

Metropolitan Education District
First Interim Financial Report
December 8, 2004

Executive Summary

Current Considerations

State Budget Status

For the third consecutive year, the final 2004-05 state budget was balanced with one-time fixes - borrowing, refinancing and creative accounting. The state continues to not address the fundamental imbalance between revenues and expenses. In its 11/17/04 "California Fiscal Outlook", the Legislative Analyst's Office projected an operating shortfall of approximately \$7.3 billion for 2005-06. This, coupled with the Governor's now limited "deal-making" options, has raised concerns within the education industry that Proposition 98 guaranteed funding for K-14 education may be a convenient target for solving the budget crisis. The Governor's 2005-06 budget proposal in January should tell us if our funding is at risk.

Reserves for Cash Flow

Some years ago, the Governing Board approved the establishment of General Reserves of \$82,000 for the General Fund and \$48,000 for the Adult Education Fund. The purpose of the General Reserve is to budget and accumulate "...such sum as the governing board may deem sufficient, for the next succeeding fiscal year, to meet the cash requirements to which the district's credit may be legally extended for that portion of said next succeeding fiscal year until adequate proceeds of the taxes levied for, or apportionment of state funds made to, the district during such succeeding fiscal year..." (E.C. 42124). ROC/P and Adult Education program do not receive state funding, unlike K-12 education, until the state budget is signed into law. A two-year evaluation of cash flow needs to cover district payroll and vendor payments during the first two months of the fiscal year indicates that combined reserves of 10% is a prudent policy. Consequently, the administration is recommending the General Reserves for the General and Adult Education Funds be set at 4% to replace the current fixed amounts. This, combined with the 6% Designation for Economic Uncertainty meets the 10% overall reserve goal. Moreover, with these two reserves in place, the administration is recommending that the reserve for state budget deficits be eliminated. MetroED is currently in discussions with its lobbyist (School Services of California) to identify strategies to include ROC/P and Adult Education with K-12 state advance funding, which will eliminate the need for the General Reserve. These adjustments to the district's reserve structure have been approved by the district Budget Advisory Committee for recommendation to the Board as part of the Budget Guidelines for 2005-06.

Employee Salaries and Benefits

The 2004-05 budget, and two projected years include only the district-paid 5% increase in benefits plus step/column movement on the salary schedules. The district is currently in negotiations with its three bargaining units for 2004-05. The administration has taken a cautious approach to salary/benefit negotiations pending the Governor's release of his proposed budget in January, and final determination of federal grants in the Adult Education program.

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Budget Adjustments

Budget transfers and adjustments for the current year are approved by the Governing Board on a monthly basis. Consequently, there are few adjustments presented in the 1st Interim Report that have not already been approved by the Board.

Multi-Year Projection Assumptions

For the General Fund 01 and Adult Education Fund 11, we have also provided detailed multi-year projections, with all budget assumptions and calculations for the 2002-03 and 2003-04 Unaudited Actuals, the 2004-05 1st Interim Budget and two subsequent years. Budget assumptions for the two projected years are based on School Services of California (SSC) “Dartboard” projections, historic spending patterns and district goals.

Budget Presentation

Presentation of the 1st Interim Report includes a “Budget at a Glance” that summarizes the proposed budgets for all the district’s funds and “Monthly Budget Adjustments” showing all changes from the last budget update approved by the Board. The Capital Outlay Fund 40 has been divided to separately show the resources available for the Central County Occupational Center (CCOC) and Metropolitan Adult Education Program (MAEP). Required state forms are provided in the sections identified in the Table of Contents.

Fund 01: General Fund (ROC/P)

Fund 01 Purpose: Fund 01 is the General Fund for the Central County Occupational Center and Programs (CCOC/P).

Fund 01 Certification: Staff is recommending a positive certification. This means that the General Fund will meet its financial obligations for the budget and subsequent two fiscal years; will maintain at least the required 3% Reserve for Economic Uncertainty and will end the year with a positive cash balance. The projections include a 6% Reserve for Economic Uncertainty, as required by Governing Board policy.

Fund 01 Budget Assumptions:

	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>
• Revenue Limit COLA:	2.41%	2.70%	2.60%
• ADA Cap Growth %:	3.67%	3.67%	3.67%
• ADA Cap Growth	142	146	151
• No increases in salary other than step, column and longevity advancement.			
• Decrease in employer PERS contributions from 10.42% to 9.952%			
• Increase in employer SUI contributions from .30% to .65%			
• 5% increase in employer paid health & welfare costs, the maximum allowed per bargaining unit agreements			
• Statutory COLA increases to appropriate expenditures for 2005-06 and 2006-07			
• General expenditures for Superintendent and Central Office support have been direct charged to the ROC/P and Adult Education on a 65%/35% basis			

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Fund 01 Revenues: See *Monthly Budget Adjustments-1st Interim Report* for changes from the last board-approved budget update.

Fund 01 Expenditures: See *Monthly Budget Adjustments-1st Interim Report* for changes from the last board-approved budget update.

Fund 01 Fund Balance: Components of Fund Balance reflect a change in how reserves are designated. The Contingency for State Deficits has been replaced with a 4% General Reserve for cash flow purposes. The Designation for Economic Uncertainty is maintained at 6%. The changes to the reserve accounts have generated a \$82,654 increase in the Undesignated Fund Balance, while maintaining prudent reserves.

Fund 01 Multi-Year Projections: The multi-year projections for General Fund (ROC/P) include summary and detail data for the two prior year Unaudited Actuals (2002-03, 2003-04), the budget year (2004-05) and two subsequent years (2005-06, 2006-07). The multi-year projections include detailed assumptions used for each of the five years, ADA information and detailed data on both revenues and expenses to a four-digit object code level. For 2005-06 and 2006-07, the fund balance is expected to increase by \$808,485 and \$1,369,753 respectively. These increases are due to projected revenue increases from COLA and growth, and there is no provision for salary increases. There is, however, provision made for increases due to step, column and longevity, a 5% increase in district contribution to employee health and welfare benefits and COLA increases for impacted expenditure accounts, such as materials, supplies and other operating expenses. The projections anticipate full funding of the district's match for Deferred Maintenance, transfers for Debt Service, transfers to the Capital Outlay Fund 40, a 6% reserves for Economic Uncertainty and 4% General Reserve for cash flow. The "Contingency for State Deficits" is eliminated.

Fund 11: Adult Education

Fund 11 Purpose: The Adult Education Fund is used to account separately for federal, state and local revenues for Adult Education programs. Expenditures in this fund must be for Adult Education purposes only; money received for programs other than Adult Education shall not be expended for adult education.

Fund 11 Certification: Staff is recommending a positive certification. This means that the Adult Education Fund 11 will meet its financial obligations for the budget and subsequent two fiscal years; will maintain at least the required 3% Reserve for Economic Uncertainty and will end the year with a positive cash balance. The projections include a 6% Reserve for Economic Uncertainty, as required by Governing Board policy.

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Fund 11 Budget Assumptions:

	<u>2004-05</u>	<u>2005-06</u>	<u>2006-07</u>
• Revenue Limit COLA:	2.41%	2.70%	2.60%
• ADA Cap Growth %:	2.50%	2.50%	2.50%
• ADA Cap Growth:	77.88	80.00	82.00
• No increases in salary other than step, column and longevity advancement			
• Decrease in employer PERS contribution from 10.42% to 9.952%			
• Increase in employer SUI contributions from .30% to .65%			
• 5% increase in employer paid health & welfare costs, the maximum allowed per bargaining unit agreements			
• Statutory COLA applied to appropriate expenditures for 2005-06 and 2006-07			
• Expenditures for Superintendent and Central Office support have been direct charged to the ROC/P and Adult Education on a 65%/35% basis			

Fund 11 Revenues: Projected local revenues are increased \$17,083 as the result of state equalization of revenue limits for Adult Education. It is expected that Federal grants will be increased approximately \$510,000 in December when final grant amounts are determined. For the current budget, however, Federal grant revenues are budgeted at the actual amount of the grant letters (before mid-year adjustments).

Fund 11 Expenditures: See *Monthly Budget Adjustments-1st Interim Report* for changes from the last board-approved budget update.

Fund 11 Other Financing Sources/Uses: At the end of fiscal year 2003-04, the district transferred \$533,333 to the Capital Outlay Fund 40 for the San Jose adult program. The 1st Interim includes a \$215,000 transfer back to cover startup costs for the San Jose Erikson Adult Center and reconfiguration of classes at the San Jose Hillsdale site.

Fund 11 Fund Balance: The 2004-05 budget reflects deficit spending, after Transfers In, in the amount of \$229,454. This is expected to be eliminated when the adult federal grants are finalized. Components of Fund Balance reflect a change in how reserves are designated. The Contingency for State Deficits has been replaced with a 4% General Reserve for cash flow purposes. The Designation for Economic Uncertainty is maintained at 6%. The changes to the reserve accounts have generated a \$210,643 increase in the Undesignated Fund Balance, while maintaining prudent reserves.

Fund 11 Multi-Year Projections: The multi-year projections for Adult Education Fund 11 include summary and detail for prior year Unaudited Actuals (2002-03, 2003-04), the budget year (2004-05) and two subsequent years (2005-06, 2006-07). The multi-year projections include detailed assumptions used for each of the five years, ADA information and detailed data on both revenues and expenses to a four-digit object code level. For 2005-06 and 2006-07, the fund balance is expected to increase by \$80,153 and \$456,220 respectively. These increases are due to revenue increases for COLA and growth, and there is no provision made for salary increases. There is, however, provision made for increases due to step, column and longevity, a 5% increase in district contribution to employee health and welfare benefits and COLA increases for impacted

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expenditure accounts such as materials, supplies and other operating expenses. The projections anticipate spend-out of the Bridge and Literature and Civics Supplemental grants in 2004-05 and 2005-06. This results in corresponding expense reductions in subsequent years, primarily in hourly wages and benefits. The projections retain 6% reserves for Economic Uncertainty and 4% General Reserve for cash flow. The “Contingency for State Deficits” is eliminated.

Fund 14: Deferred Maintenance

Fund 14 Purpose: The Deferred Maintenance Fund is used to account separately for state apportionments and the district’s contribution for deferred maintenance purposes. Principal revenues for this fund are the state Deferred Maintenance apportionment, interest earnings and district interfund transfers for the district’s match. Expenditures in this fund are intended for major repairs or replacements under the 5-year Deferred Maintenance plan approved by the Office of Public School Construction (OPSC).

Fund 14 Certification: Staff is recommending a positive certification. This means that the Deferred Maintenance Fund 14 will be able to meet its financial obligations for the budget and subsequent two fiscal years and will end the year with a positive cash balance.

Fund 14 Revenues: Fund 14 revenues anticipate 100% state match funding and critical hardship funding from the state in the amount of \$274,797 for the replacement of eight transformers on the CCOC site. The critical hardship application has not yet been approved by the Office of Public Construction (OPSC).

Fund 14 Expenditures: The project to replace 6-7 transformers is expected to cost \$439,000, which will leave this fund with a fund balance of \$432,662. Since we do not yet have state approval of the critical hardship grant, we are not budgeting expenditures for any other projects at this time. This will be amended once we are assured of receiving the state hardship funds.

Fund 21: Building Fund-Asset Management

Fund 21 Purpose: This is otherwise known as the CCOC Asset Management Fund. This fund exists primarily to account separately for proceeds from the rentals and leases of real property specifically authorized for deposit into the fund by the Governing Board. Revenues include lease payments from the Capital Auto Mall LLP and interest earnings. Expenditures are allowed only for new programs, upgrading of existing programs and necessary facility upgrades as approved by the Governing Board.

Fund 21 Certification: Staff is recommending a positive certification. This means that the Asset Management fund will be able to meet its financial obligations for the budget and subsequent two fiscal years, and will end the year with a positive cash balance.

Fund 21 Revenues: Projected revenues are budgeted at \$277,672 which includes rent from the Capitol Auto Mall LLP and interest on the fund balance.

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Fund 21 Expenditures: For the last few years, expenditures from the Asset Management Fund have been limited in order to provide secondary backup to the loss of revenue from additional state budget cuts. However, with expected improvement in the state economy and balancing of the state budget, the board has approved a 5-year expenditure plan that will start to address the many equipment and classroom reconfiguration needs at CCOC. For 2004-05, the planned expenditures total \$492,000. Unspent funds from this budget line will revert back to the fund balance at the end of each year. At all times, the fund must maintain a minimum of \$250,000 reserve, per board policy.

Fund 40: Special Reserve Fund for Capital Outlay Projects

Fund 40 Purpose: This Capital Outlay Fund exists primarily to provide for the accumulation of monies for capital outlay purposes. The only source of revenue for this fund comes from one-time revenues transferred from the ROC/P and Adult Education Funds. Monies in this fund are kept separate in their own Resource codes. Amounts are appropriated for expenditures as projects are planned and executed.

Fund 40 Certification: Staff is recommending a positive certification. This means that the Capital Outlay Fund will be able to meet its financial obligations for the budget and subsequent two fiscal years and will end the year with a positive cash balance.

Fund 40 Revenues: The facilities on the CCOC campus are showing considerable wear as they near 40 years in age, and there is need for upgraded Adult Education facilities in both San Jose and Campbell.

MetroED's funding options for building construction and modernization are severely limited. As a joint powers authority, MetroED does not qualify for state building and modernization funds. Moreover, the likelihood of passing a bond or parcel tax within the areas of MetroED's six participating districts is remote. Consequently, MetroED must generate its own funds for capital outlay internally. For 2004-05, the General Fund is projected to contribute its excess local property taxes (\$200,000). There are no projections for Adult Education transfers due to the uncertainty of federal grant revenues. This may change when the Federal grants are finalized.

Fund 40 Expenditures: There are no expenditures planned from the Capital Outlay Fund at this time.

Fund 40 Other Financing Sources/Uses: During fiscal year 2003-04, the district transferred \$533,333 to the Capital Outlay Fund 40 for the San Jose Adult program. The 1st Interim includes a \$215,000 transfer back for startup costs for the San Jose Erikson Adult Center and reconfiguration of a number of classes at the San Jose Hillsdale site.

State Legislation for Modernization: For 2003-04, MetroED sponsored legislation (AB 2035, Nakano, *School Facilities: Regional Occupational Centers*) that would allow MetroED to qualify for state school facilities funds on a matching basis. This is the second year for this legislation. The bill was passed by both the State Assembly and Senate, but vetoed by the Governor. MetroED continues to work with its lobbyist (School Services of California) to find a way to qualify for state modernization funding.