Budgeting Basics- Pt. 1

Interpreting the Interim Budgets and Multi-Year Projections

Scott Weimer
Merced Union High School District
Prepared: April 17, 2017

Overview

The Fiscal Services Department uses the Standardized Accounting Code Structure (SACS) and must use these codes when making reports to the state. The form and structure of these reports are unique and often confusing to those who are not part of the accounting world. This document lists key terms, common areas of confusion, and current issues in school budgeting that will hopefully make the budget reports easier to understand.

Key Budgeting Terms

1. **Budget & Interim Budgets-** The district submits the budget based on current information and assumptions to the board in June for approval. The 1st Interim Budget is due by mid Dec and the 2nd Interim is due in mid March. These interim budgets are based on updated information from the state and current expenses.
2. **Multi-Year Projections (MYP)**- The state requires that the budget that is submitted includes the current year plus two subsequent years. The California Association of School Business Officials recommends that you prepare the current year plus the next three years. The two main reasons for multi-year projections are to account for 1) one time grant funds that may have income in one year but expenditures over multiple years and 2) known increases in future year's expenditures like step/column or increases in STRS/PERS. This allows everyone to see how decisions made in the current year will affect future year balances.
3. **Positive Certification**- A positive certification means the district meets all state requirements in the current year as well as the two subsequent years.
4. **Supplemental & Concentration Funds**- The Local Control Funding Formula (LCFF) is the way in which the state allocates funds to schools. Along with the base funding for Average Daily Attendance (ADA), the district receives supplemental funds for each Low Income (LI), English Learner (EL), and Foster Youth (FY) student. Since these students make up more than 55% of the district population, the district also receives additional concentration funds. These funds are not restricted but the district must demonstrate how they have increased or improved services for these students in their Local Control Accountability Plan (LCAP).
5. **Restricted Funds**- The General Fund budget includes both unrestricted and restricted funds. Restricted funds like Special Education, Title 1, and College Readiness Grant may only be used for expenses that are outlined in approved plans. Resource codes (4 digit number, the 3rd through 6th in the budget string 01-3550-0-4300.90-1110-1000-110-100-025) above 3000 are restricted funds.

6. **Economic Uncertainties**- The state requires 3% to be set aside and not allocated for specific expenses in case of emergencies or cash flow issues. Professional organizations recommend two months worth of expenses which would be close to 14%. The district currently has approximately 10%. These funds can be in the unrestricted General Fund or in Fund 17. If the ending unrestricted General Fund balance and Fund 17 balance equal the Economic Uncertainty requirement the district has set then no new funds from the current year need to be set aside.
7. **Routine Restricted Maintenance Account (RRMA)**- In the past, the state required 3% to be set aside for routine maintenance. Any district that receives Prop 51 funds must again set aside 3% starting the year they receive the funds. We currently ensure that 3% is spent on routine maintenance.
8. **Transfers, General Fund & Other Funds**- The General Fund is basically the district's checking account. The other funds are savings accounts for special purposes. The budget is for the General Fund and shows any transfers out to special funds. The General Fund balance does NOT include special funds.
    a. Fund 12: Child Development Center- This fund is supported by transfers in from the General Fund.
    b. Fund 13: Cafeteria- Most funds in this account are reimbursements from the National School Lunch Program but recently this has not covered all of the costs and money has been transferred in from the General Fund.
    c. Fund 14: Deferred Maintenance- This fund is for refreshing/replacing facilities and equipment that are not routine maintenance and is supported by transfers in from the General Fund.
    d. Fund 17: Other Than Capital Outlay- This is a special reserve fund and any amounts not allocated to specific projects may be counted with unallocated money in the General Fund to meet the Economic Uncertainty requirements.
    e. Fund 20: Other Post-Employment Benefits (OPEB)- This fund is for obligations to retired employees and is supported by transfers in from the General Fund. This fund has been used by the district in the past for a rainy day fund and at one point had 13 million dollars which was used to avoid layoffs or reduced days during the Great Recession.
    f. Fund 43: Special Reserve Capital Projects- This fund is for future land or facility expenses and is funded by transfers in from the General Fund.
    g. We currently are not budgeting to transfer into: Fund 11 Adult Education, Fund 15 Transportation, Fund 21 Building, Fund 25 Capital Facilities, Fund 35 County School Facilities, or Fund 51 Bond Interest. We will need to begin budgeting for bus replacement costs in Fund 15.

Common Areas of Confusion

I. Why do the Numbers Keep Changing?

The budget is based on assumptions. What will our ADA and base funding be? At what rate will the state fund schools each year? Will there be a COLA? Will there be an increase or decrease in federal programs like Title 1? What will the step and column increase be each year? What are the STRS & PERS contribution increases? The budget is based on the best available information and each Interim Budget uses real income and expenditures along with updated information for assumptions. The budget is therefore a snapshot in time from which to make the best possible financial decisions.

II. Budget Cuts?

Multi-year projections allow the district to identify issues that will arise in the future based on current and expected expenditures. A positive certification means that the district can pay its bills for at least two years into the future which basically means there is a three year budget. If assumptions change based on the Governor's budget or other information that reduces the expected income in the next or future years, then the district will need to make budget cuts. This does not automatically mean the district will need to cut the current budgets to levels lower than the current year. As income is expected to grow in multi-year projections, budgeted expenses are also expected to grow. If there is a reduction in expected income but the new amount is still greater than expected increases in expenses then the cuts would be to the growth in expenses not in a reduction from current levels. If there is a reduction in expected income and the new amount is lower than the expected increases in expenses (such as the expected income for a year is less than the expected increase in step/column plus PERS/STRS increases) then the cuts would be actual reductions below the current levels. The multi-year projections allows the district to determine if an expected reduction can be absorbed by reducing the Ending Balance, reducing the transfers out of the General Fund or if ongoing budget cuts will be required.

III. Is It a Budget or Financial Statement?

Basically, the summary sheet you see for the approved budget and interims is a financial statement for the General Fund. It does list the expenses the way the state requires which is by object code. Object codes are the 8th through 11th numbers in the string 01-3550-0-4300.90-1110-1000-110-100-025. 1000 codes are certificated pay, 2000s are classified pay, 3000s are benefits, 4000s are supplies, 5000s are services, and 6000+ are capital and other outlay. The summary does not show you how that money is spent or by which department. It also contains restricted funds which can sometimes be confusing because the income and expenses do not always show in the same years. The other fund balances are also shown separately and not included in the budget summary. The district is currently working on creating an operating budget that separates unrestricted funds (normal yearly income and expenses) from restricted funds (limited use and often not stable funding sources) and also breaks down the budgeted expenses by division and department. Hopefully these documents will provide the information people usually expect to see when they hear "budget."

2016/2017 Expenses

	2015/2016 Unaudited Actuals	2016/2017 Adopted Budget	2016/2017 First Interim	2016/2017 Second Interim	Change
Certificated Salaries	$ 49,711,661	$ 50,824,035	$ 52,968,782	$ 53,184,213	$ 215,431
Classified Salaries	$ 17,270,699	$ 18,359,349	$ 18,041,157	$ 17,863,927	$ (177,230)
Employee Benefits	$ 24,333,886	$ 27,461,616	$ 27,984,391	$ 28,324,416	$ 340,025
Books & Supplies	$ 7,207,576	$ 10,215,402	$ 9,967,330	$ 10,303,492	$ 336,162
Services	$ 13,479,420	$ 14,720,627	$ 16,574,129	$ 15,619,337	$ (954,791)
Capital Outlay	$ 2,163,933	$ 1,673,790	$ 1,793,850	$ 3,544,703	$ 1,750,853
Other Outgo	$ 1,640,146	$ 1,720,253	$ 1,733,849	$ 2,141,462	$ 407,613
Direct Support/Indirect Costs	$ (316,099)	$ (196,544)	$ (196,544)	$ (196,544)	$ -
Subtotal	**$ 115,491,222**	**$ 124,778,527**	**$128,866,944**	**$ 130,785,006**	$ 1,918,063
Interfund Transfers Out	$ 8,277,473	$ 6,597,634	$ 4,597,634	$ 4,812,999	$ 215,365
Total	**$ 123,768,694**	**$ 131,376,161**	**$133,464,577**	**$ 135,598,005**	$ 2,133,428

IV. Are We Deficit Spending?

Not exactly. The focus of the budget presentations is often on the Ending Balance of the General Fund. During many years of the Great Recession we were spending more than we were taking in and thus deficit spending. In these years money had to be transferred out of other funds and into the General Fund to pay the bills. Currently we are transferring money from the General Fund into the other funds so overall we are not deficit spending. If there is a net decrease to the General Fund Ending Balance, the district will have to decide either to not transfer as much into the other funds or allow the reduction in the Ending Balance which would also reduce the amount/percentage for Economic Uncertainties. If this negative is based on an actual operating deficit rather than one time unbudgeted expenses, then structural changes would need to be made by either reducing transfers to other funds or making cuts to the operating budgets. The multi-year projection allows you to see if current expenses along with known future year expenses will result in operating deficits so action can be taken sooner or over a period of time to address the structural issues. The state requires the budget contain the current year and two future years but many professional organizations are now recommending that districts show three years out.

General Fund Summary Projection Combined

	2016/2017 Adopted Budget	2016/2017 First Interim	2016/2017 Second Interim	2017/2018 Projected Budget	2018/2019 Projected Budget
TOTAL REVENUE	$128,943,016	$131,951,094	$132,066,551	$130,319,569	$133,156,098
TOTAL EXPENSES	$124,778,527	$128,866,944	$130,785,006	$125,558,210	$126,683,888
Excess (Deficiency) of Revenues Over Expenditures	$4,164,489	$3,084,150	$1,281,545	$4,761,359	$6,472,210
Interfund Transfers-In	$285,000	$285,000	$2,002,106	$285,000	$285,000
Interfund Transfers-Out	$6,597,634	$4,597,634	$4,812,999	$6,812,999	$6,812,999
Other Financing Sources/Uses					
Net Increase/(Decrease)	($2,148,145)	($1,228,484)	($1,529,348)	($1,766,640)	($55,789)
Beginning Balance	$13,730,815	$13,730,815	$13,730,815	$12,201,467	$10,434,827
Ending Balance	$11,582,670	$12,502,332	$12,201,467	$10,434,827	$10,379,038

Current Issues in School Budgeting

1. Prop 98 & Gap Funding

Proposition 98 guaranteed a minimum percentage of the state general fund be spent on education. The Local Control Funding Formula established base funding from ADA with the addition of supplemental and concentration funds for districts with high percentages of Low Income, English Learner, and/or Foster Youth students. The state is not currently funding schools at the LCFF target rate and the difference between the target and actual is the gap. Each year until 2021 the state is expected to increase funding and finally reduce the gap to 0. In addition, the state provides a Cost of Living Adjustment (COLA) that is calculated from increases in the state's per capita income. The current governor's budget takes a pause in closing the gap for the 2017-2018 school year and then continues to close the gap again in 2018-2019.

2. Deferrals

A deferral is when the governor postpones an expected payment to schools. The proposed state budget has an $850 million deferral that postpones the June LCFF payment to schools to July. This essentially shifts the payment to the 17-18 year which the governor then uses to reduce the amount the state needs to pay to schools. This is part of the reason why there is no increase in funding to decrease the funding gap for the 2017-2018 school year in the proposed state budget.

3. One Time Funding

When more tax receipts come in to the state than expected, the state will often release one time funds to schools. These are not ongoing funds and do not reduce the funding gap. The legislature also creates one time grant programs like the Educator Effectiveness Funds or College Readiness Grant. These funds appear as income on school district budgets and distort the perceived amount of money available for ongoing expenses. Multi-year projections are used to help understand the long term picture. The district is expected to receive more in revenue in 2016-2017 than 2017-2018. That is not because of a reduction in ongoing funding, it is because the district received one time funds in 2016-2017 that they will not be getting again in 2017-2018.

4. Automatic Increases, STRS & PERS

These issues are the biggest area of concern and the main reason professional organizations are recommending districts prepare their current year budget and three out years rather than the two the state requires. The normal increase in expenses by inflation are usually offset by a COLA adjustment by the state. Each year a larger percentage of staff move step and column on the salary schedule. This cost is automatic and can run as high as 1.5% which is over $1.5 million. The largest increases will be the increased employer contributions to STRS and PERS that has been mandated by the state. The district's PERS contribution is projected to increase by $318,941 in 2017-2018 and by $819,147 in 2018-2019. The district's STRS contribution is projected to increase by $875,440 in 2017-2018 and by $2,091,658 in 2018-2019.

5. Taking Care of Facilities and Equipment

During the Great Recession most districts made drastic cuts and/or drained their reserves to cover basic necessities and were not able to refund or replace equipment and facilities on a regular basis. Preventative maintenance programs were replaced by only fixing equipment when it broke down and usually with the cheapest fix possible, regardless of whether that was the best long term solution. The district has aging sewer and gas lines, HVAC units, electrical systems, leaking roofs, and busses that will soon not meet state standards. These issues need to be addressed with an ongoing allocation from the General Fund.