FCMAT
FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM

CSIS California School Information Services

Lucerne Valley Unified School District

Management Review

July 11, 2012

Joel D. Montero
Chief Executive Officer

FCMAT
FISCAL CRISIS & MANAGEMENT
ASSISTANCE TEAM

CSIS California School Information Services

July 11, 2012

Suzette Davis, Superintendent
Lucerne Valley Unified School District
8560 Aliento Road
Lucerne Valley, CA 92356

Dear Superintendent Davis:

In February 2012, the Lucerne Valley Unified School District and the Fiscal Crisis and Management Assistance Team (FCMAT) entered into an agreement for a study that would perform the following:

1. The Lucerne Valley Unified School District is requesting the FCMAT Team to assist in developing viable and implementable strategic planning options to help address funding long-term debt obligations, declining enrollment, decreasing state revenues and cash deferrals while maintaining fiscal solvency.
2. The district would like the team to consider options such as but not limited to consolidation or lapsation or contracting out specific components allowable under the Education Code and to make recommendations regarding enhancing revenues or reducing expenditures while focusing on the goal of remaining fiscally solvent. Any recommendation(s) shall be included in FCMAT's multiyear analysis.
3. The FCMAT Team will complete a multiyear financial projection and cash flow analysis for the current fiscal year using the 2011-12 second interim financial report as the baseline document. This component will provide the projected timeline in which the district would be required to submit a negative certification and become cash insolvent, requiring intervention from the state.

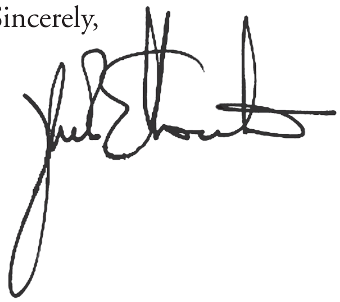
The team focused on creating a multiyear projection utilizing FCMAT's Budget Explorer software to assess the district's fiscal solvency. The team prepared a detailed projection using the 2011-12 Second Interim Financial Report as the base year, including a cash flow projection to determine whether the district could become cash insolvent and require state intervention.

FCMAT conducted fieldwork in March 2012 and conducted off-site fieldwork in April through June. To assess the district's financial condition, the team reviewed several original source documents including enrollment reports; audited financial statements; budget assumptions; adopted and interim budget files; financial system reports, unaudited actuals, payroll files, long-term debt obligations, and other financial records and third-party documentation.

This report includes the study team's findings and recommendations.

Thank you for allowing us to serve you, and please give our regards to all the staff of the Lucerne Valley Unified School District for their assistance during fieldwork.

Sincerely,



Joel D. Montero

Chief Executive Officer

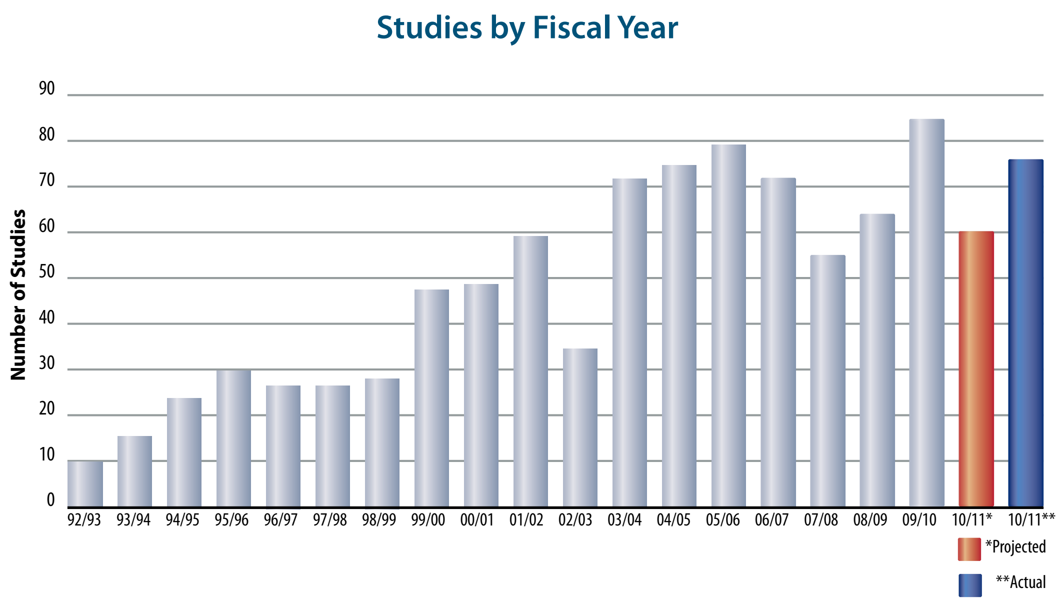
Table of contents

About FCMAT

FCMAT's primary mission is to assist California's local K-14 educational agencies to identify, prevent, and resolve financial and data management challenges. FCMAT provides fiscal and data management assistance, professional development training, product development and other related school business and data services. FCMAT's fiscal and management assistance services are used not just to help avert fiscal crisis, but to promote sound financial practices and efficient operations. FCMAT's data management services are used to help local educational agencies (LEAs) meet state reporting responsibilities, improve data quality, and share information.

FCMAT may be requested to provide fiscal crisis or management assistance by a school district, charter school, community college, county office of education, the state Superintendent of Public Instruction, or the Legislature.

When a request or assignment is received, FCMAT assembles a study team that works closely with the local education agency to define the scope of work, conduct on-site fieldwork and provide a written report with findings and recommendations to help resolve issues, overcome challenges and plan for the future.



FCMAT also develops and provides numerous publications, software tools, workshops and professional development opportunities to help local educational agencies operate more effectively and fulfill their fiscal oversight and data management responsibilities. The California School Information Services (CSIS) arm of FCMAT assists the California Department of Education with the implementation of the California Longitudinal Pupil Achievement Data System (CALPADS) and also maintains DataGate, the FCMAT/CSIS software LEAs use for CSIS services. FCMAT was created by Assembly Bill 1200 in 1992 to assist LEAs to meet and sustain their financial obligations. Assembly Bill 107 in 1997 charged FCMAT with responsibility for CSIS and its statewide data management work. Assembly Bill 1115 in 1999 codified CSIS' mission.

AB 1200 is also a statewide plan for county office of education and school districts to work together locally to improve fiscal procedures and accountability standards. Assembly Bill 2756 (2004) provides specific responsibilities to FCMAT with regard to districts that have received emergency state loans.

In January 2006, SB 430 (charter schools) and AB 1366 (community colleges) became law and expanded FCMAT's services to those types of LEAs.

Since 1992, FCMAT has been engaged to perform nearly 850 reviews for LEAs, including school districts, county offices of education, charter schools and community colleges. The Kern County Superintendent of Schools is the administrative agent for FCMAT. The team is led by Joel D. Montero, Chief Executive Officer, with funding derived through appropriations in the state budget and a modest fee schedule for charges to requesting agencies.

Introduction

Background

Located at the base of the San Bernardino Mountains near the southern end of the Mojave Desert and east of Apple Valley, the Lucerne Valley Unified School District has one elementary school and houses the middle and high school students on a separate site. The district, which has an enrollment of 844 students, was founded in 1907 and became unified in 1987.

In 2008, the Lucerne Valley Unified School District Financing Corporation issued $6,895,000 in certificates of participation (COPs) for the 2008 Financing Project. COPs are lease financing agreements in the form of tax exempt securities that enables government municipalities including school districts the ability to finance capital outlay needs without the requirements in statute for voter approval. Payments started three years after the original issuance in 2010-11 for a period of 28 years. Annual principal and interest payments of approximately $400,000 per year are pledged against the district's general fund. According to board minutes, the original intent of the COPs debt financing was to support this payment through oversight fee collections from two independent charter schools authorized by the district. Shortly afterward, one charter school closed and the district started to decline in enrollment.

In 2010, the district attempted to pass a general obligation bond to defease the COPs debt, but it was rejected 2-to-1 by the electorate. Additional general fund indebtedness includes approximately $900,000 in capital leases with payments of $298,000 per year ending in 2013-14. The total debt burden on the district's general fund with the COPs and capital leases is 11.4%, considerably more than the recommended levels of 1% to 2% and is not sustainable over the long-term under the current economic conditions.

The district is experiencing a rapid decline in enrollment. Since 2007-08, the district has lost 332 students primarily due to a surge in charter school enrollment throughout the Apple Valley region. This equates to a cumulative net loss of $4.542 million in revenue limit funding over the last five years.

Declining enrollment, a reduction in state funding, large state funding deficits, and a substantial debt burden has placed the district in a difficult financial position. Working with a fiscal advisor and the county office of education, district administration has explored debt reduction options, potential budget adjustments, consolidation of schools, lapsation and/or joint service agreements with neighboring school districts. All employee bargaining units have made concessions, including salary rollbacks, a freeze in step-and-column increases and furlough days.

As the district prepares for another round of state budget cuts, the governing board and administration requested that FCMAT complete a financial review that includes potential revenue enhancements and expenditures reductions to sustain the district's financial solvency

Created by legislation in 1991, FCMAT has prepared hundreds of studies since its inception and developed a list of 11 predictors that indicate when a school district is in fiscal distress. These are referenced in Assembly Bill 2756 and Education Code Sections 42127 and 42127.6. Several of these conditions are exhibited by Lucerne Valley Unified, including the following:

Substantial Long-Term Debt Commitments

- Certificates of Participation
- Capital Leases

Related Issues of Concern

- Student exodus from the school district (declining enrollment/charter school growth)
- Public support for public schools decreasing
- Inadequate community participation and communication

The following factors indicating fiscal distress have been identified by the San Bernardino County Office of Education and confirmed by FCMAT:

- Declining enrollment
- Unreasonable projections of average daily attendance (ADA) based on historic and state standards
- Ongoing and increasing deficit spending
- Ratio of unrestricted salaries and benefits to total unrestricted expenditures are not within the state's established standards
- Excessive debt burden supported by the general fund from certificates of participation (COPs) and capital lease agreements
- Excessive debt ratio within the general fund

Of particular concern is the impact on the unrestricted general fund from considerable long-term debt and rapidly declining enrollment. The district can sustain these factors in the short-term, but must develop a contingency plan to avoid fiscal insolvency in the long-term.

Study Team

The study team was composed of the following members:

Deborah Deal, CFE
FCMAT Fiscal Intervention Specialist
Los Angeles, CA

Eric D. Smith
FCMAT Consultant
Templeton, CA

Lynn Kamph
FCMAT Consultant
Paradise, CA

Margaret Rosales
FCMAT Consultant
Kingsburg, CA

Leonel Martínez
FCMAT Technical Writer
Bakersfield , CA

Study Guidelines

FCMAT visited the district on March 7, 2011 to conduct interviews and collect data. In April and May, the team compiled and reviewed data pending the return of the district's business manager, who was on leave, in May. This report is the result of those activities.

Executive Summary

The legislation known as Assembly Bill (AB) 1200 and AB 2756 provide the structure for fiscal accountability and the oversight process for a school district's financial condition. They include specific responsibilities for the county superintendent of schools, the superintendent of public instruction and FCMAT to assist a district in fiscal distress.

Multiyear financial projections (MYFPs) are required by AB 1200 and AB 2756 as part of the budget and interim financial reporting process. These projections allow the district and the county office to assess revenues and expenditures in the current and subsequent two fiscal years to confirm that the district can meet its fiscal obligations. A district that is unable to meet its fiscal obligations in the current or subsequent two fiscal years has either a qualified or negative budget certification. A qualified budget certification indicates that the district is deficit spending and "may not" meet its fiscal obligations; a negative certification indicates that the district "will not" meet its fiscal obligations.

Lucerne Valley Unified requested that FCMAT prepare a MFYP after the governing board self-certified the 2011-12 second interim report as qualified with San Bernardino County Office of Education. The district meets its reserve levels for economic uncertainties in the current and subsequent two fiscal years but is deficit spending at an alarming rate. The district has experienced declining enrollment for the last five fiscal years, primarily caused by a surge in charter school enrollment. Combined with long-term debt obligations, state budget cuts and large state funding deficits, the district will require state intervention during the 2014-15 school year unless revenue enhancements or additional expenditure reductions are implemented. Large reserve balances in the general fund and cash available in other funds provide sufficient cash reserves to support the district's financial obligations at present.

FCMAT utilized the Budget Explorer v.5.0 software to create the MYFP and cash flow analysis based on the district's 2011-12 second interim financial report. The team analyzed and compared salary and benefit projections to actual position control and payroll records; prepared projections for enrollment and average daily attendance based on historical trends; evaluated options for lapsation or unification; explored opportunities to convert to an all-district charter school; and examined revenue enhancements and expenditure reductions.

The latest information for the 2012-13 state budget included in the governor's May revision is incorporated in the MYFP. The governor's budget is predicated on the passage of his tax initiative at the November 2012 election; however, FCMAT prepared the MYFP based on a conservative approach and assumed that the tax initiative will fail. This means the district will experience an automatic funding decrease of $441 per average daily attendance (ADA). The MYFP is built on this and many other assumptions that are included in the multiyear financial projections section of this report.

The state continues to reduce the district's revenue limit funding. The latest estimates include a deficit of 22.272%, the largest in California school finance history. This means that for every dollar the district is entitled to from the state, the district will only realize 78 cents in actual funding.

Declining enrollment, increasing charter school enrollment, excessive long-term debt burden, and an ongoing cut to funding with a large deficit applied have combined to pose a significant threat to the district's fiscal stability.

Findings and Recommendations

Multiyear Financial Projections

Assembly Bill 1200 (Statutes of 1991, Chapter 1213) and AB 2756 (Statutes of 2004) are a part of the adoption budget and interim reporting process for school districts. AB 1200 was signed into law in 1991, and AB 2756 was signed into law in June 2004 and made substantive changes to the financial accountability and oversight used to monitor the fiscal position of school districts and county offices. Among other things, AB 2756 strengthened the roles of the superintendent of public instruction (SPI) and county offices of education and their ability to intervene during fiscal crises, including requesting assistance from FCMAT.

Education Code Section 42127 (EC) and EC 42130 establish the requirements for the governing board of each district and of the county superintendent for the budget adoption and interim reporting periods. An integral component of EC 42127 is the governing board's ability to demonstrate that the budget allows the district to meet its financial obligations in the current and subsequent two fiscal years.

Forecasting financial data is based on certain economic assumptions and criteria at a point in time. Therefore, the financial projection model should be evaluated as a forecast of anticipated revenues and expenditures based on assumptions for a particular time period within prescribed standards and criteria. The budget model should perform the following:

- Communicate the educational goals of the school district.
- Identify resources to meet those goals.
- Limit or control spending.

A multiyear financial projection model should provide the governing board and management with guidance by evaluating the long-term effects of financial decisions and be able to adjust for trends such as growing or declining enrollment, variables that cannot be controlled by the district.

The last four budget cycles have been the most challenging in the history of California school finance. Compared to all other sectors of the state budget, K-12 education has taken an inequitable share of budget cuts, forcing districts to update multiyear assumptions and projections several times during the fiscal year as assumptions continuously change at the state level. As the state continues to struggle to balance its budget, school districts must plan accordingly. Complicating the situation is a state budget predicated on voter support of tax initiatives that will be voted on four months into the 2012-13 fiscal year. Failure of the governor's November 2012 tax initiative is projected to affect school districts by $441 per ADA on the average. For Lucerne Valley Unified, this equates to more than $350,000 per fiscal year. This projection is based on current information available and may change following the passage of the budget and/or other factors that affect the state's budget.

Multiyear assumptions can fluctuate in a time of fiscal uncertainty, particularly in the subsequent fiscal years as projected revenue information from the state changes. Multiyear projections are a valuable tool for decision-making, especially with multiyear commitments. The district should continue to regularly update its MYFPs and reassess the ramifications of state-imposed budget adjustments, including the impacts of cash deferrals.

To help protect local educational agencies from economic uncertainties, the state requires school districts with ADAs of 301 to 1,000 to maintain reserves of not less than 4%. The district's current reserve requirement is 4% for fiscal year 2011-12 and two subsequent fiscal years.

AB 1200 Oversight

If at any time during the fiscal year a district is unable to meet its financial obligations for the current or two subsequent fiscal years, or has a qualified or negative budget certification, the county superintendent of schools is required to notify the district's governing board and the state superintendent of public instruction (SPI).

The county office is required to follow Education Code Section 42127.6 while assisting a school district in this situation. Assistance may include assigning a fiscal expert or fiscal advisor, conducting a study of the district's financial and budgetary conditions, and requiring the district to disclose all contracts and multiyear commitments. The MYFP is intended to help the county and district formulate a fiscal recovery plan to regain fiscal solvency and restore the required fund reserve levels.

The district governing board has issued a qualified certification to the 2011-12 second interim financial report. According to EC 42131(e), a district with a qualified or negative certification for the second report under EC 42130 is required to provide financial statement projections of its fund and cash balances through June 30 for the period ending April 30 to the county superintendent of schools, the controller and the superintendent of public instruction. In addition, EC Sections 42127.6 (a) – 42127.6 (a) (1) (E) require the district to comply with requests from the county office and conditions, including the assignment of a fiscal advisor. The San Bernardino County Superintendent of Schools has assigned a fiscal advisor to the district.

As the district works with the county office, the business office will need to ensure that multiyear financial and cash flow projections are kept up to date and that the information they contain is accurate and based on the most current economic assumptions. This is particularly important because the state's projected budget for 2012-13 is subject to a significant mid-year adjustments if the governor's tax initiative fails. The district should be prepared to make mid-year budget adjustments in conjunction with those required to balance the existing budget in light of the state's fiscal crisis and the November election since both will play a critical role in the multiyear financial projection for fiscal year 2012-13 and the subsequent two fiscal years.

FCMAT has updated the multiyear projections with the most current budget assumptions including the governor's May revision. The MYFP developed for this report indicates that the district will be able to maintain its reserve requirement in the 2013-14 fiscal year; however, the district is deficit spending at a high rate. The development of a strategic long-term financial plan is crucial for Lucerne Valley Unified. The district is heavily encumbered with long-term debt and a rapid decline in enrollment. These two issues must be addressed immediately to avoid fiscal insolvency.

The district faces substantial fiscal challenges that will require the governing board to make and implement difficult decisions immediately to maintain local governance and avoid state receivership.

The assumptions and projection rules included in FCMAT's MYFP are listed in the table below.

Assumptions/Projection Rules	2011-12	2012-13	2013-14
Statutory Cost of Living	2.24%	3.24%	2.50%
Revenue Limit Deficit	-20.602%	-22.272%	-22.272%
Trigger Reductions if Tax Initative Fails	$0	-$441/ADA	-$441/ADA
Transportation Funding	At Current Levels	At Current Levels	At Current Levels
Special Education Cost of Living	0.00%	0.00%	2.50%
State Categorical Funding	0.00%	0.00%	2.50%
Federal Funding	0.00%	0.00%	0.00%
Consumer Price Index	2.50%	2.30%	2.40%
Lottery - Unrestricted	$117.250	$118.000	$118.000
Lottery - Restricted	$23.25	$23.25	$23.25
Interest Rate	2.00%	2.30%	2.70%
Certificated Step & Column	Frozen	Frozen	Actual
Classified Step	Frozen	Frozen	Actual
Health & Welfare	Capped	Capped	Capped

Revenue Sources

The district has four categories of revenue sources that are classified as either unrestricted or restricted:

Revenue Limit Sources: The district earns most of its revenue from general purpose funding from the state called the revenue limit. Each year, the base revenue limit is multiplied by the district's ADA and adjusted for the cost of living. Other adjustments are either added to or subtracted from the base revenue limit, including local property taxes; therefore, the total revenue limit is a combination of state apportionments and local property taxes. In the last several budget cycles, adjustments have included revenue limit deficits and one-time reductions to funding. Deficits occur when the state is unable to fully fund the state appropriation.

Districts with declining enrollment are funded on the higher of the current or prior year's ADA, giving them a limited amount of time to make necessary budget adjustments.

Federal Sources: Another source of income for the district is a combination of federal grants and entitlements. Lucerne Valley Unified receives funding for Title I, No Child Left Behind; vocational and applied technology. A portion of its special education funding and pass-through grants are from the one-time funds provided by the American Recovery and Reinvestment Act as well as Federal Education Jobs Fund.

Other State Revenue: Another large portion of funds are derived from other state entitlements and grants including: Lottery; K-3 Class Size Reduction; community day schools; home-to-school transportation; special education transportation and a combination of categorical block grants programs.

Local Revenue: The district rents classroom space for county-office-operated programs; collects interest and earns oversight fees for Sky Mountain Charter School.

Unrestricted Revenue Adjustments

The following table highlights the differences in projected unrestricted revenues between the district's second interim budget and FCMAT's calculations:

Second Interim 2011-12	District 2nd Interim	FCMAT Estimates	Difference Inc/ (Dec)
Unrestricted Revenues			
Revenue Limit Sources	$4,732,617	$4,694,046	$(38,571)
Federal Revenues	-	-	-
Other State Revenues	1,067,477	1,065,351	(2,126)
Other Local Revenues	389,129	389,129	-
Total Unrestricted Revenues	$6,189,223	$6,148,526	$(40,697)

Revenue Limit Sources: The FCMAT adjustments include actual ADA to be funded based on the official attendance report, which was estimated by the district for the second interim report.

Federal Revenues: The absence of unrestricted federal revenues in the current year or prior fiscal year indicates that the district does not participate in the Medi-Cal Administrative Activities (MAA) program. MAA is a reimbursement program managed by the California Department of Health Care Services that allows districts to be reimbursed for related administrative services for eligible children and their families. These are services that the district already provides. Normally, districts do not budget for the reimbursement because these are not guaranteed funds; however, the district should apply for these funds as the amounts can be a substantial source of unrestricted funding. Once the district applies to be a Medi-Cal provider, claims for reimbursement can be processed. The provider applications are available at the following Web address: http://www.dhcs.ca.gov/provgovpart/Pages/LEAProviderEnrollment.aspx.

State Revenues: The small change in state revenues is the net effect of a $4,555 reduction in the budget for the categorical flex revenues and a $2,429 increase in lottery funds to align with School Services of California's dartboard amount of $117.25 per ADA.

Restricted Revenue Adjustments

The following table highlights the differences in projected restricted revenues between the district's second interim budget and FCMAT's calculations:

Second Interim 2011-12	District 2nd Interim	FCMAT Estimates	Difference Increase/ (Decrease)
Restricted Revenues			
Revenue Limit Sources	$137,532	$177,769	$40,237
Federal Revenues	790,333	947,624	157,291
Other State Revenues	876,542	884,159	7,617
Other Local Revenues	882,418	922,964	40,546
Total Restricted Revenues	**$2,686,825**	**$2,932,516**	**$245,691**

Revenue Limit Sources: The increase in revenue limit sources is because of an adjustment in the special education revenue limit transfer based on the official attendance report, which was estimated by the district for the second interim financial report.

Federal Revenues: Most of the increase in federal revenues was the result of program carryovers from the prior fiscal year. According to the district, carryover in Title I, Part A, Basic Grants (Title I) and Title II, Part A, Teacher Quality (Title II) was not budgeted because of the uncertainty of spending the allocation in the current year according to the business office. The district should budget all carryover and deferred revenues from the prior fiscal year to the new fiscal year.

The district had 49.5% of the original grant unused at the end of 2010-11 in Title I. Federal guidelines restrict carryover to 15% unless the district applies for a waiver; however, waiver applications can only be granted once every three years. The district has applied for a waiver for 2010-11. If approved, the waiver will allow the district to retain the entire carryover amount instead of returning funds in excess of the 15% limitation, which total $79,640. Should the wavier be approved, the district must have a plan to spend 85% of the current year allocation and the carryover or forfeit unspent funds.

The carryover in Title II, Part A was only 6.4% of the entitlement because the district took advantage of the federal transferability options available for No Child Left Behind resources and moved a large portion of the unused revenue to Title II, Part D, Enhancing Education Through Technology.

Best practice dictates that restricted revenue sources should be spent before unrestricted funds for expenditures that could be legitimately paid for with restricted funds. Whenever possible, restricted funding should be spent in the year it is earned. It is expected that current year awards will be spent on the current year students.

The team also increased the amount of carryover for Federal Education Jobs Funding (stimulus funds) by $42,155 to reflect the total amount of the 2010-11 carryover rather than just the amount the district intends to spend by the end of this fiscal year. The unspent portion from 2011-12 will carry over into 2012-13, but must be spent by September 30, 2012.

State Revenues: FCMAT increased Lottery funding by $7,617, utilizing the SSC dartboard estimates.

Local Revenues: The Desert/Mountain Special Education Local Plan Area (SELPA) issued final allocations for AB 602 special education funding based on the final attendance reports. The projected increase for the district is $42,705.

After adjusting revenue sources in the base year, FCMAT made the necessary adjustments to the two subsequent years taking into account one-time revenue, enrollment projections and projected changes to revenue. The following chart compares FCMAT's base year combined unrestricted and restricted revenues to the two subsequent years:

Combined Revenues	Base Year 2011 - 12	Year 1 2012 - 13	Year 2 2013 - 14
Revenues			
Revenue Limit Sources	$4,871,815	$4,237,773	$4,204,584
Federal Revenues	947,624	647,555	647,555
Other State Revenues	1,949,510	1,942,405	1,978,495
Other Local Revenues	1,312,093	1,234,712	1,235,043
Total Revenues	**$9,081,042**	**$8,062,445**	**$8,065,677**

The depletion of federal stimulus funding, one-time grants, declining enrollment and a projected $441 per ADA decrease in base revenue limit funding if the governor's tax initiative fails, have a significant impact on revenues for 2012-13 and beyond. The balance of one-time federal stimulus funds totaling $175,000 will be exhausted by September 2012. In addition, one-time revenues for school bus retrofit grants end June 30, 2012.

Included in the $441 per ADA decrease is an across-the-board cut to all districts that will allow the state to continue providing home-to-school and special education transportation funding at current-year levels. Current district transportation funding is $268,103, less the revenue limit reduction attributable to transportation funding of approximately $68,000 resulting in a net savings of $200,000 in transportation funding.

Many positive and negative variables affect the multiyear projection. Including all variables in the multiyear financial projection will be important because each variable has a financial consequence, and underscores the importance of multiyear projections.

Expenditure Categories

The general fund is used to account for the district's day-to-day operations. Salaries and benefits are the largest expenditure category; however, the district's ratio of unrestricted salaries and benefits to total unrestricted expenditures is not within the state's established standards. FCMAT has determined that large debt obligations and unusually large portions of the unrestricted general fund for services and other operating expenses cause ratios in other budget categories to be less than those included in the state's guidelines.

Other major expenditures categories include books, supplies, insurance, contracted services, utilities, travel, conference and capital outlay.

Salaries and Benefits: The negotiated agreement with management and the employee bargaining units is in effect through June 30, 2013. As a cost savings measure, the district negotiated six to eight furlough days depending on the work year; a salary schedule reduction, and a freeze in step/column movements. A summary of collective bargaining compromises includes:

- Certificated staff concessions through 2012-13 include a salary rollback of 4%; eight furlough days; no step-and-column movement; and a health-and-welfare cap of $9,500.
- Classified staff concessions through 2012-13 include a salary rollback of 4%; eight furlough days for 12-month employees and six furlough days for 10- and 11-month employees; no step advances; and a health-and-welfare cap of $10,500.
- Management staff concessions through 2012-13 include a salary rollback of 3.5%; 12 furlough days; step-and-column advances will continue for all positions except the superintendent; and a health-and-welfare cap of $9,500 for certificated staff members and $10,500 for the classified staff.

FCMAT projected the cost to restore the salary schedules to the 2007-08 rates along with restoration of step/column movements for 2013-14 per the negotiated agreement. The breakdown is as follows:

Cost to restore salary and benefits	$343,137
Cost to restore one year step/column movement	132,261
Cost to restore an additional step/column movement	122,046
Total	**$597,445**

The district is attempting to negotiate an extension of the agreement beyond June 30, 2013 to produce savings to offset additional budget shortfalls.

It is critical to use position control to manage salary and benefit costs in a time of fiscal uncertainty. An effective position control system populates the budget development system at major reporting intervals throughout the fiscal year and is periodically compared with actual payroll records.

The district utilizes the financial system provided by the county office, which is updating various modules including EPICS, the position control system. The district uses the old system, Magic, to make necessary benefit adjustments until this process is complete. Once adjustments for benefit rates and health insurance limits are updated, the data is transferred back to the county office system.

Anytime data is moved from one operating system to another, there is a risk associated with the validity of the data imports and exports. During this transition, the district should implement additional steps to ensure the data export is correct.

To test the accuracy of the salary and benefit amounts budgeted in the general fund; FCMAT compared the prior year actuals with current year budget, position control, and actual salaries/benefits to date. The comparison of position control and the budget found discrepancies between the two systems. Specifically, the second interim budget for unrestricted salaries and benefits was overstated by $120,168. The district should ensure that the data in position control is validated in the budget and compared with actual payroll records.

Other adjustments include 1.8295 reductions in teacher full-time equivalent (FTE) in 2012-13 and beyond based on district information. Further reductions will be required to align class sizes with the projected decline in enrollment in the 2013-14 fiscal year.

As previously mentioned, the ratio of unrestricted salaries and benefits is less than the state's established ratio to total unrestricted general fund expenditures. The state standard takes the district's historical average ratio, plus or minus the greater of 3% or the district's reserve percentage for economic uncertainties. The district's historical average ratio is 83.57% and its economic reserve percentage is 4%. The projected year end totals for 2012-13 is projected to be 83.16%.

Although the district's ratio is close to meeting the standard, the unrestricted expenditures do not include the $408,000 debt service payment for the certificates of participation in the current fiscal year; otherwise this ratio would be 77.01%. This payment is scheduled to be paid from the debt service fund in the current fiscal year, but will be charged to the unrestricted general fund in future years.

Books and Supplies: In conjunction with budget cuts, the state offered flexibility options that realigned the funding for several restricted categorical grants and entitlements as unrestricted and available for any educational purpose in 2009-10 through 2014-15. A large portion of these funds supported the purchase of instructional materials and textbooks. The flexibility sweep provisions allowed the district to offset additional cuts to the general fund but the result reduced services to students under the original instructional programs.

Services and Other Operating: An unusually large portion of the district's unrestricted general fund operating budget is dedicated to support services and other operating expenditures. Included in this category are travel, conferences, dues/memberships, insurance, utilities, rentals/leases/repairs, contracted services and interagency fees. The district should review these expenditures categories for possible savings.

Capital Outlay: This expenditure category accounts for large capital expenditures. Except for expenditures to retrofit school buses from grant sources, the district does not invest in capital outlay.

Debt Service: The district has entered into long-term debt agreements for a modular building, an energy management system, COPs and retiree benefit agreements. The following table illustrates total outstanding debt as of June 30, 2011 according to the audited financial statements and the payments due for fiscal year 2011-12:

Debt Category	Outstanding as of June 30, 2011	Payments Due 2011-12
Certificates of Participation	$6,655,000	$408,708
Capital Leases-Modular Building and Energy System	$983,960	$298,332
Other Retirement Benefits	$291,742	$25,579
Total	$7,930,702	$732,619

The COPs payment is supported by the debt service fund for 2011-12; however, this payment will require general fund support in subsequent fiscal years. Debt service is discussed at length in a separate section of this report.

Encroachments

When restricted programs require support from the unrestricted general fund, this is referred to as encroachment. Traditionally, programs that are not fully funded by either state or federal sources include community day school , special education and transportation. Other programs that encroach can be reduced or in some cases eliminated altogether.

Programs that encroach on the district's unrestricted general fund are listed in the table below. The Quality Education Investment Act (QEIA) is projected to encroach on the unrestricted general fund beginning with the 2013-14 fiscal year unless the district receives additional funding to support the program. This program was funded for seven years ending June 30, 2014. The district should evaluate continuing the QEIA program after 2013-14 without additional state funding. The following table shows all the projected encroachments for restricted programs:

Encroachments	Resource Code	Base Year 2011-12	Year 1 2012-13	Year 2 2013-14
Restricted Resources				
Community Day School	2430	$126,323	$128,263	$138,434
Special Ed: IDEA Basic Local Assistance Entitlement, Part B, Sec 611 (formerly PL 94-142)	3310	3,230	8,187	18,112
Special Education	6500	114,446	116,050	156,224
Agricultural Vocational Incentive Grants	7010	11,393	10,458	10,120
Transportation: Home to School	7230	168,861	176,704	187,288
Transportation: Special Education (Severely Disabled/ Orthopedically Impaired)	7240	9,377	12,858	15,428
Quality Education Investment Act (QEIA)	7400			76,650
Total Restricted				
Balance		**$433,630**	**$452,520**	**$602,256**

FCMAT projected revenue and expenditures based on source documents, including the California Department of Education website for revenue entitlements, enrollment reports, audited financial statements, budget assumptions, budget files, financial system reports, unaudited actuals, detailed payroll transactions, position control records, special education SELPA AB602 funding documents, nonpublic school placements, and many other financial records and third-party documentation. The team utilized all the pertinent records and documents to complete this multiyear analysis based on the district's 2011-12 second interim financial report.

Salary and benefit projections are based on actual payroll transactions through February, 2012 and compared with the district's budget and position control records; other expenditures were compared with year-to-date records and trends; long-term debt has been verified against third-party documentation.

The tables below represent FCMAT's multiyear projections. The first two tables represent FCMAT's unrestricted and restricted general fund multiyear projections.

Unrestricted Summary	Category	Object Code	Fiscal Year 2011 - 12	Fiscal Year 2012 - 13	Fiscal Year 2013 - 14
Revenues					
	Revenue Limit Sources	8010 - 8099	$4,694,046	$4,059,975	$4,025,190
	Federal Revenues	8100 - 8299	$0	$0	$0
	Other State Revenues	8300 - 8599	$1,065,351	$1,059,051	$1,074,639
	Other Local Revenues	8600 - 8799	$389,129	$389,405	$389,736
Total Revenues			**$6,148,526**	**$5,508,431**	**$5,489,565**
Expenditures					
	Certificated Salaries	1000 - 1999	$2,430,147	$2,355,075	$2,630,807
	Classified Salaries	2000 - 2999	$797,627	$808,143	$892,173
	Employee Benefits	3000 - 3999	$1,021,059	$986,602	$1,040,030
	Books and Supplies	4000 - 4999	$263,139	$249,399	$229,424
	Services and Other Operating	5000 - 5999	$799,381	$793,745	$780,231
	Capital Outlay	6000 - 6900	$9,100	$9,100	$9,100
	Other Outgo	7000 - 7299	$0	$0	$0
	Direct Support/Indirect Cost	7300 - 7399	($89,237)	($84,950)	($87,642)
	Debt Service	7430 - 7439	$336,534	$654,386	$465,491
Total Expenditures			**$5,567,750**	**$5,771,500**	**$5,959,614**
Excess (Deficiency) of Revenues Over Expenditures			**$580,776**	**($263,069)**	**($470,049)**
Other Financing Sources\Uses					
	Interfund Transfers In	8900 - 8929	$0	$0	$0
	Interfund Transfers Out	7600 - 7629	$0	$0	$0
	All Other Financing Sources	8930 - 8979	$0	$0	$0
	All Other Financing Uses	7630 - 7699	$0	$0	$0
	Contributions	8980 - 8999	($433,630)	($452,520)	($602,256)
Total Other Financing Sources\Uses			**($433,630)**	**($452,520)**	**($602,256)**
Net Increase (Decrease) in Fund Balance			**$147,146**	**($715,589)**	**($1,072,305)**

Fund Balance					
	Beginning Fund Balance	9791	$2,965,582	$3,112,728	$2,397,139
	Adjusted Beginning Fund Balance		$2,965,582	$3,112,728	$2,397,139
	Ending Fund Balance		**$3,112,728**	**$2,397,139**	**$1,324,834**
Components of Ending Fund Balance					
	Reserved Balances	9700	$0	$0	$0
	Revolving Cash	9711	$19,000	$19,000	$19,000
	Legally Restricted Balance	9740 - 9759	$0	$0	$0
	Economic Uncertainties Percentage		$0	$0	$0
	Designated for the Unrealized Gains of Investments and Cash in County Treasury	9775	$0	$0	$0
	Other Designated	9780	$560,000	$560,000	$560,000
	Reserve for Economic Uncertainties	9789	$360,099	$356,175	$366,938
	Undesignated/Unappropriated	9790	$2,173,629	$1,461,964	$378,896
	Negative Shortfall	9790	$0	$0	$0

Restricted Summary	**Category**	**Object Code**	**Fiscal Year 2011 - 12**	**Fiscal Year 2012 - 13**	**Fiscal Year 2013 - 14**
Revenues					
	Revenue Limit Sources	8010 - 8099	$177,769	$177,798	$179,393
	Federal Revenues	8100 - 8299	$947,624	$647,555	$647,555
	Other State Revenues	8300 - 8599	$884,159	$883,355	$903,858
	Other Local Revenues	8600 - 8799	$922,964	$845,307	$845,307
Total Revenues			**$2,932,516**	**$2,554,015**	**$2,576,113**
Expenditures					
	Certificated Salaries	1000 - 1999	$689,389	$657,870	$708,001
	Classified Salaries	2000 - 2999	$505,886	$493,880	$517,182
	Employee Benefits	3000 - 3999	$310,042	$299,580	$310,905
	Books and Supplies	4000 - 4999	$384,645	$239,158	$225,565
	Services and Other Operating	5000 - 5999	$690,038	$671,937	$679,047
	Capital Outlay	6000 - 6900	$80,000	$0	$0
	Other Outgo	7000 - 7299	$685,471	$685,471	$685,471
	Direct Support/Indirect Cost	7300 - 7399	$89,260	$84,973	$87,665
	Debt Service	7430 - 7439	$0	$0	$0
Total Expenditures			**$3,434,731**	**$3,132,869**	**$3,213,836**

Excess (Deficiency) of Revenues Over Expenditures			($502,215)	($578,854)	($637,723)
Other Financing Sources\Uses					
	Interfund Transfers In	8900 - 8929	$0	$0	$0
	Interfund Transfers Out	7600 - 7629	$0	$0	$0
	All Other Financing Sources	8930 - 8979	$0	$0	$0
	All Other Financing Uses	7630 - 7699	$0	$0	$0
	Contributions	8980 - 8999	$433,630	$452,520	$602,256
Total Other Financing Sources\Uses			**$433,630**	**$452,520**	**$602,256**
Net Increase (Decrease) in Fund Balance			($68,584)	($126,334)	($35,468)
Fund Balance					
	Beginning Fund Balance	9791	$230,386	$161,802	$35,468
	Adjusted Beginning Fund Balance		$230,386	$161,802	$35,468
	Ending Fund Balance		**$161,802**	**$35,468**	**($0)**
Components of Ending Fund Balance					
	Reserved Balances	9700	$0	$0	$0
	Legally Restricted Balance	9740 - 9759	$161,802	$35,468	$0
	Designated for the Unrealized Gains of Investments and Cash in County Treasury	9775	$0	$0	$0
	Other Designated	9780	$0	$0	$0
	Reserve for Economic Uncertainties	9789	$0	$0	$0
	Undesignated/Unappropriated	9790	$0	$0	$0
	Negative Shortfall	9790	$0	$0	$0

The following table includes all unrestricted and restricted general fund revenues and expenditures.

Unrestricted & Restricted Summary	Category	Object Code	Fiscal Year 2011 - 12	Fiscal Year 2012 - 13	Fiscal Year 2013 - 14
Revenues					
	Revenue Limit Sources	8010 - 8099	$4,871,815	$4,237,773	$4,204,584
	Federal Revenues	8100 - 8299	$947,624	$647,555	$647,555
	Other State Revenues	8300 - 8599	$1,949,510	$1,942,405	$1,978,495
	Other Local Revenues	8600 - 8799	$1,312,093	$1,234,712	$1,235,043
Total Revenues			**$9,081,042**	**$8,062,445**	**$8,065,677**
Expenditures					
	Certificated Salaries	1000 - 1999	$3,119,536	$3,012,945	$3,338,808
	Classified Salaries	2000 - 2999	$1,303,513	$1,302,023	$1,409,355
	Employee Benefits	3000 - 3999	$1,331,101	$1,286,182	$1,350,935

	Books and Supplies	4000 - 4999	$647,784	$488,556	$454,989
	Services and Other Operating	5000 - 5999	$1,489,419	$1,465,682	$1,459,279
	Capital Outlay	6000 - 6900	$89,100	$9,100	$9,100
	Other Outgo	7000 - 7299	$685,471	$685,471	$685,471
	Direct Support/Indirect Cost	7300 - 7399	$23	$23	$23
	Debt Service	7430 - 7439	$336,534	$654,386	$465,491
Total Expenditures			**$9,002,481**	**$8,904,368**	**$9,173,450**
Excess (Deficiency) of Revenues Over Expenditures			**$78,561**	**($841,923)**	**($1,107,773)**
Other Financing Sources\Uses					
	Interfund Transfers In	8900 - 8929	$0	$0	$0
	Interfund Transfers Out	7600 - 7629	$0	$0	$0
	All Other Financing Sources	8930 - 8979	$0	$0	$0
	All Other Financing Uses	7630 - 7699	$0	$0	$0
	Contributions	8980 - 8999	$0	$0	$0
Total Other Financing Sources\Uses			**$0**	**$0**	$0
Net Increase (Decrease) in Fund Balance			**$78,561**	**($841,923)**	**($1,107,773)**
Fund Balance					
	Beginning Fund Balance	9791	$3,195,968	$3,274,529	$2,432,607
	Audit Adjustments	9793	$0	$0	$0
	Other Restatements	9795	$0	$0	$0
	Adjusted Beginning Fund Balance		$3,195,968	$3,274,529	$2,432,607
	Ending Fund Balance		**$3,274,529**	**$2,432,607**	**$1,324,834**
Components of Ending Fund Balance					
	Reserved Balances	9700	$0	$0	$0
	Revolving Cash	9711	$19,000	$19,000	$19,000
	Legally Restricted Balance	9740 - 9759	$161,802	$35,467	$0
	Economic Uncertainties Percentage		$0	$0	$0
	Other Designated	9780	$560,000	$560,000	$560,000
	Reserve for Economic Uncertainties	9789	$360,099	$356,175	$366,938
	Undesignated/ Unappropriated	9790	$2,173,628	$1,461,964	$378,896
	Negative Shortfall	9790	$0	$0	$0

The summary of unrestricted and restricted resources combined shows how rapidly the fund balance is diminishing over the three-year period. Without any further interventions or changes in the current negotiated collective bargaining agreements, the district will deficit spend by $1,107,773 in the 2013-14 fiscal year, and this amount will grow exponentially. The fund balance is still positive, and the district maintains the required 4% fund balance reserve levels, but this will not be sustainable beyond 2013-14 without revenue enhancements or expenditure reductions. The following analysis provides a summary of the data in the above table.

Unrestricted and Restricted - Multiyear

Fiscal Year	2011-12	2012-13	2013-14
Revenues	$9,081,042	$8,062,445	$8,065,677
Expenditures	$9,002,481	$8,904,368	$9,173,450
Excess (Deficiency) of Revenues Over Expenditures	$78,561	($841,923)	($1,107,773)
Ending Fund Balance	$3,274,529	$2,432,606	$1,324,834

Revenues: The change in revenues from 2011-12 to 2012-13 shows a loss in funding of more than $1 million primarily because of declining enrollment, loss of one-time revenues and the $441 per ADA decrease to the revenue limit. In the 2013-14 year, revenues are fairly unchanged because the enrollment loss is offset by a projected cost-of-living increase with no further revenue limit adjustments.

Expenditures: The district is projected to realize an overall decrease in expenditures from 2011-12 to 2012-13. As one-time dollars are depleted, the district plans to eliminate positions that were supported by these funds. Salaries and step-and-column movements are frozen through 2012-13. However in 2013-14, additions to the expenditures budget include the following:

The salary schedule for all bargaining units is fully restored with the 4% salary adjustment and restoration of furlough days.

Step-and-column movements are included for fiscal year 2013-14 along with one "catch up" year of step-and-column movements.

Beginning in 2012-13 and beyond, the COPs payment of more than $400,000 per year will be paid from the unrestricted general fund.

Excess (Deficiency) of Revenues Over Expenditures: Deficit spending occurs when current year expenditures are greater than current year revenues. The combined effect of revenue and expenditure adjustments described above illustrate that without additional revenues or more expenditure reductions, the district will deficit spend in fiscal years 2012-13 and beyond.

Ending Fund Balance: The ending fund balance is rapidly declining. Because it is anticipated that the district will require state intervention beginning in 2014-15, it should find solutions now to balance the budget and control deficit spending.

FCMAT's MYFP shows that the district is projected to have a positive fund balance in all three years and meet the required reserve levels, but will require state intervention beyond 2013-14 without revenue enhancements or expenditures reductions.

The team lacks sufficient information to prepare a cash flow statement as part of this report. However, FCMAT will prepare an updated cash flow projection that will enable the district to determine when it will need to consider cash borrowing options subsequent to the issuance of this report.

Recommendations

The district should:

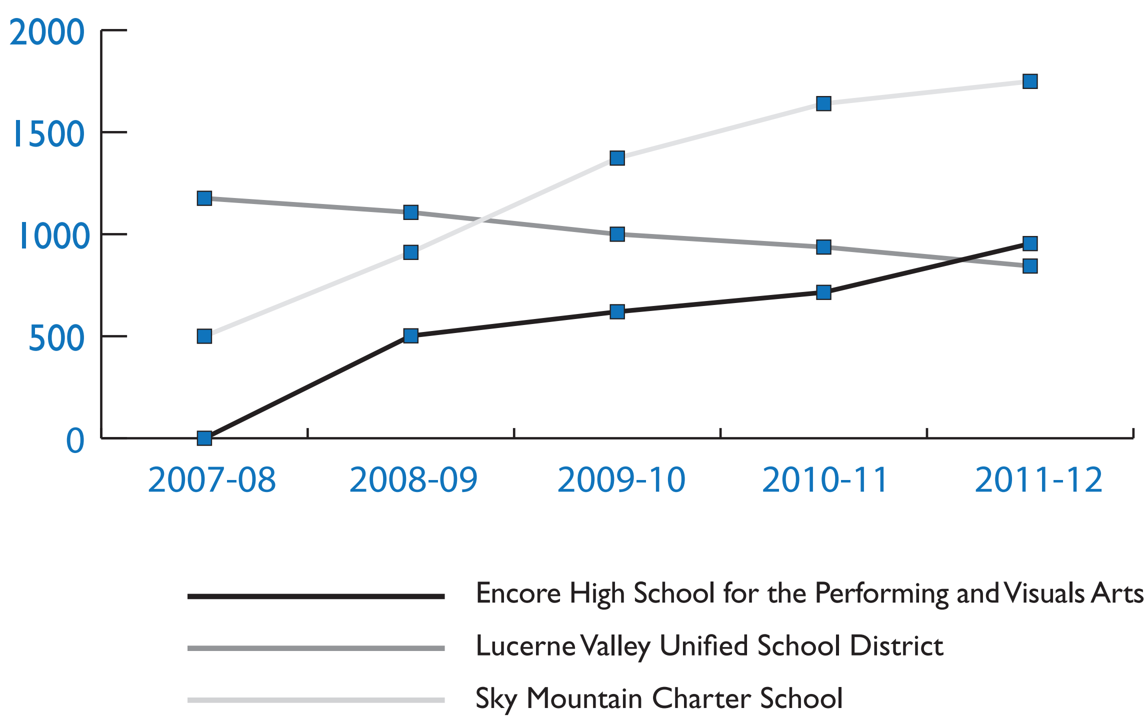
1. Explore the possibility of participating in the MAA program as a way to increase unrestricted federal revenues.
2. Regularly review restricted programs and work to ensure that restricted dollars are used in an appropriate and timely manner.
3. Budget all carryover and deferred revenues from the prior fiscal year to the new fiscal year.
4. Adhere to spending deadlines on categorical programs and limits on the annual carryover amounts.
5. Implement additional steps to ensure the data export between its financial systems is correct.
6. Negotiate with the bargaining units for an extension of the current agreements beyond June 30, 2013 to produce savings to offset budget shortfalls.
7. Ensure that what is in position control is correctly posted in the budget and compared with actual payroll records.
8. Review all expenditure categories in other services for possible savings. The budget for this section is unusually high, especially in the area of contract services.
9. Evaluate whether to continue the QEIA program after 2013-14 without additional state funding.

Enrollment

The district has 844 students, but has declined by 332 students, or 28.23%, since the 2007-08 fiscal year. The historical trend over the last two fiscal years shows an average loss of 8% per year.

During 2008-09, Encore High for the Performing & Visual Arts (Encore) charter school located in Hesperia opened and has actively recruited Lucerne Valley Unified students. In the last four years, the charter school has increased from 502 to 954 in student enrollment. In 2007-08, the district authorized Sky Mountain Charter School, a nonclassroom-based charter school that has tripled in student enrollment. Nonclassroom-based charter schools can enroll students from contiguous counties as long as more than half the students are from the county in which the charter is authorized. Therefore, Sky Mountain enrolls students from six contiguous counties including Kern, Inyo, Riverside, Orange, Los Angeles and San Bernardino. District administration indicated that none of the school's students are from within the Lucerne Valley Unified boundaries.

The line graph and table below illustrate student enrollment from 2007-08 through the current fiscal year comparing Lucerne Valley Unified with Encore and Sky Mountain charter schools.



School Year	2007-08	2008-09	2009-10	2010-11	2011-12
Sky Mountain Charter School	500	911	1,373	1,640	1,749
Encore High for the Performing and Visual Arts	0	502	620	715	954
Lucerne Valley Unified School District	1,176	1,107	1,000	927	844

The district has declined by 332 students from 2007-08 through 2011-12, which equates to a cumulative net loss of $4.542 million in revenue limit funding as demonstrated in the table below:

Fiscal Year	Cumulative Totals	2007-08	2008-09	2009-10	2010-11	2011-12
Enrollment		1,176	1,107	1,000	927	844
Student Decline	**(332)**		(69)	(107)	(73)	(83)
Deficited Revenue Limit			$5,986.55	$6,470.61	$5,531.61	$5,518.65
Historically ADA to Enrollment Factor			0.9216	0.9575	0.8206	0.8025
Net Funding			$5,517.20	$6,195.61	$4,539.24	$4,428.72
Loss in On-Going Funding 2008-09	(1,522,747.85)		$(380,686.96)	$(380,686.96)	$(380,686.96)	$(380,686.96)
Loss in On-Going Funding 2009-10	$(1,988,791.33)			$(662,930.44)	$(662,930.44)	$ (662,930.44)
Loss in On-Going Funding 2010-11	$ (662,728.58)		$		$(331,364.29)	$(331,364.29)
Loss in On-Going Funding 2011-12	$(367,583.35)		$	$		$(367,583.35)
Cumulative Loss in Funding 2008-09 through 2011-12	**($4,541,851.11)**		$(380,686.96)	$(1,043,617.41)	$(1,374,981.70)	$(1,742,565.05)

While the district enrollment has declined, both charter schools have grown substantially over this period of time, and FCMAT projects that the district enrollment will continue to decrease. Although the district anticipates a decline of 6.43% in ADA for 2012-13 and 7.97% for 2013-14, FCMAT projects an 8% annual decline based on the historical average over the last two fiscal years.

Efforts by residents and state/local officials have prevented or hindered infrastructure projects involving solar power, wind turbine plants, and water drilling that could increase the number of jobs and students in the community. Increasing the student population will likely not solve the district's declining enrollment issue although it could reduce the level of decline. The district should determine the reasons families leave the district and enroll their students in neighboring charter schools. The district should also consider options including an in-district charter school or a magnet school.

Recommendations

The district should:

1. Determine the reasons families leave the district and enroll their students in neighboring charter schools.

2. Consider several options to increase enrollment including an in-district charter school or a magnet school.

Revenue Enhancements

FCMAT has identified the following potential areas of revenue enhancement:

Enrollment and Attendance: Most funding received by the district is generated from ADA. There are various methods to enhance student attendance, including incentives as well as a system to notify parents immediately when students are absent from school. Timely parent notification can increase daily attendance and funding because the district can be funded for students that arrive late.

District administration should develop programs to attract local students that attend charter schools. Alternative choices that promote specialized learning opportunities for students include an in-district magnet school, or in-district charter school with an emphasis on vocational programs or visual and performing arts.

Medi-Cal Administrative Activities: The school personnel routinely provide services for school-based health and outreach activities including referrals to other agencies. The Medi-Cal Administrative Activities (MAA) program allows school districts to submit claims and receive reimbursements for activities that support the administration of the federal Medicaid programs such as the following:

- Referrals for Medi-Cal eligibility determinations
- Providing health care information and referrals to other agencies
- Coordination of health services between agencies
- Monitoring health services

To claim reimbursement, school site personnel submit time studies that record reimbursable activities that were performed during the normal course of their duties. These time studies generate average time and cost data used as a basis to reimburse the district. The district is encouraged to seek county office assistance and recommendations for providers that offer MAA reimbursement claiming services and training.

Restricted Funding Sources: As previously mentioned, the district has substantial carryover balances in some restricted programs. When possible, the district should use restricted funds before unrestricted funds. The following table shows a selection of programs from the state categorical funding form commonly referred to as the "CAT" form. The CAT form is a schedule used at year-end to record carryover balances or deferred revenues in federal and state categorical programs. The following table shows the deferred revenue and entitlement carryover balances or unused grant awards (not including one-time federal stimulus funding from ARRA or Federal Education Jobs grant) as of June 30, 2011:

Resource	Program	Deferred Revenue/ Carryover From 2010-11	Carryover/Unused Grant Award From 2011-12	Increase
3010	Title I	$3,701	$114,240	$110,539
3550	Carl Perkins	$0	$2,984	$2,984
7090	EIA	$8,546	$39,417	$30,871
6010	ASES	$0	$4,448	$4,448
Total		**$12,247**	**$161,089**	**$148,842**

Indirect Costs: Costs in school districts are classified as either direct or indirect. Direct costs are those that are tangible and directly associated with a specific department, school or program. Indirect costs, sometimes referred to as overhead costs, are necessary general administrative costs not directly attributable to any particular program.

An indirect cost rate is charged to restricted programs to cover districtwide administrative services such as personnel, accounting, payroll processing, accounts payable, purchasing, centralized data processing, technology infrastructure and connectivity, utilities attributable to the general administrative offices, insurance, maintenance, audit and legal services.

The indirect cost rate is calculated according to the federally approved indirect cost plan administered by the California Department of Education (CDE) based on the district's prior year actual direct and indirect expenditures and provides a method for each program to pay for its fair share of general administrative services. Once CDE certifies the rate, it is multiplied by each restricted programs' allowable expenditures unless the program guidelines specifically require a lower rate or no rate. For example, Economic Impact Aid limits indirect costs to 3.0%.

FCMAT observed that the district does not charge the full indirect cost rate to all programs, including other funds such as the cafeteria fund. Indirect costs from these restricted programs offset the unrestricted general fund and are available for other uses. The district should ensure that indirect costs are applied to all programs at the allowable rate.

Facility Use Fees: The district does not charge for facility use that could generate unrestricted funding. The district should create a facility use fee schedule in accordance with the Civic Center Act and charge for the use of district facilities in accordance with Education Code Section 38130 - 38139.

Recommendations

The district should:

1. Develop a plan to increase enrollment and attendance with incentives and/or timely parental notification.
2. Develop programs to attract local students that attend charter schools by offering an in-district magnet school, or in-district charter school.
3. Seek county office assistance and recommendations for providers that offer MAA reimbursement claiming services and training.
4. Maximize restricted funding and ensure that restricted funds are utilized before unrestricted sources whenever possible to avoid excessive carryover balances.
5. Charge the full indirect cost rate to all programs that allow it, including the cafeteria fund.
6. Create a facility use fee schedule and charge for the use of district facilities.

Expenditure Reductions

Over the last four fiscal years, the district has made several reductions in staffing and other expenditures in an attempt to maintain a balanced budget.

Staffing: FCMAT did not conduct an organizational staffing analysis as part of the scope of work. However, based on an observation of the number of positions and the total number of students, the district should evaluate staffing ratios for teachers, classified personnel and management based on industry standards and comparisons of school agencies similar in size and structure. This evaluation should include the following:

Principal positions: The district has two full-time principals and one superintendent for 844 students. The district should evaluate eliminating one principal position because of declining enrollment and consolidate the superintendent/principal duties and responsibilities.

Classified Directors. The district has a director of maintenance and operations in addition to a vacant position for a director of transportation. The district should evaluate combining these two positions and eliminating the vacant position.

Power Management: Power management options for computers are designed to conserve electricity when a desktop computer in not in use. Desktop computers can be configured to automatically go into sleep mode or shut down completely after a specified period of time.

Other conservation measures include removing personal electronic appliances such as microwave ovens, coffee machines and personal refrigerators throughout the district.

Smart Controllers: Smart irrigation systems are designed to reduce water consumption through timing devices that automatically adjust watering times according to the weather. Some systems operate remotely using real-time weather data provided by a remote provider through the Internet, radio or telephone connection. Other systems have their own weather stations to adjust watering times and are highly accurate.

Recommendations

The district should:

1. Evaluate staffing ratios for teachers, classified personnel and management staffing levels based on industry standards and comparisons of school agencies similar in size and structure.
2. Ensure that desktop computers are configured to automatically go into sleep mode, or shut down completely after a specified period of time.
3. Remove all personal electronic appliances.
4. Evaluate the usage of smart irrigation systems to reduce water consumption.

Nonvoter-Approved Debt and Compensated Absences

Issuing long-term debt allows school districts to obtain funds to acquire or construct buildings and equipment and to spread the repayment over a period of years. It also allows districts to obtain buildings or equipment that might be impossible to purchase with existing resources. Complications can develop if a school district issues too much debt without a dedicated revenue source such as tax levies to service that debt. In such cases, annual debt service payments must be made from the district's unrestricted general fund at the expense of current operations.

Any long-term debt that the district must repay from the unrestricted general fund is considered "unfunded" because it requires the use of resources typically dedicated to the current costs of education, such as employees' salaries, administration and general operating supplies. Although most districts are able to fund some long-term debt (e.g., accrued vacation) from their general fund, districts should exercise caution in dedicating general fund revenues for debt service payments because this depletes funds available for current operations. Moreover, debt service payments are one of the line-item expenditures that cannot easily be eliminated from the general fund budget and therefore place an additional burden on the unrestricted general fund during times of fiscal austerity.

On June 7, 2007, at an emergency board meeting, the governing board approved borrowing as much as $10 million through COPs for the following projects:

- The construction of an early childhood education center.
- The relocation of the Pupil Services Division to two new modular buildings.
- The construction of a district office.
- The purchase of eight air-conditioned school buses.
- The construction of maintenance buildings.
- Improvements to the Future Farmers of America (FFA) program.
- The funding of three modular buildings for the high school.
- The funding of middle school and high school landscaping projects.
- The purchase of computers.
- The construction of a transportation facility on a new site.

Of the above projects, only the early childhood center, maintenance buildings, FFA improvements and the purchase of new buses were funded.

The board approved management's request for the COPs and perceived that the loan payments would be deferred for three years. The district's plan was to apply the annual oversight revenue from the two recently approved charter schools to the debt service payments and ask the community to approve a general obligation bond only if the anticipated revenue from both charters was less than expected.

On October 24, 2007 UBS Investment Bank made a presentation to the board regarding certificates of participation (COPs), listing the following as advantages and disadvantages:

Advantages	Disadvantages
No voter approval required	Debt service is paid from general fund revenues
No additional tax burden	Interest rates and cost of issuance are generally higher than general obligation bonds
Financing can be completed quickly	Leased property is encumbered
Can be used as a "bridge" prior to state funds or bond proceeds	

The list of disadvantages did not include the fact that debt service payments on a COP represent a fixed cost in a district's operating budget that cannot be reduced or eliminated without another revenue source. Without being defeased from the proceeds of a general obligation bond, these debt service payments will burden the unrestricted general fund until the COP reaches maturity in fiscal year 2039.

Debt Management Policy

It is standard practice in many state and local governments for the governing board to adopt a comprehensive debt management policy that creates guidelines for issuing and managing debt. The Government Finance Officers Association recommends that all forms of government adopt a comprehensive debt policy. This helps ensure that underwriters and financial advisers provide the district with adequate information to analyze future debt, enabling the district to make sound business decisions.

The district does not have a debt management policy, which provides guidelines for all forms of indebtedness including voter and nonvoter approved debt. Although the issuance of debt is an appropriate method for financing capital projects and improvements, careful evaluation is required to preserve the district's credit strength and financial flexibility. FCMAT has developed a list of conditions most commonly experienced by districts needing intervention, and one of the predictors is "Substantial Long-Term Debt Commitments – Certificates of Participation." A sample debt management policy is attached as Appendix A to this report.

As indicated previously, there is no officially established level for nonvoter approved debt for a school district. Best practice is to provide guidelines for debt burden ratios and factors combined with debt affordability criteria in the debt management policy. FCMAT believes that a debt burden factor of 1 - 2% of the district's unrestricted general fund revenues is reasonable.

Debt Burden Ratio

Applying this methodology to the current debt obligation for Lucerne Valley Unified, the debt service payments are equivalent to 11.4% of the district's current unrestricted revenues, an amount that cannot be feasibly sustained by the district's unrestricted general fund.

Debt Affordability

Issuing COPs or other long-term obligations supported from the district's general fund requires a balance between the debt issued against unrestricted resources and the ability to support the debt over a long period of time. Anytime debt that is supported by the general fund is issued, the district runs a risk of encountering unknown variables that can affect the ability to support the debt obligation(s) and sustain budget flexibility, especially in a climate of fiscal uncertainty.

FCMAT analyzed the district's total long-term indebtedness to determine how much debt is serviced using the unrestricted general fund, and how much has a dedicated funding source other than the unrestricted general fund. A debt burden ratio indicates the district's ability to support annual debt payments, including principal and interest, from current unrestricted revenue sources. This ratio is calculated as follows:

Total Annual Government Revenue of Fund(s) Servicing Debt to

Total Annual Governmental Debt Obligations

Based on the audited financial statements as of June 30, 2011, the district had a total of $7,964,322 in long-term unfunded debt, as shown in the following table:

Debt Funded from the Unrestricted General Fund (Unfunded)

Type of Debt	Debt Amount
Compensated Absences	$33,620
Capital Lease Obligations	983,960
COPs	6,655,000
Other Long-Term Debt	291,742
Total Unrestricted General Fund Debt	**$7,964,322**

Compensated absences refers to the accumulated unpaid vacation earned by employees as of June 30, 2011 and is included in long-term debt on the district's audited financial statements. This amount is not included in the calculation of debt service payments from the unrestricted general fund because debt accrued for vacation generally does not require a cash payment.

The district may have access to other funding sources that can be used to make some or all of the debt payments, such as developer fees in the capital facilities fund. However, most of these revenue streams are not consistent from year to year to support the debt service obligations occurring over several years.

To determine whether a school district has too much unfunded long-term debt, the amount of the annual long-term unfunded debt payments is compared to the district's total unrestricted general fund revenues. The following table shows the unfunded long-term debt payments budgeted for fiscal year 2011-12 compared with the unrestricted general fund revenues included in the 2011-12 second interim report.

Annual Debt Service Payments Funded from the Unrestricted General Fund (Unfunded)

Debt Burden Ratio
Second Interim - Unrestricted Revenues to Budget Debt Obligation
For the Fiscal Year 2011-2012

Unrestricted General Fund Revenue Sources	
Revenue Limit Sources	$4,732,617
Other State Revenue	$1,067,477
Other Local Revenue	$389,129
Total	**$6,189,223**
Type of Debt	
COPs	$408,708
Capital Lease Obligations	$298,332
Total	**$707,040**
Debt Burden Ratio	**11.4%**

The unrestricted general fund revenues for the district for fiscal year 2011-12 are projected to be $6,189,223. Therefore, the total debt payments above are equal to 11.4% of unrestricted general fund revenues, well above the recommended level of 1 – 2%. FCMAT believes this is unsustainable beyond fiscal year 2012-13.

Measure S

In June 2010, the district attempted to pass Measure S, a general obligation bond authorized under the provisions of Proposition 39. Passage of this bond would have raised local property taxes by $60 per year per $100,000 of assessed property value for 40 years. If passed, Measure S would have granted the district the authority to issue $7.950 million in general obligation bonds to repay the remaining debt service owed on the district's 2008 COPs.

Under the provisions of Propositions 39, general obligation bond measures must pass with at least 55% of the vote. Of the 1,110 residents who voted on the measure, only 362 of them, or 32.61%, voted in favor.

COPs Restructuring

In September 2011, the district retained Governmental Financial Strategies (GFS) Inc. to evaluate whether the current debt obligations for COPs could be restructured to provide short-term budgetary relief while maintaining long-term affordability.

GFS simulated restructuring the annual debt service payments of approximately $400,000 to $0 for the next 10 years. Under this scenario, the district would avoid making $4 million in debt service payments over the next 10 years; however, the remaining 20 years of debt service payments were anticipated to increase by nearly $1.5 million to $1.9 million per year.

Under this option, the district would increase the existing payments over the life of the loan from $12.8 million to $37.5 million, adding $24.7 million to the district's long-term debt obligation. Restructuring the COPs would clearly be a benefit in the short-term, but would be a significant financial burden in the long-term. Therefore, FCMAT does not recommend that the district consider restructuring the COPs.

The district has investigated every available avenue to reduce and/or eliminate its outstanding debt related to its COPs. The use of general obligation bonds to defease the existing COPs remains the district's best option.

The failure of Measure S may indicate that the district needs to improve communication with the community and increase public support if there is another attempt to pass a general obligation bond.

A critical step in packaging a general obligation bond is to determine voter support for the measure and collect data. This data will ideally allow the district to complete the following:

- Identify baseline support for a proposed general obligation bond.
- Determine the highest achievable tax rate and total bond capacity that can be supported by the electorate.
- Determine the arguments that will increase and/or decrease support for the bond measure.
- Determine the election date that provides the district with the highest probability of success.

Recommendations

The district should:

1. Adopt a debt management policy substantially similar to the policy attached as Appendix A to this report to guide the governing board in making decisions regarding all forms of indebtedness.
2. Consider retaining professional consultants to perform a community opinion survey regarding placing another general obligation bond measure on the ballot.

Financial Hardship

The governing board agenda for June 7, 2007 indicates that by issuing the COPs, the district would qualify for financial hardship, making it eligible for funding for two new schools under the State School Facilities Program (SFP).

Financial hardship assistance is available for districts that cannot provide all or part of their funding share of a SFP project if they meet narrowly defined criteria. However, to receive financial hardship funds, a district must establish new construction and/or modernization eligibility under the program, make all reasonable efforts to increase local funding, and demonstrate its inability to contribute all or part of the matching share requirement.

Establishing New Construction Eligibility

To be eligible for new construction, a district must demonstrate that existing seating capacity is insufficient to house its current and anticipated pupils using a five-year enrollment projection. Once eligibility is determined, a "baseline" is created that remains in place as the basis of all future applications. The baseline is adjusted for changes in enrollment and for facility additions and may be adjusted for other factors such as errors and omissions or amendments to the program regulations. Except for these updates, the establishment of the eligibility baseline is a one-time process.

The State Office of Public School Construction (OPSC), which administers the program, maintains a variety of online reports on school agency participation in the program. One is the New Construction Remaining Eligibility Report, which illustrates the number of grants by grade level (a dollar value per unhoused student) that each school district has established under the SFP program referred to as "eligibility."

FCMAT's review of this report indicates that the district is not eligible for any grants at the K-6 level, only 53 grants at the 7-8 level and no grants at the 9-12 level (This information is attached as Appendix B to this report). Therefore, even if the district had qualified for financial hardship, it likely would not have established the eligibility needed to fund two new schools through the SFP.

Qualifying for Financial Hardship Assistance

To apply for financial hardship, a district must send a letter to the OPSC Financial Hardship Audit Unit stating the reasons it is requesting financial hardship. The district must submit documentation to meet the legal requirements as demonstrated in the table below.

Legal Requirement	Support Documentation Required
1. The district levies the maximum developer fee allowed.	Board resolution demonstrating that the district has approved the maximum rates allowable under law.
2. Demonstrate local effort for matching revenues.	At least <u>one</u> of the following: Debt level at 60% of bonding capacity, or Total district bonding capacity less than $5 million, or A successful registered voter bond election for at least the maximum allowed under Proposition 39 within the previous two years, or Other evidence that demonstrates that all reasonable local efforts have been made as approved by the State Allocation Board (SAB).
3. Financial inability to contribute the match.	Evidence that facility funds are not available: Financial Hardship Project worksheet. Latest independent audit reports. Encumbrances. Expenditure reports. Listing of the district's unused sites. Forms SAB 50-01 and SAB 50-02 for interim housing deduction calculation for new construction projects only. Written estimation of interim housing needs.

As previously mentioned, the law requires that a district seeking financial hardship assistance demonstrate that all reasonable efforts have been made at the local level to raise revenues in support of the SFP match.

FCMAT's review found that the district has not met the criteria necessary to obtain financial hardship status. Although the district issued nonvoter approved debt beyond the 60 percent threshold, developer fee rates have not increased since 2006.

The district levies fees at a rate of $2.63 per square foot for residential construction and 42 cents per square foot for commercial/industrial. These rates are well below the maximum legal rate of $3.20 per square foot for residential construction and 51 cents per square foot for commercial/industrial projects. The district should prepare a developer fee justification study in accordance with the School Facilities Program legal requirements listed in the table above.

Recommendations

The district should:

1. Consider retaining a consultant to update the district's developer fee justification study and increase its developer fee rates to the maximum authorized by law.

Grand Jury Report

In August 2011, a San Bernardino County grand jury issued a report regarding the district's issuance of COPs. In that report, the grand jury responded to a resident complaint that the district had issued nonvoter approved debt to increase its level of bonded indebtedness to qualify for financial hardship under the SFP.

Although grand jury members were informed that this methodology of debt encumbrance to obtain hardship status is not unique to the district, the report did not differentiate between nonvoter and voter-approved debt. This is an important distinction since voter-approved debt is backed by the full faith credit of the district's tax payers, and nonvoter approved debt becomes an obligation of the unrestricted general fund.

The grand jury found the following:

1. The regulatory criterion at the time of the financial hardship request is that the district's outstanding indebtedness must be at least 60% of its total bonding capacity. This is one of many factors the OPSC uses to determine whether a school district qualifies for hardship status. The 2007 school board decision to issue COPs created outstanding indebtedness with no guarantee that OPSC would approve the hardship status.
2. The OPSC had not approved the district application for hardship status as of the date of their report.
3. The OPSC regulations do not appear to prohibit school districts from intentionally increasing outstanding indebtedness to qualify for hardship status. However, this practice appears to conflict with the School Facilities Program's goal of requiring school districts to raise local funding to support the program match.

As a result of these findings, the grand jury made the following recommendation:

11-24 Implement policy changes that restrict the creation of outstanding indebtedness for purposes of qualifying for SFP hardship status (Findings 1 – 3.)

In response to the grand jury's recommendation, the governing board revised Board Policy 7210 (a) in September 2011 so that, among other things, the following language was added:

> The district shall not create outstanding indebtedness for purposes of qualifying for School Facility Program (SFP) hardship status.

Financial hardship is the final option for school agencies that do not have access to capital facilities funding mechanisms. However, exceptions for financial hardship include the following:

- County offices of education.
- Agencies that have bonding capacity less than $5 million.
- Agencies that have indebtedness of up to 60 percent of their bonding capacity level.

Under these conditions, an agency has little chance of raising local funds to meet the state's matching share requirement.

If the district pursues another general obligation bond measure, it may wish to distinguish between nonvoter and voter-approved debt in its board policy and include a debt management policy to provide guidance for total voter and nonvoter indebtedness. This policy should include maximum debt burden ratios and debt affordability factors.

Although the district does not appear to be eligible for the School Facilities Program and does not levy the maximum developer fee authorized by law, these factors could change over time. If the existing COP is either partially or fully retired by a future general obligation bond, the district should ensure that the Board Policy 7210 (a) does not prevent the district from accessing financial hardship funding through the School Facilities Program in the future.

Recommendations

The district should:

1. Consider revising Board Policy 7210 (a) to distinguish between nonvoter and voter-approved debt to ensure that the policy does not prevent the district from accessing financial hardship funding through the School Facilities Program in the future.
2. Create a debt management policy to provide clear guidance for total voter and nonvoter indebtedness. This policy should include maximum debt burden ratios and debt affordability factors.

District Lapsation

California Education Code (EC) Section 35780 (a) requires each county committee on school district organization (county committee) to "lapse" a school district if its ADA decreases to less than six. Lapsation involves dissolving the district and annexing its territory to one or more adjacent school districts. EC Section 35782 further requires the county committee to take action to lapse a district within 30 days of the close of the school year.

With an October 2010 enrollment of approximately 2,567, which includes the Sky Mountain Charter School, the district does not meet the conditions for mandatory lapsation in EC Section 35780. Therefore, the State Board of Education (SBE) would have to waive portions of EC sections 35780 and 35782 to facilitate the lapsation, presumably instead of the district receiving a state loan. Nevertheless, the California State Board of Education approved similar requests from the Los Alamos Elementary School District (ESD) in Santa Barbara County on March 11, 2011 and the West Fresno Elementary School District in Fresno County on May 11, 2011. Additionally, at its May 2009 meeting, the board approved other requests from the Chinese Camp Elementary School District in Tuolumne County, the Delta View Joint Union Elementary School District in Kings County, and the Montebello Elementary School District in Santa Clara County. The district would be the first unified school district to seek such a waiver.

Because the request would take the form of a general waiver, the SBE would have to cite one of the following seven reasons in EC 33051(a) before a denial:

> The state board shall approve any and all requests for waivers except in those cases where the board specifically finds any of the following: (1) The educational needs of the pupils are not adequately addressed. (2) The waiver affects a program that requires the existence of a schoolsite council and the schoolsite council did not approve the request. (3) The appropriate councils or advisory committees, including bilingual advisory committees, did not have an adequate opportunity to review the request and the request did not include a written summary of any objections to the request by the councils or advisory committees. (4) Pupil or school personnel protections are jeopardized. (5) Guarantees of parental involvement are jeopardized. (6) The request would substantially increase state costs. (7) The exclusive representative of employees, if any, as provided in Chapter 10.7 (commencing with Section 3540) of Division 4 of Title 1 of the Government Code, was not a participant in the development of the waiver.

The process of lapsation could theoretically be accomplished through merging with one of the district's adjacent unified school districts. However, since the former Lucerne Valley Unified School District's assets and liabilities, including nonvoter approved debt, would become those of the recipient district, it is unlikely that any neighboring districts would participate in this merger.

All Charter School District

The district has approved the petition for Sky Mountain Charter School, an independent study school managed by a nonprofit public benefit education corporation called Innovative Education Management. This is a non-classroom based program; therefore, the charter school can accept students from contiguous counties including San Bernardino, Inyo, Kern, Los Angeles, Orange, and Riverside.

Conversion to an all-charter school district requires the approval of the State Board of Education and the superintendent of public instruction (SPI). The process requires approval of the petition by the California Department of Education and the Advisory Commission on Charter Schools; the commission reviews the petition and recommends approval or denial to the SPI. If the petition is approved by the SPI, it is placed on the State Board of Education agenda for a vote, and if the board approves the petition, it is considered the authorizer of the petition.

According to EC Section 47606(a), a school district may convert all of its schools to charter status if the petition meets the following conditions:

1. Fifty percent of the district teachers sign the charter petition.
2. The petition specifies the alternative attendance arrangements for pupils living in the district who choose not to attend charter schools.
3. The petition contains all the requirements included in EC Section 47605(b), (c), (d), (e), and (f).

District conversions must also address the requirement for both students and staffs to have other options. This usually takes the form of a joint powers agreement or memorandum of understanding to permit inter-district transfers for students and the opportunity for staff to leave the charter district if so desired and go to another school district. Once the charter district is established, it would be subject to the renewal criteria contained in Assembly Bill 1137. If the entire district were converted to a charter school district, the San Bernardino County Office of Education would retain fiscal oversight over the district.

FCMAT prepared a preliminary calculation to determine if this would benefit the district financially assuming all other requirements were met. Charter school funding rates were applied to the current grade level configuration and the district's current funding level, which includes additional funding for a necessary small high school. It was determined that this option would not be financially beneficial to the district.

Appendices

A. - Sample Debt Management Policy
B. - Grant Eligibility Data
C. - Study Agreement

Appendix A. - Sample Debt Management Policy

SAN LUIS OBISPO COUNTY OFFICE OF EDUCATION
P.O. Box 8105, San Luis Obispo, CA 93403-8105

(P) #3266 SAMPLE DEBT MANAGEMENT POLICY

Purpose

The County Office of Education recognizes that the foundation of a well-managed debt program is a comprehensive debt policy.

This debt policy sets forth a set of comprehensive guidelines for the financing of capital expenditures. It is the objective of this policy that: 1) the County Office of Education obtain financing only when necessary, 2) the County Office of Education will use a process for identifying the timing and amount of debt or other financing that is efficient, and 3) the County Office of Education will obtain the most favorable interest and other costs in issuing the debt.

This policy will be reviewed by the County Board of Education at least annually and updated as necessary.

Responsibilities

County Superintendent & Deputy Superintendent

Under the general direction of the Superintendent, the Deputy Superintendent will have the primary responsibility for developing financing recommendations and ensuring the implementation of the debt policy. In developing the recommendations, the Deputy Superintendent will be assisted by the Director of Internal Fiscal Services and the County Superintendent. These individuals will comprise the Debt Management Committee. The responsibilities of the committee will be to:

$ Meet at least quarterly to review the County Office's capital improvement program and consider the need for financing to maintain the progress on the capital improvement program.

$ Develop a Request for Proposal (RFP) that will be used in the selection of bond counsel, financial advisor and/or underwriter beginning in the Spring of 2002 if necessary.

$ Select the financing participants for each debt issue, ensure the debt issue is integrated with the County Office's overall financing program, approve the structure of each debt issue, and review and approve all documentation for each issue.

$ Oversee the preparation of the information for the official statement for debt issues.

$ Meet as necessary in preparation for a financing or to review changes in state or federal laws or regulations.

$ Prepare all information for the bond rating agencies and make presentations as necessary.

$ Meet annually to review the County Office of Education=s compliance with the existing debt agreements.

$

$ A Meet annually to review the services provided by the financial advisor, bond counsel, paying agents and other service providers to evaluate the extent and the effectiveness of the services provided.

$ Administer the investment and expenditure of the debt proceeds and ensure that the debt payments are made on time.

$ Ensure that the arbitrage requirements are monitored and that the appropriate reports are filed with the federal government.

Bond Counsel

The bond counsel will issue an opinion as to the legality and tax exempt status of any obligations. The County Office will also seek the advice of the bond counsel on questions involving the state or federal law or arbitrage. The bond counsel is also responsible for the preparation of the bond documents (including the authorizing resolutions that the County Board of Education will adopt) and most of the closing documents. The bond counsel will ensure that all legal requirements for the debt issue are met. The bond counsel will perform other services as defined by the contract approved by the County Superintendent of Schools.

Financial Advisor/Underwriter

The County Office staff will seek the advice of the financial advisor and/or underwriter when necessary. The financial advisor will advise on the structuring of the debt obligations that will be issued, inform the County Office of the options available for each issue, advise the County Office of Education as to how choices will impact the marketability of the County Office of Education=s obligations, and will provide other services as defined by the contract approved by the County Superintendent of Schools.

County Office Auditors

The County Office of Education will include a review of any official statements issued in connection with a debt issue in its contract for services with the County Office of Education=s independent auditors.

<u>Short-Term Operating Debt Policy</u>

The expenditures associated with the day-to-day operations of the County Office of Education will be covered by current revenues. However, because the County Office of Education does not receive its revenues in equal installments each month and the largest expenditures occur in equal amounts, the County Office of Education may experience temporary cash shortfalls. To finance these temporary cash shortfalls, the County Office of Education may incur short-term operating debt, typically, tax and revenue anticipation notes (TRANS). The County Office of Education will base the amount of the short-term operating debt on cash flow projections for the fiscal year and will comply with applicable federal and state regulations. The County Office of Education will pledge operating revenues to repay the debt, which will be repaid in one year or less. The County Office of Education will minimize the cost of the short-term borrowings to the greatest extent possible and may participate in pooled TRANS to meet this goal.

Long-term Capital Debt Policy

The following will apply to the issuance of long-term debt:

- $ The County Office of Education will not use long-term obligations for operating purposes.

- $ The life of the long-term obligations will not exceed the useful life of the projects financed.

- $ The County Office of Education will strive to maintain level debt service payments.

- $ The County Office of Education will not issue unfunded long-term debt in excess of 3% of annual general fund revenues, unless there is a dedicated tax levy, surplus property sale, fixed lease payments from another public agency or redevelopment revenue stream committed to service the debt.

Bonds

The County Office of Education, upon approval of the County Board of Education, may issue general obligation bonds to finance significant capital improvements for the purposes set forth by the voters in the bond election. The County Office of Education may also issue revenue bonds to finance significant capital improvements without voter authorization, through Certificates of Participation (COP=s) or through Qualified Zone Academy Bonds (QZAB=s).

The County Office of Education staff will prepare a resolution authorizing the issuance of Certificates of Participation, Qualified Zone Academy Bonds, and General Obligation Bonds for presentation to the County Board of Education at least 45 days prior to the issuance.

Negotiated Versus Competitive Sale Versus Private Placement

When feasible and economical, the County Office may issue bonds either by competitive or negotiated sale. The County Office of Education will issue by negotiated sale when the issue is predominantly a refunding issue or in other non-routine situations that require more flexibility than a competitive sale allows. Whenever the option exists to offer an issue either for competition or negotiation, the Debt Management Committee will undertake an analysis of the options to aid in the decision making process.

Refunding

The County Office of Education will consider refunding debt whenever an analysis indicates the potential for present value savings of approximately 5% of the principal being refunded or at least $200,000. The financial advisor will compute the economic gain or loss on the refunding and the members of the Debt Management Committee will verify the computation. The County Office of Education will not refund less than 5% of its outstanding debt at one time except in unusual circumstances such as when it intends to change bond covenants.

Capital Leases

Capital leasing is an option for the acquisition of equipment or other assets with a cost of less than $500,000.
The County Office of Education will not consider leasing when there are available funds on hand for the acquisition unless the interest expense associated with the lease is less than the interest that can be earned by investing the funds on hand or when other factors such as budget constraints override the economic consideration.

When a lease is arranged with a private sector entity, the County Office of Education will seek a tax-exempt rate. When a lease is arranged with a government or other tax-exempt entity, the County Office of Education will try to obtain an explicitly defined taxable rate so that the lease will not be counted in the County Office of Education=s total annual borrowings subject to arbitrage rebate.

The lease agreement will permit the County Office of Education to refinance the lease at no more than reasonable cost. A lease that can be called at will is preferable to one that can merely be accelerated.

The County Office of Education staff may obtain at least three competitive proposals for any major lease financing. In evaluating the proposals, the net present value of the competitive bids will be compared, taking into account how and when the payments are made. If required by statute, the purchase price of equipment will be competitively bid.

Bond Rating

The County Office of Education=s goal is to maintain or improve its bond ratings. The County Office of Education=s staff will make a full disclosure to the bond rating agencies when necessary.

Arbitrage Liability Management

The County Office of Education will make every effort to minimize the cost of the arbitrage rebate and yield restriction while strictly complying with the law. The federal arbitrage law is intended to discourage entities from issuing tax exempt obligations unnecessarily. In complying with the spirit of the law, the County Office of Education will not issue obligations except for identifiable projects with very good prospects of timely initiation. Obligations will be issued as closely in time as feasible to the time contracts are awarded so as to minimize the time the debt proceeds are unspent.

The County Office of Education=s bond counsel and financial advisor will review, in advance, all arbitrage rebate payments and forms sent to the IRS.

Internal Interim Financing

In order to defer the issuance of debt obligations, when sufficient non-restricted funds are on hand, consideration will be given to appropriating them to provide interim financing for large construction projects. When the debt obligation is subsequently issued, the non-restricted funds will be repaid.

REVIEWED BY SCHOOLS LEGAL SERVICE __DC 7/19/01_______

APPROVED BY COUNTY BOARD OF EDUCATION _10/4/01_______

Appendix B - Grant Eligibility Data

New Construction Remaining Eligibility April 27, 2012

County	District	Attendence Area	Dist Code	HSAA Number	Eligibility SAB Date	K-6	7-8	9-12	Non-Sev	Severe
Riverside	Coachella Valley Unified	K-12 and West Sh	73676	1	5/23/2001	1,047	167	147	230	45
Riverside	Corona-Norco Unified		67033	0	6/23/1999	6,844	899	1,122	509	106
Riverside	Desert Sands Unified		67058	0	5/26/1999	4,354	29	3,340	0	274
Riverside	Hemet Unified		67082	0	4/28/1999	4,100	0	694	0	300
Riverside	Jurupa Unified		67090	0	10/25/2000	150	127	0	0	0
Riverside	Lake Elsinore Unified		75176	0	5/26/1999	2,664	0	0	0	249
Riverside	Menifee Union Elementary		67116	0	4/28/1999	2,458	938	0	289	145
Riverside	Moreno Valley Unified		67124	0	8/25/1999	1,714	0	1,570	89	168
Riverside	Murrieta Valley Unified		75200	0	2/24/1999	2,770	71	2,154	141	81
Riverside	Nuview Union		67157	0	9/22/1999	301	1	0	10	0
Riverside	Palm Springs Unified		67173	0	3/23/2011	2,067	1,040	447	0	151
Riverside	Palo Verde Unified		67181	0	10/22/2003	27	0	0	46	0
Riverside	Perris Elementary		67199	0	1/26/2000	2,931	0	0	21	0
Riverside	Perris Union High		67207	0	2/23/2000	0	1,705	1,711	388	58
Riverside	Riverside County Office of Educ	Community Schoc	10330	99	10/25/2000	16	42	42	0	0
Riverside	Riverside County Office of Educ	Special Ed.	10330	98	3/28/2001	0	0	0	0	837
Riverside	Riverside Unified		67215	0	7/28/1999	7,533	0	2,349	1,105	430
Riverside	Romoland Elementary		67231	0	2/23/2000	2,403	514	0	27	0
Riverside	San Jacinto Unified		67249	0	4/28/1999	1,658	170	353	148	130
Riverside	Temecula Valley Unified		75192	0	3/24/1999	0	0	1,298	177	169
Riverside	Val Verde Unified		75242	0	6/23/1999	2,204	149	615	137	61
Sacramento	Arcohe Union Elementary		67280	0	9/27/2000	50	10	0	0	0
Sacramento	Center Joint Unified		73973	0	1/26/2000	0	0	164	0	0
Sacramento	Elk Grove Unified		67314	0	4/28/1999	11,622	1,366	4,407	0	1,096
Sacramento	Folsom-Cordova Unified	Cordova High	67330	24	2/23/2000	766	0	333	100	45
Sacramento	Folsom-Cordova Unified	Folsom	67330	21	4/28/1999	1,291	0	153	33	3
Sacramento	Galt Joint Union Elementary		67348	0	4/28/1999	1,356	0	0	0	58
Sacramento	Galt Joint Union High		67355	0	7/26/2000	0	0	0	28	0
Sacramento	Grant Joint Union High	Foothill/Grant/Higl	67363	2	4/26/2000	0	0	0	0	10
Sacramento	Grant Joint Union High	Rio Linda	67363	1	4/26/2000	0	365	610	14	129
Sacramento	Natomas Unified		75283	0	5/26/1999	1,806	421	420	218	150
Sacramento	River Delta Joint Unified	Delta High	67413	1	2/27/2008	0	0	0	1	3
Sacramento	River Delta Joint Unified	Rio Vista High	67413	2	2/27/2008	211	0	0	0	14
Sacramento	Sacramento City Unified		67439	0	8/28/2002	0	0	0	210	397
Sacramento	Sacramento County Office of Education		10348	0	5/23/2001	0	125	0	0	354
San Benito	Aromas-San Juan		75259	0	7/26/2000	0	66	166	0	0
San Benito	Hollister Elementary		67470	0	3/24/1999	2,357	636	0	83	0
San Benito	San Benito County Office of Education		10355	0	7/12/2011	11	0	0	0	0
San Benito	San Benito High		67538	0	10/25/2000	0	0	320	112	10
San Benito	Southside Elementary		67553	0	7/28/1999	22	4	0	0	0
San Bernardino	Adelanto Elementary		67587	0	6/27/2001	0	0	0	0	62
San Bernardino	Alta Loma Elementary		67595	0	9/22/1999	158	0	0	0	0
San Bernardino	Apple Valley Unified		75077	0	12/8/1999	1,527	448	2,150	24	63
San Bernardino	Bear Valley Unified		67637	0	8/28/2002	194	2	51	0	1
San Bernardino	Central Elementary		67645	0	2/24/1999	0	16	0	14	0
San Bernardino	Chaffey Joint Union High		67652	0	2/24/1999	0	0	4,008	0	64
San Bernardino	Chino Valley Unified		67678	0	9/22/1999	0	0	1,616	86	83
San Bernardino	Colton Joint Unified		67686	0	7/28/1999	1,866	0	0	0	0
San Bernardino	Cucamonga Elementary		67694	0	8/28/2002	0	110	0	38	0
San Bernardino	Etiwanda Elementary		67702	0	4/28/1999	3,743	0	0	59	27
San Bernardino	Fontana Unified		67710	0	4/28/1999	3,344	820	1,434	267	272
San Bernardino	Hesperia Unified		75044	0	10/22/2003	3,579	628	2,813	198	103
San Bernardino	Lucerne Valley Unified		75051	0	8/22/2001	0	53	0	0	0
San Bernardino	Morongo Unified		67777	0	4/25/2007	1,410	309	159	236	163
San Bernardino	Mountain View Elementary		67785	0	2/27/2002	1,247	0	0	6	5
San Bernardino	Ontario-Montclair		67819	0	6/27/2001	731	412	0	0	155
San Bernardino	Oro Grande Elementary		67827	0	5/28/2003	292	0	0	0	0
San Bernardino	Redlands Unified		67843	0	7/28/1999	61	190	0	189	96
San Bernardino	Rialto Unified		67850	0	2/23/2000	1,482	0	0	33	19
San Bernardino	Rim Of The World Unified		67868	0	4/3/2002	0	0	0	299	0
San Bernardino	San Bernardino City Unified		67876	0	12/8/1999	141	0	0	231	0
San Bernardino	San Bernardino County Office c	Desert Mountain	10363	3	9/22/1999	130	100	121	353	0
San Bernardino	San Bernardino County Office c	East Valley	10363	4	9/22/1999	0	874	275	0	0
San Bernardino	San Bernardino County Office c	West End Consort	10363	2	1/26/2000	4	95	0	157	0
San Bernardino	Silver Valley Unified		73890	0	7/5/2000	242	0	88	0	0
San Bernardino	Snowline Joint Unified		73957	0	3/22/2000	3,989	1,219	3,182	1	116
San Bernardino	Upland Unified		75069	0	1/26/2000	0	0	369	78	0
San Bernardino	Victor Elementary		67918	0	2/24/1999	8,288	0	0	34	28
San Bernardino	Victor Valley Union High		67934	0	4/3/2002	0	898	0	60	72
San Bernardino	Yucaipa-Calimesa Joint Unified		67959	0	8/25/1999	756	338	635	199	58

Appendix C - Study Agreement

FCMAT
FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM
CSIS California School Information Services

FISCAL CRISIS & MANAGEMENT ASSISTANCE TEAM
STUDY AGREEMENT
January 4, 2012

The FISCAL CRISIS AND MANAGEMENT ASSISTANCE TEAM (FCMAT), hereinafter referred to as the Team, and the Lucerne Valley Unified School District, hereinafter referred to as the District, mutually agree as follows:

1. **BASIS OF AGREEMENT**

The Team provides a variety of services to school districts and county offices of education upon request. The District has requested that the Team provide for the assignment of professionals to study specific aspects of the Lucerne Valley Unified School District operations. These professionals may include staff of the Team, County Offices of Education, the California State Department of Education, school districts, or private contractors. All work shall be performed in accordance with the terms and conditions of this Agreement.

In keeping with the provisions of AB1200, the County Superintendent will be notified of this agreement between the District and FCMAT and will receive a copy of the final report. The final report will be published on the FCMAT website.

2. **SCOPE OF THE WORK**

A. Scope and Objectives of the Study

The scope and objectives of this study are to:

1. The Lucerne Valley Unified School District is requesting the FCMAT Team to assist in developing viable and implementable strategic planning options to help address funding long term debt obligations, declining enrollment, decreasing state revenues and cash deferrals while maintaining fiscal solvency.

2. The District would like the team to consider options such as but not limited to consolidation or lapsation or contracting out specific components allowable under the education code and to make recommendations regarding enhancing revenues or reducing expenditures while focusing on the goal of remaining fiscally solvent. Any recommendation(s) shall be included in FCMAT's multi-year analysis.

3. The FCMAT Team will complete a multi-year financial projection and cash flow analysis for the current fiscal year using the 2011-12 Second Interim Financial Report as the base line document. This component will provide the projected timeline in which the district would be required to submit a negative certification and become cash insolvent, requiring intervention from the state.

B. Services and Products to be Provided

Orientation Meeting - The Team will conduct an orientation session at the District to brief District management and supervisory personnel on the procedures of the Team and on the purpose and schedule of the study.

On-site Review - The Team will conduct an on-site review at the District office and at school sites if necessary.

1. Exit Report - The Team will hold an exit meeting at the conclusion of the on-site review to inform the District of significant findings and recommendations to that point.

2. Exit Letter - The Team will issue an exit letter approximately 10 days after the exit meeting detailing significant findings and recommendations to date and memorializing the topics discussed in the exit meeting.

3. Draft Reports - Sufficient copies of a preliminary draft report will be delivered to the District administration for review and comment.

4. Final Report - Sufficient copies of the final study report will be delivered to the District administration following completion of the review.

5. Follow-Up Support – Six months after the completion of the study, FCMAT will return to the District, if requested, to confirm the District's progress in implementing the recommendations included in the report, at no cost. Status of the recommendations will be documented to the District in a FCMAT Management Letter.

3. PROJECT PERSONNEL

The study team will be supervised by Anthony L. Bridges, CFE, Deputy Executive Officer, Fiscal Crisis and Management Assistance Team, Kern County Superintendent of Schools Office. The study team may also include:

A. Diane Branham	***FCMAT Fiscal Intervention Specialist***
B. Eric Smith	***FCMAT Consultant***
C. To Be Determined	***FCMAT Consultant***

Other equally qualified consultants will be substituted in the event one of the above noted individuals is unable to participate in the study.

4. PROJECT COSTS

The cost for studies requested pursuant to E.C. 42127.8(d)(1) shall be:

A. $500.00 per day for each Team Member while on site, conducting fieldwork at other locations, preparing and presenting reports, or participating in meetings.

B. All out-of-pocket expenses, including travel, meals, lodging, etc. The District will be invoiced at actual costs, with 50% of the estimated cost due following the completion of the on-site review and the remaining amount due upon acceptance of the final report by the District.

Based on the elements noted in section 2 A, the total cost of the study is estimated at $15,000.

C. Any change to the scope will affect the estimate of total cost.

Payments for FCMAT services are payable to Kern County Superintendent of Schools - Administrative Agent.

5. **RESPONSIBILITIES OF THE DISTRICT**

A. The District will provide office and conference room space while on-site reviews are in progress.

B. The District will provide the following (if requested):

1. A map of the local area
2. Existing policies, regulations and prior reports addressing the study request
3. Current or proposed organizational charts
4. Current and two (2) prior years' audit reports
5. Any documents requested on a supplemental listing
6. Any documents requested on the supplemental listing should be provided to FCMAT in electronic format when possible.
7. Documents that are only available in hard copy should be scanned by the district and sent to FCMAT in an electronic format.
8. All documents should be provided in advance of field work and any delay in the receipt of the requested documentation may affect the start date of the project.

C. The District Administration will review a preliminary draft copy of the study. Any comments regarding the accuracy of the data presented in the report or the practicability of the recommendations will be reviewed with the Team prior to completion of the final report.

Pursuant to EC 45125.1(c), representatives of FCMAT will have limited contact with pupils. The District shall take appropriate steps to comply with EC 45125.1(c).

6. **PROJECT SCHEDULE**

The following tentative schedule outlines the planned completion dates for key study milestones:

Orientation:	***February/March 2012 pending board approval***
Staff Interviews:	***to be determined***
Exit Interviews:	***to be determined***
Preliminary Report Submitted:	***to be determined***
Final Report Submitted:	***to be determined***
Board Presentation:	***to be determined***
Follow-Up Support:	***If requested***

7. CONTACT PERSON

Name of contact person: Sheri Staszewski

Telephone: (760) 248-6108 x4135 FAX: (760) 248-6677

E-Mail: sheri_staszewski@lvsd.k12.ca.us

Suzette M Davis 2/6/12

Suzette Davis, Superintendent Date
Lucerne Valley Unified School District

Anthony L. Bridges January 4, 2012

Anthony L. Bridges, CFE Date
Deputy Executive Officer
Fiscal Crisis and Management Assistance Team