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

December 18, 2013

Mr. George Velarde
Assistant Superintendent, Business Services
Yucaipa-Calimesa Jt. Unified School District
12797 Third Street
Yucaipa, CA 92399

Dear Mr. Velarde:

Thank you for the submission of the district's **2013-14 First Interim Financial Report**. We recognize the district's efforts in the development of this financial plan.

The Office of the San Bernardino County Superintendent of Schools has reviewed the First Interim Financial Report submitted by the Yucaipa-Calimesa Joint Unified School District for the period ending **October 31, 2013**. This review has been conducted in the context of the 2013-14 State Budget Act, which changed the way funds are allocated to school districts with the enactment of the Local Control Funding Formula (LCFF). Based on our analysis, the data provided supports the board's ***Qualified certification*** of the district's financial condition which indicates the district may not be able to meet its financial obligations in the current or subsequent two fiscal years. Additionally, we noted that the district has aligned its budgeted revenues to the LCFF model.

Implications of a Qualified Certification

By submitting a qualified First Interim report for the period ending October 31, 2013, the following requirements in the Education Code apply:

1. Copies of the interim report and this letter will be forwarded to the Superintendent of Public Instruction and the State Controller. [Education Code Section 42131(a)(2)]

2. During fiscal years 2013-14 and 2014-15, the district must obtain approval from SBCSS prior to the issuance of all nonvoter approved debt, including Tax and Revenue Anticipation Notes (TRANS) and Certificates of Participation (COPs). [Education Code Section 42133(a)]

3. The County Superintendent is required to present an annual report to a school district's governing board and the Superintendent of Public Instruction regarding the fiscal solvency of any school district with a qualified certification. This annual report will be issued by June 2014. [Education Code Section 1240(e)]

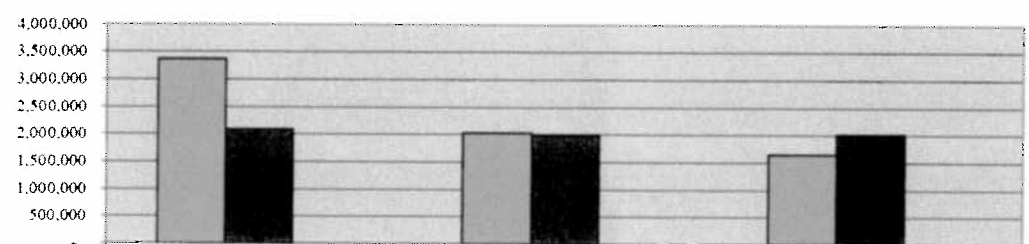
4. The County Superintendent is also required to perform at least one of the actions identified in Education Code Section 42127.6(a)(1)(A) through (G).Our review included an assessment and analysis of the following major components of the district's report:

- Unrestricted Ending Fund Balance and State Minimum Reserve
- Unrestricted Deficit spending trends
- Average Daily Attendance (ADA) & Enrollment
- Revenue and Expenditure Projections
- Ending cash and Monthly cash flows
- Staffing Projections/Salary Settlements
- Multi-year Financial Projections
- Long Term Debt
- Charter Schools

- **UNRESTRICTED ENDING FUND BALANCE AND STATE MINIMUM RESERVE** – As certified by the district's Governing Board, the First Interim Financial Report projects an unrestricted ending balance reserve in the General Fund of 4.8%. The district is projecting unrestricted ending fund balance reserves at 3.1% in 2014-15 and at 2.5% in 2015-16. The District's State Required Minimum Reserve percentage is 3.0%.

For fiscal year 2015-16, the district does not meet the state required minimum reserve. We recommend that the district's Governing Board approve a contingency or fiscal action plan to ensure the district meets is minimum reserve levels in the current and both subsequent fiscal years by the Second Interim Financial Report submission. The contingency plan will need to identify the actions planned by the district to ensure its solvency, including any changes to Gap funding assumptions, identifying any expenditure reductions as one-time or ongoing, negotiable or non-negotiable, the object/expenditure category, an estimated dollar amount of savings, and fiscal year of implementation. Only expenditure reductions that do not require negotiations can be included in the Second Interim Financial Report MYP. This additional information must be provided as part of the Interim Report submission in order to justify a "Positive" certification. If the district board has not taken action to meet the minimum reserve in all years, then a "Qualified" certification would be applicable. The Second Interim report is due to our office no later than March 17, 2014.

UNRESTRICTED FUND BALANCE RESERVES



	2013-14 Projected	2014-15 Projected	2015-16 Projected
Available Reserves	3,372,986	2,029,096	1,656,298
Minimum State Required Reserves	2,093,753	1,994,183	2,011,370
Unrestricted Available Reserves %	4.8%	3.1%	2.5%

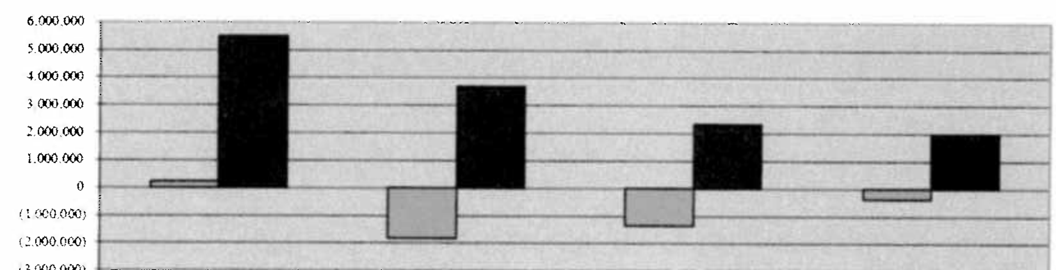
The First Interim Financial Report provides the Governing Board with the opportunity to revise and review its operating budget plan based on the most recent State Budget information and local decisions made since the Adopted Budget. This plan should incorporate any updated revenue projections and utilization 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:

- **UNRESTRICTED DEFICIT SPENDING** – The district is projecting unrestricted expenditures to exceed unrestricted revenues by $1,806,664 in the current fiscal year, primarily due to projected expenditure of carryover balances and other operational costs. The district is continuing this trend of deficit spending in fiscal year 2014-15 by $1,348,397 and in fiscal year 2015-16 by $372,798. This ongoing deficit spending appears to be attributed to ongoing operational costs. Anticipated deficit spending should be for one time, non-recurring expenditures to avoid depletion of the district's on-going unrestricted reserves.

  The district's projected deficit spending is not within the established state standard for the current and first 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, the projected change based on the First Interim Report, and board approved multi-year financial projections for the 2014-15 and 2015-16 fiscal years.

CHANGE IN UNRESTRICTED FUND BALANCE TRENDS



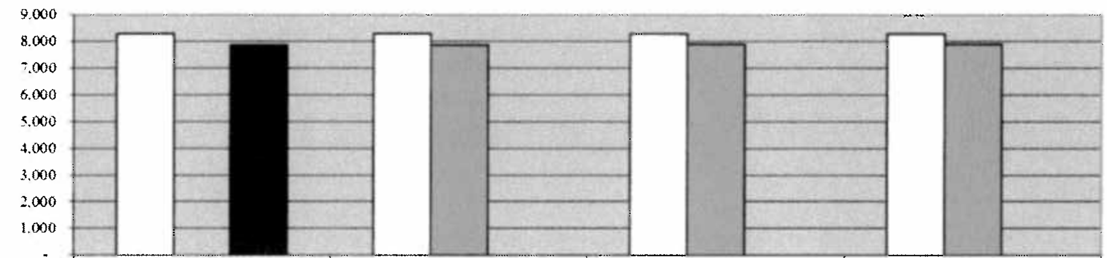
	2012-13 Actual	2013-14 1st Interim	2014-15 Projected	2015-16 Projected
Change in Unrestricted Fund Balance	221,019	(1,806,664)	(1,348,397)	(372,798)
Unrestricted Fund Balance	5,497,652	3,690,988	2,342,591	1,969,793

- **AVERAGE DAILY ATTENDANCE (ADA) & ENROLLMENT PROJECTIONS** – The district is projecting 2013-14 K-12 P-2 ADA of 7,867 or no change over the prior year P-2 ADA. Based on an enrollment projection of 8,289, the district is anticipating a current year attendance ratio of 94.91%. The district is projecting no change in ADA and a 95.24% attendance ratio for 2014-15 and 2015-16. Additionally, the district is projecting it's percentage of Target Pupils (unduplicated count of English Learners, Free and Reduced Price Meal students, and Foster Youth) to be 51.72% in 2013-14, 2014-15, and 2015-16.

  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 within the state standard of 95.5% for each of those years. The district is projecting ADA to remain static for the current and two subsequent years, which is not in line with its historical trend. Over the past 6 years, the district's enrollment has declined and average of 2.8% per year. 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



	2012-13 Actual	2013-14 1st Interim	2014-15 Projected	2015-16 Projected
Enrollment	8,282	8,289	8,289	8,289
ADA Projections		7,867	7,895	7,895
Actual ADA	7,867			
ADA/Enrollment Ratio	94.99%	94.91%	95.24%	95.24%

- **REVENUE AND EXPENDITURE 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.

  The district has incorporated adjustments to recognize Local Control Funding Formula (LCFF) revenues in the budget and projections for the two subsequent fiscal years.

  Our review of district current and projected expenditures indicates that the district has made $705,511 of reductions in salary costs in the 2014-15 fiscal year. The district has indicated that this is an adjustment for one-time costs in the 2013-14 fiscal year. The district is currently maintaining a 180-day school year.

- **ENDING CASH POSITION AND MONTHLY CASH FLOWS** – Due to the current State Budget including ongoing deferrals of state revenues, changes in apportionment distribution schedules, inclusion of Education Protection Account (EPA) funds, and ongoing state funding reductions, the monitoring and projection of monthly cash balances have become increasingly critical to ensure fiscal solvency. These changes 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 indicates that the district will have a positive cash balance at the end of each month and at the end of the fiscal year. The district's cash flow reflects the June 30 cash balance as 150% of the projected 2013-14 Ending Fund Balance, including cash from temporary borrowing. With temporary borrowing excluded, the district's cash balance would be negative at June 30, 2014.

  Additionally, the district's LCFF funding is computed to be 12% Property Taxes and 88% State Aid, which means your district will realize a greater loss of cash due to state deferrals than a higher property tax district. Our projections indicate that the state will defer approximately $8.2M of the district's 2013-14 state aid into the 2014-15 fiscal year. The district has utilized Inter-fund borrowing, Tax Revenue Anticipation Notes, a Constitutional Advance, and projects the use of a Midyear TRANs of

$6.8M in February 2014, to maintain a positive cash position during the current fiscal year. The Midyear TRANs requires repayment by August 2014. 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		6,039,912
Cash Minus Temp. Borrowing		(760,088)
Ending Fund Balance	4,026,193	
Cash Balance Without Deferrals*		7,182,407

*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.

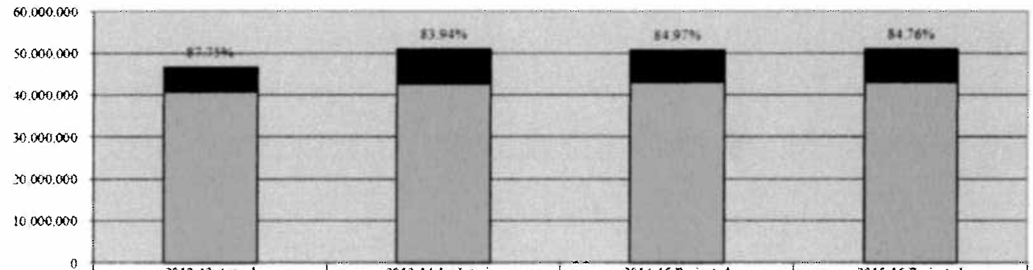
- **STAFFING PROJECTIONS/SALARY SETTLEMENTS** – The district has indicated that negotiations have not been finalized with the certificated and/or classified bargaining units. The documents also indicate that there are no potential salary schedule increases or decreases included in the current projected budget or subsequent fiscal years other than annual step and column advancements. Please keep our office apprised of any changes to the district's negotiations status.

Pursuant to AB1200/AB2756 and the district's Qualified Certification, an analysis of the costs or savings associated with any proposed or tentative agreement(s) or MOUs must be provided to our office **at least ten days prior to adoption by the board**. The analysis must include the agreement's impact on the current operating budget and multi-year financial projections. Budget transfer documents implementing any adjustment(s) must be input into the financial system no later than 45 days after approval of the agreement by the Governing Board. If the costs associated with a negotiated salary or benefit increase reduce the available unrestricted ending balance below the required state minimum reserve level in the current and/or two subsequent fiscal years, the district Governing Board will be required to take action to maintain the required state reserves.

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, adopted budget, 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 not within the state's established standard for the current year, however almost 84% of unrestricted expenditures are being consumed by salary and benefit costs. If salaries and benefits are growing 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.

RATIO OF UNRESTRICTED SALARIES AND BENEFITS TO UNRESTRICTED EXPENDITURES



	2012-13 Actual	2013-14 1st Interim	2014-15 Projected	2015-16 Projected
Ratio Salaries & Benefits	87.75%	83.94%	84.97%	84.76%
Total Other Unrestricted Expenditures	5,689,903	8,165,794	7,627,371	7,742,371
Total Unrestricted Salaries and Benefits	40,767,776	42,689,220	43,110,294	43,076,205

- **MULTI-YEAR PROJECTIONS** – The district is not projecting to meet minimum state reserves in all fiscal years with 4.8% in 2013-14, 3.1% in 2014-15 and 2.5% in 2015-16. The district's moderate approach in projecting Gap funding percentages has mitigated some of the risk to future funding. More information on Gap funding will be known after the Governor issues his first 2014-15 Budget proposal in mid-January. **Our office recommends that the district continue to be proactive by developing contingency plans in response to the current state economy's potential for further changes in the Governor's 2014-15 January Budget proposals.**

- **LONG TERM DEBT** – The district's 2012-13 Audit Report indicates non-voter approved long-term debt of $5,518,608 which constitutes 7.91% of the district's projected general fund budget. The debt repayment is budgeted in the General and Self-Insurance Funds. The district should monitor 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.

- **CHARTER SCHOOLS** – As required by Education Code 47604.33, our office has received the First Interim report(s) from the following charter schools:
    - Competitive Edge Charter Academy (CECA)
    - Inland Leaders Charter School (ILCS)

As a charter school sponsor, the district maintains fiscal oversight responsibilities, particularly in the key areas of accounting, attendance accounting, budgeting, and payroll. As part of this oversight, sponsoring school districts are also responsible for reviewing charter financial reports, including interim reports. Should any adverse circumstances arise related to the district's charter school responsibilities that would negatively impact the financial condition of the district, please notify this office as soon as possible.

CECA is a dependent charter of the district and is reported in the district's Charter Schools Special Revenue Fund (Fund 09). Once the district has completed the review and assessment of the fiscal and budgetary condition of ILCS, please submit the fiscal review analysis document reflecting the district's oversight review of the charter's First Interim documents to our office.

If you have any questions concerning our review of the district's 2013-14 First Interim Financial Report, please contact the undersigned.

Sincerely,

Thomas G. Cassida Jr., MBA
Business Services Advisor
Business Advisory Services
(909) 386-9676

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