



San Diego County Office of Education Main Campus
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858-292-3500 | www.sdcoe.net

August 7, 2019

Mr. Kevin Pike, Board President
Karen Janney, Ed.D., Superintendent
Sweetwater Union High School District
Chula Vista, CA 91911-1997

Re: 2019-20 Adopted Budget

Dear Mr. Pike and Dr. Janney:

Our office has completed its review of the 2019-20 Adopted Budget for the Sweetwater Union High School District (District) in compliance with the provisions of Education Code Section 42127 et seq. The San Diego County Office of Education (SDCOE) is required to review the budget to determine if it meets the criteria and standards for fiscal stability and allows the District to meet its financial obligations during the current fiscal year and satisfy its multiyear financial commitments.

The District's Adopted Budget has been analyzed in the context of the guidance provided by SDCOE, the Governors 2019-20 May Revision and the 2019-20 State Adopted Budget.

The 2019-20 Adopted Budget of the Sweetwater Union High School District has been reviewed and **Disapproved** pursuant to the provisions of Education Code Section 42127 (c)(d).

The disapproval of the Adopted Budget is based on an assessment and analysis of the following major components of the District's budget:

- Projected 2019-20 negative unrestricted beginning fund balance
- Projected 2019-20 adopted budget expenditures understated
- Structural deficit in current and upcoming fiscal years
- Cash concerns
- Insufficient supporting documentation

Projected 2019-20 Negative Unrestricted Beginning Fund Balance

In the 2018-19 estimated actuals, the District projects a negative ending fund balance in the unrestricted general fund of \$4.3 million. In reviewing actual payroll expenditures for the fiscal year, it appears that budgeted expenditures were understated by as much as \$3.0 million; however, we do not have access to the budgetary status of non-payroll expenditure categories to analyze any potential impact to the ending balance. Our office will review the unaudited actuals report in September 2019 to determine the impact to the ending fund balance, but final audited numbers will not be available until December. The projected negative ending fund balance in 2018-19 becomes the beginning fund balance for 2019-20 and is the basis for the adopted budget.

Projected 2019-20 Adopted Budget Expenditures Understated

The District's adopted budget projects total expenditures in the General Fund of \$461 million, which is a reduction of approximately \$22 million from the 2018-19 estimated actuals budget. In our analysis, the District reduced expenditures by approximately \$6.3 million from January through June 2019 due to the early retirement of 214 employees in December 2018. However, the retirement incentive will cost the district \$4 million annually from 2019 through 2024, and many costs relating to retiree health and welfare benefits will remain in effect throughout that period. Our projection of the district's salary and benefit costs for fiscal year 2019-20 assumes step and column increases based on current salary schedules, the restoration of two furlough days that all employees took in 2018-19, as well as the estimated SERP savings over the full year. Based on this analysis as well as a comparison to actual July 2019 payroll costs, expenditures in the 2019-20 adopted budget appear to be understated by \$15 to \$20 million; whereas, the District's presentation to the governing board on June 17, 2019 identified only \$11 million in intentional negative budget placeholders.

Structural Deficit in Current and Upcoming Fiscal Years

The multi-year projection (MYP) in the adopted budget includes unidentified budget reduction placeholders of \$9.2 million and \$3.1 million in fiscal years 2020-21 and 2021-22, respectively. In addition, the MYP reserves \$5 million in the 2020-21 ending balance to pay off the Qualified Zone Academy Bond in August 2021; however, this payment is not incorporated in the 2021-22 budget, thereby increasing the required reductions to \$8.1 million. These unidentified reductions do not incorporate any potential understatements from the 2018-19 and 2019-20 budgets, which would have a compounding effect in the MYP, more than doubling the reductions required in 2020-21 if current year reductions do not materialize. When we remove the District's placeholders for reductions, we forecast significant deficit spending throughout the MYP.

Cash Concerns

The District had an outstanding balance due to the Mello-Roos Fund (Fund 49) of \$12 million on June 30, 2019. While this is a significant improvement over the previous fiscal year's outstanding balance of \$40 million, it is still out of compliance with California Education Code Section 42603 and is an indicator of possible cash insolvency. Due to the ongoing AB 139 extraordinary audit and the open SEC inquiry, the District opted not to participate in the TRAns pool for borrowing purposes, instead requesting a temporary transfer of funds from the San Diego County Treasury. The District projects cash borrowing needs of up to \$73 million from the Treasury during fiscal year 2019-20 to meet spending requirements, and forecasts paying back the outstanding \$12 million to Fund 49 in June 2020. However, these cash flow projections are based on the 2019-20 adopted budget, which appears to be understated.

Insufficient Supporting Documentation

Our office has requested a comprehensive fiscal recovery plan since September 2018. Subsequently, the District governing board approved a supplemental early retirement plan (SERP) in December 2018, and we have requested detailed analysis of the results since that time. To date, we have not received sufficient information from the district necessary to perform an analysis of the actual savings attributed to the SERP, as well as to the other initiatives the District has taken to reduce spending.

In the Adopted Budget presentation to the governing board on June 17, 2019, the District presented 2019-20 budget solutions as follows:

Management Eliminations and Furloughs	\$ 4,775,000
Central Office (transportation, maintenance, non-management staff)	\$ 3,000,000
School Based Resource Allocations	\$ 4,224,000
Bargaining 2-Day Furloughs	\$ 3,900,000
Pending Bargaining Considerations TBD	<u>\$ 7,000,000</u>
Total Solutions	\$22,899,000

These budget solutions are incorporated in the 2019-20 Adopted Budget; however, as indicated in the District's description, \$10.9 million are yet to be determined and/or require continued negotiations with bargaining units.

In support of our review of the District's adopted budget, on July 1 we requested detailed budget transactions, including position budgeting. On August 1, the district provided the 2019-20 salary budget file containing salaries budgeted in the General Fund that were \$20 million higher than represented in the adopted budget. On July 8, the District provided a 2,459-page PDF document and stated it contained

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all 2019-20 budget development entries. Upon further review, we noted the document did not tie to the General Fund budgeted expenditures by approximately \$22.7 million and asked the District about the discrepancy. On July 12, the District provided detailed budget transactions in Excel that reconciled to the adopted budget. Upon review of the second submission, we noted negative budget entries totaling \$39.9 million that appear to have been intentionally left out of the initial document.

Conclusion and Recommendations for Budget Approval

We have serious concerns that the District's adopted budget submission does not accurately reflect the current financial status.

In order for our office to approve the District's budget, expenditure assumptions need to accurately reflect the financial status of the district as of the date of submission with sufficient evidence that the budget submitted contains all pertinent revenues and expenditures. As discussed in our weekly meetings prior to budget adoption, a district beginning the current fiscal year with a negative fund balance must not include unrealized expenditure reductions in the current year (negative budget placeholders).

Once an accurate budget is established, a detailed comprehensive fiscal recovery plan must be developed and submitted to our office with the revised adopted budget. The governing board should approve a fiscal action and/or contingency plan for all three fiscal years that clearly identifies whether the board-approved reductions are one-time or ongoing, the fiscal year(s) in which the reductions will occur, whether the reductions need to be negotiated with the bargaining units, and an estimated dollar amount of savings. Revised multiyear financial projections and assumptions must be included in the SACS2019 software along with all previously required supplemental forms. The District governing board will need to adopt the revised budget after holding a public hearing regarding the proposed revisions. This public hearing must be conducted pursuant to Education Code 42103. Attached please find the timeline requirements.

Our office is available to assist in any way possible and should you have any questions concerning this timeline or our office's requirements, please feel free to call me at (858) 292-3618.

Sincerely,



Michael L. Simonson
Deputy Superintendent, Chief Business Officer

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cc: Members of the School Board, Sweetwater Union High School District
Paul Gothold, Ed. D, San Diego County Superintendent of Schools
Nick Schweizer, Deputy Superintendent, California Department of Education
Lisa Constancio, Director, School Fiscal Services Division, California Department of Education
Lupita Cortez Alcala, Chief Deputy Superintendent, California Department of Education
Michael Fine, Chief Executive Officer, Fiscal Crisis and Management Assistance Team
Brent Watson, Executive Director, District Financial Services, SDCOE
Mark Skvarna, Ed.D., Fiscal Advisor
Natalie Schuff, Director, Business Advisory Services, SDCOE
Jenny Salkeld, Ph.D., Chief Financial Officer, Sweetwater Union High School District