California School Boards Association Winter Conference

Financial Insolvency Predictors Is Your District At Risk?

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FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM
CSIS California School Information Services

Our Definition of “Financially Troubled”

- What do we mean when we say a district is in financial trouble? A troubled district:
  - May have a history of deficit spending
  - May have qualified or negative interim reports
  - May have its budget disapproved by the County Office of Education
  - May not be able to conform to multi-year projection standards
  - May not have enough cash to meet its obligations
  - Probably has poor oversight and monitoring of its finances
- In short, it is a district that cannot meet state standards on its own

Our Definition of "Financially Troubled"

- There are always troubled districts – normally district fortunes rise and fall in tandem with state economics but some are chronic
  - The number of qualified districts in the state has increased in past years in some cases through no fault of their own!
  - A district is qualified when it is determined that it may not be able to meet its financial obligations in the current and two subsequent years—the focus is budget
  - The number of Negative Certification districts ebbs and flows and again are on the rise at 2nd Interim 2012
  - A district is negative when it is determined that it will not meet its financial obligations in the current and next fiscal year—the focus is cash

Thirteen Ways Districts Get in Trouble

- #1 Estimates of State Economics
  - Exposure
    - Significant
  - Professional Standard
    - Maintain knowledge of state economics forecast
    - Anticipate effect on your district
    - Consider state economics in budget projections and revisions
  - Definition
    - State economics determine the allocations to Proposition 98 school funding based upon state revenues

Thirteen Ways Districts Get in Trouble

- #2 Average Daily Attendance
  - Exposure
    - Critical
  - Professional Standard
    - The district must have policies and procedures in place to appropriately forecast and track enrollment and ADA
  - Definition
    - Enrollment drives costs
    - ADA drives revenues
    - ADA is equal to the average number of pupils actually attending classes who reenrolled for at least the minimum school day

Thirteen Ways Districts Get in Trouble

- #3 Budget Assumptions
  - Exposure
    - Critical
  - Professional Standard
    - The district budget must be based upon a foundation of verifiable facts, and assumptions must be clearly stated
  - Definition
    - Budget assumptions are planning factors that stand in place of facts until those facts are known

Thirteen Ways Districts Get in Trouble

- #4 Control of Staff Costs
  - Exposure
    - Critical
  - Professional Standard
    - Maintain staffing discipline within parameters adopted by the Board of Education
  - Definition
    - Staffing control means that numbers of people, pay rates, assignments, overtime, etc., are kept within plans and budgets adopted by the Board

Thirteen Ways Districts Get in Trouble

- #5 Estimating Step and Column
  - Exposure
    - Critical
  - Professional Standard
    - Districts must have tools and procedures to estimate the annual increase of salary and statutory benefit costs incurred each year as the result of step and column
  - Definition
    - Step: Dollar change between salary steps based on years of service
    - Column: Dollar change between columns based on educational units or accomplishments
      - Automatic pay raises for employees returning to work from the previous year

Thirteen Ways Districts Get in Trouble

- #6 Use of One-Time Dollars
  - Exposure
    - Significant
  - Professional Standard
    - Ongoing expenses must be covered by ongoing revenues
    - One-time dollars should not be used for ongoing expenses
  - Definition
    - One-time dollars include ending balances, audit adjustments, retroactive revenues, and other nonrecurring revenues

Thirteen Ways Districts Get in Trouble

- #7 Negotiations
  - Exposure
    - To be determined by district
      - Critical – Significant – Minor
  - Professional Standard
    - Maintain comparable compensation and working conditions within the district's ability to pay
    - Balance compensation needs with student needs
  - Definition
    - Collective bargaining is required by the Rodda Act
    - Must negotiate in good faith

Thirteen Ways Districts Get in Trouble

- #8 Multiyear Planning
  - Exposure
    - Critical
  - Professional Standard
    - Multiyear Planning current plus 2 years
    - Long-term impact must be assessed
  - Definition
    - MYP considers the out-year impact of today’s decisions

Thirteen Ways Districts Get in Trouble

- #9 Execution of the Budget
  - Exposure
    - Significant
  - Professional Standard
    - The district must adhere to the approved spending
    - Revisions should be approved before different decisions are implemented
  - Definition
    - Execution of the budget means sticking to the spending plan adopted by the Board

Thirteen Ways Districts Get in Trouble

- #10 Budget Monitoring
  - Exposure
    - Critical
  - Professional Standard
    - AB 1200 requires districts to monitor and perform self-assessment
    - The budget should be revised when necessary
  - Definition
    - Budget monitoring means actual results are compared with planned results and adjustments are made

Thirteen Ways Districts Get in Trouble

- #11 Deficit Spending
  - Exposure
    - Critical
  - Professional Standard
    - The budget should be balanced
    - Any deficit spending should be visible and explained
  - Definition
    - Deficit spending means the district is spending beyond its means

Thirteen Ways Districts Get in Trouble

- #12 Estimating the Ending Fund Balance (EFB)
  - Exposure
    - Critical
  - Professional Standard
    - A district must have the ability to accurately reflect its net ending balance throughout the budget monitoring process. The first and second interim reports should provide valid updates of the district's projected net ending balance. The district should have tools and procedures that ensure an early warning of any discrepancies between the budgeted and actual revenues and expenses
  - Definition
    - When all is said and done and the books have been closed, it is the amount of money remaining in the fund, net of any designations in the restricted and unrestricted accounts. Budget to actuals

Thirteen Ways Districts Get in Trouble

- #13 Management of Cash
  - Exposure
    - Critical
  - Professional Standard
    - All districts must project cash balances on a weekly basis and prepare appropriate cash flow documents in order to assess the need for short term borrowing and the potential of cash insolvency.
  - Definition
    - Cash is not budget and understanding the difference between these two things is critical for boards, superintendents and staff. Cash position represents the actual available dollars at any given time held in the county treasury.

The Basics of AB 1200/2756
What does this mean to you?

- **County Office Review at a Minimum of Three Specific Data Collection Points**
  - Budget Approval
  - First and Second Interim Reporting
    - Positive, Qualified and Negative Certifications
    - COE <u>Must</u> Assess Solvency for the Current Plus One or Two Years
  - Disclosures

The Basics of AB 1200/2756
What does this mean to you?

- **Possible Actions Under a Qualified Certification (Budget)**
  - Fiscal Expert Assignment
  - Budget Analysis and New Financial Projections
  - Approval of New Debt Issuance
  - Longer Period of Review for Collective Bargaining Agreements
  - Encumber all Contracts and Other Obligations
  - Withhold Compensation from Superintendent and Governing Board

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The Basics of AB 1200/2756
What does this mean to you?

- **Possible Actions Under a Negative Certification (Cash)**
  - All Actions Under a Qualified plus:
  - Develop and Impose a Budget in Consultation with the district and CDE
  - Stay or Rescind Any Action of the Board that is Inconsistent with Fiscal Recovery
  - In Consultation with the District Develop a Fiscal Recovery Plan
  - Assign a Fiscal Advisor
  - May Not Abrogate any Provisions of the Collective Bargaining Agreement

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What is Cash Insolvency?

- Generally speaking Cash Insolvency occurs when the cash in payroll exceeds the cash available in the county treasury (or other possible sources of cash) and all options for borrowing have been exhausted.
- Cash insolvency is a limited function of deficit spending, erosion of fund balance, sustained negative cash flow over time, and is impacted by cash deferrals and entitlement reductions to the RL made by the state.

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What Does It Mean To Be Insolvent?

- You have negative cash flow
- Your options for borrowing are nonexistent
- You cannot meet your cash obligations for the current plus one year
- You cannot make payroll
- You will lose your superintendent and local governance option
- Most likely in a state takeover your fiscal situation gets worse not better

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What Happens If Your District Gets into Financial Trouble?

- Intervention by the County Office of Education
- The role of FCMAT
- Responsibilities of a Fiscal Advisor
- Responsibilities of a Trustee
- Responsibilities of a State Administrator
- Responsibilities of the District

Intervention by the County Office of Education

- Intervention under the law starts with the County Superintendent
  - Level of intervention is progressive and can be tailored to the severity of the problem
  - An adverse interim report or disapproved budget puts the COE in charge to determine the level of corrective action needed
  - A fiscal expert may be appointed when a district has a qualified report. A fiscal expert has limited authority
- Remember, the goal of the COE is to assist the district in resolving its financial problem at the lowest level of outside intervention
  - The COE can be more helpful when you are candid and get it involved early
  - A Budget Review Committee is used to adjudicate disputes between the district and the COE if they do not agree on the problem
- Try to help the COE to help you

The Role of FCMAT

- FCMAT is a support agency for county offices of education, school districts, charter schools, and community colleges
- The primary function of FCMAT is to assist county offices in helping school districts avoid emergency loans and state takeover
- FCMAT has multiple roles including professional and product development, auditing for fraud, managing student data systems, and intervening in fiscal emergencies
- FCMAT is a resource not only for professional staff but for school board members as well
- FCMAT staff report to the Legislature and Governor and are active on several state boards and commissions

Getting Out of Trouble

- Characteristics of districts that make a successful turnaround
  - Recognize they have a problem
  - Don’t mask the problem
  - Take advantage of financial expertise available
  - Work collaboratively with oversight agencies
  - Are part of the solution
- Characteristics of districts that require severe measures
  - Deny they have a problem
  - Resist scrutiny from outsiders
  - Don’t seek external assistance
  - Combative with oversight agencies

What to do back at home?

- Maintain reserves
- Preserve cash and avoid the need to get a TRAN. If you don't have to borrow, don't
- Project enrollment conservatively and don't create new classes until the students materialize
- Communicate accurately and regularly to your constituents and reinforce the concept that things could deteriorate
- Consider carefully all of the regulations related to the Education Protection Account (EPA)

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What to do back at home?

- Consider carefully whether or not furlough days still make sense for your district
- Consider carefully the impact of TK and Transportation
- Maximize the use of the flexibility options
- Resist the temptation to enter into non-voter approved debt as your general fund cannot bear debt service payments in the future
- Create your own district Profile!!!

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Is There Any Real Reason To Feel Positive???

- Proposition 30
- The economic landscape has changed significantly from just one year ago some things positive
- Education polls more strongly than any other issue in California
- Districts and County Offices have had to look seriously at what is really important
- Most districts have survived
- Potential economic growth in 2013-14 and 2014-15

Some Realities

Old School

- Education Will Get Adequate Funding
- Solutions Will Come From Sacramento
- You Can Do More With Less
- Reacting to Budget Reductions Suggested by Someone Else
- Averages Applied to Most Districts
- Mid-year cuts? Never!
- Cash is an afterthought

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Some Realities

New School

Funding For Education Is Not Going To Increase Dramatically in the Near Term

Every District Is Different Now

We Must Use Productivity Tools and Advanced Communication Techniques

Operating With Increased Efficiency and Effectiveness is a Must

Conservation of Staff

Budget Solutions Are Generated Locally

Mid-year cuts—Annual Possibility

Cash is a Continuing Challenge

What Works

- Honesty and Integrity
- Focusing on the Big Picture First
- Having Good Materials and Information Tailored to the Specific Audience
- A Common Message and Purpose With Many Voices
- Trusting Your Public

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Questions

- Proposition 30—Are we saved?
- I’m a basic aid district, do I need to worry about any of this?
- What might we expect in the Governor’s January budget?
- Our assessed valuation has fallen too much for us to be able to sell our GO bonds. Should we get a Bond Anticipation Note (BAN)?
- As a board member, what is the most significant fiscal issue of which I should be aware today?

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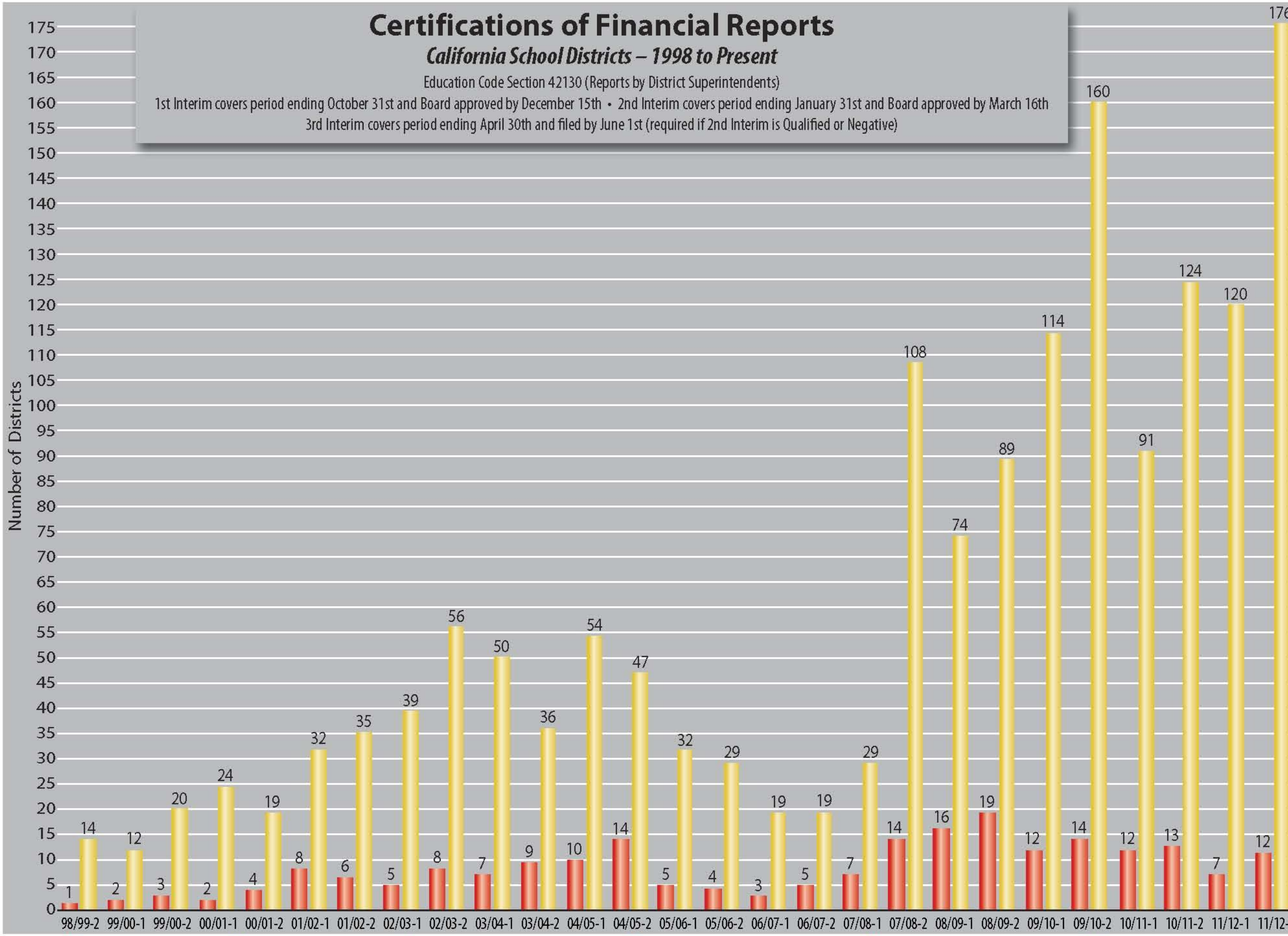

Negative Certification · Qualified Certification · Preliminary Negative Certification · Preliminary Qualified Certification · Projected Negative Certification · Projected Qualified Certification

Positive Certification: Shall be assigned to any school district that, based upon current projections, will meet its financial obligations for the current fiscal year and subsequent two fiscal years.

Qualified Certification: Shall be assigned to any school district that, based upon current projections, may not meet its financial obligations for the current fiscal year or two subsequent fiscal years.

Negative Certification: Shall be assigned to any school district that, based upon current projections, will be unable to meet its financial obligations for the remainder of the fiscal year or the subsequent fiscal year.

Projected results are based on an informal survey of educational agencies.

Fiscal Crisis & Management Assistance Team 5/24/12