FCMAT
FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM
CSIS California School Information Services

Sweetwater Union High School District

Fiscal Health Risk Analysis

December 17, 2018

Michael H. Fine
Chief Executive Officer

Contents

About FCMAT

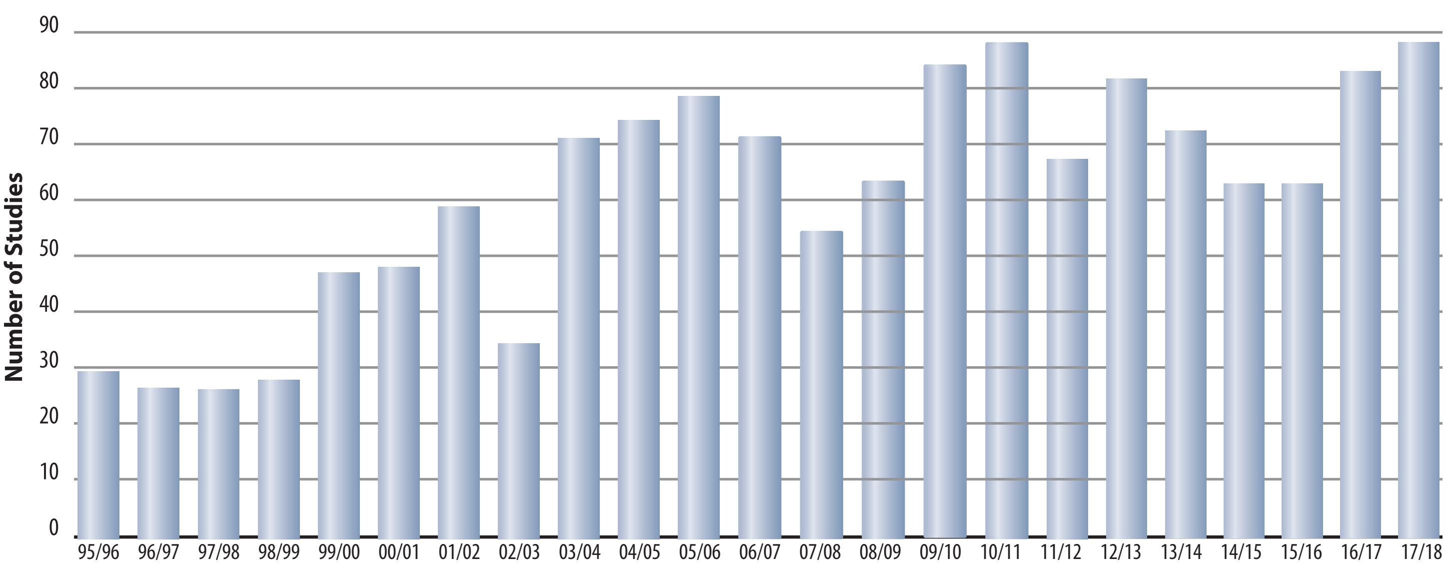
FCMAT's primary mission is to assist California's local K-14 educational agencies to identify, prevent, and resolve financial, human resources and data management challenges. FCMAT provides fiscal and data management assistance, professional development training, product development and other related school business and data services. FCMAT's fiscal and management assistance services are used not just to help avert fiscal crisis, but to promote sound financial practices, support the training and development of chief business officials and help to create efficient organizational operations. FCMAT's data management services are used to help local educational agencies (LEAs) meet state reporting responsibilities, improve data quality, and inform instructional program decisions.

FCMAT may be requested to provide fiscal crisis or management assistance by a school district, charter school, community college, county office of education, the state Superintendent of Public Instruction, or the Legislature.

When a request or assignment is received, FCMAT assembles a study team that works closely with the LEA to define the scope of work, conduct on-site fieldwork and provide a written report with findings and recommendations to help resolve issues, overcome challenges and plan for the future.

FCMAT has continued to make adjustments in the types of support provided based on the changing dynamics of K-14 LEAs and the implementation of major educational reforms.

Studies by Fiscal Year



FCMAT also develops and provides numerous publications, software tools, workshops and professional development opportunities to help LEAs operate more effectively and fulfill their fiscal oversight and data management responsibilities. The California School Information Services (CSIS) division of FCMAT assists the California Department of Education with the implementation of the California Longitudinal Pupil Achievement Data System (CALPADS). CSIS also hosts and maintains the Ed-Data website (www.ed-data.org) and provides technical expertise to the Ed-Data partnership: the California Department of Education, EdSource and FCMAT.

FCMAT was created by Assembly Bill (AB) 1200 in 1992 to assist LEAs to meet and sustain their financial obligations. AB 107 in 1997 charged FCMAT with responsibility for CSIS and its statewide data management work. AB 1115 in 1999 codified CSIS' mission.

AB 1200 is also a statewide plan for county offices of education and school districts to work together locally to improve fiscal procedures and accountability standards. AB 2756 (2004) provides specific responsibilities to FCMAT with regard to districts that have received emergency state loans.

In January 2006, Senate Bill 430 (charter schools) and AB 1366 (community colleges) became law and expanded FCMAT's services to those types of LEAs.

On September 17, 2018 AB 1840 became effective. This legislation changed how fiscally insolvent districts are administered once an emergency appropriation has been made, shifting the former state-centric system to be more consistent with the principles of local control, and providing new responsibilities to FCMAT associated with the process.

Since 1992, FCMAT has been engaged to perform more than 1,000 reviews for LEAs, including school districts, county offices of education, charter schools and community colleges. The Kern County Superintendent of Schools is the administrative agent for FCMAT. The team is led by Michael H. Fine, Chief Executive Officer, with funding derived through appropriations in the state budget and a modest fee schedule for charges to requesting agencies.

Introduction

Historically, FCMAT has not engaged directly with school districts showing distress until it has been invited to do so by the district or the county superintendent. The state's 2018-19 Budget Act provides for FCMAT to offer "more proactive and preventive services to fiscally distressed school districts by automatically engaging with a district under the following conditions:

- Disapproved budget
- Negative interim report certification
- Three consecutive qualified interim report certifications
- Downgrade of an interim certification by the county superintendent
- "Lack of going concern" designation

Under these conditions, FCMAT will perform a fiscal health risk analysis to determine the level of risk for insolvency. FCMAT has updated its Fiscal Health Risk Analysis (FHRA) tool that weights each question based on high, medium and low risk. The analysis will not be performed more than once in a 12-month period per district, and the engagement will be coordinated with the county superintendent and build on their oversight process and activities already in place per AB 1200. There is no cost to the county superintendent or to the district for the analysis.

Study Guidelines

FCMAT entered into the study agreement with the Sweetwater Union High School District on September 27, 2018.

FCMAT visited the district on October 17-19, 2018 to conduct interviews, collect data and review documents. This report is the result of those activities.

FCMAT's reports focus on systems and processes that may need improvement. Those that may be functioning well are generally not commented on in FCMAT's reports. In writing its reports, FCMAT uses the Associated Press Stylebook, a comprehensive guide to usage and accepted style that emphasizes conciseness and clarity. In addition, this guide emphasizes plain language, discourages the use of jargon and capitalizes relatively few terms.

Study Team

The team was composed of the following members:

Deborah Deal
FCMAT Intervention Specialist
Los Angeles, CA

Colleen Patterson
FCMAT Consultant
San Clemente, CA

Scott Sexsmith
FCMAT Intervention Specialist
Auburn, CA

Jeff Potter
FCMAT Intervention Specialist
Dublin, CA

Laura Haywood
FCMAT Technical Writer
Bakersfield, CA

Each team member reviewed the draft report to confirm accuracy and achieve consensus on the final recommendations.

Fiscal Health Risk Analysis

For K-12 Local Educational Agencies

FCMAT
FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM
CSIS California School Information Services

The Fiscal Crisis and Management Assistance Team (FCMAT) has developed the Fiscal Health Risk Analysis (FHRA) as a tool to help evaluate a school district's fiscal health and risk of insolvency in the current and two subsequent fiscal years.

The FHRA includes 20 sections, each containing specific questions. Each section and specific question is included based on FCMAT's work since the inception of AB 1200; they are the common indicators of risk or potential insolvency for districts that have neared insolvency and needed assistance from outside agencies. Each section of this analysis is critical to an organization, and lack of attention to these critical areas will eventually lead to financial insolvency and loss of local control.

The greater the number of "no" answers to the questions in the analysis, the higher the score, which points to a greater potential risk of insolvency or fiscal issues for the district. Not all sections in the analysis, and not all questions within each section, carry equal weight; some are deemed more important and thus count more heavily toward or against a district's fiscal stability percentage. For this tool, 100% is the highest total risk that can be scored. A "yes" or "n/a" answer is assigned a score of 0, so the risk percentage increases only with a "no" answer.

To help the district, narratives are included for responses that are marked as "no" so the district can better understand the reason for the response and actions that may be needed to obtain a "yes" answer.

Identifying issues early is the key to maintaining fiscal health. Diligent planning will enable a district to better understand its financial objectives and strategies to sustain a high level of fiscal efficiency and overall solvency. A district should consider completing the FHRA annually to assess its own fiscal health risk and progress over time.

District or LEA Name: Sweetwater Union High School District

Dates of Fieldwork: October 17-19, 2018

Annual Independent Audit Report

	Yes	No	N/A
• Can the district correct the audit findings without affecting its fiscal health (i.e., no material apportionment or internal control findings)?	☐	☒	☐

Based on the 2016-17 annual audit, the district had a material audit adjustment relating to the understatement of accounts payable equal to $3.2 million. Auditor calculations and adjustments to the 2017-18 audit reflect a local control funding formula (LCFF) recalculation that will result in reductions that will further deteriorate the district's financial position. (See LCFF discussion below.)

	Yes	No	N/A
• Has the independent audit report been completed and presented to the board within the statutory timeline?	☐	☒	☐

The 2016-17 annual independent audit was due by December 15, 2017. Statutory deadlines require the board to accept the audit by January 31, 2018. The audit report was dated February 22, 2018. FCMAT acknowledges that the district requested and received an extension from the State Controller's Office.

	Yes	No	N/A
• Did the district receive an independent audit report without material findings?	☒	☐	☐
• Has the district corrected all audit findings?	☒	☐	☐
• Has the district had the same audit firm for at least three years?	☒	☐	☐

Budget Development and Adoption

	Yes	No	N/A
• Does the district develop and use written budget assumptions and projections that are reasonable, are aligned with the Common Message or county office of education instructions, and have been clearly articulated?	☒	☐	☐

- Does the district use a budget development method other than a rollover budget, and if so, does that method include tasks such as review of prior year estimated actuals by major object code and removal of one-time revenues and expenses? . . . . ☐ ☒ ☐

  The district's past practice has been to roll over the prior year budget. During the last budget cycle, several negative budget entries were entered at estimated actuals without explanation. In addition, the assumptions used in the 2018-19 adopted budget were not reasonable.

- Does the district use position control data for budget development? . . . . ☐ ☒ ☐

  The district uses a Position Action Memorandum form, which results in a subsequent Position Action Request for additions and changes to personnel. However, there is no direct, automated link between the form or process and the budget. According to management in the human resources department, open positions are determined by viewing a list of currently posted positions reflected in manually prepared spreadsheets that list employees, including programmatic relationships, gross pay, benefit elections, withholdings and stipends.

- Is the Local Control Funding Formula (LCFF) calculated correctly? . . . . ☐ ☒ ☐

  LCFF calculations were provided by the district for the prior three years along with adjusting entries prepared by the independent auditors. These calculations compared the lump sum total district general ledger postings to the independent auditor's calculations for 2017-18.

  LCFF variances noted by the auditors are as follows:

  1. *Fiscal year 2015-16, district revenues are overestimated by $1,549,669.97,*
  2. *Fiscal year 2016-17, district revenues are underestimated by $2,553,536.88,*
  3. *Fiscal year 2017-18, district revenues are overestimated by $3,641,955.42. In addition, the auditor extrapolated 895 nonqualifying unduplicated pupils, resulting in a reduction of $720,342.42, for a total overestimated LCFF revenue of $4,361,995.42.*

  FCMAT used auditor adjusted calculations for fiscal years 2015-16, 2016-17 and 2017-18 to recalculate the LCFF funded revenue for the 2018-19 fiscal year based on prior year adjusted ADA.

  Based on the recalculation, funded 2018-19 LCFF revenue is $380,098,966. The district submitted its revised October 8, 2018 budget showing $386,173,688, which is overestimated by $6,074,722.

- Has the district's budget been approved unconditionally by its county office of education in the current and two prior fiscal years? . . . . ☐ ☒ ☐

  While the district received approved budgets in 2016-17 and 2017-18, the district's 2018-19 adopted budget was not approved. The district submitted a revised budget dated October 8, 2018, which the county office subsequently approved.

  Following fieldwork, San Diego COE appointed a fiscal advisor to assist in the fiscal recovery efforts.

- Does the budget development process include input from staff, administrators, the governing board, the community, and the budget advisory committee (if there is one)? . . ☐ ☒ ☐

  The district does not have a budget advisory committee. Interviews reveal that the 2018-19 adopted budget had limited input from site and department administrators and was prepared by the director of fiscal services and chief financial officer, although the October 8 budget revision did include more stakeholder input.

FCMAT found that more than $9 million included in the original Special Education Department budget at estimated actuals was reduced by the former director of fiscal services prior to board adoption, some of which was subsequently restored by the new chief financial officer in September 2018.

Sweetwater UHSD is a year-round school district. When the original adopted budget was not approved by San Diego COE, many administrators were off duty and did not participate in the 2018-19 Budget Solutions plan. A review of the detail budget entries that support the October 8, 2018 revised budget documentation shows across the board percentage reductions, such as 10% cuts to operating budgets, with no evidence of stakeholder input. As part of the 2018-19 Budget Solutions plan, many expenses approved by the LCAP committee and board to be paid by supplemental/concentration dollars were realigned to other sources of funding, and many of the expenses previously approved were severely reduced.

- Are clear processes and policies in place to ensure that the district's Local Control and Accountability Plan (LCAP) and budget are aligned with one another? . . . . ☐ ☒ ☐

FCMAT was not provided a document demonstrating that the LCAP and the budget are aligned. The 2018-19 LCAP does not show increases for step and column movements or health insurance in base salaries and benefits between 2018-19 and 2019-20 to match the district's multiyear budget.

The 2018-19 Budget Solutions that accompany the revised October 8, 2018 budget revision include substantial reductions in action items that support the LCAP goals paid from supplemental and concentration grant funds. The district should consider whether a revision to the LCAP is necessary, as there may be material changes to the initially approved plan resulting from the October 8 budget revision. If deemed necessary, a revised LCAP would be created through a public engagement process and subsequent governing board approval and county office approval.

- When appropriate, does the district budget and expend restricted funds before unrestricted funds? . . . . ☒ ☐ ☐
- Are the LCAP and the budget adopted within statutory timelines established by Education Code Sections 42103 and 52062, and are the documents filed with the county superintendent of schools no later than five days after adoption, or by July 1, whichever occurs first? . . . . ☒ ☐ ☐
- Has the district refrained from including carryover funds in its adopted budget? . . . . . ☒ ☐ ☐
- Has the district refrained from using negative or contra expenditure accounts (excluding objects in the 5700s and 7300s and appropriate abatements in accordance with CSAM) in its budget? . . . . ☐ ☒ ☐

During the year-end closure of 2017-18 unaudited actuals, the district discovered over 300 budget reduction entries in the 2018-19 adopted budet in the cumulative amount of ($66,555,425), with negative budget balances not in the 5700-5799 or 7300-7399 object code ranges, or 1400 resource. All but 18 entries representing $2,712,049 in negative budgets are related to salaries and benefits. The correction of these entries was part of the October 8 budget revision.

Detail budget line items that are accessible to schools and departments may lead to overspending due to the use of districtwide contra budget lines, exposing the district to significant over-budget expenditures.

- Does the district adhere to a board-adopted budget calendar that includes statutory due dates and major budget development tasks and deadlines? . . . . ☐ ☒ ☐

The district provided an overview LCAP calendar but not a budget calendar of budget development tasks or deadlines. The district did not provide evidence of a joint LCAP and LCFF budget development group meeting.

Budget Monitoring and Updates

	Yes	No	N/A
• Are actual revenues and expenses consistent with the most current budget?	☐	☒	☐

The district audit reports for 2015-16 and 2016-17 document large variances with projected revenues and expenses between budget adoption and closing as follows:

1. *The June 30, 2016 report reveals that the variance for the combined unrestricted and restricted general fund from the estimated actuals and audited financial statements is $8,391,469.*
2. *The June 30, 2017 report reveals that the variance for the combined unrestricted and restricted general fund from the estimated actuals and audited financial statements is ($8,943,040).*

The 2017-18 estimated actuals unrestricted ending fund balance as of June 30, 2018 and included with the board-approved adopted budget on June 25, 2018 showed $15,241,798. After closing the books for 2017-18, the unaudited actuals unrestricted ending fund balance as of June 30, 2018 presented to the board on September 24, 2018 was ($3,558,363), a variance of $18,800,161.

The district has made several revisions in the 2018-19 budget since budget adoption, including budget solutions to address the disapproved budget by San Diego COE. Several of the planned 2018-19 Budget Solutions may not be achievable in the current fiscal year, especially related to reductions in special education, transportation, and in interfund transfers.

While the district has worked diligently with labor partners and has tentative agreements for furlough days, the total savings are insufficient to mitigate the severity of the structural deficit.

Additionally, the district overestimated LCFF revenue by over $6 million, impacting the current fiscal year and projections in the subsequent two fiscal years. This will be discussed in greater detail later in this report.

	Yes	No	N/A
• Are budget revisions completed in the financial system, at a minimum, at each interim report?	☒	☐	☐
• Are clearly written and articulated budget assumptions that support budget revisions communicated to the board, at a minimum, at each interim report?	☒	☐	☐
• Following board approval of collective bargaining agreements, does the district make necessary budget revisions in the financial system before next financial reporting period?	☐	☒	☐

The district did not properly forecast the fiscal impact of the most recent settlement for all bargaining groups related to a 3.75% wage increase, approved by the board June 26, 2017.

The AB 1200, Column 1 "Latest Board-Approved Budget Before Settlement" was labeled "Second Interim," yet it was a combination of the district's 2016-17 second interim report combined with classified salaries (object code 2000), benefits (object code 3000), and components of fund balance unrelated to any publicly reported document.

The AB 1200 filing was compared to the 2016-17 and 2017-18 unaudited actuals to test the reliability of the district's calculation and ability to support the ongoing salary and benefit increase. FCMAT tested the AB 1200 budget amounts prior to the increase, which revealed that the district failed to include the latest budget for total *benefits and classified salaries, did not include the cafeteria and adult education funds which require a general fund contribution, and did not account for the complete retroactive costs for certificated salaries and benefits.*

The AB 1200 Disclosure was dated June 26, 2017 for certificated teachers. By this time, the board had approved the 2017-18 adopted budget which did not account for the 3.75% ongoing negotiated agreement with the teachers union retroactive back to January 2017. In addition, the district may have underestimated the actual cost of salaries because at least four months of actual payroll data had not been posted into the district's financial system at the time the estimated actuals were prepared, even though the county office had provided the information.

FCMAT identified that the difference between the AB 1200 in June 20, 2017 and the unaudited actuals in September for 2016-17 for general fund salaries without benefits is $1.5 million, and another $7 million when adult education and cafeteria funds are included. Not all benefits are impacted with a negotiated settlement; therefore, this discussion focuses on the salary impact although statutory benefits and retirement accounts will increase with the negotiated settlement, compounding the district's miscalculation.

The table below shows the impact to the general fund of underestimating general fund salaries and benefits by $9,027,011 prior to the addition of underestimating the ongoing increase of $1,066,942 for salary alone without the compounding effects beyond 2016-17 as well as other errors in the MYFP estimates.

	District's AB 1200 Disclosure Dated 6-26-17	*FCMAT's Recalculation*
Salaries		
Certificated Unrestricted General Fund	$166,118,891.00	$167,289,442.00
Certificated Restricted General Fund	$43,775,706.00	$44,071,123.00
Certificated Adult Education	$ -	$6,975,569.35
Classified Unrestricted General Fund	$49,001.994.00	$50,442,407.74
Classified Restricted General Fund	$23,953,317.00	$24,340,439.31
Classified Adult Fund	$ -	$2,666,420.22
Classified Cafeteria Fund	$ -	$5,442,913.85
Total Salaries	$282,849,908.00	$301,228,315.47
Benefits		
Unrestricted General Fund Benefits	$64,127,908.00	$64,108,743.18
Restricted General Fund Benefits	$34,877,348.00	$40,630,019.89
Adult Fund Benefits	$ -	$4,008,611.46
Cafeteria Fund Benefits	$ -	$1,745,319.48
Total Benefits	$99,005,256.00	$110,492,694.01
Total Salaries and Benefits	$381,855,164.00	$411,721,009.48
Salaries Calculation Only	$282,849,908.00	$301,228,315.47
Percentage Increase	0.0375	0.0375
Shortfall Salaries Only	$10,606,872	$11,296,062
District Document - AB 1200 Impact	$10,229,119	$10,229,120
Annual Impact	$377,753	$1,066,942

Exacerbating these errors, the AB 1200 filing did not disaggregate the impact on unrestricted and restricted funds, causing no disclosure of the impact to contributions on the Routine Restricted Maintenance Account and special education programs. As a result, the district was forced to reduce indirect cost charges and increase general fund contributions.

- Does the district provide a complete response to the variances identified in the criteria and standards? . . . . ☐ ☒ ☐

For conditions "Not Met" in the 2018-19 Criteria & Standards - Adopted Budget, the district provided limited and insufficient responses.

Not Met Criteria	District Response (abbreviated)	FCMAT Concern
1.a. ADA for 2017-18 overestimated from adopted budget to unaudited actuals	Declining Enrollment.	Does not provide sufficient explanations that describe future methods and assumptions, or internal procedures that will be used for forecasting.
4.B. Projected change in LCFF revenue falls outside standard for 2018-19 & 2019-20	District used DOF Gap Rate. Enrollment based on Cohort Survival Method.	Does not provide sufficient explanations that describe future methods and assumptions, or internal procedures that will be used for forecasting. DOF gap rate for the district at target is zero, and zero was used; therefore, the response does not correlate with the standard.
5.B. Ratio of unrestricted salaries & benefits to total expenditures	Due to PERS & STRS rate increases.	Limited response does not provide sufficient explanation for the variance test for this standard. Should provide reasons, methods and assumptions along with changes to be made in the future to address the variance.
6.B. Change in major object levels - revenue	Various.	Insufficient response for increase in local revenue of $3.4M in 2019-20, which is subsequently reduced by $1.4M in 2020-21.
6.B. Change in major object levels - expenses	"…other new grants." "carryover."	Object code 4000 shows an increase in 2020-21 of approximately $4M not sufficiently identified. District should include more information about the type and nature of the new grant.
6.D., 1.a. Change in total operating revenues & expenditures	Various.	Insufficient response for increase in local revenue of $3.4M in 2019-20, which is subsequently reduced by $1.4M in 2020-21.
8.C. 1.a. District deficit spending	Due to PERS & STRS rate increases.	Insufficient explanation for deficit spending. While PERS and STRS are contributing factors, the largest impact is from certificated and classified salaries.

- Has the district addressed any deficiencies the county office of education has identified in its oversight letters? . . . . ☐ ☒ ☐

In 2016-17, both the first and second interim letters from San Diego COE identified projected deficit spending in the unrestricted general fund in 2016-17. However, the county office acknowledged that the cause was likely high carryover from 2015-16, budgeted in 2016-17.

In a letter dated February 21, 2018 regarding the district's first interim for 2017-18, San Diego COE notes that the "district continues to deficit spend in the unrestricted general fund in 2017-18 by $2.6 million and also in the projected 2018-19 fiscal year by $2.3 million."

By the 2017-18 second interim, the county office stated that "The district was able to implement 2018-19 Budget Solutions to eliminate their deficit spending in the projection period reported at First Interim. The Second Interim Report projects a surplus in all projection years …"

Other concerns identified were not actionable items and included monitoring cash closely and continued oversight of the district's charter schools.

- Does the district prohibit processing of requisitions or purchase orders when the budget is insufficient to support the expenditure? . . . . ☐ ☒ ☐

  Interviews indicate that sites and divisions are prohibited from processing requisitions or purchase orders when the budget is insufficient to support the expenditure, but this internal control can be overridden by various central office personnel including the director of finance.

  FCMAT reviewed year-to-date financial activity from July 1, 2018 to mid-October 2018. Seven object codes totaling $124,633 were identifiable between 4000-6999 in which the budget was insufficient to cover the encumbrances plus year-to-date expenditure activity. Since the district did not provide detailed budgets in the unrestricted general fund that tied to the adopted budget, expense detail had to be rolled up to the SACS level, which obfuscated most of the detail level budgets.

- Does the district encumber salaries and benefits? . . . . ☐ ☒ ☐

  This process is inconsistent. The district's financial system, True Course, has the ability to encumber salaries. According to district interviews, this is a manual process done at the beginning of each fiscal year.

  The district's payroll is generated in the PeopleSoft system hosted by San Diego COE. After payroll is processed, the county office provides a PeopleSoft file to the district that should be posted each month to True Course. This posting reverses the applicable month's encumbrances. The posting of the file in the prior fiscal year was not uploaded timely in the district's True Course system. FCMAT reviewed records that correlate with staff interviews showing unposted payroll up to four months. Accordingly, the release of the encumbrances may not be done timely and managers are unaware of available balances. Staff indicate that when errors occur in the encumbrances, it is very difficult to correct the rest of the year. This manual process and untimely posting of the actual payrolls may result in spending beyond the budgeted salary amounts.

- Are all balance sheet accounts in the general ledger reconciled, at a minimum, at each interim report? . . . . ☐ ☒ ☐

  Staff interviews reveal that reconciliation of the general ledger only occurs during the year-end closing process.

Cash Management

Yes No N/A

- Are accounts held by the county treasurer reconciled with the district's and county office of education's reports monthly?. . . . . ☐ ☒ ☐

  Payroll is processed on the county's PeopleSoft system, whereas the commercial warrants are processed on the district's TrueCourse financial system.

  Staff interviews describe the latest bank reconciliation for July through September 2018 as having been done in October 2018.

- Are all bank accounts reconciled with bank statements monthly? . . . . ☐ ☒ ☐

  While bank reconciliations are regularly completed, the detailed reconciliation reports show outstanding items totaling over $1 million dating back to June 2017, representing voided checks and other items that have not been reconciled to date.

- Does the district forecast its cash receipts and disbursements at least 18 months out, updating the actuals and reconciling the remaining months to the budget monthly to ensure cash flow needs are known? . . . . ☐ ☒ ☐

The chief financial officer recently implemented a detailed cash flow spreadsheet and is training staff on how to use it. The district provided cash flow projections up to June 30, 2019.

The same accountant that reconciles the bank statement and has access to the county treasury accounts has sole responsibility to monitor daily cash. The process involves reviewing available cash at the county treasury, notifying personnel in accounts payable for daily commercial warrant batches to analyze the district's available cash on any given day.

When this employee takes vacation, she estimates cash needs to ensure available cash during her absence.

- Does the district have a plan to address cash flow needs during the current fiscal year? . . ☐ ☒ ☐

Records indicate that the district has borrowed significant amounts over the last two fiscal years. The district's cash flow calculations fail to show a correction even though the district has implemented significant budget adjustments indicating a compounding structural deficit from prior fiscal years.

Given that the state has provided substantial prior and current year funding for cost of living, supplemental and concentration along with additional one-time funds, it is expected that the district's cash position would not require substantial cash borrowing; yet the district is relying heavily on internal interfund borrowing from the Capital Projects Fund for Blended Component Units, fund 49. This could have a significant potential impact on the district's ability to be fiscally stable.

It is highly recommended that the county office perform a limited scope audit of the prior two fiscal years' cash transactions and bank reconciliations.

The district's cash flow shows an amount due fund 49 as of July 1, 2018 of $36.2 million, increasing to $68.2 million by June 30, 2019. By June 30, 2019 the district is unable to set aside sufficient funds to pay the outstanding balance due at June 30, 2019.

- Does the district have sufficient cash resources in its other funds to support its current and projected obligations? . . . . ☐ ☒ ☐

Funds 11 (adult education) and 13 (cafeteria) are both relying on Fund 49 for cash flow needs, and as explained below, this borrowing does not comply with Education Code requirements.

- If interfund borrowing is occurring, does the district comply with Education Code Section 42603? . . . . ☐ ☒ ☐

Absent contrary information from the audit recommended above, at the current time the district meets this requirement. However, interfund borrowing occurring through the 2018-19 fiscal year, as projected in the district's cash flow document, demonstrates that borrowing in fund 49 will exceed the Education Code thresholds of 75% of the fund balance at various times. According to the district's cash flow statement, as of September 30, 2018 the district owes $77.7 million and continues to borrow, with some repayments through June 30, 2019, leaving a balance due fund 49 of $68.2 million at June 30, 2019.

Education Code 42603 requires that amounts borrowed during the fiscal year be repaid within that same fiscal year unless the borrowing takes place within the last 120 calendar days of the fiscal year. Based on this provision the balance as of March 31, 2019 is projected to be $68.2 million; therefore, the district is required to repay that amount but will likely be unable to satisfy the requirement.

- If the district is managing cash in all funds through external borrowing, has the district set aside funds attributable to the same year the funds were borrowed for repayment? . . ☐ ☐ ☒

Charter Schools

	Yes	No	N/A
• Are all charters authorized by the district going concerns?	☒	☐	☐
• Has the district fulfilled and does it have evidence of its oversight responsibilities in accordance with Education Code Section 47604.32(d)?	☒	☐	☐
• Does the district have a board policy or other written document(s) regarding charter oversight?	☒	☐	☐
• Has the district identified specific employees in its various departments (e.g., human resources, business, instructional, and others) to be responsible for oversight of all approved charter schools?	☒	☐	☐

Collective Bargaining Agreements

	Yes	No	N/A
• Has the district quantified the effects of collective bargaining agreements and included them in its budget and multiyear projections?	☐	☒	☐

While the district prepared an AB 1200 disclosure and included the effects of the proposal, key calculations were incorrect, including but not limited to all funds as discussed more fully in the Budget Monitoring and Updates section of this report.

	Yes	No	N/A
• Did the district conduct a presettlement analysis and identify related costs or savings, if any (e.g., statutory benefits, and step and column salary increase), for the current and subsequent years, and did it identify ongoing revenue sources or expenditure reductions to support the agreement?	☐	☒	☐

At the time of fieldwork, the district and its associations were bargaining. Subsequent to FCMAT's fieldwork, the district announced tentative agreements with SEA and SCGA through June 2019, and with CSEA and NAGE through June 2021. The board of education is expected to consider each of these tentative agreements on December 10, 2018.

FCMAT was not provided with any presettlement analysis.

As noted previously, the presettlement analysis for 2016-17 did not utilize correct reporting periods, budget amounts or include all funds with the true cost of salary and benefits, which underestimated ongoing expenditures and sufficient fund balance to support the proposals.

	Yes	No	N/A
• Has the district settled the total cost of the bargaining agreements at or under funded cost of living adjustment (COLA), and under gap funding if applicable?	☒	☐	☐
• If settlements have not been reached, has the district identified resources to cover the estimated costs of settlements?	☒	☐	☐
• Did the district comply with public disclosure requirements under Government Code 3540.2, 3543.2, 3547.5 and Education Code Section 42142?	☐	☒	☐

While the district prepared an AB 1200 disclosure and included the effects of the proposal, key calculations were incorrect as previously stated.

	Yes	No	N/A
• Did the superintendent and CBO certify the public disclosure of collective bargaining agreement prior to board approval?	☒	☐	☐
• Is the governing board's action consistent with the superintendent's and CBO's certification?	☒	☐	☐
• Has the district settled with all its bargaining units for at least the prior three year(s)?	☐	☒	☐

The prior year negotiated agreement has reopeners that have not been closed as of FCMAT's fieldwork for both classified and certificated bargaining units. The board of education is expected to consider tentative agreements on December 10, 2018.

	Yes	No	N/A
• Has the district settled with all its bargaining units for the current year?	☐	☒	☐

As noted above, at the time of fieldwork, the district had not settled for 2018-19 with either classified or certificated bargaining units. However, subsequent to FCMAT's fieldwork, tentative agreements have been reached for the current year with all bargaining units. Those agreements have been ratified by their respective associations, with the board of education scheduled to consider the agreements on December 10, 2018.

Contributions and Transfers to Other Funds

	Yes	No	N/A
• Does the district have a plan to reduce and/or eliminate any increasing contributions from the general fund to other resources?	☒	☐	☐
• If the district has deficit spending in funds other than the general fund, has it included in its multiyear projection any transfers from the general fund to cover the deficit spending?	☐	☒	☐

The 2018-19 Budget Solutions plan proposes to adjust the adult education program in a variety of ways to ensure that the program is sustainable without a contribution from the general fund, saving the general fund $2,017,830 in the current year. The 2018-19 plan reduces the cafeteria fund contribution to $400,000 plus $125,833 in partial indirect cost. A review of the 2017-18 cafeteria fund estimated actuals compared with the 2017-18 unaudited actuals shows that revenues were overestimated by $959,535, expenditures were overestimated by $36,168 and general fund transfers were increased by $862,565 to compensate for the differences between projection and actual differences.

The district made reductions of $1 million between the adopted budget in June 2018 and the revised budget in October 2018 for the cafeteria fund. The magnitude of this adjustment requires changes in the district's cafeteria operations to result in such improved fiscal outcomes in the cafeteria fund. The district did not share, and FCMAT did not review, the nature of the proposed changes in food service that would support such a reduction in general fund support.

	Yes	No	N/A
• If any transfers were required for other funds in the prior two fiscal years, and the need is recurring in the current year, did the district budget for them?	☐	☒	☐

FCMAT reviewed the last two fiscal years of interfund transfer activity for temporary borrowing and found that the district has experienced significant cash shortfalls in the general fund, as well as other funds, borrowing from fund 49. Fund 49 accounts for special taxes collected from 21 separate community facilities districts, also known as Mello-Roos, used to finance public facilities in designated areas of the district.

As of the June 30, 2018, unaudited actuals report, fund 49 reported $143.9 million in the ending fund balance and outstanding debt of $103 million. Special tax levies within the boundaries of the identified community facilities districts provide the fund with an ongoing revenue stream, with anticipated interest payments of $7.5 million over the next two years. While these interest payments were properly budgeted, the principal repayment for 2018-19 did not match the independent audit report or the long-term debt payment schedule provided by the district. The principal payment budgeted for 2018-19 is $519,991, or 7% less than the payment obligation.

Unaudited actuals reveal that fund 49 is due $43,755,162 from temporary borrowing from all funds, including $36.2 million from the general fund, as of June 30, 2018. The general fund also owes $10.1 million to other funds; therefore, total general fund *obligations due other funds is $46,273,130. The district projects temporary borrowings from fund 49 to increase to $68.2 million by June 30, 2019.*

The interfund transfers submitted with the October 8, 2018 revised budget do not agree with the SACS documents because the 2017-18 unaudited actuals - interfund "due to/due from" transactions and "temporary interfund loans" are combined. That is why the 2017-18 unaudited actuals amount of $43,755,162 does not agree with the loan activity amount listed below of $40,740,000.

The district provided a separate ledger with the following temporary loan activity from fund 49 to other funds for fiscal year 2017-18:

General Fund	
Total temporary loans for fund 01 from fund 49	$168,668,550
Total of liquidated loans	132,468,550
Net temporary loan outstanding	**$36,200,000**
Adult Education Fund	
Total temporary loans for fund 11 from fund 49	$5,255,568
Total of liquidated loans	3,805,568
Net temporary loan outstanding	$1,450,000
Cafeteria Fund	
Total temporary loans for fund 13 From fund 49	$4,910,000
Total of liquidated loans	1,820,000
Net temporary loan outstanding	$3,090,000
Total Due Fund 49 - Other Funds as of June 30, 2018	$40,740,000

During the 2017-18 school year, the adult education liability to fund 49 combined temporary loans with due to/from other funds as described above. This accounting treatment does not document the ongoing liability from fund 11 to fund 49.

For transparency, proper budgeting of interfund borrowing and repayment, proper accounting treatment of long-term debt, related payments, outstanding liabilities, and borrowing is critical. This is particularly important given the extensive and increased borrowing by the general fund and other funds from fund 49.

Deficit Spending

	Yes	No	N/A
• Is the district avoiding a structural deficit in the current and two subsequent fiscal years? (A structural deficit is when ongoing unrestricted expenditures and contributions exceed ongoing unrestricted revenues.)	☐	☒	☐

The October 8, 2018 revised budget shows no unrestricted structural deficit in the current fiscal year. However, the multiyear financial projection shows deficits in 2019-20 and in 2020-21.

	Yes	No	N/A
• Is the district avoiding deficit spending in the current fiscal year?	☐	☒	☐

Immediately preceding FCMAT's fieldwork, the district took action to revise its current year budget to eliminate deficit spending in the current year. Subsequent to fieldwork, the county office of education identified additional deficiencies in the district's assumptions that include an overstatement of average daily attendance, impacts from adverse audit adjustments, and lower levels of state aid through the Local Control Funding Formula. Each of these deficiencies, if not mitigated by additional budget solutions, will contribute to current year deficit spending.

	Yes	No	N/A
• Is the district projected to avoid deficit spending in the two subsequent fiscal years?	☐	☒	☐

The October 8, 2018 revised budget shows no unrestricted deficit spending in the current fiscal year. However, the multiyear financial projection shows a $10.4 million deficit in 2019-20, and a $5.6 million deficit in 2020-21.

	Yes	No	N/A
• If the district has deficit spending in the current or two subsequent fiscal years, has the board approved and implemented a plan to reduce and/or eliminate deficit spending?	☐	☒	☐

The district's current board approved plan does not eliminate deficit spending in 2019-20 or 2020-21.

	Yes	No	N/A
• Has the district decreased deficit spending over the past two fiscal years?	☐	☒	☐

The district's fund balance has diminished over the last two fiscal years due to deficit spending.

Employee Benefits

	Yes	No	N/A
• Has the district completed an actuarial valuation to determine its unfunded liability under Governmental Accounting Standards Board (GASB) other post-employment benefits (OPEB) requirements?	☒	☐	☐
• Does the district have a plan to fund its liabilities for retiree benefits?	☐	☒	☐

The district has not identified funding sources for plan assets under GASB 45. The district's unfunded actuarial accrued liability at July 1, 2016 is $102,050,003 (including $71,428,876 for the district's explicit contribution and $30,621,127 for the implicit rate subsidy).

The actuarial report states that the estimated district contribution for retiree health benefits for 2016-17 was approximately $4,310,400 (including $1,238,275 for the implicit rate subsidy). This amount included payments for employees expected to retire during the 2016-17 fiscal year.

The district funds its retiree health program on a pay-as-you-go basis. Because there is no ongoing commitment to cover the unfunded liability, the district may not have an adequate plan to sufficiently fund the future liability.

While the district states that "retiree benefits are included in the budget process," the district does not have a segregated funding source to cover long-term retiree benefits. Budgetary pressures could jeopardize future obligations as, according to the 2017 audit report, "other postemployment benefits are generally paid by the General Fund."

	Yes	No	N/A
• Has the district followed a policy or collectively bargained agreement to limit accrued vacation balances?	☐	☒	☐

The CSEA negotiated agreement states that classified employees are subject to a vacation accrual cap of 40 days. FCMAT was able to verify that while the cap is in place, it has not been previously followed even though the district reported that management has implemented a plan to monitor and reduce accrued vacation balances. While the most recent audit report does not cite a finding in this area, the long-term portion of compensated absences as of June 30, 2017 is $9,638,609, which is a three-year high growing from $8,070,445 in June 2015.

	Yes	No	N/A
• Within the last five years, has the district conducted a verification and determination of eligibility for benefits for all active and retired employees and dependents?	☒	☐	☐
• Does the district track and reconcile employees' leave balances?	☒	☐	☐

Enrollment and Attendance

	Yes	No	N/A
• Has the district's enrollment been increasing or stable for the current and three prior years?	☒	☐	☐
• Does the district monitor and analyze enrollment and average daily attendance (ADA) data at least monthly through the second reporting period (P2)?	☐	☒	☐

The district has provided several examples of individual attendance tracking spreadsheets with summary data, and also generated corresponding reports from its attendance system (Infinite Campus). The spreadsheets and reports are separated by site but are not combined into a single districtwide document for ADA analysis.

While the spreadsheets show the flow of data from the attendance system, the district was unable to provide evidence of a complete process used to monitor and analyze the data or compare this data to district projections. FCMAT was unable to verify that there is a process to analyze actuals to projections at least monthly through P2.

During the current fiscal year, the district did not take into account historical ADA downward trends by grade level. In addition, the staff did not include auditor adjustments prepared in June 2018. The auditor worksheets would have provided the exact calculation of ADA based on the prior year P2 including auditor adjustments for the overidentification of students eligible for supplemental and concentration grant funds.

Instead, district staff used current year enrollment with an incorrect ADA ratio to project the LCFF funding. During the 2018-19 fiscal year, the enrollment calculation was fairly accurate; however, the ADA was approximately 500 less than projected.

The district's most recent enrollment projections report dated May 29, 2018 was compiled by the district's architect who, as a former employee, is very familiar with the district's enrollment patterns. This report demonstrates the use of historical data in projecting enrollment, which can be used for building capacity and allow the district to plan for available teaching spaces and for future housing.

Projecting student ADA for funding purposes uses a different methodology and requires district staff to regularly monitor student attendance rates because school districts are funded on ADA. School districts are funded on the higher of the current or prior fiscal year, which gives the district time to make adjustments if it experiences declining enrollment, as is the case with the district.

The district reported that the chief financial officer has worked with staff to create internal procedures that calculate the enrollment and ADA factors based on declining enrollment and more accurate historical trend factors, and plans to have this information verified by a consultant familiar with these calculations.

	Yes	No	N/A
• Does the district track historical enrollment and ADA data to establish future trends?	☒	☐	☐
• Do school sites maintain an accurate record of daily enrollment and attendance that is reconciled monthly at the site and district level?	☒	☐	☐
• Did the district certify its California Longitudinal Pupil Achievement Data System (CALPADS) Fall 1 data by the required deadline?	☒	☐	☐
• Are the district's enrollment projection and assumptions based on historical data, industry-standard methods, and other reasonable considerations?	☒	☐	☐
• Do all applicable sites and departments review and verify their respective CALPADS data and correct it as needed before the report submission deadlines?	☒	☐	☐
• Has the district planned for enrollment losses to charter schools?	☒	☐	☐

	Yes	No	N/A
• Has the district developed measures to mitigate the effect of student transfers out of the district?	☒	☐	☐
• Does the district meet the average class enrollment for each school site of no more than 24:1 class size ratio in K-3 classes or does it have an alternative collectively bargained agreement?	☐	☐	☒

Facilities

	Yes	No	N/A
• If the district participates in the state's School Facilities Program, has it met the 3% Routine Repair and Maintenance Account requirement?	☐	☒	☐

A supplemental report for resource 8150 shows that the revised budget as of October 8, 2018 for the current year is $9,318,159, whereas the amount required per the Criteria & Standards is $9,426,236. The district reports that additional budget adjustments are needed to bring the district in compliance.

	Yes	No	N/A
• Does the district have sufficient building funds to cover all contracted obligations for capital facilities projects?	☐	☒	☐

The district's robust Capital Improvement Status Report presented to the governing board on September 24, 2018 summarizes capital improvement projects throughout the district.

According to the report, all committed resources are from funds other than the general fund for contracted obligations. Less than 1% of the funding relies on developer fees. None of the capital projects are budgeted in the general fund for 2018-19, and the Criteria & Standards item S5B 1.d. states that there are no capital projects that may impact the district's general fund budget.

As previously discussed, the district is borrowing extensively from the CFDs in fund 49. This fund is vital to supporting the ongoing cash needs of the district. Interfund borrowing is projected to exceed 75% of the fund balance for fund 49 in the current fiscal year. The capital outlay report presented to the governing board shows that fund 49 is the primary revenue source for over 28% of active projects.

Depleting cash resources from fund 49 will reduce or eliminate the district's ability to borrow from this fund and therefore the district's ability to meet the general fund obligations. Until the district is able to contain temporary borrowing from fund 49, cash availability will be unstable for active projects.

	Yes	No	N/A
• Does the district properly track and account for facility-related projects?	☒	☐	☐
• Does the district use its facilities fully in accordance with the Office of Public School Construction's loading standards?	☒	☐	☐
• Does the district include facility needs when adopting a budget?	☐	☒	☐

The facilities department is not consulted during the budget development process. Instead, the department's budget is prepared by the business office.

	Yes	No	N/A
• Has the district met the facilities inspection requirements of the Williams Act and resolved any outstanding issues?	☒	☐	☐
• If the district passed a Proposition 39 general obligation bond, has it met the requirements for audit, reporting, and a citizens' bond oversight committee?	☒	☐	☐
• Does the district have an up-to-date long-range facilities master plan?	☒	☐	☐

Fund Balance and Reserve for Economic Uncertainty

	Yes	No	N/A
• Is the district able to maintain the minimum reserve for economic uncertainty in the current year (including funds 01 and 17) as defined by criteria and standards?	☐	☒	☐

The district's adopted budget was disapproved. The October 8, 2018 revised adopted budget was approved by the county office. The district is unable to maintain the minimum 2% reserve for economic uncertainty in the current and two subsequent fiscal years. Substantial work has been done to create the 2018-19 Budget Solutions, which is part of the October 8, 2018 budget, containing over $23 million in adjustments. However, it is questionable if all of these solutions will materialize in the current fiscal year, especially related to special education cuts and interfund transfers to support the cafeteria and adult education funds.

	Yes	No	N/A
• Is the district able to maintain the minimum reserve for economic uncertainty in the two subsequent years?	☐	☒	☐

The district is experiencing fiscal distress following the 2017-18 unaudited actuals report in September 2018. This reporting period showed an unrestricted fund balance of ($3,558,363).

Once the fund balance was adjusted for 2018-19, the district's reserve for economic uncertainty is $9,426,236, yet the amount available to fund this reserve level is projected to be ($10,074,009).

The governing board has approved 2018-19 Budget Solutions for the current and subsequent two fiscal years that will, if fully implemented, restore the fund balance reserve levels. This plan, approved October 8, 2018, shows 2018-19 Budget Solutions as follows:

2018-19: Total 2018-19 Budget Solutions of $23 million,

2019-20: Additional 2018-19 Budget Solutions of $10.4 million, and

2020-21: Additional 2018-19 Budget Solutions of $5.5 million.

	Yes	No	N/A
• If the district is not able to maintain the minimum reserve for economic uncertainty, does the district's multiyear financial projection include a board-approved plan to restore the reserve?	☐	☒	☐

As noted above, preceding FCMAT's fieldwork, the district took action to adopt 2018-19 Budget Solutions that impacted the current and subsequent two years. All else remaining the same, these solutions may have been sufficient to restore reserves to minimum levels. However, subsequent to fieldwork, the county office of education identified additional deficiencies in the district's assumptions that include an overstatement of average daily attendance, impacts from adverse audit adjustments, and lower levels of state aid through the Local Control Funding Formula. Each of these deficiencies, if not mitigated by additional budget solutions, will contribute to current year deficit spending and decreasing the already minimal fund balance as the district transitions to 2019-20 and 2020-21. Additionally, amounts slated for reductions in the subsequent fiscal years appear in the multiyear projections as "other adjustments" representing aspirational high-level targets without board-approved supporting details as to specifics on how the savings will be achieved, including the specific expenditure categories to be reduced and a timeline for implementation.

	Yes	No	N/A
• Is the district's projected unrestricted fund balance stable or increasing in the two subsequent fiscal years?	☐	☒	☐

As indicated on the multiyear financial projection dated October 5, 2018, the district's unrestricted fund balance is stable or increasing. However, as noted above, the district's adopted budget solutions are likely not sufficient to restore the fund *balance to minimum levels given the subsequent findings around ADA and revenues. Additionally, amounts slated for reductions in the subsequent fiscal years appear in the multiyear projections as "other adjustments" representing aspirational high-level targets without board-approved supporting details as to specifics on how the savings will be achieved. The subsequent findings and the lack of detail associated to out-year reductions call into question the basis for increasing unrestricted fund balance in the two subsequent years.*

- If the district has unfunded or contingent liabilities or one-time costs, does the unrestricted fund balance include any assigned or committed reserves above the recommended reserve level? . . . . ☒ ☐ ☐

General Fund - Current Year

	Yes	No	N/A
• Does the district ensure that one-time revenues do not pay for ongoing expenditures?	☐	☒	☐

FCMAT was not provided records that demonstrated that one-time revenues are isolated from ongoing expenditures. The district has no tracking ability to isolate one-time revenues.

	Yes	No	N/A
• Is the percentage of the district's general fund unrestricted budget that is allocated to salaries and benefits at or under the statewide average for the current year?	☐	☒	☐

The statewide average for salaries and benefits for high school districts is 85.43% as of 2016-17 (the latest data available). The district's Criteria & Standards at the adopted budget period for 2018-19 calculates the historical average ratio of 85.5% based on the prior three fiscal years' actual data (2014-15 through 2016-17), yet the projected ratio of unrestricted salaries and benefits is projected to be 90.2% for 2018-19. Therefore, the district is exceeding the statewide average by 5.47%.

	Yes	No	N/A
• Is the percentage of the district's general fund unrestricted budget that is allocated to salaries and benefits at or below the statewide average for the three prior years?	☐	☒	☐

The Criteria & Standards at the adopted budget period for 2018-19 calculates the historical average ratio of 85.5% based on the prior three fiscal years' actual data (2015-16 through 2017-18), yet the projected ratio of unrestricted salaries and benefits in 2017-18 was 89.1%, or 3.67% higher than the state average.

	Yes	No	N/A
• If the district has received any uniform complaints or legal challenges regarding local use of supplemental and concentration grant funding, is the district addressing the complaint(s)?	☐	☐	☒
• Does the district either ensure that restricted dollars are sufficient to pay for staff assigned to restricted programs or have a plan to fund these positions with unrestricted funds?	☒	☐	☐
• Is the district using its restricted dollars fully by expending allocations for restricted programs within the required time?	☒	☐	☐
• Does the district consistently account for all program costs, including allowable indirect costs, for each restricted resource?	☐	☒	☐

FCMAT found that indirect costs attributable to other funds such as cafeteria and adult education were not fully charged. The Criteria & Standards from the unaudited actuals report calculated the approved indirect cost rate of 6.01%, yet many restricted programs were charged rates considerably lower than what is allowable, ranging from 1.31% to 6.03%, as one program exceeded the approved rate.

Information Systems and Data Management

	Yes	No	N/A
• Does the district use an integrated financial and human resources system?	☐	☒	☐
The financial (True Course) and HR (Lawson) systems are different and do not interface in real time with each other or with the county office PeopleSoft system. Information for new employees (all employee demographic data) and adjustments for existing employees are manually entered into the county's PeopleSoft system by the HR department following departmental approvals.			
• Can the system(s) provide key financial and related data, including personnel information, to help the district make informed decisions?	☒	☐	☐
• Does the district accurately identify students who are eligible for free or reduced-price meals, English learners, and foster youth, in accordance with the LCFF and its LCAP?	☐	☒	☐
While the district does project the percentage of students who are eligible for free or reduced-price meals, English learners and foster youth in support of its revenue projections under the Local Control Funding Formula, the accuracy of the district's reporting of students in these categories has been questioned by the recent adjustment downward of 895 students who were reported to qualify in these categories. A 1% change in unduplicated student counts equates to a significant impact on the district's unrestricted supplemental and concentration revenue. Additionally, counts of unduplicated students influence revenues over three years, enhancing the impact of inaccurate counts and projections. The most recent questioned costs reduce the district's revenue by over $700,000.			
• Is the district using the same financial system as its county office of education?	☐	☒	☐
The district uses True Course for financials and Lawson for HR, and the county office of education uses PeopleSoft.			
• If the district is using a separate financial system from its county office of education and is not fiscally independent, is there an automated interface with the financial system used by the county office of education?	☐	☒	☐
The district is fiscally accountable. Specific procedures have been identified by San Diego COE as to how the district provides information to it. There is no automated interface between the two systems.			
• If the district is using a separate financial system from its county office of education, has the district provided the county office with direct access so the county office can provide oversight, review and assistance?	☐	☒	☐
The county office of education does not have access to the district's information systems. The COE has plans to require the district to provide required data for uploading and verification within the PeopleSoft system by December 2018.			

Internal Controls and Fraud Prevention

	Yes	No	N/A
• Does the district have controls that limit access to and authorizations within its financial system?	☐	☒	☐
Cash reconciliation and cash monitoring are critical elements that require separation of duties and managerial oversight. One classified non-managerial accountant performs all of these duties. FCMAT found this same employee has complete access to cash between funds and is given complete access to the county treasury district accounts. While this employee seeks management approval prior to processing interfund temporary borrowings, this process does not require a manager's signature and login. Instead, the employee has the only login to the county treasury accounts			

and ability to move money between funds. It is not clear if the employee has access to move funds outside of the treasury accounts.

- Are the district's financial system's access and authorization controls reviewed and updated upon employment actions (i.e. resignations, terminations, promotions or demotions) and at least annually? ☐ ☒ ☐

  The district does not verify that terminated employees are removed from district financial systems or ensure that former employees are not given authorization to financial information. For example, FCMAT discovered a San Diego COE email list that notifies the district that the payroll file is available for download. Included on the list were former employees. Also attached to the email was the payroll file.

- Does the district ensure that duties in the following areas are segregated, and that they are supervised and monitored?
  - Accounts payable (AP) ☒ ☐ ☐
  - Accounts receivable (AR) ☒ ☐ ☐
  - Purchasing and contracts ☒ ☐ ☐
  - Payroll ☐ ☒ ☐

    As previously mentioned, the district payroll is processed through the county office PeopleSoft system. When completed, the county office provides a file to the district to upload into the True Course financial system. However, before this process can be accomplished, district staff contact the original system vendor in Canada who has online access to the financial system to clear and reset the payroll tables.

    This process is not monitored by management to ensure that the uploaded data matches actual payroll paid during the period, or that other controls are in place. A classified employee is the only employee in the district that has the instructions and knows the process for approximately $28 million to $32 million of payroll transactions each month.

  - Human resources ☒ ☐ ☐
  - Associated student body (ASB) ☒ ☐ ☐
  - Warehouse and receiving ☒ ☐ ☐
- Are beginning balances for the new fiscal year posted and reconciled with the ending balances for each fund from the prior fiscal year? ☒ ☐ ☐
- Does the district review and clear prior year accruals by first interim? ☐ ☒ ☐

  According to business office staff, reversing entries are made in the new fiscal year but there is no method for tracking receivables.

- Does the district reconcile all suspense accounts, including salaries and benefits, at least at each interim reporting period and at the close of the fiscal year? ☐ ☒ ☐

  According to business office staff, this process is only done at year end.

- Has the district reconciled and closed the general ledger (books) within the time prescribed by the county office of education? ☒ ☐ ☐
- Does the district have processes and procedures to discourage and detect fraud? ☒ ☐ ☐
- Does the district maintain an independent fraud reporting hotline or other reporting service(s)? ☒ ☐ ☐
- Does the district have a process for collecting and following up on reports of possible fraud? ☒ ☐ ☐

	Yes	No	N/A
• Does the district have an internal audit process?	☒	☐	☐

Leadership and Stability

	Yes	No	N/A
• Does the district have a chief business official who has been with the district more than two years?	☐	☒	☐

A chief financial officer was hired in August 2018 who has extensive school business experience.

	Yes	No	N/A
• Does the district have a superintendent who has been with the district more than two years?	☒	☐	☐
• Does the superintendent meet regularly with all members of their administrative cabinet?	☒	☐	☐
• Is training on financial management and budget offered to site and department administrators who are responsible for budget management?	☒	☐	☐
• Does the governing board adopt and revise policies and administrative regulations annually?	☒	☐	☐
• Are newly adopted or revised policies and administrative regulations communicated to staff and implemented?	☒	☐	☐
• Is training on the budget and governance provided to board members at least every two years?	☒	☐	☐
• Is the superintendent's evaluation performed according to the terms of the contract?	☒	☐	☐

Multiyear Projections

	Yes	No	N/A
• Has the district developed multiyear projections that include detailed assumptions aligned with industry standards?	☒	☐	☐
• To help calculate its multiyear projections, did the district prepare an LCFF calculation with multiyear considerations?	☒	☐	☐
• Does the district use its most current multiyear projection when making financial decisions?	☒	☐	☐

Non-Voter-Approved Debt and Risk Management

	Yes	No	N/A
• Are the sources of repayment for non-voter-approved debt stable such as certificates of participation (COPs), bridge financing, bond anticipation notes (BANS), revenue anticipation notes (RANS) and others, predictable, and other than unrestricted general fund?	☐	☒	☐

The district has two Qualified Zone Academy Bonds (QZAB), which are essentially COPs issuances that do not have separate repayment sources. The unrestricted general fund must support these debt obligations. Given the current budgetary pressures on the general fund, this is not a stable or reliable funding source.

Per the district and confirmed with the district's June 30, 2017 audited financial statements, there are four issuances of non-voter-approved debt, as shown below:

1. *2005 QZAB (COPs) – Private placement. Repayment source: general fund (01). Annual base rental payment of $312,500 must be deposited with US Bank each year to generate sufficient income to repay the $5 million certificate upon maturity on September 29, 2021.*

2. *2010 QZAB (COPs) – Private placement. Repayment source: general fund (01), of which $396,125 is due in fiscal year 2018-19.*

3. *2016 Lease Revenue Refunding Bonds. Repayment source: redevelopment & lease revenue fund (40), of which $2,506,302 is due in fiscal year 2018-19.*

4. *2017 Refunding COPs. Repayment source: Mello-Roos/CFD special taxes (49), of which $5,647,144 is due in fiscal year 2018-19.*

The long-term debt schedule provided by the district did not reconcile to the June 30, 2017 independent audit report, the official SACS extract for 2017-18 unaudited actuals, or the 2018-19 October 8, 2018 revised budget. The district failed to disclose the total amount of debt on the long-term debt section of the 2018-19 SACS report.

- If the district has issued non-voter-approved debt, has its credit rating remained stable or improved? . . . . ☐ ☒ ☐

On October 26, 2018 (after FCMAT's fieldwork), Fitch Ratings-San Francisco downgraded the district's rating and issued the following:

> *Long-Term Issuer-Default Rating (IDR) to 'BBB+' from 'A'.*
>
> *At the same time, the Rating Outlook for the IDR has been revised to Negative from Stable. The downgrade and Outlook revision are triggered by significant deterioration in the district's financial position compared to prior expectations and Fitch's concern that expenditure control needed to stabilize its finances will be a challenge for the district.*

The following is a link to the complete article: https://www.fitchratings.com/site/pr/10048678

- If the district is self-insured, does the district have a recent (every 2 years) actuarial study and a plan to pay for any unfunded liabilities?. . . . . ☐ ☐ ☒

- If the district has non-voter-approved debt (such as COPs, bridge financing, BANS, RANS and others), is the total of annual debt service payments no greater than 2% of the district's unrestricted general fund revenues? . . . . ☒ ☐ ☐

Position Control

Yes No N/A

- Does the district account for all positions and costs? . . . . ☐ ☒ ☐

During 2014-15 FCMAT prepared a multiyear financial projection report for the district and identified that the position control system should be fully integrated. A properly functioning position control system is integrated or at least reconciled with what is in budget, payroll and human resources records. While the district recognizes the critical importance of having a fully integrated system, this has not occurred. Most recently, the district identified key employees and formed a working group to develop a manual system as an interim solution. The district plans to eventually replace the 20-year old True Course financial system with a system that is fully integrated with position control.

FCMAT cannot determine that all positions and costs are accounted for in the district's budget. Based on the last two fiscal years' audit reports, the district has experienced large variances from budgeted salaries and benefits at estimated actuals to the unaudited actuals reporting period. According to district staff interviews, the March 2018 payroll report was used to project 2018-19 salaries and benefits.

As previously reported, the district runs the actual payroll on the county office PeopleSoft system and produces a file for the district to upload into its True Course financial system. During the 2017-18 fiscal year, four months of actual payroll was *not uploaded in the True Course system during the budget development period. Generating payroll and benefits projections is the single largest component of the district's general fund budget.*

With four months of payroll and benefit information not posted to the district's system, along with budget entries that augmented and artificially adjusted the working budget, the district overreported the fund balance at estimated actuals by $15 million. By the time the district's books were closed in September 2018 for the unaudited actuals, a negative fund balance of $3 million was reported – a total variance of $18 million, which caused immediate fiscal uncertainty and financial distress.

	Yes	No	N/A
• Does the district analyze and adjust staffing based on staffing ratios and enrollment?	☐	☒	☐

The district is using a staffing allocation formula developed and implemented in 2000, when enrollment was presumably higher. While the district provided evidence that regular analysis of staffing is compared with actual enrollment for the current year, FCMAT could not confirm that adjustments were made in accordance with site needs, nor that either the analysis or adjustments were made in prior years.

	Yes	No	N/A
• Does the district reconcile budget, payroll and position control regularly, meaning at least at budget adoption and interim reporting periods?	☐	☒	☐

The district reported that a working group was formed following FCMAT's fieldwork. A manual process will be developed until an integrated position control system is in place.

	Yes	No	N/A
• Does the district identify a budget source for each new position before the position is authorized by the governing board?	☐	☒	☐

The district uses a Position Action Request form to initiate a new position requisition. The district was unable to provide evidence that that form is routed to Fiscal Services to identify a budget source prior to board approval, although the district claims that all new positions are authorized by the governing board before hiring.

	Yes	No	N/A
• Does the governing board approve all new positions before positions are posted?	☐	☒	☐

Because the district lacks a comprehensive position control process, board minutes do not reflect that the board approves all new positions before they are posted, and, if so, whether accurate information is provided to accomplish this effectively.

The human resources department stated that vacancies are tracked by reviewing the current listing of posted positions. This is further evidence that a comprehensive process, including board approval of new positions, is not in place and used reliably.

	Yes	No	N/A
• Does the district have board-adopted staffing ratios for certificated, classified and administrative positions?	☐	☒	☐

According to the cabinet responses to the FCMAT fiscal risk questionnaire, the board-approved staffing ratios are for certificated positions only.

	Yes	No	N/A
• Do managers and staff responsible for the district's human resources, payroll and budget functions meet regularly to discuss issues and improve processes?	☐	☒	☐

The district did not provide evidence that personnel from human resources, budget and payroll meet except occasionally when a need arises. The district reported following FCMAT's fieldwork that regular meetings were established.

Special Education

	Yes	No	N/A
• Are the district's staffing ratios, class sizes and caseload sizes in accordance with statutory requirements and industry standards?	☒	☐	☐

- Does the district access available funding sources for costs related to special education (e.g., excess cost pool, legal fees, mental health)? . . . . ☒ ☐ ☐
- Does the district use appropriate tools to help it make informed decisions about whether to add services (e.g., special circumstance instructional assistance process and form, transportation decision tree)?. . . . . ☐ ☒ ☐

The district hired an experienced director of special services during this fiscal year. While the district tracks total paraprofessional staffing, there is no correlation to the number of students, which is tracked separately. FCMAT was not provided evidence of management tools utilized by the district to make informed decisions for classified staffing and other support needs such as transportation services.

Staff interviews indicate that the transportation department is notified of IEP meetings. However, it was noted that personnel from the transportation department rarely attend. While IEP teams are provided written criteria to determine if students qualify for transportation, the document is not a decision tree with proper justification. This could lead to overidentified transportation services.

- Does the district account correctly for all costs related to special education (e.g., transportation, indirect costs, service providers)? . . . . ☐ ☒ ☐

Staff interviews indicate that special needs transportation will not be a large component of the 2018-19 Budget Solutions plan, and the plan itself does not contain a specific mention of the service, yet the budget has been reduced by $1,013,587 (20.5%) over prior year actual expenditures.

Home-to-school transportation, which may include special needs students, has been reduced by $422,515 over prior year actual expenses.

- Is the district's contribution rate to special education at or below the statewide average contribution rate? . . . . ☐ ☒ ☐

The district's contribution to special education has increased in each of the last three fiscal years, as follows:

2015-16 – increased by $4.6 million (60% general fund contribution),

2016-17 – increased by $5.4 million (62% general fund contribution),

2017-18 – increased by $6.0 million (64% general fund contribution).

The 2018-19 Budget Solution reduces the general fund contribution by $2,837,269, attempting to hold special education costs at 2015-16 levels. This decrease seems unreasonable while the population of students with high-cost services continues to increase, which is reflected in the prior year increases to annual contributions. The district's contribution to special education transportation is not included in this calculation.

According to the Coalition for Adequate Funding for Special Education: 2016-17 Maintenance of Effort Reports by Special Education Local Plan Area, the statewide average district contribution to special education at that time was 64.5%.

The reporting for special education revenues is not integrated. Three different source documents were provided to support 2018-19 revenue. Two of these were provided by the SELPA and the third came from district staff. The 2018-19 special education budgeted revenues did not match any of the three source documents provided, with the exception of federal mental health, which was maintained at prior year levels.

The district has a budget analyst who monitors the special education budgets. Budgets are tracked and reported by individual resource, not as a program. Interviews indicate that the special education director only had access to the primary special *education budget. To properly manage the entire special education program and contribution levels, the special education director should have access to all program budgets, with full access to review revenue and expenditures.*

At the time of FCMAT's fieldwork, the specific implementation plan had yet to be identified. FCMAT's review of the 2018-19 budget identified potential deficiencies in legal fees; equipment repair; transport services including district provided transportation; NPS and NPA tuition, room and board; and tuition for students served in county operated programs.

- Is the district's rate of identification of students as eligible for special education comparable with countywide and statewide average rates? . . . . ☐ ☒ ☐

    The district's identification rate for the 2017-18 school year was 12.6%, which is 2% higher than the statewide average rate for students enrolled in special education of similar age (generally grades 7– 12). While this identification rate is close to the statewide average rate, the district rate has increased by 9.7% in 2017-18. This rate is substantially lower than the 14.3% countywide average of similarly aged students enrolled in special education (generally grades 7-12).

- Does the district monitor, and reconcile the billing for, any services provided by nonpublic schools and/or nonpublic agencies? . . . . ☒ ☐ ☐
- Does the district analyze and plan for the costs of due process hearings?. . . . . ☐ ☒ ☐

    The district has hired a dedicated director for the 2018-19 school year to provide pre-intervention support for special education students and families in an attempt to minimize due process hearings. While filings and prior year legal fees are minimal, the district did not provide evidence of any analysis or planning for the costs of due process hearings.

- Does the district analyze whether it will meet the maintenance of effort (MOE) requirement at each reporting period? . . . . ☒ ☐ ☐

Total Risk Score, All Areas **57.7%**

Key to Risk Score

High Risk: 40% or more

Moderate Risk: 25-39%

Low Risk: 24% and lower

Summary

Ultimately, the district's budget is the responsibility of its governing board. So that the board can make informed decisions, the superintendent and senior management have a fiduciary duty to present sound financial information supported by historical trends, and budget projections, assumptions and multiyear projections that are based on reliable information.

Throughout this report, FCMAT has identified signs of the district's fiscal distress. Of particular concern is a history of internal cash borrowing, especially when the state budget has provided large amounts of state aid and one-time monies, and no deferrals or deficits of state aid.

District-provided documents show that cash borrowing from Mello-Roos will increase from $36 million as of July 1, 2018 to $68 million by June 30, 2019. This amount exceeds Education Code limits, and the district has no apparent ability to repay the debt in the foreseeable future.

While the district prepares budget revisions throughout the fiscal year, detailed information provided by the district shows that budget revisions totaling millions of dollars include negative budget entries that lack sufficient supporting documentation.

FCMAT reviewed approximately $9 million of budget revisions done in an attempt to right-size the current year budget to actuals since the 2017-18 unaudited actuls expenditures were so much higher than originally estimated. This is an indication that the adopted budget did not represent the total amount necessary to support district obligations for salaries, benefits and other operating expenditures.

The district will need to fully analyze the current year budget to determine if the total adjustments for increases coupled with decreases from 2018-19 Budget Solutions is a fair representation of anticipated obligations.

FCMAT's analysis determines that the cost estimate by the district for the general fund shown in the Criteria & Standards for a 1% certificated salaries and benefits increase may be understated. While this amount was originally left blank in the district's adopted budget Criteria & Standards, the revised budget dated October 8, 2018 states that the cost of 1% is $2,162,393. Based on projected salaries and benefits in the October 8, 2018 revised budget, the likely cost of 1% for certificated salaries and benefits is approximately $2.7 million, an approximately $538,000 difference.

Based on information provided and the analysis by the FCMAT team, large variances in the district's budget to actual expenditures demonstrates the district's inability to properly budget and adequately monitor the district's multifund budget, or to adequately carry out the board-approved recovery plan to address fiscal solvency in the current and subsequent two fiscal years.

Concerns include but are not limited to deficit spending; inadequate fund balance; insufficient reserve levels; approval of bargaining agreements that exceed the district's ability to support them; lack of position control; no reconciliation of payroll with budget or human resources records; inadequate internal controls over cash and other vital operational areas; the ability of management personnel to post millions of dollars of negative budget entries; financial and operating systems that are not integrated with one another and that rely on a single programmer to troubleshoot and clear monthly payroll tables; and millions of dollars of county-office-processed payroll left unposted for months in the district's financial system.

The county office of education has acted immediately to avoid further erosion of the district's reserve levels and possible fiscal emergency by appointing a fiscal advisor.

The district's governing board should act immediately to balance the budget, eliminate deficit spending, evaluate options for a fully integrated financial system, and ensure that it has proper internal controls and conducts internal audits of key operational areas.