Board of Education Report
No. 079-17/18
For 09/12/17 Board Meeting

INTEROFFICE CORRESPONDENCE
Los Angeles Unified School District
Office of the Chief Financial Officer

INFORMATIVE

DATE: September 6, 2017

TO: Members, Board of Education
Michelle King, Superintendent

FROM: Scott S. Price, Ph.D.
Chief Financial Officer

SUBJECT: **2016-17 CLOSING OF THE BOOKS (UNAUDITED ACTUALS REPORT) AND MULTI-YEAR PROJECTIONS**

At the end of each fiscal year, the District closes the books, reviews actual revenues and expenditures, and calculates ending balances. This work results in the Unaudited Actuals Report. The Board of Education is requested to approve the Report for submittal to the Los Angeles County Office of Education (LACOE), as required under Education Code Section 42100. The District's external auditors will review the Report, and the results will be included in the Comprehensive Annual Financial Report (CAFR) in mid-December. The CAFR serves as the District's official audited financial records for the 2016-17 year.

I. MAJOR HIGHLIGHTS

In 2016-17, the District was able to meet its financial commitments and ending balance requirements, as set forth in the District's Budget and Finance Policy. The Unaudited Actuals report focuses on ending balances for the recently-concluded fiscal year. Although a multi-year projection is included, this estimated three-year budget will be recalculated after norm day enrollment data has been finalized. The official multi-year budget will be presented to the Board in December, at the First Interim, using the State Account Code Structure (SACS) reporting.

The total General Fund ending balance is $1.8 billion, which consists of $1.6 billion of unrestricted and $163.1 million of restricted ending balances (see Appendix section, Table 4, page 6). The General Fund-Unrestricted unassigned balance is $721.3 million, which has been factored to balance the budget out years.

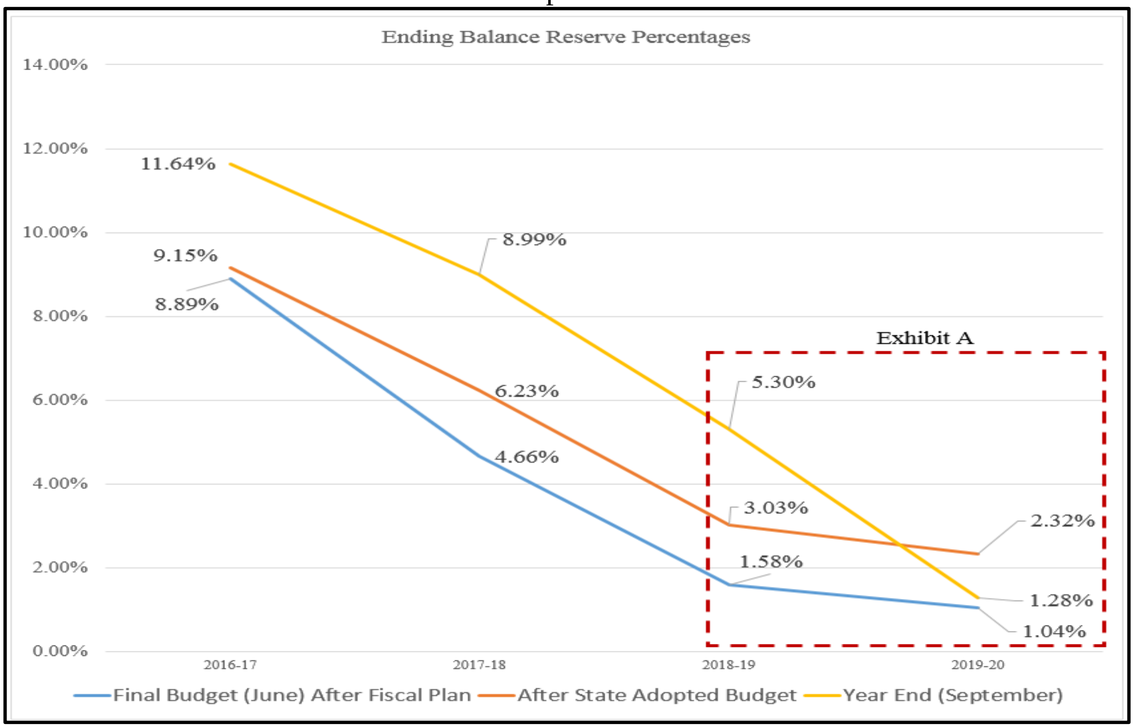
II. FISCAL ISSUES

- Estimated ending balances reflect positive unrestricted balances from 2017-18 and 2018-19, for a cumulative positive ending balance of $20.3 million by 2019-20 (See Appendix, General Fund Unrestricted Multi-Year Projection section, page 6). There are three main factors that contributed to these balances: (1) changes in revenue due to the 2017-18 State Adopted Budget; (2) the fiscal stabilization plan adopted as part of the final budget that addresses out-year deficits; and (3) one-time ending balances from prior years.
    - Addressing the ongoing structural deficit – even with the recent revenue increases, the District's year-over-year revenues continue to be lower than estimated expenditures. Major expenditure drivers continue to grow, such as increased pension, health & welfare, and Special Education costs. Managing these fixed costs will continue to be made more challenging in a declining enrollment environment.

- ○ Use of one-time ending balances – as a result of on-going deficit spending, the District's reserve level is estimated to drop from 11.64% in 2016-17 down to 1.28% by 2019-20. The District's statutory reserve for economic uncertainty is 1% of total expenditures and other financing uses.

  The State's adopted budget resulted in an increase in reserve levels, mainly due to the one-time mandated cost block grant, an administrator to teacher (R2) ratio waiver for 2016-17 and 2017-18, and changes in the Local Control Funding Formula revenues. In Exhibit A of the chart below, these increases are reflected by the change from the blue to orange trend lines. In addition, balances from year-end and changes in expenditure requirements for the out years resulted in an increased reserve level (orange to yellow trend line).

  As stated, the District's reserve level reflects changes in our financial condition. In the short run, the changes are positive. However, the 2019-20 reserve level is projected to be only slightly above the statutory reserve requirement due to the reversal of class size increases. Any significant new expenditures will further increase the decline in the reserve level and may necessitate an additional fiscal stabilization plan.



- The District continues to expect a negative net position in its government-wide financial statements. This is primarily due to long-term pension and unfunded health benefit obligations.

If you have any questions, please contact us at (213) 241-7888.

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Appendix – Table Charts

CHANGES IN GENERAL FUND REVENUES, EXPENDITURES, AND ENDING BALANCES FOR 2016-17

Table 1
Summary of 2016-17 General Fund Revenue
(in millions)

	Unrestricted			Restricted		
	Unaudited Actuals (UA)	Third Interim	Variance UA vs. 3P	Unaudited Actuals (UA)	Third Interim	Variance UA vs. 3P
LCFF Sources	$ 5,447.5	$ 5,447.2	$ 0.3			
Federal Revenues	10.0	9.4	0.6	$ 605.1	$ 623.1	$ (18.0)
Other State Revenues	205.4	205.7	(0.3)	737.5	799.9	(62.4)
Other Local Revenues	140.1	125.9	14.2	18.9	9.8	9.1
Total Revenues	**$ 5,803.0**	**$ 5,788.2**	**$ 14.8**	**$ 1,361.5**	**$ 1,432.8**	**$ (71.3)**

Revenues

- General Fund – Unrestricted actual revenue increased by $14.8 million, which represents a 0.26% variance compared to the Third Interim projection. This net increase (offset slightly by lower miscellaneous revenues) is mainly in other local revenue sources and is attributed primarily to the following:
    - $7.3 million revenue was recognized after reconciliation of CalPERS and PARS retirement contributions.
    - $4.4 million revenue was realized from the release of balances from the attendance incentive program.
    - $2.1 million higher interest income was due to higher cash balances and a higher rate of return. The County interest rate increased from 1.15% in the third quarter to 1.29% in the fourth quarter.
    - $1.6 million higher income resulted from prepaying CalPERS Safety Plan employer share contributions.

- General Fund – Restricted actual revenue decreased by $71.3 million. This consisted primarily of CalSTRS on-behalf pension contributions ($52.5 million) and categorical programs ($16.6 million) that are recognized when related expenditures are incurred.

Table 2
Summary of 2016-17 General Fund Expenditures
(in millions)

	Unrestricted			Restricted		
	Unaudited Actuals (UA)	**Third Interim**	**Variance UA vs. 3P**	**Unaudited Actuals (UA)**	**Third Interim**	**Variance UA vs. 3P**
Certificated Salaries	$ 2,108.3	$ 2,122.8	$ (14.5)	$ 753.6	$ 772.7	$ (19.1)
Classified Salaries	571.7	582.6	(10.9)	392.0	399.1	(7.1)
Employee Benefits	1,140.0	1,151.8	(11.8)	686.0	745.1	(59.1)
Books & Supplies	146.4	223.2	(76.8)	113.1	115.5	(2.4)
Services & Operating Expenses	385.4	454.1	(68.7)	415.4	421.7	(6.3)
Capital Outlay	12.5	9.2	3.3	36.0	16.6	19.4
Other Outgo	6.0	8.5	(2.5)	-	-	-
Total Expenditures	**$ 4,370.3**	**$ 4,552.2**	**$ (181.9)**	**$ 2,396.1**	**$ 2,470.7**	**$ (74.6)**

Expenditures

- General Fund – Unrestricted actual expenditures decreased by $181.9 million, which represents a 4 % variance compared to the Third Interim. The net decrease is primarily due to the following:
  - $37.2 million lower salaries and benefits due to the implementation of a hiring freeze in preparation for the reduction in force in FY17-18.
  - $25.4 million lower reserve for liability self-insurance claims based on updated estimates.
  - $12.0 million lower actual expenditures incurred for software licenses, hardware maintenance, E-Rate, and other ITD projects.
  - $7.8 million decrease in Risk Management insurance and other legal costs.
  - $7.1 million lower utilities costs than projected due to lower electricity and water rates and lower actual water consumption.
  - $5.9 million lower than anticipated school spending on the student attendance incentive.
  - $4.0 million lower reserve for uncollectible salary overpayments.
  - Decreases in program expenditures, which will be carried over to the following year, mainly from textbooks ($41.1 million) and Target Student Population Program ($6.8 million).

- General Fund – Restricted actual expenditures are lower by $74.6 million, resulting in an offsetting decrease in revenues. The portion of underspending related to categorical programs ($16.6 million) is re-budgeted in the subsequent year and will be recognized as revenues when expenditures are incurred then.

Table 3

Summary of 2016-17 General Fund Other Financing Sources/Uses/Indirect Cost

(in millions)

	Unrestricted			Restricted		
	Unaudited Actuals (UA)	**Third Interim**	**Variance UA vs. 3P**	**Unaudited Actuals (UA)**	**Third Interim**	**Variance UA vs. 3P**
Indirect Cost	$ 80.5	$ 82.2	$ (1.7)	$ (60.9)	$ (62.3)	$ 1.4
Transfers In	36.0	36.2	(0.2)	1.3	0.2	1.1
Other Sources	78.8	10.1	68.7			-
	195.3	128.5	66.8	(59.6)	(62.1)	0.3
Transfer Out	(78.7)	(86.3)	7.6	-	-	-
Contribution	(1,074.6)	(1,091.2)	16.6	1,074.6	1,091.2	(16.6)
	(1,153.3)	(1,177.5)	24.2	1,074.6	1,091.2	(16.6)
Net	**$ (958.0)**	**$ (1,049.0)**	**$ 91.0**	**$ 1,015.0**	**$ 1,029.1**	**$ (14.1)**

Net Contributions/Transfers/Indirect Costs[1] – the overall Net Contributions, Transfers, and Indirect Costs decreased by $91.0 million, which represents an 8.67% variance compared to Third Interim projections. Primary reasons for this decrease are:

- Revenue recognized from spectrum usage rights relinquished by KLCS in connection with the Federal Communications Commission reverse auction ($65.3 M).
- Lower support to Special Education ($14.2 million) primarily due to lower actual personnel expenditures.
- Lower support for the Child Development Fund ($5.6 million) due to higher revenue and the Cafeteria Fund ($1.9 million) due to higher revenue from donated commodity, combined with lower food costs.

[1] Contributions represent inter-program support within the General Fund when expenditures incurred for a given restricted resource (e.g., Special Ed program) exceed the amount available for expenditure. Transfers are inflows/outflows of moneys between funds (e.g. Cafeteria Fund) for various purposes including support for program activities.

Table 4

Summary of 2016-17 General Fund Ending Balance

(in millions)

	Unrestricted			Restricted		
	Unaudited Actuals (UA)	Third Interim	Variance UA vs. 3P	Unaudited Actuals (UA)	Third Interim	Variance UA vs. 3P
Nonspendable	$ 23.5	$ 31.1	$ (7.6)			
Restricted			-	$ 163.1	$ 174.0	$ (10.9)
Assigned	783.9	653.4	130.5			-
Unassigned-Reserve for Economic Uncertainties	73.4	73.4	-			-
Unassigned/Unappropriated	721.3	556.5	164.8			-
Ending Balance	**$ 1,602.1**	**$ 1,314.4**	**$ 287.7**	**$ 163.1**	**$ 174.0**	**$ (10.9)**

General Fund Ending Balances –The summary of changes as discussed above resulted in an overall increase in the unrestricted ending balance by $287.7 million and a decrease in the restricted ending balance by $10.9 million. The restricted ending balance represents an unspent balance from legally restricted funding sources. The unrestricted ending balance is composed of non-spendable, assigned, and unassigned categories, and will be used as beginning balances in the 2017-18 fiscal year.

- Assigned Ending Balance: Certain account balances remain available to schools and offices for future use. Carryover accounts include General Fund School Program account, school discretionary accounts, and funds reserved for fire damage. The Assigned Fund Balance increased by $130.5 million, mainly due to set-asides for the KLCS spectrum auction proceeds and schools accounts (textbooks, Targeted Student Population, and Proportionality).
- Unassigned (Undesignated) Ending Balance: The year-end actual unassigned ending balance is $164.8 million higher than Third Interim.

GENERAL FUND UNRESTRICTED MULTI-YEAR PROJECTION

The year-end closing numbers resulted in a one-time increase in the unassigned balance of $164.8 million, to a total unassigned beginning balance of $721.3 million for 2017-18. The estimate from the Third Interim was $556.5 million. The chart below provides an update on changes subsequent to the final budget.

(Dollars in Millions)	2016-17	2017-18	2018-19	2019-20	Cumulative Balance
Non-cumulative Balances @ Final Budget	$556.5	($281.1)	($232.4)	($41.5)	$1.5
Ending Balances @Final Budget		**$275.3**	**$43.0**	**$1.5**	
State Budget Adoption Changes	$18.6	$99.8	($9.5)	($14.3)	$94.6
Reversal of Class Size Increase	$0.0	$0.0	$0.0	($76.0)	($76.0)
Other Changes	$146.2	$55.3	($35.8)	($165.5)	$0.2
Non-cumulative Balances @ Year End	$721.3	($126.0)	($277.7)	($297.3)	$20.3
Revised Ending Balances @ Year End		**$595.3**	**$317.6**	**$20.3**	

Revenue and expenditure information received after the Final Budget resulted in an overall positive revised ending balances for 2017-18 through 2019-20.

- **Changes in Revenues** - Estimated revenues increased by approximately $97.1 million in 2017-18 and decreased by $11.0 million in 2018-19 and $15.7 million in 2019-20. This is mainly due to the changes in LCFF gap funding and one-time Mandated cost funding in the State-adopted Budget.

- **Changes in Expenditures, Contributions and Assigned Balances –** The estimated expenditure increase is mostly attributable to the settlement agreement, partly offset by onetime decrease in the Title I set aside, reduction in force delay in implementation set aside, ongoing decreases in PE uniforms, and other base line expenditures.

  The FY 2019-20 ending balance reflects the reversal of the $76 million class size increase (part of fiscal stabilization plan). In June, the 2017-18 Final Budget Fiscal Stabilization plan also reflected a savings of $246 million to zero-out general fund school program (13027) carryover by 2019-20. These savings have been revised to $100 million mainly due to the spending of carryover balances by school sites.