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Superintendent

May 9, 2023

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Ms. Maria Leon-Vazquez, Board President
Santa Monica-Malibu Unified School District
1651 16th Street
Santa Monica, CA 90404

Dear Ms. Leon-Vazquez:

Pursuant to Education Code (EC) Section 42131, the Los Angeles County Superintendent of Schools (County Superintendent) has completed our review of the Santa Monica-Malibu School District's (District) 2022-23 Second Interim Report. Our analysis of the data provided indicates that the District should be able to meet its financial obligations for the current fiscal year and subsequent two fiscal years. **We therefore concur with the District's positive certification** and offer our comments and concerns below.

LOCAL RESERVE CAP

EC 42127.01 prohibits school districts from having assigned and unassigned fund balances in excess of 10 percent in the fiscal year immediately after a fiscal year in which the amount of moneys in the Public School System Stabilization Account, also known as the Proposition 98 Rainy Day Fund, exceeds 3 percent of the combined total of General Fund revenues appropriated for school districts statewide. This provision is commonly known as the reserve cap, **and is operative for the 2023-24 fiscal year.** School districts identified as Basic Aid or that have fewer than 2,501 ADA are exempt from the reserve cap.

FISCAL STABILIZATION PLAN

In our review of the District's 2022-23 Second Interim Report, we noted that the District has implemented the budget reductions that were identified in the Fiscal Stabilization Plan (FSP) developed in accordance with Resolution #19-13 that the Governing Board adopted on December 12, 2019. The resolution and FSP addressed the District's structural deficit spending, and the Second Interim Report projects that the district will meet the minimum reserve requirement of 3.00 percent for 2022-23, 2023-24, and 2024-25. We appreciate the efforts of the District staff and the commitment of the District Board to address the District's fiscal solvency in a methodical and transparent approach.

DEFICIT SPENDING

The District is projecting an operating deficit of approximately \$21.95 million, representing 14.57 percent of the District's Unrestricted General Fund budgeted expenditures and other outgo for fiscal year 2022-23. The District is also projecting operating deficits of \$5.00 million, or 3.67 percent, and \$1.82 million, or 1.32 percent, for 2023-24 and 2024-25, respectively. According to our review of the District's Adopted Budget data and assumptions, and as confirmed by the District, these projected deficits are primarily due to the increased costs of salaries and benefits related to the recent bargaining unit settlement. As a result of the deficit spending, the District's Unrestricted General Fund balance is projected to decrease as illustrated in the following table.

Unrestricted General Fund Projections (\$ millions)

	<u>2022-23</u>	<u>2023-24</u>	<u>2024-25</u>
Beginning Fund Balance	\$46.78	\$24.83	\$19.83
Projected Deficit Spending	(\$21.95)	(\$5.00)	(\$1.82)
Ending Fund Balance	<u>\$24.83</u>	<u>\$19.83</u>	<u>\$18.01</u>
Reserve Amount	\$6.48	\$19.80	\$17.99
Reserve Percent	3.08%	9.99%	8.97%

The Unrestricted General Fund balance is projected to decrease from a beginning balance of approximately \$46.78 million in 2022-2023 to an ending balance of approximately \$18.01 million in 2024-25, **a decline of approximately \$28.77 million, or 61.50 percent over three years**. We are concerned about the projected trend of deficit spending and its impact on the District's ability to maintain minimum required REU in future years. Therefore, we recommend the District monitor the causes for deficit spending in order to keep it manageable and to minimize further erosion of the fund balance.

RESERVE FOR ECONOMIC UNCERTAINTIES

The District is projecting a Reserve for Economic Uncertainties (REU) of 3.00 percent for 2022-23, 9.99 percent for 2023-24, and 8.97 percent for 2024-25. While the projected reserves meet the State Criteria and Standards minimum reserve requirement, the District included

nonspecific and unallocated expenditure reductions of \$1,450,000 million in 2023-24 and 2024-25 that are to adjust for enrollment driven attrition.

When the District's projections are adjusted for these nonspecific and unapproved expenditure reductions, the Unrestricted General Fund balance in each of the two years decreases to \$18,352,784 for 2023-24 and \$15,085,365 for 2024-25. The corresponding reserve for 2023-24 and 2024-25 decreases to 9.19 percent and 7.47 percent, respectively, as illustrated in the following table.

Reserve for Economic Uncertainties (REU)
(\$ millions)

<u>District Adopted Reserves</u>	<u>2023-24</u>	<u>2024-25</u>
Ending Fund Balance	\$19.83	18.01
Reserve Amount	\$19.80	\$17.99
Reserve Percent	9.99%	8.97%
<u>Reserves Without Reductions</u>		
Unallocated Expenditure Reductions	(\$1.45)	(\$1.45)
Adjusted Reserve Amount	\$18.35	\$15.09
Adjusted Reserve Percent	9.19%	7.47%

The adjusted reserves for 2023-24 and 2024-25 are above the State Criteria and Standards minimum reserve requirement of 3.00 percent.

ENROLLMENT/ATTENDANCE AND STATE FUNDING

The District's 2022-23 Second Interim Report reflects declining enrollment of 8,835 for 2022-23, 8,495 for 2023-24 and 8,168 for 2024-25, with projected average daily attendance (ADA) of 8,393, 8,070 and 7,760, respectively. The estimated impact on the District's projected ADA reflects a two-year loss totaling 633 ADA, representing a 7.54 percent decrease from the District's 2022-23 ADA.

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While Basic Aide districts are primarily funded through local property taxes, the decline in enrollment and ADA may represent a loss of some revenue for the district in future years. We recommend that the District carefully monitor its enrollment and attendance trends, and adjust financial projections for the current and subsequent fiscal years accordingly to reflect the resulting impact. Staffing needs and facilities planning should also be assessed and adjusted based on the projected rate of decline in enrollment.

LABOR CONTRACT NEGOTIATIONS

According to our review of the District's Second Interim Report, certificated and classified labor contract negotiations for 2022-23 remain unsettled, and potential changes have not been calculated and incorporated into projected salary and benefit expenditures. As a reminder, before the District's Board of Education takes any action on a proposed collective bargaining agreement, the District must meet the public disclosure requirements of Government Code Section 3547.5 and the California Code of Regulations Title V, Section 15449. The document used for this analysis is included in Informational Bulletin No. 6570, dated July 20, 2022, and titled "2022-23 Forms for Assembly Bill 1200: Public Disclosure of Proposed Collective Bargaining Agreements." This document can be found at the following website:

<https://www.lacoe.edu/Portals/0/zBulletins/6570.pdf>

CASHFLOW

The District's cash flow projection reflects sufficient cash balances for 2022-23 to meet its financial obligations by utilizing \$11.00 million of inter-fund borrowing in November 2022 which was repaid in January 2023. The District has a Board-approved inter-fund borrowing resolution in place with cash available in other funds in order to address any potential shortfalls during the year. We request that the District notify the County Office immediately if a cash shortfall is projected that cannot be covered through local means.

CONCLUSION


Thank you for providing documentation that supports the District's positive certification. The multiyear projections, with narrative and assumptions, were helpful in our analysis and verifying the District's financial condition. The information provided reflects the District's financial position and assumptions as of January 31, 2023, and further adjustments will be made during the year as additional data becomes available.

We hope these comments are helpful to the District's administration and Board as you plan for the remainder of 2022-23, and develop your projections for 2023-24, 2024-25 and 2025-26. We

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express our appreciation to the District staff for their cooperation during our review. If our office may be of further assistance, please call me at (562) 922-6779.

Sincerely,


Sean Lewis (May 9, 2023 16:44 PDT)

Sean Lewis
Business Services Consultant
Business Advisory Services

SL:lm

c: Dr. Mark Kelly, Interim Superintendent
Melody Canady, Assistant Superintendent, Business and Fiscal Services
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