FCMAT

Fiscal Crisis & Management Assistance Team

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February 8, 2007

Dianne Talarico, Superintendent
Santa Monica-Malibu Unified School District
1651 Sixteenth Street
Santa Monica, CA 90404

Dear Superintendent Talarico:

The purpose of this letter is to confirm the findings and recommendations identified by the Fiscal Crisis and Management Assistance Team (FCMAT) during fieldwork conducted at the district on December 5 and 6, 2006 and discussed in our telephone conference on December 12, 2006.

In November 2006 the district requested that FCMAT perform the following as described in the study agreement:

1. Prepare a multiyear financial projection of the district's general fund using FCMAT's Budget Explorer software to identify the financial condition of the district's general fund in 2007-08 and 2008-09 using identified industry variables. The projection will be based on revenue and expenditure trends of recent years as well as enrollment projections, identified district assumptions, and the impact of scenarios that may be considered in upcoming negotiation sessions.

The Fiscal Crisis and Management Assistance Team (FCMAT) was created by Assembly Bill 1200 in 1992 as a service to assist local educational agencies in complying with fiscal accountability standards. AB 1200 was established to help ensure that local educational agencies throughout California were adequately prepared to meet and sustain their financial obligations. AB 1200 is also a statewide plan for county offices of education and school districts to work together on a local level to improve fiscal procedures and accountability standards. The legislation expanded the role of the county office in monitoring school districts under certain fiscal constraints to ensure that these districts could meet their multiyear financial commitments. Assembly Bill 2756 gives FCMAT specific responsibilities with regard to districts that have received emergency state loans. These include comprehensive assessments in five major operational areas and periodic reports that identify the district's progress in those areas.

Since 1992, FCMAT has performed more than 600 reviews for local educational agencies, ranging from fiscal crisis intervention to management review and assistance. FCMAT also provides professional development training and is involved in software development. The Kern County Superintendent of Schools is the administrative agent for FCMAT. The agency is guided under the leadership of Joel Montero, Chief Executive Officer, with funding provided by appropriations in the state budget and modest fees charged to requesting agencies.

FCMAT reviewed district records, interviewed staff and examined financial reports to gather the information needed for this multiyear financial projection (MYFP). FCMAT has prepared the MYFP using the district's budget report dated November 29, 2006 as the 2006-07 base year data.

Multiyear Financial Projection Overview

The initial overview by FCMAT included a preliminary review of the district's 2005-06 unaudited actuals, the 2006-07 adopted budget and the budget report dated November 29, 2006. The review included a fiscal analysis of the projected revenues, expenditures, transfers and components of the ending fund balance for the general fund.

The district's primary objectives in developing and implementing the MYFP are to achieve and sustain a balanced budget, improve academic achievement and maintain local governance. The MYFP will identify specific planning milestones that will assist the district. The district is confronted by significant fiscal challenges that require difficult decisions to be made and implemented. The MYFP's goal of sustaining a balanced budget will be extremely difficult because of continued declining enrollment and future demands for salary and benefit compensation.

Any forecast of financial data has inherent limitations. *These limitations include issues such as unanticipated changes in enrollment trends and changing economic conditions at the state and local level.* Therefore, the budget forecasting model should be viewed as a trend based on certain criteria and assumptions rather than a prediction of exact numbers. The projection should be updated at each interim financial reporting period to maintain the most accurate data.

The MYFP developed for this report indicates that the district **will be** able to maintain its required reserve of 3% in the current and two subsequent fiscal years with the proposed 5% salary increase for certificated staff only, provided that the recommendations and MYFP assumptions in this letter are followed. The board, administration and community will need to begin identifying potential revenue increases to eliminate deficit spending and sustain fiscal solvency should funding continue to decline because of declining enrollment. Otherwise, the district may need outside financial assistance and may face the loss of local governance and decision-making authority.

Multiyear Forecast Assumptions

Multiyear financial projections are a part of the budget, interim and AB 1200 requirement for districts; they should be timely and accurate. These projections allow both the district and the county to predict revenue and expenditures, and to ensure that the district will be able to meet its financial obligations in the current and two subsequent fiscal years. If the district is not able to meet its financial obligations for the current or two subsequent fiscal years, the county superintendent of schools must notify the district's governing board and the Superintendent of Public Instruction of the determination. The county office must also adhere to Education Code section 42127.6 in assisting the district. This assistance can include assigning a fiscal expert to advise the district on financial problems, conducting a study of the financial and budgetary conditions of the district, and submitting a proposal for addressing the district's fiscal condition. The MYFP is intended to assist the county and the district in forming a plan to maintain fiscal solvency.

FCMAT reviewed the district's budget assumptions to validate the 2006-07 budget and MYFPs. Budget assumptions depict conservative economic factors and estimates addressed in the governor's budget proposal presented in January of 2007 and outlined by School Services of California in its Financial Projection Dartboard.

The following assumptions are included in the multiyear financial projection:

- Cost of living adjustment: 2007-08, **4.04%**; 2008-09, **2.70%.**
- Enrollment (CBEDS): 2006-07:**11,902;** 2007-08:**11,718**; 2008-09:**11,369**
- Average daily attendance: 2006-07: **11,339;** 2007-08: **11,163;** 2008-09: **10,831**
- Certificated compensation: **5%**
- Certificated staff: **2%** annual step and column increase.
- Classified staff: **1.5%** annual step increase.
- Health & welfare benefits: **10%** annual increase.
- Utilities: **5%** annual increase.
- Transfer: **$500,000** annually from the Building Fund to Routine Restricted Maintenance.
- Realign certificated staffing commensurate with the historical and future decline in student enrollment: 2007-08 **10** FTE.
- Includes interfund transfer of **$3,000,000** from Fund 17 to Fund 40.
- Includes recommendation to adopt reimbursement resolution of **$2,941,986** to the general fund for the payment of certificates of participation (COPs).
- Includes annual revenue of **$1,149,882** from 16th Street lease.

Enrollment Analysis

The district's enrollment has decreased over the past two years and is projected to continue declining in the current and two subsequent fiscal years. Proper enrollment tracking and analysis of average daily attendance (ADA) are essential to budget planning. When enrollment and ADA are flat or declining, the district must ensure its fiscal solvency by exercising extreme caution regarding budgetary issues such as negotiations, staffing and deficit spending. Diligent planning can enable the district to better understand its financial objectives and strategies to sustain financial solvency. The district must continually update the budget as new information becomes available from district sources or from other funding and regulatory agencies.

The following snapshot of the district's enrollment demonstrates that the district's grade-level cohorts in the primary grades are significantly lower than those in the secondary grades. Thus, through natural grade level attrition, the district's enrollment is declining.

Enrollment	Historical 2001 - 02	Historical 2002 - 03	Historical 2003 - 04	Historical 2004 - 05	Historical 2005 - 06	Base Year 2006 - 07	Year 1 2007 - 08	Year 2 2008 - 09
K	835	847	856	833	832	795	799	804
1	876	870	855	883	798	814	784	766
2	862	883	890	841	852	784	799	769
3	927	870	896	887	833	851	799	806
4	955	941	885	909	874	836	852	784
5	924	953	947	878	887	875	830	847
Subtotal (K - 5)	5,379	5,364	5,329	5,231	5,076	4,955	4,863	4,776
6	1,087	1,002	1,060	991	932	915	920	869
7	1,027	1,125	1,033	1,074	1,009	932	925	930
8	1,001	1,048	1,140	1,047	1,056	973	918	911
Subtotal (6 - 8)	3,115	3,175	3,233	3,112	2,997	2,820	2,763	2,710
9	1,152	1,001	1,070	1,105	1,035	1,025	954	899
10	1,093	1,167	1,033	1,023	1,068	1,053	1,016	946
11	1,017	1,078	1,129	963	1,011	1,098	1,043	1,012
12	927	1,004	1,048	1,111	1,004	951	1,079	1,026
Subtotal (9 - 12)	4,189	4,250	4,280	4,202	4,118	4,127	4,092	3,883
Ungraded Elementary	0	0	0	0	0	0	0	0
Ungraded Secondary	25	0	0	0	0	0	0	0
Total	12,708	12,789	12,842	12,545	12,191	11,902	11,718	11,369

Enrollment Projection Methodology

The cohort survival technique is the most frequently used method of preparing school enrollment forecasts and can use weighted or average techniques to account for the changing dynamics of each district. This modification permits current district-specific information to be incorporated in enrollment forecasts. Percentages are calculated from the historical enrollment data to determine a reliable percentage of increase or decrease in enrollment between any two grades.

For example, if 100 students enrolled in first grade in 2004-05 and increased to 104 students in second grade in 2005-06, the percentage of survival would have been 104%, or a ratio of 1.04. Ratios such as this are calculated between each pair of grades or years in school over several recent years. The ratios used are the key factors that determine the reliability of the projections, given the validity of the data at the starting point. The advantage of using ratios is that each ratio encompasses collectively the variables that could account for an increase or decrease in the size of a grade cohort as it moves on to the next grade. Each ratio represents the cumulative effect of the following factors:

- Migration patterns in or out of schools
- Retention in the same grade
- Changes in school program
- Drop-outs, inter-district transfers, etc.
- Birth rates
- Residential housing starts

To project for the future, the ratios thus selected are applied to the present enrollment statistics for a predetermined number of years. If any of these assumptions need to be altered in the future, it is critical that the projection be updated. This process provides an opportunity for the district to plan for any changes that may occur.

The district has an excess of requests for inter-district student transfers into the district. As the district's enrollment continues to decline, it should consider allowing additional inter-district transfers in accordance with available facilities and staffing.

Recommendation

The district should:

1. Conduct an enrollment and staffing analysis that is commensurate with the past and projected future decline in student enrollment, and make adjustments to sustain the district's financial solvency.

Fund 17 Special Reserve Fund for Other Than Capital Outlay Projects

In the 2004-05 fiscal year the district transferred $3,000,000 from Fund 40, special reserve fund for capital outlay projects, to Fund 17, special reserve for other than capital outlay projects, to meet the district's general fund reserve requirement. The district's criteria and standards for reporting state that any funds reserved in Fund 17 may be combined with the general fund to meet the 3% reserve requirement. However, all funds used to meet the reserve requirement must be discretionary and unrestricted.

These funds transferred were originally generated from payments the district received from the Santa Monica Redevelopment Agency Earthquake Recovery Project area and are restricted by law. As defined by AB 1290, Education Code section 42238 and Health and Safety Code section 33607.5, the district's annual redevelopment agency (RDA) payments can only be used for educational facilities (56.7%) or to offset a portion of the district's revenue limit (43.3%) The district's current fund balance in Fund 40 should be restated at $2,865,408.48 prior to this transfer. **The MYFP prepared by FCMAT includes this transfer in the analysis and the 43.3% of the payment received in 2006-07 posted as an offset to the district's revenue limit, per AB 1290.**

Recommendation

The district should:

1. Adopt a resolution to transfer $3,000,000 from Fund 17, special reserve for other than capital outlay projects, to Fund 40, special reserve fund for capital outlay projects.

Reimbursement Resolution for Certificates of Participation

In the 2003-04, 2004-05 and 2005-06 fiscal years the district used unrestricted revenue generated from certain ground leases to make annual debt service payments for certificates of participation (COPs) in accordance with the following:

2003-04 COP Payment =	$898,531.50
2004-05 COP Payment =	$895,961.50
2005-06 COP Payment =	$1,147,493.50
Total Payments:	**$ 2,941,986.50**

The district had revenues available in Fund 40, special reserve for capital outlay projects, to repay the certificates of participation; the district thus may reimburse the general fund for these types of expenditures. Monies in Fund 40 were generated from redevelopment tax increment payments from the Santa Monica Earthquake Recovery Project Area. Tax increment payments received pursuant to the Community Redevelopment Law, commencing with Section 33000 of the Health and Safety Code, may be used for land acquisition, facility construction, reconstruction, remodeling and deferred maintenance. **The MYFP prepared by FCMAT includes this proposed reimbursement in the analysis.**

Recommendation

The district should:

1. Adopt a resolution to reimburse the general fund in the amount of $2,941,986.50 for expenditures made over the previous three fiscal years for debt service payments related to certificates of participation financing.

16th Street Ground Lease

According to district documents, the district entered into a joint occupancy lease in May 1984 for the ground leasing of three district properties at 16th and Olympic, 9th and Olympic and Olympic and 4th streets. The joint occupancy structure was authorized under sections of the Education Code currently re-codified in Section 17515 and following. The lease contains a complex ground rent and rent offset credit formula. The district receives quarterly payments from STG Asset Management, Inc.

FCMAT found that payments received from this lease are not recorded on the district's financial records. Payments are received in the form of a check and, rather than being deposited to the county treasurer, are sent directly to Wells Fargo Bank to offset payments for certificates of participation. The district receives a quarterly reconciliation of the checks, interest, debt service payments and other items. Annual payments for the 2006-07 fiscal year in the amount of $1,149,882 will be budgeted in the unrestricted general fund under other local revenue and are included in FCMAT's analysis.

Recommendation

The district should:

1. Receipt and record all financial transactions, including amounts received from STG Asset Management, Inc for the 16th Street Ground Lease.

RDA Payments from the Santa Monica Redevelopment Agency

Redevelopment agency (RDA) or 2% payments are the inflationary revenues resulting from growth in the base year value of real property within a specified redevelopment project area. In no event shall the percentage increase for any assessment year determined pursuant to the Revenue and Taxation Code section 110.1(f) exceed 2% of the prior year's value. This statutory requirement is consistent with Proposition 13 and subsequent initiatives which, in the absence of new construction or certain changes in ownership, states that assessed value increases in the current fiscal year may not exceed 2% or the percentage of increase in the consumer price index (CPI) for the previous calendar year, whichever is less.

The district began receiving payments from the Santa Monica Earthquake Recovery Project Area in the 1996-97 fiscal year. The payments are received approximately six months after the end of the fiscal year to which they apply. For example, payments shown below for the 1997-98 fiscal year should be recognized as 1996-97 RDA payments. In accordance with AB 1290, payments received should be deposited and recorded as follows: 43.3% of the total payment to object 8047, revenue limit offset, in the general fund; and 56.7% of the total payment to object 8625, other local revenue, in Fund 40.

Payments received and posted in compliance with AB 1290 Revenue Limit Offset

Fiscal Year	Fund 01 (43.3 %)	Fund 40 (57.6%)	Total Payments
1997-98	10,280.89	13,462.51	23,743,.40
1998-99	48,839.53	63,953,.84	112,793.37
1999-00	112,268.97	147,012.72	259,281.69
2000-01	240,743.67	315,246.33	555,990.00
2006-07	750,794.64	983,142.17	1,733,936.81

Payments not posted in compliance with the Revenue Limit Offset, per AB 1290

Fiscal Year	Fund 01 (43.3 %)	Fund 40 (57.6%)	Total Payments
2001-02	252,098.29	330,114.84	582,213.13
2002-03	383,022.78	501,556.38	884,579.16
2003-04	479,716.60	628,173.92	1,107,890.52
2004-05	488,945.77	640,259.25	1,129,205.02
2005-06	581,608.29	761,597.92	1,343,206.21
Total R.L. Offset	**$2,185,391.73**		

After considering the recommended transfer from Fund 17 to Fund 40 in the amount of $3,000,000, the estimated balance is projected to be $5,865,408.48. The following recap regarding the priority of expenditures for Fund 40 is provided:

Projected Fund Balance as of January 29, 2007	**$5,865,408.48**
Restrict for payments not in compliance with AB 1290 (3 years)	(1,550,270.66)
Transfer from Fund 40 to Fund 01 for COP reimbursement	(2,941,986.50)
Debt service for certificates of participation	(1,149,500.00)
Current year expense (projected)	(200,000.00)
Projected Fund Balance as of February 7, 2007	**23,651.32**

Because of the timing and delivery of this management letter, FCMAT cannot provide a conclusive response regarding the recommended set aside for prior year payments received by the district that did not meet AB 1290 requirements for the revenue limit offset (43.3%). Representatives of FCMAT will be meeting with the California Department of Education and Department of Finance to determine the district's liability, if any, regarding retroactive payments and will provide a written response to the district.

Recommendation

The district should:

1. Restrict $1,550,270.66 in Fund 40 until a final determination can be made regarding retroactive payment requirements in accordance with AB 1290.

Capital Projects Fund (Developer Fees) Fund 25

Based on this analysis, the district will continue to have a shortfall between the current RDA payments (57.6%) and the debt service on the certificates of participation. In the 2006-07 fiscal year, the shortfall is projected to be $187,841. Although the district has a small residual balance in Fund 40 from RDA payments less the recommended restrictions, the balance in the capital facilities fund is projected to be $2,751,140.34. FCMAT recommends that the district review the expenditure requirements of developer fees with their local legal counsel to determine if all or part of the current debt service payments for certificates of participation can be funded from the capital facilities fund.

Government Code section 66006(b) requires local agencies, including school districts, which collect development fees (including statutory school facilities fees and other impact mitigation payments) to provide an annual accounting of such fees or payments. A separate accounting should be provided for each type of fee or payment deposited into each separate account or fund. Each accounting must include the following:

1. A brief description of the type of fee in the account or fund.
2. The amount of the fee.
3. The beginning and ending balance of the account or fund.
4. The amount of the fees collected and the interest earned.
5. An identification of each public improvement on which fees were expended and the amount of the expenditures on each improvement, including the total percentage of the cost of the public improvement that was funded with fees.
6. An approximate date by which the construction of the public improvement will commence if the local agency determines that sufficient funds have been collected to complete financing on an incomplete public improvement, as identified in paragraph (2), subdivision (a), of section 66001, and the public improvement remains incomplete.
7. A description of each interfund transfer or loan made from the account or fund, including the public improvement on which the transferred or loaned fees will be expended and, in the case of an interfund loan, the date on which the loan will be repaid and the rate of interest that the account or fund will receive on the loan.
8. The amount of refunds made pursuant to subdivision (e) of section 66001 and any allocations pursuant to subdivision (f) of section 66001. (Government Code section 66001(e) requires districts to refund developer fees that are not appropriated within five years from the date of collection. Government Code section 66001(f) provides a method for allocating such non-appropriated fees if the administrative costs of refunding exceed the amount to be refunded.)

Recommendations

The district should:

1. Review with its legal counsel the potential to make debt service payments for certificates of participation from the capital facilities fund.
2. Prepare and present the annual accounting of developer fees to the board, as required by the government code sections cited.

Multiyear Financial Projection Methodology

California school districts and county offices of education use many different methods and software products to prepare reliable MYFPs. FCMAT's projections were prepared using FCMAT's Budget Explorer version 2.0 multiyear projection software. The software is SACS compliant and has been formatted to report the district's financial information. The software is also available free of charge to districts for their own use.

When evaluating a multiyear projection, much attention is focused on the bottom line, which indicates the district's undesignated, unappropriated fund balance. For example, if the bottom line indicates a positive fund balance, this amount may be used by the board and/or the superintendent to improve educational programs, increase employee compensation or spend in other categories. However, if the unappropriated fund balance is negative, the deficit balance is the amount by which the budget must be reduced to sustain the recommended reserve in accordance with AB 1200 guidelines. The projection must be viewed comprehensively and the district must determine the compounding effects that using any or all of the unappropriated fund balance will have on the projection.

Multiyear Financial Projection

FCMAT has developed this MYFP scenario with a 5% salary increase for the certificated bargaining unit effective July 1, 2006. In addition, the scenario includes an adjustment for salary compression in 2006-07 and a second adjustment in 2007-08; the addition of 1.6 full time equivalent (FTE) certificated staff to account for fewer teaching periods for department chairs at both high schools; a reduction of 10 certificated staff in 2007-08 because of declining enrollment; a reduction in the one-time retirement incentive in 2007-08 and 2008-09; and elimination of the $200 annual district-paid tax sheltered annuity (TSA) for certificated bargaining unit members beginning in 2006-07.

The following is a summary of Scenario 1, which reflects deficit spending in the current year, 2007-08 and 2008-09. *For illustrative purposes only, the projection restates the district's unrestricted general fund balance in object 9795, other restatements, to include reserves from Fund 17 and the reimbursement of $2,941,986 for previous COP payments.* The two subsequent fiscal years are adjusted to include interest on the reserves in Fund 17. Detailed calculations for this scenario are attached and include all unrestricted and restricted resources:

Unrestricted General Fund

Name		Object Code	Historical Year 2005-06	Base Year 2006-07	Year 1 2007-08	Year 2 2008-09
Revenues						
	Revenue Limit Sources	8010 - 8099	$62,858,084.54	$64,293,519.57	$65,448,405.87	$66,163,946.46
	Federal Revenues	8100 - 8299	$91,061.75	$120,187.00	$120,000.00	$120,000.00
	Other State Revenues	8300 - 8599	$5,020,207.92	$6,029,918.00	$4,788,197.04	$4,776,737.64
	Other Local Revenues	8600 - 8799	$13,288,110.93	$13,912,339.00	$14,401,806.00	$14,740,913.38
Total Revenues			**$81,257,465.14**	**$84,355,963.57**	**$84,758,408.91**	**$85,801,597.48**
Expenditures						
	Certificated Salaries	1000 - 1999	$40,822,289.96	$43,997,673.00	$44,326,654.80	$45,172,096.24
	Classified Salaries	2000 - 2999	$9,466,049.53	$9,556,194.00	$9,679,208.48	$9,804,145.42
	Employee Benefits	3000 - 3999	$13,691,013.16	$14,425,474.00	$15,080,910.80	$15,937,500.04
	Books and Supplies	4000 - 4999	$826,453.37	$804,942.00	$792,516.56	$772,375.88
	Services and Other Operating Expenditures	5000 - 5999	$4,487,989.35	$5,535,439.00	$5,574,017.48	$5,836,275.94
	Capital Outlay	6000 - 6900	$164,240.38	$68,789.00	$68,789.00	$68,789.00
	Other Outgo	7000 - 7299	$6,790.57	$6,800.00	$6,800.00	$6,800.00
	Direct Support/Indirect Cost	7300 - 7399	($464,175.05)	($443,616.87)	($583,464.96)	($570,259.59)
	Debt Service	7430 - 7439	$55,080.59	$25,483.00	$25,483.00	$25,483.00
Total Expenditures			**$69,055,731.86**	**$73,977,177.13**	**$74,970,915.16**	**$77,053,205.93**
Excess (Deficiency) of Revenues Over Expenditures			**$12,201,733.28**	**$10,378,786.44**	**$9,787,493.75**	**$8,748,391.55**
Other Financing Sources\Uses						
	Interfund Transfers In	8910 - 8929	$700,000.00	$700,000.00	$500,000.00	$500,000.00
	Interfund Transfers Out	7600 - 7629	$1,075,000.00	$575,000.00	$75,000.00	$75,000.00
	All Other Financing Sources	8930 - 8979	$0.00	$0.00	$0.00	$0.00
	All Other Financing Uses	7630 - 7699	$0.00	$0.00	$0.00	$0.00
	Contributions	8980 - 8999	($9,585,986.81)	($12,630,146.00)	($12,978,599.07)	($13,675,746.69)
Total Other Financing Sources\Uses			**($9,960,986.81)**	**($12,505,146.00)**	**($12,553,599.07)**	**($13,250,746.69)**
Net Increase (Decrease) in Fund Balance			**$2,240,746.47**	**($2,126,359.56)**	**($2,766,105.32)**	**($4,502,355.14)**
Fund Balance						
	Beginning Fund Balance (as of July 1 - Unaudited)	9791	$3,744,794.02	$5,985,540.49	$11,253,166.93	$8,732,977.61
	Audit Adjustments	9793	$0.00	$0.00	$0.00	$0.00
	Other Restatements	9795	$0.00	$7,393,986.00	$245,916.00	$254,031.00
	Adjusted Beginning Fund Balance		$3,744,794.02	$13,379,526.49	$11,499,082.93	$8,987,008.61
	Ending Fund Balance		$5,985,540.49	$11,253,166.93	$8,732,977.61	$4,484,653.47
Components of Ending Fund Balance						
	Fund Balance, Reserved	9700 - 9709	$0.00	$0.00	$0.00	$0.00
	Revolving Cash	9711	$20,000.00	$0.00	$0.00	$0.00
	Stores	9712	$15,291.73	$0.00	$0.00	$0.00
	Prepaid Expenditures	9713	$2,875.00	$0.00	$0.00	$0.00
	Other Reserves	9719	$0.00	$0.00	$0.00	$0.00
	General Reserve	9730 - 9739	$1,002,801.00	$0.00	$0.00	$0.00
	Legally Restricted Balance	9740 - 9759	$0.00	$0.00	$0.00	$0.00
	Economic Uncertainties Percentage		3%	3%	3%	3%
	Designated for Economic Uncertainties	9770 - 9774	$3,254,703.19	$3,647,815.22	$3,539,954.76	$3,604,658.42
	Designated for the Unrealized Gains of Investments and Cash in County Treasury	9775	$0.00	$0.00	$0.00	$0.00
	Other Designated	9780	$0.00	$631,442.00	$631,442.00	$0.00
	Undesignated/ Unappropriated	9790	$1,689,869.57	$6,973,909.71	$4,561,580.85	$879,995.05
	Negative Shortfall	9790	$0.00	$0.00	$0.00	$0.00

Other Considerations

The district is required to contribute 3% of its total annual general fund expenditures (approximately $3.5 million per year) to the routine restricted maintenance account in the general fund. The multiyear projection includes the continued annual transfer of $500,000 from the district's building fund to the routine restricted maintenance account in the 2006-07 fiscal year. Depending on facility needs, the district may wish to seek a legal opinion from bond counsel regarding the ability to increase the amount of this annual transfer, thereby making more of the district's unrestricted revenues available for other purposes.

The 2006-07 general fund budget includes a one-time inter-fund transfer of $500,000 to the retiree benefits fund. The district may wish to reconsider this inter-fund transfer in the current year depending on the amount needed to fund the district's other post-employment benefit obligations. This would allow the district to fund retiree benefits on a pay-as-you-go basis.

The district is in the process of obtaining an actuarial report to determine the unfunded liability for post-employment benefits.

The district will include one-time state funding for district and site discretionary block grants in its 2006-07 second interim financial report. Careful consideration and planning should be given to the expenditure of these funds as they may help to offset some of the district's one-time expenditures in the current fiscal year.

When reviewing the MYFP scenario, the district should also evaluate the impact of the proposed salary increases on its other funds and resources. For example, the district currently contributes $75,000 to the child development fund from the general fund. Unless additional funding is forthcoming from other resources or other expenditures are reduced, the contribution from the general fund may need to be increased. This holds true for other district programs such as special education and transportation; the contributions to these funds are likely to increase. Rather than show an additional contribution from the general fund, FCMAT reduced expenditures in the restricted resources where possible to cover the amounts proposed for salary increases. However, this action also affects programs by reducing the amounts budgeted for supplies, services and capital outlay.

The district should also be extremely mindful of current local income sources, including two parcel taxes: Measure S and Measure Y. The MYFP calculations include these funding sources. Measure S provides approximately $6.5 million per year, while Measure Y provides approximately $3.7 million per year. However, Measure S expires in 2009 and Measure Y in 2011. The district has also entered into a facilities use agreement with the City of Santa Monica, which provides $6.5 million in annual revenue to the district. Unless the district and the city agree to an extension, this agreement expires in 2009.

Summary

The district has approximately $7.3 million in its special reserve (Fund 17) which can be used to meet the 3% required reserve for economic uncertainties; however, these funds do not address the ongoing deficit spending reflected in the MYFP scenario. In the 2006-07 fiscal year, approximately 92% of the district's unrestricted general fund is committed to salary and benefit compensation. While CBEDS enrollment has declined by 940 students over the past three years, staffing has increased during this same time period. As stated earlier, the district will need to make and act on decisions regarding enrollment, inter-district transfers, staffing and available facilities if it is to sustain any financial solvency beyond this projection.

We appreciate the opportunity to serve you and we extend our thanks to all the staff of the Santa Monica-Malibu Unified School District for their help in providing information to the FCMAT study team. Please contact me at (805) 462-1426 or abridges@fcmat.org if you have any questions regarding information contained in this management letter.

Sincerely,

Anthony L. Bridges,
Deputy Executive Officer

c: Diane Branham, Fiscal Intervention Specialist, FCMAT
Joel Montero, Chief Executive Officer, FCMAT
Barbara Dean, Deputy Administrative Officer, FCMAT
Steve Hodgson, Interim Chief Financial Officer, SMMUSD