewood Unified School District did not meet the requirements for additional apportionment specified in EC 42163(b).

Education Code Section 42163(e) requires that the activities identified in subdivision (c) be determined in the annual Budget Act based on joint recommendations from FCMAT and the Los Angeles County Superintendent of Schools. FCMAT consulted with the county administrator and the county superintendent, and all parties agreed to recommended that Section 42163(c) be changed to add specificity to read as follows:

> (c) Disbursement of funds specified in subdivision (b) shall be contingent on the Inglewood Unified School District's progress toward completion of activities specified in the prior year Budget Act to improve the school district's fiscal solvency. These activities shall include, but are not limited to, all of the following:

1. Obtaining and/or developing updated comprehensive operational reviews that compare the needs and allocation of resources of the school district with similar school districts of similar size and provide data and recommendations regarding changes the school district can make to achieve fiscal sustainability. Areas for consideration **shall** include:

    a. Enrollment, staffing and compensation

    b. Administration, departmental organization and staffing

    c. Facility use for educational purposes

    Additional areas for consideration **may** include:

    a. Special education program

    b. Transportation program

    c. Budget development and fiscal management – processes and procedures

    d. Fixed Asset/Inventory and valuation of assets

    e. Associated Student body fiscal management – processes and procedures

2. Establishing, implementing, and maintaining detailed budget reductions identified in the district's fiscal recovery plan.

3. Completion and implementation of multiyear, fiscally solvent budgets that include detailed budget reductions identified in the district's fiscal recovery plan.

4. Qualification for positive budget certification pursuant to Article 3 (commencing with Section 42130) of Chapter 6.

5. Reallocation/rightsizing of district facilities, including sale or lease of surplus property.
6. Growth and maintenance of budgetary reserves at or greater than the required minimum.
7. Approval of school district budgets by the Los Angeles County Superintendent of Schools.
8. Prompt appointment following a competitive process for any cabinet-level vacancy.
9. Progress in resolving all findings identified in the prior year audit report and implementing practices necessary to prevent repeat audit findings in each area noted.
10. Reducing the number of comprehensive review standards (see EC 41327.1) with a **score** lower than the minimum threshold of four (measured by an increase in the individual standard **score** from lower than four to four or higher) by at least 50 percent during each comprehensive review cycle.
11. Reaching the comprehensive review minimum average score of six in the operational areas of 1) personnel management and 2) facilities management by July 2024.
12. Preparation of a detailed fiscal recovery plan identifying specific expenditure reductions supported by documents and/or estimated cost savings calculations. The detailed fiscal recovery plan and documentary support shall be updated and presented in conjunction with each fiscal reporting period. Only those proposed reductions that are certain to take place shall be included in the district's multiyear financial projections. The impact of any other potential cost saving measure or revenue increases that may be subject to negotiation, contractual commitment, collective bargaining, or other form of official notice shall be presented only in an alternative model to demonstrate potential impact.

Respectfully,

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FCMAT Intervention Specialist

C: Debra Duardo, Ed.D., Los Angeles County Superintendent of Schools

Brooks Allen, Executive Director, California State Board of Education

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Abel Guillen, Deputy Superintendent, California Department of Education

Elizabeth Dearstyne, Director, School Fiscal Services Division, California Department of Education

James Morris, Ed.D., county administrator, Inglewood Unified School District

Appendices

Click on any appendix title to view and download that appendix.

Appendix A — Inglewood USD 2022-23 First Interim Letter from LACOE

Appendix B — Inglewood USD 2022-23 Second Interim General Fund Report Form 01

Appendix C — Inglewood USD 2022-23 Second Interim MYP

Appendix D — Inglewood USD 2021-22 Audit Report