FCMAT

FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM

Alum Rock Union School District

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Fiscal Crisis & Management Assistance Team

- FCMAT was established by Assembly Bill 1200 in 1992 to help local educational agencies (LEAs) comply with fiscal accountability standards.
- FCMAT provides management assistance, fiscal crisis intervention and other services to LEAs.
- FCMAT is an external, independent agency of the state.

2018-19 State Budget Act

- The 2018-19 State Budget Act provides for FCMAT to offer more proactive and preventive services to fiscally distressed school districts by automatically engaging with a district under the following conditions:
  - Disapproved budget
  - Negative interim report certification
  - Three consecutive qualified interim report certifications
  - Downgrade of an interim certification by the county superintendent
  - Lack of going concern designation
- Under these conditions, FCMAT will perform a fiscal health risk analysis to determine the level of risk for fiscal insolvency.

2018-19 State Budget Act

- FCMAT's engagement builds on the county superintendent's oversight process and activities already in place.
- There is no cost to the county office or to the district for the analysis.
- The Alum Rock Union School District's 2017-18, 2018-19 and 2019-20 first and second interim reports were all certified as qualified.
- The district's 2017-18, 2018-19 and 2019-20 adopted budgets were all conditionally approved with its 2018-19 budget receiving disapproval.

Determining Fiscal Risk

- FCMAT developed the Fiscal Health Risk Analysis tool to assess a district's risk of financial insolvency.
- The tool consists of 137 yes/no questions across 20 areas FCMAT has identified that most often lead to fiscal insolvency as well as 18 of the 137 yes/no questions that indicate material weaknesses.
- The analysis focuses on essential functions and processes to determine the level of risk at the time of fieldwork.
- Each question is weighted, and each of the 20 areas is weighted based on high, moderate and low risk.
- Total risk score
  - High risk: 40% or more
  - Moderate risk: 25-39.9%
  - Low risk: 24.9% and lower
- However, the existence of any condition in the Budget and Fiscal Status section and/or a material weakness will supersede the score above because it elevates the district's risk level.

Determining Fiscal Risk

- FCMAT virtually visited the district on June 1-4, 2020.
- The team conducted interviews, collected data and reviewed numerous documents and financial reports provided by the district. Following fieldwork, FCMAT continued to review and analyze the documents.
- The district’s 2019-20 second interim report was used as the baseline for the fiscal health risk analysis.
- District’s Risk Score: 37.2% (High Risk).
  - The district’s score is attached to moderate risk; however, it had one condition in the Budget and Fiscal section and eight material weaknesses, which elevated the risk to high.

Summary of Responses

Topic	Yes	No	N/A
Annual Independent Audit Report	3	1	0
Budget Development and Adoption	7	5	0
Budget Monitoring and Updates	4	6	0
Cash Management	2	3	2
Charter Schools	3	1	1
Collective Bargaining Agreements	6	2	1
Contributions and Transfers	0	3	0
Deficit Spending (Unrestricted General Fund)	1	3	0
Employee Benefits	2	1	2
Enrollment and Attendance	9	1	0
Facilities	1	7	0

Topic	Yes	No	N/A
Fund Balance and Reserve for Economic Uncertainty	1	3	1
General Fund - Current Year	2	4	1
Information Systems & Data Management	4	0	2
Internal Controls and Fraud Prevention	8	5	0
Leadership and Stability	7	1	0
Multiyear Projections	3	1	0
Non-Voter-Approved Debt and Risk Management	0	4	0
Position Control	5	1	0
Special Education	3	4	0
Totals	**71**	**56**	**10**

Major Risk Factors

- Budget Development and Adoption^
- Budget Monitoring^
- Contributions and Transfers^
- Deficit Spending^
- Fund Balance and Reserve for Economic Uncertainty^
- Internal Controls and Fraud Prevention
- Non-Voter-Approved Debt and Risk Management

^ Sections where material weaknesses were also found

Budget Development and Adoption

- The district’s 2019-20 second interim report multiyear projection included “Other Adjustments” totaling approximately $4.7 million and $1.7 million for 2020-21 and 2021-22, respectively. The assumption attached to the $4.7 million reduction was related to 30 certificated FTEs, 1 administrator FTE and 2 classified FTEs; however, FCMAT was unable to find board action related to these reductions. The assumption attached to the $1.7 million was related to a reduction of 20 certificated FTE and an unspecified reduction of $517,918.
- The district’s budget has not been approved unconditionally for the last three years and its 2018-19 budget was disapproved.
- The district uses negative or contra expenditure accounts within its general ledger.

Budget Monitoring

- Comparison of actual revenues and expenses as of June 19, 2020 showed some account lines were overexpended.
- Budget assumptions have been provided to the board in the district’s adopted budget and first and second interim reports for 2017-18, 2018-19 and 2019-20; however, they were not present in the district’s third interim reports for those years.
- The district has not addressed deficiencies raised by the county office in its oversight letters such as the deficit spending concerns raised in 2017-18, 2018-19 and 2019-20.
- Balance sheet accounts were not consistently reconciled for 2019-20.
- The district’s 2017-18 unaudited actuals were not approved by the board until October 11, 2018, which violates Ed Code Section 42100. The district’s 2018-19 third interim report is not reflected in the minutes of the May 9, 2019 meeting where it was to be presented.

Contributions and Transfers

- The district lacks a board approved plan to eliminate, reduce or control contributions/transfers from the unrestricted general fund to restricted programs.
- Contributions to restricted programs have been growing for fiscal years 2018-19 and 2019-20 at 5.3% over the contributions in 2017-18 and 2.9% over the contributions in 2018-19. Special education is experiencing the largest increase (93.07%) from its 2018-19 contribution.

Deficit Spending

- The district’s 2019-20 second interim report projects deficit spending in the current year and both of the two subsequent fiscal years. The unrestricted general fund portion of the projected deficit is:
    - $3.41 million in 2019-20
    - $2.2 million in 2020-21
    - $1.6 million in 2021-22
- The district has not approved and implemented a plan to reduce and/or eliminate deficit spending to ensure fiscal solvency.

Fund Balance and Reserve for Economic Uncertainties

- The district's 2018-19 second interim report projects that the district can maintain the 3% minimum reserve requirement in the two subsequent years. However, that is based on the assumption that the district can effect reductions of:
  - $4.7 million in 2020-21
  - $1.7 million in 2021-22
- The district's Adopted Budget shows that these reductions change to maintain the district's minimum 3% reserve requirement as follows:
  - $4.2 million in 2020-21
  - $17.9 million in 2021-22
  - $22.0 million in 2022-23

Internal Controls and Fraud Prevention

- The district had not completed clearing accruals as of June 19, 2020, which is well beyond its first interim report.
- The district lacks a documented process for collecting reports of possible fraud and for ensuring reports are appropriately addressed.
- The district lacks an internal audit process.

Non-Voter-Approved Debt and Risk Management

- The district plans to use funds other than the general fund (Funds 21, 25 and 35) to make payment and/or retire the COP debt ($22.5 million as of July 1, 2019). However, the availability of these funds is questionable.
  - Fund 21 (Bonds Fund): Measure I Bond proceeds are currently unissued and not available.
  - Fund 25 (Capital Facilities Fund): Revenue estimates in this fund are overly optimistic.
  - Fund 35 (County School Facilities Fund): Its balance was $576,247 as of July 1, 2019, with no additional revenue anticipated.

Non-Voter-Approved Debt and Risk Management

- The district's credit rating on both its COPs and GO bonds were downgraded by Moody's in June 2019, citing the district's declining enrollment and rising pension costs, creating a structural deficit and a weakened fiscal outlook.
- Its credit rating on its GO bonds were downgraded by S&P Global Ratings in September 2017. This downgrade was related to concerns about an active investigation by the district attorney, timely cash reconciliations and difficulties obtaining information from the district.
- The district's 2018-19 annual audit shows that its self-insurance fund (Fund 67) has a positive net position; however, no actuarial valuation has been conducted to support the premiums charged or the expected costs and liability of providing the insurance.
- The annual payments due on the district's COPs exceed 2% of the district's unrestricted general fund revenue in the current and two subsequent years.

Summary

- The growth in the amount of reductions necessary for the district to maintain its 3% minimum reserve requirement are worrisome.
- If the district cannot achieve these cost reductions and continues to spend more than it receives, it will deplete its cash resources and become fiscally insolvent.
- The risk factors described in the fiscal health risk analysis will require the board and administration to continue to make and implement difficult decisions.
- Failure to act quickly and decisively may result in fiscal insolvency. The consequences of becoming insolvent are severe and result in the loss of local control and governance.