B U E N A   P A R K   S C H O O L   D I S T R I C T
Buena Park, California 90620

March 13, 2017

TO: Governing Board

FROM: Kelvin Tsunezumi, Assistant Superintendent, Administrative Services

SUBJECT: **2016-17 SECOND INTERIM FINANCIAL REPORT**

BACKGROUND:

Pursuant to Education Code 42130, the Governing Board is required to certify within 45 days of the close of the period ending January 31 (second interim reporting period) that the District will be able to meet its financial obligations for the budget year and for two subsequent years. The Second Interim Report updates the District's Board approved General Fund budget with the most current information available. The following report is presented for your approval as an action item. The report has been reviewed in accordance with the State Board of Education Criteria & Standards.

CURRENT CONSIDERATIONS:

The State

The 2017-18 Governor's Proposal was released on January 10th and assumptions from this proposal are incorporated as part of the Second Interim Report.

Over the past four years, public education in California has enjoyed unprecedented growth in funding largely due to restoration of past reductions, growth in the economy, and passage of Proposition 30 in November of 2012. In three of the past four years, State revenue collections exceeded forecasts by a substantial amount. However, even after the State lowered its revenue forecast for 2016-17, revenues are coming in below even the lowered estimates. Revenue estimates have fallen short five of the last seven months. As a result, the Governor's Proposal has lowered revenue projections even more substantially.

Compared to the revenue forecast accompanying the current-year Budget, State revenues are projected to be down $5.8 billion over the three-year period of 2015-16, 2016-17, and 2017-18. Year over year however, revenues are still proposed to increase. On the specifics of the 2017-18 Budget, General Fund revenues and transfers are proposed at $124 billion (a 4.4% increase year over year) compared to expenditures of $122.5 billion (a 0.2% decline). The State would end the 2017-18 fiscal year with a fund balance of $2.5 billion, plus $7.9 billion in the Rainy Day Fund.

The Governor continues to call for prudent fiscal practices that provide a balanced budget while continuing to plan and save for the future. He warns that the State will inevitably face a recession. The Department of Finance forecasts deficits of $18 billion over three years if the State were to experience even a modest recession.

Specific to Education, the Governor's budget proposal assumes the following:

- Proposition 98. For the current year, 2016-17, the Proposition 98 guarantee is estimated at $71.4 billion, down $506 million from the enacted level, given lower than expected General Fund tax revenues. For 2017-18, the Governor proposes a Proposition 98 guarantee of $73.5 billion, an increase of $2.1 billion from 2016-17 but nearly $953 million less than November projections from the Legislative Analyst's Office.
- COLA. The estimated statutory COLA for 2017-18 is estimated at 1.48%, and is applied to the LCFF base grant targets and education programs funded outside of LCFF including Special Education and Child Nutrition.
- Local Control Funding Formula (LCFF). The Governor's Proposal revises funding rates with significant lowering of funding in 2017-18.

	2017-18	2018-19	2019-20
2016-17 State Adopted Budget	72.99%	40.36%	73.98%
2017-18 Governor's Proposal	23.67%	53.85%	68.94%

With 2016-17's gap closure funding, LCFF is now roughly 96% of the way towards full implementation. While the 2017-18 funding rate makes no additional progress toward LCFF full funding, it does prevent erosion in LCFF implementation by proposing funding equal to the cost of the COLA increase on LCFF target rates.

- Apportionment Deferral. The Governor proposes a "one-time" cash deferral given a decrease in the 2016-17 Proposition 98 minimum funding guarantee caused by lower-than-projected State revenues of $859.1 million in LCFF expenditures from June 2017 to July 2017.
- One-Time Discretionary Fund. The Governor proposes one-time discretionary funds totaling $287 million or $48 per ADA (approximately $225K for BPSD). This compares to discretionary funding of $529 and $214 per ADA for 2015-16 and 2016-17 respectively.
- Mandate Block Grant. The Mandate Block Grant (MBG) continues to be funded outside of LCFF and will be increased to reflect the addition of the Training for School Employee Mandated Reporters program. This translates to an estimated $1.40 per ADA increase to the MBG for a proposed total funding of $29.40 per ADA.
- CalSTRS & CalPERS. Employer costs for CalSTRS and CalPERS will increase significantly over the next several years. While the Budget acknowledges the challenges posed by these increases coupled with the CalPERS recent decision to lower its discount rate (a move which CalSTRS could follow legislatively) from 7.5 to 7.0 percent, the Budget does not further address the funding challenges faced by school districts.
- Federal Program Funding. The Governor's Proposal specifies that there are significant funding unknowns facing K-14 education at the federal level given the November 2016 election.

The Governor's plan is only a proposal. Legislature approval is required for the proposal to be enacted into law.

<u>Buena Park School District</u>

The District has made the following key budget changes for Second Interim Reporting purposes:

- Total revenues increased by $121,564 (vs. First Interim) with Unrestricted revenues increasing $59,358 and Restricted by $62,206.
- The Unrestricted revenue increase is attributable to:
    - An increase in unrestricted lottery revenue of $28.8K given State estimates of a higher funding level.
    - Local revenue increase of $43.0K due to an increase in Interest Income and Leases & Rentals revenues.
- The Restricted revenue increase is attributable to:
    - Federal revenues increase of $40.0K due to receipt of Medi-Cal revenues. Due to the uncertainty in timing on the receipt of these funds, revenues are not recorded until actually received.
    - An increase in restricted lottery funding of $22.2K given State estimates of a higher funding level.
- Total General Fund Combined expenditures decreased by $305,070 (-0.5%) vs. First Interim. General Fund Unrestricted expenditures decreased vs. First Interim by $157,071 while Restricted expenditures decreased by $147,999.
    - The decrease in General Fund Unrestricted expenditures is driven by lower than anticipated year-to-date expenditures in Books & Supplies and reclassification of $157.5K in budget dollars (formerly budgeted in Books & Supplies) to Services & Other Operating Expenditures to ensure that amounts are budgeted in the same line item as where actual expenditures will be recorded.
    - The decrease in General Fund Restricted expenditures is driven by reduced funding for Routine Restricted Maintenance Account (RRMA). At First Interim, the District was advised that to be eligible for facility state matching funds, the District needed to fund RRMA at a minimum of 3% of total General Fund expenditures. Therefore, at First Interim, the District budgeted RRMA at the 3% mark. Post First Interim, School Services of California clarified that a 3% contribution is mandated only after a District receives its first apportionment of state matching funds. Given this new direction, the District reduced RRMA funding by $178.3K.
- Contributions decreased by $178,319 due to the lowered RRMA funding level.

The following table provides additional information about income, one-time transfers and one-time dollars.

INCOME

Budget Item	First Interim Report 2016-17	Second Interim Report 2016-17
LCFF Funding Rate	54.18%	55.28%
Funded LCFF ADA	4,729 ADA (Despite projected student enrollment loss, given protection afforded to school districts, still funded at previous year's ADA.)	4,729 ADA (Despite projected student enrollment loss, given protection afforded to school districts, still funded at previous year's ADA.)
Unduplicated Student Percentage	80.17%	79.68%
COLA	0.00%	0.00%
Lottery ($/ ADA)	$140.00 unrestricted $41.00 restricted	$144.00 unrestricted $45.00 restricted
Special Education Transfer	$5,484,237	$5,484,237
Interest Income	$90,000	$118,000
Deferred Maintenance	$250,000 Contribution	$250,000 Contribution
Mandated Costs	$133,547 (Block Grant) $0 (One-time)	$133,547 (Block Grant) $0 (One-time)

ONE-TIME TRANSFERS IN BPSD 2016-17 BUDGET

One-time transfers are assumed as follows:

Category	From	To
Federal Categorical Transfer	Title 2 Teacher Quality: $200,000	Class Size Reduction: $200,000
Interfund Transfer	General Fund: $250,000	Deferred Maintenance Fund: $250,000

DEFICIT SPENDING AND ENDING BALANCE

At Second Interim the District reports an overall General Fund (Unrestricted & Restricted combined) operating deficit of $2,101,444. The deficit is a result of an unrestricted deficit of $1,136,702 and a restricted deficit of $964,742. Please note that the restricted deficit spending is attributable to funding carryovers that were credited as revenues in the prior year, but are budgeted to be spent in the current year.

In comparison to First Interim, the deficit for the General Fund Combined decreased by $426,634. The Unrestricted deficit was reduced by $394,748 while the deficit for Restricted was reduced by $31,886.

As noted later in the "Multi-Year Projection Considerations" section, given the Governor's Proposal, 2017-18 revenues are anticipated to be significantly lower than forecasted at First

Interim. In preparation of this downturn, the district has already implemented budgetary reductions in the current year (i.e., RRMA contribution reductions, reductions in Books & Supplies budget, etc.) As previously noted, in comparison to First Interim, the District's unrestricted deficit has improved by $394,748 at Second Interim. We will designate and set aside these dollars in reserves and release them in 2017-18 (or when needed) to partially offset the anticipated 2017-18 revenue reductions.

The projected Unrestricted General Fund ending balance of $5,780,143 is comprised of $2,135,424 in Designation for Economic Uncertainties to provide sufficient funding to allow for a 3% economic reserve for uncertainty, revolving cash of $55,000, Stores of $37,436, and $3,552,283 for designated amounts including reserves for: IMFRP, Kid Connection program surplus, provisions for Other Post-Employment Benefits (OPEB), one-time discretionary funds from 2015-16 and 2016-17 to be spent in 2017-18 and/or released in future periods to meet the required 3% reserve requirement, and the aforementioned 2017-18 Deficit set aside reserve.

MULTI-YEAR PROJECTION (MYP) CONSIDERATIONS

The MYP covers the period 2016-17 through 2018-19. The following assumptions are incorporated into the MYP:

- Enrollment. At First Interim, preliminary 2016-17 CBEDS was utilized which reflected an enrollment loss of 46 students vs. the 100 students originally projected. Further refinement of this number revealed a loss of 38 additional students for a total enrollment loss of 84 students. While disappointing, the enrollment loss is still less than the 100 students originally projected. Enrollment projections vs. First Interim are shown below:

	At First Interim	At Second Interim	Change
2016-17	4,822	4,784	<38>
2017-18	4,702	4,664	<38>
2018-19	4,617	4,579	<38>

Updated enrollment projections for 2017-18 forward are currently under development by Decision Insite, the District's demographers.

- LCFF Funding Rate:

	2016-17	2017-18	2018-19
Department of Finance (DOF)	55.28%	23.67%	53.85%
School Services of California (SSC)	55.28%	23.67%	34.42%
BPSD (at Second Interim)	55.28%	23.67%	53.85%
BPSD (at First Interim)	54.18%	72.99%	40.36%

The lowered funding rate has a material impact on projected 2017-18 LCFF revenues. Revenues are reduced by $1.3 million due to the reduced rate. Coupled with the final 2016-17 CBEDS enrollment count which revealed greater enrollment loss, total LCFF revenues are $1.7 million less than budgeted at First Interim.

- Unduplicated Student Percentage Assumption. The MYP assumes unduplicated student percentage over the three-year period as follows.

	2016-17	2017-18	2018-19
Unduplicated Students as a Percentage of Total Enrollment	79.68%	79.68%	79.68%

- CalSTRS & CalPERS. Employer costs related to CalSTRS & CalPERS will increase significantly over the next several years. Rates are as follows:

	2016-17	2017-18	2018-19
CalSTRS	12.58%	14.43%	16.28%
CalPERS	13.888%	15.80%	18.70%
Projected Cost Increase (vs. 2016-17 rate)	---	$603,090	$1,267,078

- Federal Revenues. While no formal direction has been issued by the Federal government, California Department of Education projects a Federal revenue loss of approximately 16% for BPSD vs. 2016-17 funding levels. In the absence of clearer direction, we are assuming a 16% Federal revenue reduction for 2017-18 forward with the expectation that categorical program managers will reduce expenditures to avoid an encroachment.
- Budget Reductions. The following budget actions are assumed to ensure that the District maintains a minimum 3% reserve requirement in all three years covered by the MYP:
    1. Certificated staffing is reduced commensurate with enrollment decline 2017-18 forward. (Unrestricted teacher reductions of 8 plus another 3 teachers are projected in 2017-18 and 2018-19 respectively.)
    2. Suspension of future contributions to IMFRP (i.e., textbook) reserves
        - IMFRP reserves are held constant at $1.1 million
    3. 2016-17 one-time discretionary funds (totaling $1.0 million) held in reserves is released in 2017-18 or 2018-19
    4. Proposed 2017-18 one-time discretionary funds (totaling $225K) to be utilized to offset anticipated 2017-18 deficit.
    5. 2017-18 Deficit set aside reserve of $394.7K released (in 2017-18) to offset anticipated 2017-18 deficit.
    6. Assumes authorization of Supplementary Early Retirement Plan (SERP) for certificated management and non-management. Net savings of $134.7K, $119.3K and $103.7K are projected for 2017-18 through 2018-19 respectively.
    7. Unspecified, on-going budget reductions of $400K are assumed 2017-18 forward. Orange County Department of Education (OCDE) requires the District to provide specifics on the budget reductions with 2017-18 Budget adoption.

- Unrestricted Reserves. Unrestricted reserves are set aside in 2016-17 for Kid Connection ($124.5K), Instructional Materials ($1,122.5K), OPEB or Other Post-Employment Benefits ($592.1K), 2015-16 & 2016-17 one-time funding reserves ($1,713.2K), and 2017-18 Deficit set aside reserves ($394.7K).

Building off of the assumptions above coupled with our 2016-17 projections, we anticipate the unrestricted General Fund to have deficits (revenues vs. expenditures) of $2,101,444, $2,015,349, and $917,414 in 2016-17 through 2018-19 respectively. We further estimate District reserves (i.e. Designation for Economic Uncertainties) for 2016-17 through 2018-19 as follows: 3.0%, 3.0% and 3.2%.

OTHER FUNDS:

The Board previously authorized acceptance of a pre-school grant, totaling $378.1K. These funds are budgeted as mandated by the State in the Child Development Fund (i.e., Fund 12). The Building Fund (i.e., Fund 21) has been updated to reflect the second issuance of our General Obligation bond in April 2017 estimated at $12.2 million. Of this amount, $4.2 million will be utilized to repay our outstanding 2016 Bond Anticipation Note (BAN) and the remaining $8.0 million utilized to fund construction projects including the Gilbert and Whitaker modernization projects.

STAFF RECOMMENDATIONS:

Administration recommends that the Governing Board approve the District's 2016-17 Second Interim Report with a positive certification as well as the attached Fiscal Solvency Statement.

****STRATEGIC PLAN:** Provide a Safe and Positive Learning Environment

2016-17 Second Interim Report – Fiscal Solvency Statement

In submitting the 2016-17 Second Interim report, the Board understands its fiduciary responsibility to maintain fiscal solvency for the current and subsequent two fiscal years.

The District faces the following challenges including:

- Volatility of State general fund revenues
- Deficit spending in the unrestricted general fund
- Declining enrollment
- Increasing operational expenses, such as employer rate increase for CalSTRS and CalPERS

Given the above challenges, the school district will implement ($400,000) in ongoing budget reductions in 2017-18 and an additional ($0) reductions in 2018-19 to maintain fiscal solvency. It is further recognized that the school district will submit a detailed list of Board approved ongoing budget reductions as part of the 2017-18 Preliminary Budget.