MENDOCINO COUNTY OFFICE OF EDUCATION
WARREN GALLETTI, SUPERINTENDENT OF SCHOOLS
2240 Old River Road • Ukiah, CA 95482-6156 • 707 467-5001 • Fax 707 462-0379

INTEGRITY • CUSTOMER SERVICE • ACCOUNTABILITY • TEAMWORK • INNOVATION • PASSION

February 14, 2017

Brent Cushenbery, Superintendent
Members, Board of Trustees
Point Arena Schools District
P.O. Box 87
Point Arena, California 95468

SUBJECT: REVIEW OF 2016/17 FIRST INTERIM POINT ARENA SCHOOLS DISTRICT BUDGET

Dear Superintendent and Members of the Board:

We have reviewed your 2016/17 First Interim Report in accordance with Education Code Section 42130, regarding our fiscal oversight responsibilities. Mendocino County Superintendent of Schools is required to review Interim Reports to ensure expenditures will not exceed available resources and projected revenues are realistic. Education Code Section 33127 further explains the guide used to monitor the fiscal stability of school districts shall be the adopted State Board of Education's Standards and Criteria. School districts shall also use these same Standards and Criteria in developing their budgets and managing their expenditures. AB1200 and AB2756 charge County Offices of Education with certain fiscal oversight responsibilities for school districts. In order to comply with these requirements, MCOE must assure all budget documents are complete and accurate. Any technical corrections to the budget brought to our attention are being addressed with your district Business Manager.

As a result of our review, we concur with the positive certification of your First Interim Report with the following comments:

State Budget: On January 10, 2017 the Governor released his proposed spending plan for 2017/18, which identified a budget deficit of **<$1.6 billion>**, due to deteriorating projected revenue, particularly from personal income tax, and increased general fund expenditures largely associated with Medi-Cal, the state's Medicaid program. In order to balance the budget, the Governor proposes $3.2 billion in spending cuts that are expected to eliminate the deficit and generate $1.6 billion in discretionary reserves to be deposited in the state's rainy day fund.

Federal Action: Changes in the political tenor at the federal level could have a negative impact on the state's budget. Shifts in federal education and immigration policy have the potential to reduce statewide federal funding as well as ADA levels at districts; while a major shift or full repeal of the Affordable Care Act could reduce federal funding for the state's health insurance program, thereby increasing the state's projected deficit.

Education Funding: Schools and Community Colleges are expected to take the brunt of the projected spending cuts, through a **<$1.7 billion>** reduction to the Proposition 98 minimum funding guarantee. The Governor's budget proposes to reallocate $859 million (related to 15/16 and 16/17 funding) to 2017/18, thereby making it unavailable for current year expenditures, and reducing the 17/18 minimum guarantee by $953 million, and creating a $264 million Maintenance Factor reduction.

The proposed 2017/18 budget only provides Local Control Funding Formula (LCFF) funding to meet the statutory cost-of-living adjustment, currently estimated at just 1.48%. This translates to an LCFF appropriation of $744 million, versus $2.2 billion anticipated when the First Interim report was prepared, and much lower than prior year actuals:

LCFF Funding (Billions)	2013-14	2014-15	2015-16	2016-17	2017-18	2018-19
Actual 1st Int (Oct 2016)	*$2.1*	*$4.7*	*$6.0*	*$2.9*	$2.2	$0.835
Budget Proposal (Jan 2017)					$0.744	$1.9
COLA	1.57%	0.85%	1.02%	0	1.48%	2.40%
Gap Funding	12.02%	29.99%	51.97%	55.28%	23.67%	53.85%
% of Target funded	72%	80%	90%	96%	96%	97%*

**estimated*

Over the three-year period, School Services of California projected that districts will be worse off than at First Interim by about $400 per ADA.

The TK-3 CSR grade span adjustment will increase slightly to $748 per ADA, as will the grade 9-12 adjustment, slated to increase to $226 per ADA. Supplemental and Concentration entitlements will continue to be calculated as they have been in prior years; and Pupil Transportation and Targeted Instructional Improvement Grants will continue as add-ons to LCFF, and will not receive a COLA.

Deferral and Cash Flow: As a result of lower-than-projected revenues in the current year, the Governor proposes deferring $859 million owed to LEAs as part of their 2016/17 LCFF funding from June 2017 to July 2017. This "one-time LCFF cost shift", as the Governor describes it, will result in lower cash balances at the close of 2016/17 for all LEAs. **Districts will need to closely monitor their cash flow to insure enough positive cash to complete the year.**

Discretionary Funding: The Governor's budget provides $287 million in one-time Proposition 98 funds for school districts, charters and county offices to be used at the discretion of each LEA. This discretionary funding is expected to be about $48 per ADA, and will be counted toward offsetting any outstanding prior-year mandate reimbursement claims of each LEA.

Mandate Block Grant (MBG): The Governor proposes to increase the MBG by $8.5 million to fund the addition of the Training for School Employee Mandated Reporters program, adding roughly $1.40 per ADA to the MBG.

PERS and STRS Employer Rate Increases: Rising pension costs will continue to vie for more of school district budgets. The CalPERS board recently lowered its assumed rate of return by a half percentage point to 7%, causing district contribution rates to go up. STRS recently followed PERS and reduced its assumed rate of return as well. However, due to differing regulations, the employer STRS rate cannot increase without legislative action, therefore they will remain the same for now:

CalPERS Employer Rates	2016-17	2017-18	2018-19	2019-20	2020-21	2021-22	2022-23	2023-24
Old Rate of Return	13.89%	15.8%	17.7%	19.7%	21.1%	na	na	na
New Rate of Return	13.89%	15.8%	18.7%	21.6%	24.9%	26.4%	27.4%	28.2%
CalSTRS rates	12.56%	14.43%	16.28%	17.93%	19.58%	21.23%	22.88%	24.53%

Returning to the status of your District's First Interim Budget, we note that your **District's Fiscal Crisis Indicators include the following risk factors, which must be monitored and addressed to ensure the district's fiscal solvency:**

- **Reserves:** The MYP projection indicates the district's unrestricted general fund ending balance will decline from $1.97 million at the beginning of 2016-17 to $1.34 million at the end of 2018-19. We commend the district for maintaining a Board Reserve for Economic Uncertainty of 12% in each of the current and two subsequent years, eight points higher than the state required minimum. Reserves provide a safety net that allows the district to meet its financial obligations as unplanned changes in revenue and expenditures occur. The national Government Finance Officers Association (GFOA) and the California Department of Education (CDE) have both issued guidance, recommending that as a "best practice" districts, regardless of size, should consider setting aside two-months of general fund expenditures, which is 17%.

- **Deficit Spending:** The district projects deficit spending in each of the current and two subsequent years, resulting in a projected **<$631,838>** decline in the unrestricted general fund balance over the 3-year period. The district has made great strides in reducing deficit spending since budget adoption. **We continue to encourage the district to bring projected expenditures in line with projected revenue. If at any point it becomes apparent that the state minimum required reserve cannot be met, the district will need to develop a detailed board approved spending plan.**

Now in our eighth year of economic expansion, we are beginning to see signs of a weakening economy and lower projected tax revenues, which drives the Prop 98 obligation to schools. Uncertainty and risk were the major themes of the Governor's budget proposal, which he believes will be the most difficult budget facing the state since 2012. Given the unpredictability surrounding the economy and federal policy, it seems clear that districts will once again be required to do more with less, reigniting the mantra of the past recession of, "hope for the best, but plan for the worst."

As we prepare for the Second Interim reporting period, we remind districts to continue to align expenditures with the district's LCAP. We want to take this opportunity to remind districts that as we complete this year's Annual Update, districts will be required to include measurable outcome data to support the effectiveness of meeting stated goals.

We thank you for your budget presentation and assumptions, and value this opportunity to support you in your efforts to maintain the fiscal health of your district. Please know we are here to help you in the good work that you do to ensure success of your students, staff and community.

Sincerely,

Becky Jeffries

Becky Jeffries
Assistant Superintendent, Business Services

cc: Catherine Chin, Business Manager, PASD
Warren Galletti, County Superintendent
Paul Joens-Poulton, Associate Superintendent Educational Services, MCOE