FISCAL REPORT

PUBLIC EDUCATION'S POINT OF REFERENCE FOR MAKING EDUCATED DECISIONS

2021-22 Second Interim Report Considerations

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posted January 24, 2022

The Second Interim budget report is a snapshot in time of a local educational agency's (LEA) revenue and expenditure forecasts for the current fiscal year, as well as a projection of the two subsequent fiscal years. It is a time to adjust the budget based upon Governor Gavin Newsom's proposed January State Budget and subsequent trailer bills, discuss changes from the First Interim budget report, adjust revenues and expenditures, and begin projecting the ending balances for your funds and resources. The Second Interim report covers the period of time from July 1 through January 31, and must be submitted to the county office of education (COE) no later than March 17 (45 days after the close of the reporting period per Education Code Section [EC §] 42131[a]).

School Services of California Inc.'s (SSC) School District and Charter School Financial Projection Dartboard is updated to include the financial factors needed for your budget.

Below are legal considerations and "best practices" to help with the Second Interim budget report.

Attendance/LCFF

A welcome component of the Governor's Budget released on January 10, 2022, is a proposal to address the dramatic declines in enrollment and average daily attendance (ADA) that LEAs are experiencing during the pandemic and beyond. The proposal is as follows:

Governor's Budget Proposal
Beginning in 2022-23, and for future years, would amend EC § 42238.05(a)(1) and allow a third option for funded ADA which would use the actual ADA from the prior three years. If enacted, this would allow a school district in 2022-23 to be funded on the greater of the following: • Actual ADA from 2022-23 • Actual ADA from 2021-22 • Average ADA based on actuals from 2019-20, 2020-21, and 2021-22 In its current format, the third option would only apply to school districts.

We recommend that you measure the impact of the Governor's Budget proposal on your own school district; however, consult your COE before including it in your Second Interim report. Should the decision be made along with your COE to include the Governor's ADA proposal, we recommend assigning the resulting growth in revenues in your ending fund balance in the event that the proposal does not make it into law.

In addition to the Governor's ADA proposal, there are four bills in the Legislature that we will be watching closely. At this time, we would recommend not including them in your Second Interim report projections. Below is a summary of the four proposals:

Assembly Bill (AB) 1607 (Muratsuchi, D-Torrance)	Beginning in 2022-23, and for future years, replaces the current law in EC § 42238.05(a)(1) with a rolling three-year average of ADA which would mirror the methodology used for unduplicated pupil count by using the current year and two prior years.
AB 1609 (Muratsuchi)	For the 2022-23 fiscal year only, amends EC § 42238.05(a)(1) to use the greater of 2019-20, 2020-21, 2021-22, or 2022-23 ADA. Effectively, this allows districts to continue to use 2019-20 ADA for an additional year, plus any growth, as applicable, in 2020-21.
Senate Bill (SB) 579 (Allen, D-Santa Monica)	For the 2022-23 fiscal year only, amends EC § 42238.05(a)(1) to use the greater of 2019-20, 2021-22, or 2022-23 ADA. Effectively, this allows districts to continue to use 2019-20 ADA for an additional year.
SB 830 (Portantino, D-La Cañada Flintridge)	Beginning in 2023-24, adds a new funding stream that relies on "average daily membership," which is based on enrollment. This new categorical calculates the additional funds a school district or COE would receive if the Local Control Funding Formula (LCFF) allocation was based on enrollment figures rather than on ADA. At least 50% of the new funds must be spent to supplement efforts to combat chronic absenteeism and habitual truancy. In order to access the additional funds, an LEA must maintain the same per-pupil spending level from 2019-20 for addressing chronic absenteeism and habitual truancy.

Multiyear Projections

Every year at industry standard checkpoints, SSC uses the services of a Wall Street Journal award winning economist for its out-year statutory cost-of-living adjustment (COLA) projections. This year, consistent with past years, we had independent estimates run for comparison to the Department of Finance (DOF) projected statutory COLAs. Per usual, the estimates from the two sources were very close so we are moving forward with the projections from the DOF.

	2022-23	2023-24	2024-25	2025-26
DOF Statutory LCFF COLA	5.33%	3.61%	3.64%	3.62%

Although comparisons will be made to the funded COLA from 2021-22, it's important to remember that the prior-year COLA of 5.07% consisted of two years' worth of COLA, plus an augmentation of 1.00%. The proposed COLA for 2022-23 reflects the significant increase in the cost of goods and services purchased by state and local governments, and does not include any additional augmentations.

In addition, the Governor's Budget proposal includes the full 5.33% COLA for programs outside the LCFF. Recall that in 2021-22, the LCFF received a COLA of 5.07% while programs outside of the LCFF received COLAs of either 4.05% or 1.70%.

The projected COLA of 5.33% is still an estimate as the final two data points are released in late January and late April.

Accounts Receivable/Accounts Payable

The California School Accounting Manual (CSAM) defines "accounts receivable" as amounts due from private persons, firms, and corporations. LEAs typically err on the side of overstating the balance of their accounts receivable.

To enhance the accuracy of your agency's accounts receivable, review the large entries recorded in the accounts receivable ledger to ensure that they are accurate and meet CSAM's criteria for an accrual. Any unresolved accounts receivable from the prior year should be investigated to determine whether they are still valid and collectible according to CSAM. At this point in the year there should be very few balances remaining in accounts receivable.

An accounts receivable reconciliation report will assist in fully understanding amounts due that are still outstanding and allow you to clear any recorded receivables that will not materialize this fiscal year. Unverified accounts receivable that remain may be falsely increasing revenue and ending balance projections.

CSAM defines "accounts payable" as amounts due to private persons, firms, or corporations for services rendered and goods received on or before the close of the year. In contrast to the accounts receivable, LEAs often inadvertently understate the balance of their accounts payable by failing to accrue an amount due to an outside vendor.

As with accounts receivable, any accounts payable items remaining that were accrued the prior year should be investigated to ensure that they are still outstanding. If they are not, then an adjusting entry should be made to clear that item from the accounts payable balance. Unverified accounts payable that remain may be falsely increasing expenditure projections and decreasing ending balance projections. At this point in the year there should be very few balances remaining, if any, in accounts payable from the prior year.

Budget Adjustments/Carryover Balances

Begin adjusting expenditure lines for unspent funds that will be carried over to subsequent years. Estimates of funds that are anticipated to be unspent can be entered into the expenditure budget in contra-accounts in order to reduce the volatility of the fund balance when the Estimated Actuals and Unaudited Actuals are prepared. Ensure that any carryover expenditures are budgeted as one-time activities when preparing the multiyear projection for 2022-23 and 2023-24. Unspent funds that need to be separately identified as carryover should be done so by creating an assignment or commitment in the ending fund balance.

Cash Flow

As quickly as the deferrals reared their ugly head, they disappeared again. The 2020 Enacted Budget deferred state aid payments from February 2021 through June 2021 to July 2021 through November 2021.

Due to the rapid recovery of the stock market, aided by historic levels of federal funding, the 2021 Enacted Budget accelerated the repayment of the deferrals so that the balances were extinguished by August 2021.

Ensure that as you prepare your cash flow for 2021-22 and 2022-23, the repayments of deferrals are removed from the revenue section, and appropriately reflected in the balance sheet section of the Form CASH. For more information, see our article, “Recording Deferral Repayments in Cash Flow” in the October 2021 *Fiscal Report*.

Charter Schools

Concentration (S/C) grants for charter schools are limited in that the unduplicated pupil percentage (UPP) can be no more than the UPP of the school district where the charter is physically located. A charter school physically located in more than one district can use the UPP of the district with the highest UPP. EC § 42238.02(f)(2) notes that a charter school’s authorizing school district will be included when determining its physical location.

Payments for in-lieu property taxes are required to be received and recorded monthly unless the sponsoring LEA is a basic aid district, in which case the payments must be made in no fewer than two installments per EC § 47635(b)(5). If you are a chartering authority, ensure that the in-lieu property taxes between your financial statements and your authorized charter schools net to zero.

Clearing Funds

As stated in its title, clearing funds are cash conduits used by the LEA to account for receipts due to agencies such as the Internal Revenue Service, the California State Teachers’ Retirement System (CalSTRS), and the California Public Employees’ Retirement System (CalPERS). The clearing funds should have a zero balance after the payment has been sent to the agency. Over the course of the year, the clearing funds should be reconciled and cleared on a monthly basis.

Collective Bargaining Agreements

If your collective bargaining agreements have been settled for the current and subsequent years, ensure that your budget includes any adjustments to salary as well as professional development costs, substitute costs, or other changes to the agreements that need to be budgeted.

COVID-19 Resources

LEAs have been allocated more than $26 billion in one-time federal dollars. The largest swaths of federal stimulus—more than $20 billion—known as Elementary and Secondary School Emergency Relief (ESSER) II and III must be spent by September 30, 2023 and 2024, respectively. LEAs that are using the funds for one-time costs should back out revenues and expenditures in the multiyear projection accordingly.

LEAs that are using these funds to support current operations, or that are using these funds for ongoing expenditures, should be able to identify how much of the ESSER expenditures are ongoing. These funds should be reviewed as part of each budget period over the next two years to ensure that the LEA has a plan to subsume the ongoing expenditures without jeopardizing the fiscal health of the LEA.

Local Control and Accountability Plan and Supplement

LEAs are in the second round of adopting a Local Control and Accountability Plan (LCAP) after the one-year abeyance for the 2020-21 fiscal year. Although the template continues to morph, the requirement for adoption is the same. The LCAP must accompany the budget in a public hearing, and in a separate, and subsequent, meeting the LCAP and budget must be adopted. This must all take place by June 30, 2022. Note that while charter schools must hold public hearings for review and adoption, there is no requirement that the LCAP accompany the budget.

The additional wrinkle this year is the LCAP Supplement that must be considered by the governing board no later than February 28, 2022. More information on the LCAP Supplement can be found on the California Department of Education's (CDE) website here. Also, see our article, "*Ask SSC* . . . LCAP Supplement Due in February 2022" in the November 2021 *Fiscal Report*.

Lottery

The most recent projections from the CDE estimate unrestricted Lottery at $163 per ADA and restricted Lottery at $65 per annual ADA, multiplied by an enrollment factor of 1.04446. Updated factors are expected when the 2022-23 State Budget is enacted in the late spring/early summer.

Reserves

Adequate reserves are critically important, but the existence of adequate reserves does not mean that there is sufficient cash on hand. Reserves are an accumulation of resources, including accounts receivable. Cash is king, so make sure that the cash flow is updated and don't rely on just the fund balance number.

School districts should be familiar with the laws that govern the reserve cap, but should not be in a rush to spend down reserves in the event that the reserve cap is triggered. All four criteria to require a deposit into the Public School System Stabilization Account were met in 2020-21 and 2021-22, and a third deposit is expected in 2022-23. The sum of these three deposits—approximately 11.1% of the K-12 portion of the minimum guarantee—is sufficient to trigger the reserve cap for school districts in 2022-23. The result is that non-exempt school districts must limit their unassigned and assigned reserves in Funds 01 and 17 to a limit of no more than 10.0%.

SSC has always encouraged LEAs to maintain sufficient reserves to meet their LEA-specific needs, which is invariably higher than the state-required minimum. Given the triggering of the reserve cap, school districts might consider taking board action to commit funds for specific costs such as special education cost increases, increasing CalSTRS/CalPERS contributions, or other district priorities. School districts can also apply for a waiver that can be approved by the COE for two consecutive years in a three-year period. If you believe you will be subject to the reserve cap, initiate the conversation with your COE sooner rather than later.

As a reminder, law has excluded charter schools, small school districts (less than 2,501 ADA), and community-funded districts from the reserve cap.

Routine Restricted Maintenance Account

The contribution to the Routine Restricted Maintenance Account (RRMA) is in full effect for the 2021-22 year and beyond. Any LEA that qualifies based on EC § 17070.75(b)(2) must contribute no less than 3% of total General Fund expenditures to Resource Code 8150 on an annual basis.

Various bills from 2019-20 through 2021-22 amended the definition of total General Fund expenditures for the purpose of calculating the RRMA contribution by excluding the following:

- Expenses coded to Resource Code 7690
- Expenses of one-time pandemic funding sources in Resource Codes 3210, 3212, 3213, 3214, 3215, 3216, 3218, 3219, 3220, 5316, 7027, and 7420

Compliance with this law is monitored through the Criteria and Standards, but ultimate compliance is measured against total General Fund expenditures as of Unaudited Actuals, adjusted for the exceptions above. Note that the law does not contemplate how much is spent in the RRMA, but only that the contribution is no less than 3%.

SACS Software

The Standardized Account Code Structure (SACS) software is the same software that was used for reporting the 2020-21 Unaudited Actuals. A link to the software is located on the CDE's website and can be accessed by clicking here.

Special Education Maintenance of Effort and Excess Costs

Now that the books are closed for the prior year, evaluate the cost factors that may have increased your LEA's maintenance of effort (MOE) level. Ensure that your agency is properly recording expenditures and that the time charged for special education staff represents time working with students on an Individualized Education Program (IEP). Many LEAs allow 100% of a staff member's time to be charged to special education when they may actually be working with students prior to eligibility for services having been or being determined during the IEP. Review the factors from your Program Cost Report Allocations Form to ensure that centralized costs are distributed accurately as well.

Utilize the SACS forms for MOE during the interim periods. These are voluntary at this point, but will assist in getting an up-to-date peek at where you stand. The FORM SEMAI can be accessed in the Reports section of SACS.

Once you review your agency’s special education costs as they are budgeted, you can then project whether your agency will meet the MOE requirement by year’s end. You may also want to review the excess cost data to ensure that your agency has met those requirements prior to using funds. If your agency is not projected to meet the MOE, contact your Special Education Local Plan Area for assistance in reviewing your agency’s costs to ensure you have captured all appropriate expenditures.

Current law allows five exceptions to reduce the current-year MOE. The four most commonly used are:

- Voluntary or just cause departure of special education or related personnel
- A decrease in special education enrollment
- The termination of the LEA’s obligation to provide services because a high-cost student has either left the agency, reached the age at which the agency is no longer required to provide free and appropriate public education, or no longer needs special education
- Costly expenditures such as equipment or facilities are terminated

The CDE has developed an LEA MOE exemption worksheet that must be completed and included with the submission of the LEA’s MOE report. The LEA MOE exemption worksheet is available here.

Transportation

Expenditures recorded against the transportation programs (Resource Code 0000 and Function 3600) should be reviewed to ensure that they are all appropriate and the MOE requirement is met.
As a reminder, the MOE is measured by the lesser of the following:

1. Expenditures for transportation in 2012-13
2. State revenues received for home-to-school transportation and small school bus replacement in 2012-13

For most LEAs, number two will be the operative test. The penalty for non-compliance with this MOE is a finding in the annual audit report, but there is no fiscal penalty. For more information on the topic, please see our article, “*Ask SSC . . . What Are the Requirements for the Transportation MOE?*” in the August 2020 *Fiscal Report*.

Additional Information

Ensure that the filing of reports is done in a timely manner. Key reporting deadlines for specific programs can be found in our “Critical Deadlines and Funding Opportunities” *Fiscal Report* series.