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DATE: August 10, 2011

TO: Dr. Jonathan Greenberg, District Superintendent
Mr. Eric J. Kroencke, Board President
Ms. Candace Reines, Assistant Superintendent
Perris Union High School District

FROM: Kenneth M. Young, Riverside County Superintendent of Schools
By: Paul C. Jessup
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SUBJECT: 2011-12 ADOPTED BUDGET–CONDITIONAL APPROVAL

In accordance with California Education Code (EC) Section 42127, our office has reviewed the district's 2011-12 Adopted Budget to determine whether it complies with the criteria and standards adopted by the State Board of Education and whether it allows the district to meet its financial obligations for the 2011-12 fiscal year.

Assembly Bill 114 (Chapter 43, Statutes of 2011) as signed by the Governor on June 30, 2011, requires the district to budget in 2011-12 the same level of revenue per average daily attendance (ADA) as it received in 2010-11, and to maintain staff and program levels commensurate with that level. Furthermore, AB 114 prohibits the county superintendent, as a condition for approving the 2011-12 Adopted Budget, from requiring the district to demonstrate its ability to meet its financial obligations in the two subsequent fiscal years. Although AB 114 imposes minor limitations on the county superintendent's budget reviews, it does not eliminate the county superintendent's overall fiscal oversight responsibilities. Our office will continue to advise and intervene in the district's budget adoption and interim reporting processes, as necessary, to ensure the district's fiscal solvency.

Current law, as enacted through AB 2756 (Chapter 52, Statutes of 2004), also requires the county superintendent to review and consider any studies, reports, evaluations, or audits that may contain evidence that a district is showing fiscal distress. For 2010-11, the district issued a qualified certification for the 2010-11 Second Interim Financial Report.

Based on our analysis of the information submitted, the county superintendent conditionally approves the district's budget due to the following concerns:

- *2011-12 Budget Shortfall* – The district's 2011-12 Adopted Budget includes more than $3.8 million in reductions to salaries and benefits expenditures, which are still subject to negotiation with the district's bargaining units. Without these reductions, the district does not meet the minimum reserve requirement in the current year, assuming flat revenue limit funding in 2011-12. **In a scenario assuming a $300 per ADA revenue limit reduction and without these reductions, our office projects the district will close the 2011-12 fiscal year with a negative ending General Fund balance.**

- *Employee Negotiations* – The district is currently at impasse with the certificated bargaining unit, and continues to negotiate with the classified bargaining unit. As noted above, the district is relying heavily on negotiated salary and benefit concessions to balance the 2011-12 budget.

- *Operating Deficit* – Multi-year financial projections indicate a substantial General Fund operating deficit for the current fiscal year, assuming an ongoing $330 per ADA revenue limit reduction (estimated at $3.0 million). Over the prior two fiscal years, the district has reduced its combined General Fund balance by $6.3 million, spending down reserves and using one-time funds, such as a $5.0 million transfer from the Special Reserve Fund for Capital Outlay, to support ongoing expenditures.

In addition, although not a condition for approval, our office has evaluated the district's budget to determine whether it is consistent with a financial plan that will enable the district to meet its multi-year financial commitments. Based on our analysis of the information submitted, we note the following significant concerns regarding the two subsequent fiscal years:

- *2012-13 & 2013-14 Budget Shortfalls* – Multi-year financial projections indicate a $9.7 million budget shortfall in 2012-13 and an $11.2 million shortfall in 2013-14, assuming a $330 per ADA revenue limit reduction (estimated at $3.0 million annually). Even in a flat-funding scenario, our office projects a negative ending General Fund balance in the two subsequent fiscal years.

- *Flat Enrollment* – ADA projections reflect a slight decrease in 2011-12 and no growth in the two subsequent fiscal years.

- *Choice Online Audit Finding* – The district continues its efforts to eliminate an audit finding regarding instructional time and attendance accounting procedures for one of its sponsored charter schools, Choice 2000 On-line. Based on the 2009-10 Audit Report, the cumulative audit penalty is approximately $5.7 million. The district has not included this cost in its multi-year financial projections.

Implications of Conditional Approval

As a result of the conditional approval, our office is requiring that the district takes the following actions **by September 8, 2011**:

- *2010-11 Unaudited Actuals* – Close prior year accounts, and certify 2010-11 Unaudited Actuals.

- *2011-12 Revised Budget* – Identify and make necessary budget revisions to rebuild the district's reserves in order meet the minimum-required level in 2011-12.

- *Multi-Year Financial Projections* – Submit revised multi-year financial projections, including up-to-date ADA and enrollment estimates, and a plan to address the budget shortfalls identified in the two subsequent fiscal years.

- *Cash Flow* – Provide our office with updated 2011-12 cash flow projections with actuals through August 31, 2011, and reflecting the July 2011 Advance Apportionment payment schedule.

Our office will review the district's response, and approve or disapprove the district's revised budget no later than October 8, 2011.

Contingency Planning

The 2011-12 Budget Act provides for an automatic reduction to state appropriations, including K-12 education funding, if state revenues fall short of projections.

The K-12 education reductions would impact revenue limits ($1.5 billion) and Home-to-School Transportation ($248 million) funding; however the actual revenue limit reduction depends on the amount of the shortfall in revenues and could range from zero to four percent of the district's undeficited base revenue limit. While the district by law cannot budget for these reductions, the risk to Perris Union High's budget is as follows:

- *Home-to-School Transportation* – The district's budget includes $693,783 in Home-to-School and Special Education Transportation revenues. Our understanding is the triggered reduction would reduce transportation funding by half. Since these program funds flow to districts on a monthly basis, a triggered reduction would result in no transportation payments for the last six months of the fiscal year, thereby impacting the General Fund cash flow.

- *Revenue Limit* – Assuming the state triggers a full four percent reduction, our office estimates a potential revenue limit cut of $2.7 million for Perris Union High in 2011-12 ($300 per 9,003 funded ADA).

As noted in our most recent guidance letter, the final State Budget package includes optimistic revenue assumptions, which if not realized could very likely result in the state's implementation of the K-12 education trigger reductions outlined above. In order to prudently plan for this possibility, our office strongly recommends the district develop contingency plans to address a potential mid-year funding reduction. **As the district's current budget appears to lack sufficient reserves to cover a potential 2011-12 revenue loss, we urge the district to either work with its bargaining units <u>now</u> to secure the flexibility necessary to reduce the school year, as authorized in AB 114, or develop another expenditure reduction plan.** Furthermore, we advise the district to act quickly and implement additional solutions to rebuild its reserve, and balance its revenues and expenditures to ensure its long-term fiscal health.

If our office can be of any support, or if you have any questions regarding this letter, please do not hesitate to contact me or the District Fiscal Services staff.

PJ:NS:mh