October 28, 2020

Jorge A. Aguilar, Superintendent
Sacramento City Unified School District
5735 47th Avenue
Sacramento, CA 95824

SUBJECT: 2020-2021 Re-Adopted Budget

Dear Superintendent Aguilar:

BACKGROUND
In our August 4, 2020 letter, the Sacramento County Office of Education (SCOE) disapproved the Sacramento City Unified School District's (SCUSD) 2020-2021 Adopted Budget. Per Education Code requirements, the district was instructed to revise the 2020-2021 Adopted Budget and submit it to this office no later than October 8, 2020. The district was also required to submit a viable, board-approved, budget-balancing plan that would reverse the deficit spending trend and support on-going expenditures from on-going revenue sources, and include a timeline showing when and how each line item adjustment would be implemented. Our office continues to provide a fiscal advisor to assist the district during this process. It is also noted that the district is operating under expired Collective Bargaining Agreements with all of its employee units.

STRUCTURAL DEFICITS/RESERVE REQUIREMENTS
In accordance with the provisions in Education Code sections 42127 and 33127, we have examined the district’s Re-Adopted Budget to determine if it complies with the Criteria and Standards adopted by the State Board of Education. Based on our review, it appears that the district's unrestricted General Fund balance will decrease by approximately $18 million in 2020-2021, approximately $34 million in 2021-2022, and approximately $50.9 million in 2022-2023. It appears that the district will meet its minimum reserve requirement in the current and first subsequent fiscal year, but will fall short in the second subsequent fiscal year, leaving a negative unrestricted ending fund balance of approximately $18.3 million in 2022-2023.
CASH FLOW SHORTAGES

Fiscal Year 2020-2021
Cash flow projections show the district anticipates a negative cash balance from May 2021 to September 2021 due to the Principal Apportionment Deferrals. The district will try to utilize cash flow management options such as TRANs or deferral waivers. We will work closely with the district on cash management strategies as much as is practicable.

Fiscal Year 2021-2022
Due to the use of the above-mentioned options, it appears the district may avoid cash flow insolvency in the 2020-2021 fiscal year. However, the 2021-2022 cash flow projection shows that the district anticipates a negative cash balance beginning in March 2022, again due to the Principal Apportionment Deferrals. The district continues to show negative cash flow projections even after the cash deferrals are repaid or forgiven. It appears the district will not have the ability to repay any cash flow borrowing after March 2022, therefore, the cash management options available to the district in 2020-2021 may be limited, and possibly nonexistent by 2021-2022. This would lead to insolvency and the need for an emergency apportionment.

FCMAT LETTER
In May of 2020, SCUSD and FCMAT entered into an agreement for FCMAT to provide management assistance to the district by developing an independent, multi-year financial projection and cash flow analysis to determine whether the district will need an emergency appropriation. On September 15, 2020, following completion of their fieldwork, FCMAT issued a letter of their findings and recommendations. Education Code provides that the County Superintendent shall review and consider studies, reports, evaluations, or audits that contain evidence that shows fiscal distress when determining whether the adopted budget of a school district will allow the district to meet its financial obligations. In our review of the FCMAT letter, we noted some significant items as follows in bold:

- The position control reports provided to FCMAT cannot be relied upon for staffing or Multi-year Financial Projections. FCMAT comments that despite repeated observations over the years about the district’s lack of position control, the district still has an unreconciled and inaccurate position control system. Many improvements have been made, but many are still needed. The system/process is insufficient to serve in the traditional role of a position control system, which provides gatekeeper functionality for over 90% of the district’s expenditures.
SCOE agrees with this finding and has noted that the district is hindered by the lack of accurate position control data to be used in the budgeting process. In the current system, cumbersome and time-consuming reconciliations must be performed, at minimum, on an annual basis. Without such procedures, the position control reports cannot be relied upon for budget projections. Per our past recommendations, the district is currently working on implementing changes to the position control system procedures to allow for budget-ready position control data.

- The FCMAT review indicates that, based on information they obtained from the California Department of Education (CDE), the district’s average students per teacher ratios appear to be below the state limit and those in the certificated collective bargaining agreement. While the FCMAT letter compares current staffing ratios to state and Collective Bargaining Agreement (CBA) limits, further analysis of the CDE data and the district’s records shows that when necessary adjustments are made to account for Special Education, charter schools, and the preparation periods required by the CBAs, the district class-size averages are extremely close to those limits, except in certain specialty programs. We know these specialty programs continue to be analyzed by the district as part of a potential Fiscal Recovery Plan.

- The FCMAT letter concluded that an emergency appropriation will likely be necessary in 2020-2021 if internal and external borrowing options are not available and/or the district does not receive apportionment deferral exemptions. Furthermore, even if borrowing options are available and/or deferral exemptions are received in 2020-2021, without substantial corrective action, an emergency appropriation is likely needed in 2021-2022. The cash flow statements prepared by FCMAT for 2020-2021 and 2021-2022, along with those prepared by SCUSD, show the district running out of cash in March 2022 with no ability to recover, even after the deferrals are repaid or forgiven.

**DISAPPROVED RE-ADOPTED BUDGET**

We recognize recent successes at reducing the current-year budget for anticipated vacancies and pandemic-related savings, however, more budget balancing efforts are required. Based on our review of the district’s financial reports showing an on-going structural deficit, extreme cash flow issues, negative fund balance projections, and the conclusion presented in the FCMAT letter, the district’s Re-Adopted Budget is **disapproved**.
In response to disapproval of the Re-Adopted Budget, and pursuant to Education Code sections 42127.1 through 42127.3, the County Superintendent must call for the formation of a Budget Review Committee (BRC) unless the governing board of the district and the County Superintendent agree to waive this requirement. If the district opts for the formation of the committee, the committee shall be composed of three persons from a list of candidates provided by the California State Superintendent of Public Instruction (SPI) and selected by the district’s governing board. The selection must be made within five (5) working days after receipt of the list. The SPI shall convene the committee no later than five (5) working days following the selection of the committee members. No later than November 30, 2020, the BRC shall review the proposed budget of the district and transmit to the SPI, the County Superintendent, and the governing board of the district either of the following:

1. The recommendation that the school district budget be approved; or

2. A report disapproving the school district budget and setting forth recommendations for revisions to the school district budget that would enable the district to meet its financial obligations in the current fiscal year and two subsequent fiscal years.

If the district’s governing board and the County Superintendent agree to waive the formation of the BRC, the California Department of Education must approve the waiver. November 8, 2020 is the deadline for a board-approved waiver to be submitted to the California Department of Education. Enclosed with this letter is a copy of the waiver request form. If your board pursues the option of waiving the committee, we will need to act quickly. Given the multiple reviews, audits, and the most recent FCMAT letter, along with the fact that the district is ready to present its Fiscal Recovery Plan next month, we recommend the district waive the formation of the BRC, as there is no need for a duplicative process.

Upon approving a waiver of the BRC, CDE shall ensure that a balanced budget is adopted by December 31, 2020. The County Superintendent must perform his duties under Education Code section 42127.3(b), which include the responsibility to stay or rescind any action inconsistent with a budget that will govern the district and allow the district to meet its financial obligations. While the district must reverse its deficit spending in time to meet minimum reserve levels in 2022-2023 and beyond, this office recommends that the district make cuts immediately. The fiscal advisor sponsored by the County Superintendent will remain in place to assist the district during this process.

To meet the December 31, 2020 deadline, the district shall submit a viable board-approved budget and multi-year expenditure plan that will reverse the deficit spending trend with the 2020-2021 First Interim Report, which is due by December 15, 2020. Our understanding is that a draft fiscal recovery plan will be discussed at the November 19, 2020 district board meeting, with a follow-up discussion and action on December 10, 2020. We look forward to seeing the presentation of these items.
We continue our request that the district provide the following:

- Commit to using only on-going funding sources to pay for on-going expenditures.
- Recognize the one-time nature of savings due to COVID-19, and project future budgets accordingly.
- Immediately address attendance-taking strategies of classroom teachers, assuring current-year enrollment and attendance accounting is accurate, ensuring full funding for the district.
- Expedite development and implementation of procedures to update position control and reconcile it to budget and payroll on a periodic basis, and no less than at each financial reporting period.
- Notify us and the fiscal advisor immediately, and provide for our review, any changes to the budget.
- Continue to closely monitor future enrollment trends and inform us of budget adjustments should enrollment trends fluctuate.

If you have any questions or concerns regarding this review, please feel free to call Tamara Sanchez at 916-228-2551.

Sincerely,

David W. Gordon
Sacramento County Superintendent of Schools

DWG/TS/dw

Enclosure: CDE Waiver Request Form

cc:  Jessie Ryan, Board President, SCUSD
     Rose Ramos, Chief Business Officer, SCUSD
     Dr. Nancy Herota, Deputy Superintendent, SCOE
     Tamara Sanchez, Associate Superintendent, SCOE
     Debra Wilkins, District Fiscal Services Director, SCOE
     Terri Ryland, Fiscal Advisor, SCOE
     Michael H. Fine, Chief Executive Officer, FCMAT