Marguerite D. Bulkin
County Superintendent of Schools

TUOLUMNE COUNTY
Superintendent of Schools

January 17, 2017

Kathy Ankrom, Board President
Sonora Union High School District
10401 Slate Rim Road
Sonora, CA 95370

Patrick Chabot, District Superintendent
Sonora Union High School District
100 School Street
Sonora, CA 95370

Subject: 2016/17 First Interim Report

Dear Ms. Ankrom and Mr. Chabot:

In accordance with the provisions of Education Code (E.C.) Section 42131, a review of the Sonora Union High School District's (District) First Interim Report for fiscal year 2016/17 has been completed by the Tuolumne County Superintendent of Schools (County Superintendent). The District filed a First Interim Report with a qualified certification. Based on the multiyear projections and assumptions provided by the district, with data current as of October 31, 2016, it appears that the District may not meet its financial obligations for the current fiscal year or two subsequent fiscal years without the implementation of specific actionable Board approved budget reductions.

We are aware that the information provided reflects the District's financial position and assumptions as of October 31, 2016, and that further adjustments will be made during the year as additional data becomes available. Any technical comments relative to the report have been directed to the District's Chief Business Official (CBO).

Per E.C. 42131, the District Governing Board makes a finding of positive, qualified or negative.

> *"Positive certification shall be assigned to any school district that, based upon current projections, will meet its financial obligations for the current fiscal year and subsequent two fiscal years."*
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> *"Qualified certification shall be assigned to any school district that, based upon current projections, may not meet its financial obligations for the current fiscal year or two subsequent fiscal years."*
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> *"Negative certification shall be assigned to any school district that, based upon current projections, will be unable to meet its financial obligations for the remainder of the fiscal year or the subsequent fiscal year."*

"These certifications shall be based upon the financial and budgetary reports required by Section 42130 but may include additional financial information known by the governing board of the school district to exist at the time of each certification."

This letter discusses the various areas of concern noted by the County Superintendent in her review of the District's 2016/17 First Interim report. The areas of concern include deficit spending, fund balance/reserves, fiscal recovery plan, and the Governor's proposed budget.

Deficit Spending: The District is projecting deficit spending of ($523,762) in 2016/17, ($619,576) in 2017/18, and ($764,249) in 2018/19 leaving a projected ending fund balance in the general fund of ($443,465). The projected deficit spending not only reduces the reserves, but also greatly reduces the District's available cash. Failure to minimize deficit spending will jeopardize the financial standing of the District, including its ability to meet the state recommended minimum reserve for economic uncertainties. Although some deficit spending may be the result of one-time costs from prior year funding sources, ongoing structural deficits threaten the school district's future educational programs. Districts that wait too long to address and correct structural deficits are forced to make dramatic corrections all at once. In contrast, carefully planned and phased-in structural corrections lessen the impact on children.

Fund Balance/Reserves: The District projects an ending fund balance in the general fund of $320,784 with an unappropriated component of ($314,890) at June 30, 2018 and a projected ending fund balance of ($443,465) with an unappropriated component of ($1,086,626) at June 30, 2019. The District projects a reserve for economic uncertainties of approximately $1,100,000 in Fund 17 for 2016/17, 2017/18, and 2018/19. Even with the District's projected reserve for economic uncertainties in Fund 17, the District fails to maintain the state-required 4% minimum reserve for economic uncertainty in the second subsequent year (2018/19).

Fiscal Recovery Plan: The District's Fiscal Recovery Plan identifies five areas to begin addressing the structural deficit forecasted in the District's 2016-2019 multi-year financial projections (MYFP). The plan identifies the following measures:1. Reduction in Sonora Union High School District management, 2. Reduction in certificated/classified staff, 3. Graduation Requirements and Master Schedule, 4. Negotiations, and 5. Other Measures. The County Superintendent fully expects that the District will follow through on these measures while keeping in mind some important statutory requirements and deadlines outlined below in addition to amending the District's Fiscal Recovery Plan to accompany the District's 2nd Interim Report:

1. **Reduction in Sonora Union High School District Management:** The Fiscal Recovery Plan identifies a planned reduction of the work year for certificated management, classified management, and for the Superintendent in the current year (2016-2017) and following two consecutive years (2017-2018 and 2018-2019). The County Superintendent fully expects this to be reflected in the 2nd Interim report, with the following assurances to be included in the District's 2nd Interim Report:

   a. Revising certificated management contracts for each affected employee to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan.

   b. Revising classified management contracts for each affected employee to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan.

   c. Revising the Superintendent's contract to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan.

   d. Resolution for Board Approval identifying the reductions and/or change of contracts.

2. **Reductions in Sonora High School Classified, Certificated, and Confidential Staff:** The Fiscal Recovery Plan identifies a reduction of at least 5.8 full time equivalent (FTE) certificated reductions, 2.5 FTE classified reductions, and a reduction in the work year for confidential employees. As such, these reductions are dependent upon adherence to statutory timelines, an adopted Board resolution based on the Superintendent's recommendations regarding reduction in service for both classified and certificated personnel, and any administrative personnel reductions.

As a condition of avoiding a negative certification, the County Superintendent fully expects that the District will adhere to the timely delivery of preliminary layoff notices on or before March 15, 2017 for certificated personnel followed by a timely delivery of final termination notices and/or contract reductions on or before May 15, 2017 for certificated personnel, and on or before April 28, 2017 (or 60 days prior to the effective date of the layoff) for classified personnel. With a number of other anticipated actions related to the right of employees to request a hearing with the Office of Administrative Hearings, which has the potential to delay planned personnel reductions, the County Superintendent encourages the District to seek legal counsel as they proceed with classified and certificated reductions, including reductions in contracts for management and confidential personnel. The County Superintendent expects these reductions to be reflected in the 2nd Interim report along with the following assurances to be included in the District's 2nd Interim report:

a. A revision of confidential employee contracts to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan.

b. Resolution for Board approval identifying the reductions outlined in the District's Fiscal Recovery Plan.

3. **Restructuring the graduation requirements and the Sonora High School master schedule:** According to the District's proposed restructuring of graduation requirements, the District is effectively considering reducing the total graduation credit requirement from 230 to 210, by reducing the elective course requirement from 70 to 50 course credits. However, it is unclear in the Fiscal Recovery Plan what the impact will be on deficit spending. As the District considers a possible revision to the graduation requirements in order to reduce deficit spending, the District is encouraged to consider expanding dual enrollment options made available under Assembly Bill 288 and the benefit it could provide to students affected by the proposed reductions. Should the District proceed with this restructuring, please include the following assurances in the 2nd Interim report:

a. Board approved revision of graduation requirements.

b. Projected personnel reductions (in FTE) for <u>this</u> proposed change in graduation requirements.

4. **Negotiations and Bargaining Units:** It is unclear in the District's brief narrative in the Fiscal Recovery Plan what impact negotiations will have on reducing deficit spending. The County Superintendent encourages the negotiating team to look carefully at contract language, which may limit the ability to budget conservatively, drawing critical attention to articles regarding class size and salary caps for incoming teachers. Furthermore, recognizing that the District's Fiscal Recovery Plan indicates that the District will work beginning in January 2017 to address negotiations, there remains a very short period of time (of less than two months) to align contract language with anticipated layoff notices and resulting staffing ratios limited by class size "goals" mentioned in XI of the certificated contract. Finally, due to the qualified status of the District's budget, the County Superintendent shall have at least 10 working days to review and comment on any proposed agreement made to determine the financial impact of the proposed agreement. The County Superintendent fully expects that the District's 2nd Interim report will include the following assurance:

a. Collective Bargaining Public Disclosure, if any, as per Government Code 3540.2

5. **Other District and Site Measures:** Please provide assurances in the District's 2nd Interim report of the following measures sited in this section of the District's Fiscal Recovery Plan, namely:

a. The District intends to implement the 25 recommendations from the FCMAT report. Please include a summary of progress made on the 25 recommendations.

b. As the District evaluates its capacity to assume responsibility for special education programs and services for SUHSD students currently provided by TCSOS, please provide a summary of the District's decision, and the fiscal impact its decision will have in reducing the structural deficit for the NEXT fiscal year and the subsequent TWO years out (2017-2020). Furthermore, the District should cautiously weigh its practice of not directly serving certain populations of special needs students and consider the rights of these students to a general education first and untapped opportunities for the school to augment the inclusion of special needs students in the general school population, the cost of which should be examined with equity.

c. The District is evaluating the option for an outside agency's review of the District's food services, maintenance and operations, transportation, facilities, and special education operations. Should the District proceed in exercising the option for an outside agency's opinion, please provide the County Superintendent with a copy, pursuant to E.C. 42127.6, of any study, report, evaluation, or audit that contains evidence that the school district is showing fiscal distress.

d. Provide a summary of cost savings in supplies, materials and services and how this will reduce deficit spending over the MYFP.

e. Career and Technical Education Incentive Grant (CTE). The CTE program grant funds require matching funds to which the District would have to obligate $1,306,050 over the current year and two consecutive years. The Fiscal Recovery Plan intends on using the one-time CTE grant award of $500,000 to reduce deficit spending through 2019. The practice of using one-time funds to resolve long-term debt **must** be avoided. The district should serve precautionary layoff notices to FTE's affected by this program, should the District be unable to meet the matching fund requirements for 2018-2019 and beyond once the grant period ends.

f. College Readiness Block Grant of $75,000. As with the advice above, the District is using one-time grant awards to fund ongoing FTE's. The District should serve precautionary layoff notices to FTE's affected by this grant funded position to safeguard against economic uncertainties and or unexpected reductions in the grant award and beyond when the grant period ends.

g. Consideration of reducing Board member stipends and/or benefits. Please provide a copy of Board action should any action be taken on this item.

h. Off campus passes to students for lunch. The Fiscal Recovery Plan lacks an explanation of the impact this measure will have on deficit spending. Should the District act on this measure, please provide a summary of how the measure will reduce deficit spending.

Further recommendations: The Fiscal Recovery Plan does not address a number of areas of going concern identified in the FCMAT study (November 6, 2016). The County Superintendent expects that a revision to the District's Fiscal Recovery Plan will accompany the 2nd Interim report to include areas of going concern, and offers the following suggestions.

While the County Superintendent has no authority to review voter approved bond expenditures (that is the duty of the Bond Oversight Committee), there are a number of new facilities, maintenance and operations expenses for which there is no identified revenue and or approved facilities master plan. The FCMAT report found that:

- Although a modernization project and construction of an aquatics center were covered in part by the district's Measure J bond proceeds, both have had **significant cost overruns and have included additional infrastructure improvements to remaining facilities that were not in the original project.**

- The District's chief business official (CBO) has worked diligently to direct facilities funding and set-asides for capital project funds toward each project, but **these and other resources have been exhausted, leaving no reserves for unexpected facility maintenance or future deferred maintenance projects, or for contingencies and cost overruns.**

For this reason, the County Superintendent cautions the District in adopting future new unfunded obligations and/or borrowing through inter-fund transfers to address the lack of sufficient reserves. For example, the District's General Fund borrowed $500,000 in September 2016 and another $250,000 in October 2016 from Fund 17. Both of these amounts were paid back in December 2016. Based on the District's Cash Flow form, the District anticipates borrowing another $125,000 in March and paying it back in April 2017. While inter-fund short-term borrowing is an approved practice when property taxes and/or State apportionments have not come in, the District needs to **cure the dependency on inter-fund borrowing by increasing reserves.**

The District's 1st Interim MYFP reflects reserves at 8.05% for 2016-2017 and 6.16% for 2017-2018**. However, in 2018-2019 the reserve is projected to drop significantly to 0.31%.** The minimum State standard for a district of this size is 4%. The anticipated follow through of the District's Fiscal Recovery Plan provides for planned reductions that must bring the District's reserve above the state minimum. Due to a number of uncertainties and concerns enumerated above, the District should not only be very concerned about the first and second subsequent year, but should plan beyond 2018-2019.

Given the uncertainty of student enrollment and the District's history of deficit spending, the County Superintendent **strongly** recommends that the District increase the number of PRELIMINARY layoff notices for certificated personnel and PRECAUTIONARY layoff notices to classified staff this year. Absent additional reductions guided by conservative estimates, all indicators suggest that the District will face a negative certification in the subsequent years. Perpetuating a qualified budget status must be avoided; a positive certification should be the only budget status the District should settle for. **In addition to the proposed actions to reduce deficit spending to meet or exceed the minimum State standard for reserves in order to achieve a POSITIVE certification for 2017/18 Budget, please amend the Fiscal Recovery Plan to include the development of a Facilities Master Plan.**

The Fiscal Recovery Plan does not address FCMAT's finding that the district's ADA is 90.84% of its enrollment, which is impacting the District's per pupil funding. Furthermore, with chronic absenteeism as an indicator on the State's Accountability Plan for 2017/2018, **the County Superintendent strongly suggests that the District amend its Fiscal Recovery Plan to address the ADA revenue stream**.

The District has agreed to provide consulting services to the incoming CBO For the period January 2017 – June 30, 2017. It may also be prudent for the District to invest in on-site fiscal support and technical assistance from FCMAT for the incoming Chief Business Official as she works to formulate the District's 2nd Interim report due in two months, and next year's budget and MYFP due in June, in addition to any (or all) of the workshops listed on Page 9 of this letter.

<u>Other Factors to consider as the District prepares the 2nd Interim report:</u>

Statutory Requirements for Collective Bargaining Public disclosure and Debt Issuance: Because the District filed a qualified First Interim report certification, this letter is also a reminder of the statutory requirements for collective bargaining public disclosure and debt issuance for school districts with qualified or negative interim report certifications. These requirements are specifically addressed by the following code sections:

Collective Bargaining Public Disclosure: Government Code 3540.2 (a) states *"A school district that has a qualified or negative certification pursuant to Section 42131 of the Education Code shall allow the county office of education in which the school district is located at least 10 working days to review and comment on any proposed agreement made between the exclusive representative and the public school employer, or designated representatives of the employer, pursuant to this chapter. The school district shall provide the county superintendent of schools with all information relevant to yield an understanding of the financial impact of that agreement."*

Debt Issuance: Education Code Section 42133(a), which reads: *"A school district that has a qualified or negative certification in any fiscal year may not issue, in that fiscal year or in the next succeeding fiscal year, certificates of participation, tax anticipation notes, revenue bonds, or any other debt instruments that do not require the approval of the voters of the district, nor may the district cause an information report regarding the debt instrument to be submitted pursuant to subdivision (e) of Section 149 of Title 26 of the United State Code, unless the county superintendent of schools determines, pursuant to criteria established by the Superintendent of Public Instruction, that the district's repayment of that indebtedness is probable. A school district is deemed to have a qualified or negative certification for purposes of this subdivision if, pursuant to this article, it files that certification or the county superintendent of schools classifies the certification for that fiscal year to be qualified or negative."*

Annual Report: Pursuant to the provisions of Education Code Section 1240(e), 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 disapproved budget, qualified or negative interim certification, or that has been determined at any time during the year to be in a position of fiscal uncertainty pursuant to Education Code Section 42127.6. This report will be issued on or before September 15, 2017.

Submission of Studies, Reports, Evaluations, and/or Audits: EC Sections 42127 and 42127.6 require districts to submit to the County Office any studies, reports, evaluations, or audits done of the district that contain evidence that the district is showing fiscal distress. The Education Code also requires the County Office to incorporate that information into its analysis of budgets, interim reports, and the district's overall financial condition.

The County Superintendent requests that the District submit to her office any such documents commissioned by the District (e.g., reports done by the Fiscal Crisis and Management Assistance Team, independent consultants commissioned by the District, etc.), or by the State Superintendent of Public Instruction and/or a state control agency any time they are received by the District.

<u>Fiscal Forecast/Governor's Proposed Budget:</u> Governor Jerry Brown has used the word "prudent" several times to describe his January budget proposal for 2017-18, announced in Sacramento on January 10. Brown alluded to the likelihood of another recession beginning in the next few years, and hinted at budget uncertainty stemming from the new administration in Washington, which could very well result in California receiving fewer federal dollars than anticipated, as he outlined a generally cautious budget proposal. The State Controller Betty Yee reported "Given the state's revenue shortfall and an inevitable future economic downturn, coupled with unpredictable federal funding under the new president, Governor Brown is right to be cautious." The District should pay close attention to the Governor's proposals and May Revision, and align the 2017-2018 Budget accordingly. We recommend the Chief Business Official attend workshops associated with the Governor's May Revision as noted on Page 9 of this letter.

Conclusion: The District is expecting to deficit spend and decrease the General Fund balance in the current fiscal year and subsequent years. In fiscal year 2018/19, the District is expecting a negative ending fund balance caused by continuous structural deficit spending. In order to remain solvent, it is necessary for the District to make significant reductions in fiscal years 2017/18 and 2018/19. Therefore, for this interim period, we agree with the Board's qualified certification. The substantive actions to implement the necessary reductions and accompanying detailed actionable Board approved **amended** Fiscal Recovery Plan in the District's 2nd Interim budget, **due March 17, 2017**, will be the basis for the County Superintendent's evaluation of the need to invoke the provisions of Ed Code Section 42127.6.

We wish to express our appreciation to the District staff for their cooperation during the review of the 2016/17 First Interim Report. If our office can be of further assistance, please call (209) 536-2020.

Sincerely,

Marguerite D. Bulkin — *Elizabeth Rico*

County Superintendent — *Assistant Superintendent Business Services*

ER:djh

cc: *Marguerite D. Bulkin, County Superintendent*
Dana Vaccarezza, Chief Business Official
California Department of Education
State Controller's Office

Check List for Amended Fiscal Recovery Plan and Assurances to Accompany the District's 2nd Interim Report due March 17, 2017

☐ Resolution for Board Approval identifying the reductions and/or changes to the following contracts:

- Revision of certificated management contracts for each affected employee to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan
- Revision of classified management contracts for each affected employee to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan.
- Revision of the Superintendent's contract to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan
- A revision of confidential employee contracts to reflect the reduction of contracted days as described in the District's Fiscal Recovery Plan

☐ Board approved revision of graduation requirements.

☐ Projected personnel reductions (in FTE) for proposed change in graduation requirements.

☐ Collective Bargaining Public Disclosure, if any, as per Government Code 3540.2

☐ The District intends to implement the 25 recommendations from the FCMAT report. Please include a summary of progress made on the 25 recommendations.

☐ As the District evaluates its capacity to assume responsibility for special education programs and services for SUHSD students currently provided by TCSOS, please provide a summary of the District's decision, and the fiscal impact its decision will make in reducing deficit spending for NEXT school fiscal year and the subsequent TWO years out (2017-2020).

☐ The District is evaluating the option for an outside agency's review of the District's food services, maintenance and operations, transportation, facilities, and special education operations. Should the District proceed in exercising the option for an outside agency's opinion, please provide the County Superintendent with a copy, pursuant to E.C. 42127.6, of any study, report, evaluation, or audit that contains evidence that the school district is showing fiscal distress.

☐ Provide a summary of cost savings in supplies, materials and services, as proposed in the Fiscal Recovery Plan, and describe how this measure will reduce deficit spending over the MYFP.

☐ Career and Technical Education Incentive Grant (CTE). The CTE program grant funds require matching funds to which the District would have to obligate $1,306,050 over the current year and two consecutive years. The Fiscal Recovery Plan intends on using the one-time CTE grant award of $500,000 to reduce deficit spending through 2019. The practice of using one-time funds to resolve long-term debt **must** be avoided. The district should serve precautionary layoff notices to FTE's affected by this program, should the District be unable to meet the matching fund requirements for 2018-2019 and beyond once the grant period ends.

☐ College Readiness Block Grant of $75,000. As with the advice above, the District is using one-time grant awards to fund all/or part of ongoing FTE's. The District should serve precautionary layoff notices to FTE's affected by this grant funded position to safeguard against economic uncertainties and or unexpected reductions in the grant award and beyond when the grant period ends.

☐ Consideration of reducing Board member stipends and/or benefits. Please provide a copy of Board action should any action be taken on this item.

- [ ] Off campus passes to students for lunch. The Fiscal Recovery Plan lacks an explanation of the impact this measure will have on deficit spending. Should the District act on this measure, please provide a summary of how the measure will reduce deficit spending.
- [ ] Please amend the Fiscal Recovery Plan to include the development of a Facilities Master Plan.
- [ ] The County Superintendent strongly suggests that the District amend its Fiscal Recovery Plan to address the ADA revenue stream.
- [ ] The County Superintendent strongly recommends that the District increase the number of PRELIMINARY layoff notices for certificated personnel and precautionary layoff notices to classified staff this year.

Recommended Workshops for Incoming Chief Business Official:

FCMAT Workshops: http://fcmat.org/professional-development

- Local Control Funding Formula and Accountability Plans Workshop

School Services of California:

- The Basics of School Construction and School Construction Accounting
- Special Education: Both Sides of the Equation
- May Revision Workshop
- Year End Close
- SSC Online Workshops: http://www.sscal.com/workshops.cfm
    - Associated Student Body
    - Attendance Accounting
    - Fiscal Aspects of Negotiations
    - Fiscal Solvency for School Districts

CASBO Workshops: https://www.casbo.org/event/standardized-account-code-structure-basic-concepts-42717-sacramento-area

- Standardized Account Code Structure Concepts (Basic)
- Standardized Account Code Structure Concepts (Advanced)