EDUCATION: TOMORROW'S FUTURE
SAN BERNARDINO COUNTY SUPERINTENDENT OF SCHOOLS
Gary S. Thomas, Ed.D., Superintendent

April 5, 2012

Mr. Casey Cridelich, Assistant Superintendent Business Services
Rialto Unified School District
182 East Walnut Avenue
Rialto, CA 92376-3598

Dear Mr. Cridelich:

Thank you for the submission of the **Rialto Unified School District 2011-12 Second Interim Financial Report**. However, it was noted that the district board did not take action on the Second Interim Financial Report until March 28, 2012 which was after the state authorized deadline of March 17, 2012. We understand that the delay was to allow further time to develop a fiscal action plan that could be board approved in order to meet ongoing fiscal obligations in the subsequent fiscal years.

The Office of the San Bernardino County Superintendent of Schools has reviewed the Second Interim Financial Report for the period ending **January 31, 2012**. Based on our analysis, the data provided supports the board's ***Positive Certification*** of the district's financial condition and ability to meet its financial obligations in the current and two subsequent fiscal years upon implementation of a fiscal action plan reducing staffing and services costs in the subsequent fiscal years.

Our review included an assessment and analysis of the following major components of the district's report:

- Ending Cash Position and Monthly Cash Projections
- Current and Multiyear Unrestricted Reserve Levels
- Unrestricted Deficit Spending Trends
- Average Daily Attendance (ADA) & Enrollment Projections
- Current and Multiyear Projections
- Negotiations Status and Salary and Benefit Trends
- Long Term Debt
- Ongoing Implications

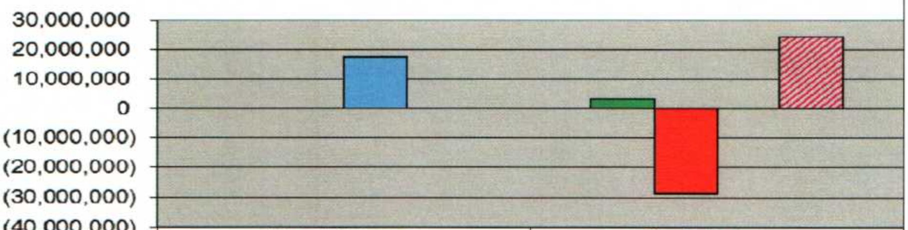
The Second Interim Financial Report provides the Governing Board with the opportunity to revise and review its operating budget plan based on the most recent State Budget information and local decisions made since the First Interim Financial Report. This plan should incorporate any updated revenue projections and utilization of expenditures to meet the goals and financial obligations of the school district in the current and two subsequent fiscal years. To ensure that the district's operating budget continues to reflect that plan, our office noted the following items that should be taken into consideration:

- **ENDING CASH POSITION AND MONTHLY CASH PROJECTIONS** – Due to the current State Budget including significant deferrals of state revenues, changes in apportionment distribution schedules, and ongoing state funding reductions, the monitoring and projection of monthly cash balances have become increasingly critical to ensure fiscal solvency. The deferral of state revenues and changes in distribution schedules by the state can cause a district's cash balances to be depleted, even if budget plans indicate a positive fund balance. Our review of the cash flow provided by the district, in conjunction with our internal cash analysis, indicates that the district will have a positive cash balance at the end of each month and at the end of the current fiscal year through the use of temporary interfund borrowing and Tax and Revenue Anticipation Notes (TRANs). To maintain a positive cash position, the district issued TRANs of $15 million in July 2011 that was repaid in January 2012 and issued $24.9 million in February 2012 that must be repaid with the district's deferred 2011-12 apportionments projected to be received in July and August 2012. The district is also projecting additional temporary interfund borrowing of $7 million in May and June 2012, which, if borrowed, will require repayment by June 30, 2013. Our analysis of the district's cash flow reflects the June 30 cash balance is estimated to be 17.66% of the projected 2011-12 Ending Fund Balance, <u>including</u> cross-year temporary borrowing. Without including cross-year temporary borrowing the district's cash balance is depleted to -165.2% of the projected 2011-12 Ending Fund Balance.

Currently the state is deferring approximately $50 million of the district's 2011-12 state aid into the 2012-13 fiscal year. Additionally, the district's revenue limit is computed to be 6.6% Property Taxes and 93.4% State Aid, which means your district will realize a greater loss of cash due to state deferrals than a higher property tax district.

A good cash projection will allow the district to schedule expenditures in months when adequate cash will be available.

COMPARISON OF FUND BALANCE AND CASH BALANCE



	Fund Balance	Cash Balance
June 30 Cash Balance		3,140,076
Cash Minus Temp. Borrowing		(28,779,924)
Ending Fund Balance	17,781,115	
Cash Balance Without Deferrals*		24,535,190

*Cash Balance Without Deferrals is informational only. Deferrals are included in Fund Balance but do not provide any actual cash until received in the next fiscal year.

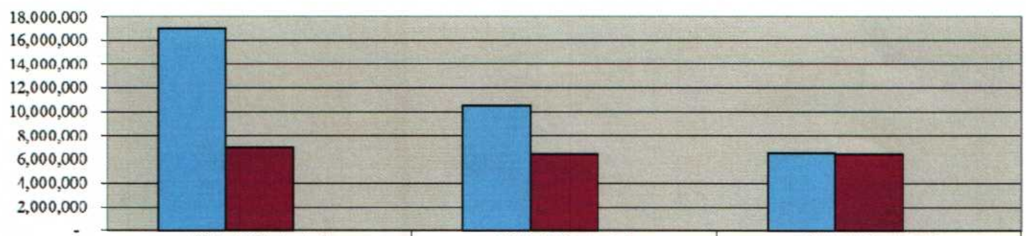
- **CURRENT AND MULTIYEAR UNRESTRICTED RESERVE LEVELS** – As certified by the district's Governing Board, the Second Interim Financial Report projects an unrestricted ending balance reserve in the General Fund of 7.3%. The district is projecting unrestricted ending fund balance reserves of 4.9% in 2012-13 and of 3.0% in 2013-14.

The district is projecting to meet minimum state reserves in all fiscal years through the use of board approved reductions. The district has incorporated approximately $10.7 million in ongoing budget reductions that were approved by resolution of the governing board on February 17 and 22, 2012 in the projections for the 2013-14 fiscal year. The district has supplied our office with a fiscal action plan for implementation of these expenditure reductions. If these reductions are not implemented as planned, the district will not be able to meet ongoing fiscal obligations.

The district has not included the potential $370 per ADA state aid trigger reduction in the 2012-13 projections, if the Governor's Tax Initiative fails. However, the Governing Board has identified and approved a contingency plan to implement expenditure reductions should the tax initiatives fail. This contingency plan has identified up to $14.1 million in ongoing reductions to be implemented in the 2012-13 fiscal year. Some of the reductions identified require negotiation with the bargaining units. The district should specifically identify what reductions have been implemented and incorporated into the 2012-13 Adopted Budget and what reductions are still pending negotiations. Our office recommends that the district not include planned reductions that while board approved, are not yet negotiated with the bargaining units in the multiyear financial projections to present a clearer picture of actual reductions that can be implemented.

The district has incorporated a 2.40% Cost of Living Adjustment (COLA) in the 2013-14 fiscal year as estimated by the School Services of California's (SSC) dartboard, but has **not** set aside any unrestricted reserves in the event that this COLA isn't funded. If these revenues are not realized, the district may not meet the minimum state recommended reserves in the 2013-14 fiscal year. **Our office recommends that the district continue to be proactive by developing contingency plans in response to the current state economic forecasts and ever-changing budget proposals.**

UNRESTRICTED FUND BALANCE RESERVES



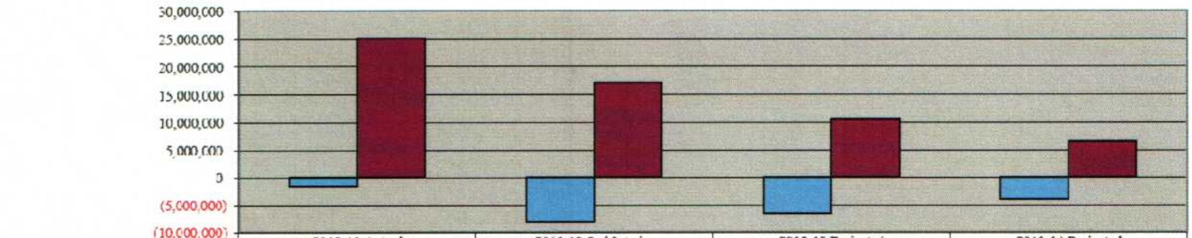
	2011-12 Projected	2012-13 Projected	2013-14 Projected
Available Reserves	16,992,864	10,513,949	6,518,028
Minimum State Required Reserves	7,006,376	6,401,795	6,425,948
Unrestricted Available Reserves %	7.3%	4.9%	3.0%

- **UNRESTRICTED DEFICIT SPENDING TRENDS** – The district is projecting unrestricted expenditures to exceed unrestricted revenues by $8,160,789 in the current fiscal year, primarily due to loss of one-time federal revenues, state aid reductions, budgeted expenditure of prior year carryover, and ongoing operational costs. The district is continuing this trend of deficit spending in fiscal year 2012-13 by $6,478,915 and in fiscal year 2013-14 by $3,995,921. This ongoing deficit spending appears to be attributed to loss of one-time federal revenues, increased state aid reductions, and ongoing operational costs. If the proposed $370 per ADA state aid trigger is implemented in 2012-13, this level of deficit spending will increase substantially causing fiscal insolvency and instability, unless the district is able to negotiate the planned reductions included in the contingency plan. Anticipated deficit spending should be for one-time, non-recurring expenditures to avoid depletion of the district's on-going unrestricted reserves. Ongoing deficit spending will cause an even greater reliance on district cash reserves.

The district's projected deficit spending is **not** within the established state standard for the current and two subsequent fiscal years. The State's established standard is one-third (1/3) of the district's available unrestricted reserve percentage.

The following chart displays the actual Unrestricted General Fund balance change for the prior fiscal year and the projected change based on the Second Interim Report and board approved multi-year financial projections for the 2011-12 through 2013-14 fiscal years.

CHANGE IN UNRESTRICTED FUND BALANCE TRENDS



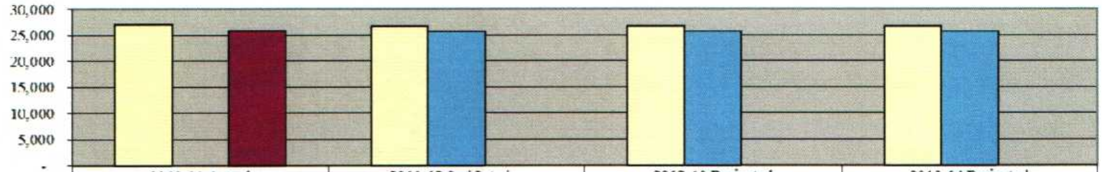
	2010-11 Actual	2011-12 2nd Interim	2012-13 Projected	2013-14 Projected
Change in Unrestricted Fund Balance	(1,455,623)	(8,160,789)	(6,478,915)	(3,995,921)
Unrestricted Fund Balance	25,113,331	17,125,865	10,646,950	6,651,029

- **AVERAGE DAILY ATTENDANCE (ADA) & ENROLLMENT PROJECTIONS** – The district is projecting 2011-12 K-12 P-2 ADA of 25,746 representing a 0.26% decline over prior year P-2 ADA. Based on an enrollment projection of 26,763, the district is anticipating a current year attendance ratio of 96.2%. The district is projecting a 0% change in ADA for 2012-13 and 2013-14, resulting in an attendance ratio of 96.2% for 2012-13 and 2013-14.

  The state's standard is based on the average ratio of P-2 ADA to enrollment over the past three years. Based on the enrollment and ADA projections for the current and two subsequent fiscal years, the district is **not** within the state standard of 94.8% for each of those years. The district attributes the higher projected ratio to aggressive attendance recovery programs it has implemented. The district has indicated they have experienced an average increase of 1.1% to the attendance ratio over the past two years. The current projections of ADA and enrollment show that the district expects a 0.72% increase over the prior year ratio and future year attendance ratios to remain at the 2011-12 projection, which is 96.2%. Although the district appears to be projecting ADA at a reasonable level based on that assumption, we recommend that the district continue to monitor changes in attendance and enrollment closely. If the projected ADA or enrollment does not materialize as anticipated, the board will need to adjust the budget accordingly.

  The following chart displays the district's actual P-2 ADA and enrollment in the prior year, along with the district's projected ADA and enrollment for the current and two subsequent fiscal years. Since a significant portion of a school district's revenue is derived from ADA, it is imperative to monitor the correlation between enrollment and ADA closely.

COMPARISON OF ATTENDANCE TO ENROLLMENT TRENDS



	2010-11 Actual	2011-12 2nd Interim	2012-13 Projected	2013-14 Projected
Enrollment	27,026	26,763	26,763	26,763
ADA Projections		25,746	25,746	25,746
Actual ADA	25,812			
ADA/Enrollment Ratio	95.51%	96.20%	96.20%	96.20%

- **CURRENT AND MULTIYEAR PROJECTIONS** – Our review included an analysis of the district's projection of revenues and expenditures in the current and two subsequent fiscal years. The district's projection of current and subsequent state aid appears to be reasonable, but does not include the potential $370 per ADA state aid trigger reduction, in the event the tax initiative is not voter-approved.

  The district is projecting a decline in current year ADA and is utilizing the state's prior year guarantee of ADA in the state aid revenue limit projections. The state allows districts to utilize the current or prior year P-2 district ADA whichever is higher to determine annual state aid revenue limit projections. Any ADA related to county operated programs or contracted programs such as Non Public School (NPS) are always funded on the current year reported annual attendance.

  The district has projected for one-time Federal Education Jobs revenues received or deferred to the current fiscal year in the amount of $5,068,710. It appears that the district has adjusted the multiyear revenue projections to remove that funding. These funds must be fully spent by September 30, 2012.

  Our review of the district's current and projected expenditures indicates $10.7 million of salary and benefit cost reductions reflected in the 2012-13 fiscal year projections. The fiscal action plan indicates these reductions have been fully approved and represent a reduction of 89 certificated and 75 classified FTE. The district is currently maintaining a 177-day school year which includes five (5) Certificated non-work days (furloughs).

- **NEGOTIATIONS STATUS AND SALARY AND BENEFIT TRENDS** – The district has indicated that negotiations have been finalized with the certificated bargaining unit, but not finalized for the classified bargaining unit. The term of the certificated agreement is July 1, 2011 through June 30, 2014 and includes five (5) furlough days (three instructional, two non-instructional), annual step and column adjustments, and 100% district-paid health and welfare benefits. Reopeners are provided for the 2012-13 and 2013-14 fiscal years.

  Additionally, the district has included in the assumptions for future years, an estimated increase in health benefit costs of 3.8%, since the district currently does not have a cap on the employer cost of health benefits. This escalating cost increase for full health benefit coverage is one of the factors contributing to the ongoing deficit spending projected by the district.

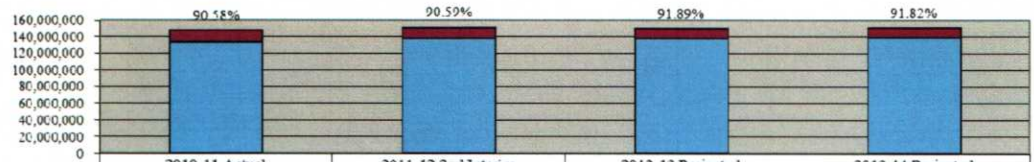
  Pursuant to AB1200/AB2756, please provide an analysis of the costs or savings associated with any proposed or tentative agreement(s), or MOUs including the impact on the current operating budget and multi-year financial projections, **at least ten days prior to adoption by the board**. Budget transfer documents implementing any adjustment(s) must also be reflected in the financial system no later than 45 days after approval of the agreement by the Governing Board. If the costs associated with a negotiated change in salaries or benefits reduce the district's available unrestricted ending balance below the minimum required state reserve level in the current and/or two subsequent fiscal years, the district Governing Board will be required to take action to reduce other expenditures in order to maintain the required state reserves in all fiscal years.

An outline of the disclosure procedures and a copy of the required disclosure documents are available in an EXCEL format on the San Bernardino County Superintendent of Schools, Business Administrators website (**http://www2.sbcss.k12.ca.us/sbcss/busServe/bas FormFI.php**), under AB1200/AB2756 Salary disclosure. Instructions for completing these forms are also available on the website. These forms must be completed and disclosures taken to the board for all contract changes regardless of fiscal impact. This includes contract wording, furlough or non-work days, etc.

The majority of a school district's budget is spent on salaries and benefits. The following chart shows the percentage of unrestricted salaries and benefits to the total unrestricted general fund expenditures for the prior year, Second Interim, and multi-year projections. The state's established standard is based on an average of the district's prior three years of unrestricted salaries to total unrestricted expenditures.

The district's ratio of unrestricted salaries and benefits to total unrestricted expenditures are within the state's established standard. However, with the ratio at 90.59%, this leaves only 9.41% of the budget for other expenditures such as supplies and utilities. If salaries and benefits are changing at a rate faster than total expenditures, these costs will consume a disproportionately greater share of the district's resources, putting significant pressures on the rest of the budget. This could happen as well with reduced ongoing revenues or uses of one time state or federal revenues. We recommend that the district monitor these ratios and take them into consideration prior to staffing changes or entering into a collective bargaining agreement.

RATIO OF UNRESTRICTED SALARIES AND BENEFITS TO UNRESTRICTED EXPENDITURES



	2010-11 Actual	2011-12 2nd Interim	2012-13 Projected	2013-14 Projected
Ratio Salaries & Benefits	90.58%	90.59%	91.89%	91.82%
Total Other Unrestricted Expenditures	13,908,253	14,247,250	12,150,929	12,323,439
Total Unrestricted Salaries and Benefits	133,785,633	137,220,854	137,731,202	138,265,681

- **LONG TERM DEBT** – At June 30, 2011, the district had non-voter approved long-term debt of $27,469,967 which constitutes 13.01% of the district's projected general fund budget. The debt repayment is budgeted in the General, Capital Facilities, and Debt Service Funds. The district should monitor the revenue stream of these funds closely to ensure that adequate revenues are received to provide for the current debt repayment schedule for principal and interest payments, and take appropriate action should revenues not materialize as anticipated. **It is recommended that a district with a debt ratio greater than 25% increase its minimum unrestricted reserve levels to twice the state standard to ensure funds will be available to meet the repayment obligations.**

- **ONGOING IMPLICATIONS** – On January 5, 2012, Governor Brown released his initial 2012-13 State Budget Proposal that includes major changes for the Education Community. Some of the main points of the proposal are:
  - ➢ State revenues are based on the passage of the Governor's Temporary Tax Initiative in November 2012. If the tax initiative is not successful, school districts and county offices of education will be facing a \$370 per ADA mid-year Trigger Cut.
  - ➢ Elimination of Home to School Transportation funding was included in the initial proposal. Subsequently, the Governor has proposed to fund Home to School Transportation for the 2012-13 fiscal year and include it as a one-time only adjustment to the weighted student funding formula. By including ongoing support of home to school transportation funding, the state will need to reduce state aid revenues by an estimated additional \$85 per ADA, potentially increasing the state aid reduction for 2012-13 to \$455 per ADA should the tax initiative be unsuccessful. If the tax initiative is passed, the one-time transportation funding for 2012-13 would be paid from funds set aside to reduce state aid deferrals.
  - ➢ Implementation of school finance reform using a "Weighted Student Funding Formula", consolidating many major state categorical programs, including EIA, Transportation, K-3 CSR, with the Tier III programs and State Revenue Limit state aid funding. These categorical programs would be combined with revenue limit components and apportioned to districts as a base grant estimated at \$4,920 (no differential is included for high school districts or unified districts compared to elementary districts) plus add-ons for concentrations of English Learners (EL) and Free and Reduced Lunch Program students. Funding would be pro-rated in an increasing ratio between existing and new formulas over the next six years.
  - ➢ An estimated 3.17% COLA that will be <u>unfunded</u>. Instead of increasing the level of funding to schools, the Governor is proposing to buy down a portion of the current state deferrals, but only if his Tax Initiative passes.

Based on these current ever-changing proposals, districts have been advised to "Plan for the Worst and Hope for the Best". As additional information becomes known with the Governor's May Budget Revision, our office will continue to provide updates regarding assumptions to be utilized for the 2012-13 Adopted Budget and subsequent fiscal year multi-year projections.

If you have any questions concerning our review of the district's 2011-12 Second Interim Financial Report, please contact the undersigned.

Sincerely,

Thomas G. Cassida Jr., MBA
Business Services Advisor
Business Advisory Services
(909) 777-0761

C:

Dr. Gary S. Thomas, Ed.D., County Superintendent (SBCSS)
Mr. Ted Alejandre, Assistant Superintendent-Business Services (SBCSS)
Mrs. Teri Kelly, Director-Business Advisory Services (SBCSS)

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