

Financial Statement Projections, or Third Interim Reporting Requirements

Background

Because of the state of California's continued and growing budget deficit and declaration of a statewide fiscal emergency status, a large number of school districts have self-certified with either a qualified or negative certification for the 2007-08 second interim financial reporting period. FCMAT has received numerous questions and provides the following clarification regarding the process and requirement to submit a financial statement projection or a third interim financial report by June 1, 2008. The term "third interim report" does not exist in the California Education Code, but is used to describe the requirement for this report in California Education Code Section 42131 (e).

Reporting Requirements

What is the legal requirement?

Education Code Section 42131 (e) states the following:

The governing board of each school district filing a qualified or negative certification for the second report required under Section 42130, or classified as qualified or negative by the county superintendent of schools, shall provide to the county superintendent of schools, the Controller, and the Superintendent of Public Instruction no later than June 1, financial statement projections of the district's fund and cash balances through June 30 for the period ending April 30. The governing boards of all other school districts are encouraged to develop a similar financial statement for use in developing the beginning fund balances of the district for the ensuing fiscal year.

What reporting format should our district or county use?

A financial statement projection is not truly an interim report as it does not have the content or reporting requirements of the first and second interim financial reports. Instead, it is focused more on cash and fund balances for the current fiscal year. Local educational agencies (LEAs) are not required to submit a complete standardized account code structure (SACS) interim report via the state reporting software. However, LEAs may choose to use the state's SACS software, which includes an end of year projection tool to accommodate this reporting requirement.

Supplemental forms beyond what is stated above are not required. LEAs should provide any additional information that may assist the county or the state of California in the review process. If in doubt, each LEA should consult with its respective oversight agency as the reporting format may vary by region and/or county. Fund balance and cash balance projections should be provided for each fund, with the data summarized in the same object code format as the state SACS software for fund related forms (i.e. revenue summarized by revenue limit sources, state revenues, federal revenues and so forth).

The final submission should be transmitted both electronically and by paper copy. The education code refers to the reporting requirements for the current fiscal year; however FCMAT recommends best practices and therefore suggests that each LEA submit fund and cash balances for the current and two subsequent fiscal years whenever possible.

Does the district or county have to designate a certification for the end of year projection?

The end of year financial statement projection reporting requirement does not require LEAs to certify as positive, qualified or negative, nor does it require the submission of the criteria and standards.

Can the state or county change the second interim certification based upon our end of year projection submittal?

The Education Code is silent on the issue of whether an oversight agency can change an LEA's second interim financial certification based on data contained in the required financial statement projections as outlined in Education Code Section 42131 (e).). In point of fact, the so called third interim report serves somewhat of a different purpose than either the first or second interims. The purpose of the third interim is to help determine whether the district has an immediate need for cash. Additionally, the third interim allows the opportunity for the district to fine tune its ending fund balances and report that information to its county office. Clearly, this code section is intended to create a process by which a district closes the information gap between second interim and the end of the fiscal year to better inform decision-making related to budget development. The second interim report certification is viable until budget adoption by July 1 in any given fiscal year, and the subsequent analysis and certification of that budget by the county office of education.

Cash Management Strategies and Time Lines

LEAs that have certified as qualified or negative at the second interim reporting period may not be able to exercise options regarding non voter-approved debt (i.e. tax and revenue anticipation notes) in accordance with Education Code section 42133.

Some districts may need to rely on other internal or external options to meet cash flow requirements. External borrowing for cash management may require additional time because it requires an LEA to go outside its own agency for funds. Options for cash management strategies include the following:

- **Internal borrowing between district funds is authorized by Education Code section 42603 and allows LEAs to borrow between funds temporarily to address cash flow shortages.** This situation will need to be assessed monthly and will depend on the spending patterns of the LEA in the last three months of the fiscal year. This is the most common method used by LEAs; however, it only works if there is cash in other funds.

The limitations associated with this type of borrowing stipulate that no more than 75% of the money held in any fund during the current fiscal year may be transferred. In addition, funds must be repaid in the same fiscal year (that is, by June 30) if the transfer is completed prior to the last 120 days of the fiscal year. If funds are transferred within the last 120 days of the fiscal year, repayment must be made prior to June 30 of the subsequent year.

- **Borrow from the county office of education in accordance with Education Code sections 42621 and 42622.** This option depends upon the county office's willingness and ability to provide funds and may not be an option given the current economic outlook. County offices of education are monitoring their own cash balance and are **unlikely to be able** to meet this type of request.
- **Education Code section 42620 also allows districts to borrow from the county treasurer.** Under Article XVI, Section 6 of the California Constitution, the county treasurer must provide funds to an LEA should the LEA be unable to meet its obligations. However, the county treasurer cannot loan LEAs money after the last Monday in April of the current fiscal year. In addition, this type of borrowing requires approval by a formal resolution of the governing board. The loan cannot exceed 85% of direct taxes levied on behalf of the LEA. The advantage to having the county treasurer provide the funds is that the treasurer is able to take repayment directly from property tax receipts prior to any distribution to the LEA. Repayment must be made from the first monies received by the school district before any other obligation is paid.

Where can districts go for additional assistance?

LEAs should contact their respective oversight agencies or visit FCMAT's Web site at www.fcmat.org and review the FCMAT *Fiscal Oversight Guide*, which is located under the Fiscal Documents and Resources menu link.