Westside Union School District

Administrative Services

Long-Term Fiscal Structural Concerns

August 16, 2016

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Nothing Lasts Forever

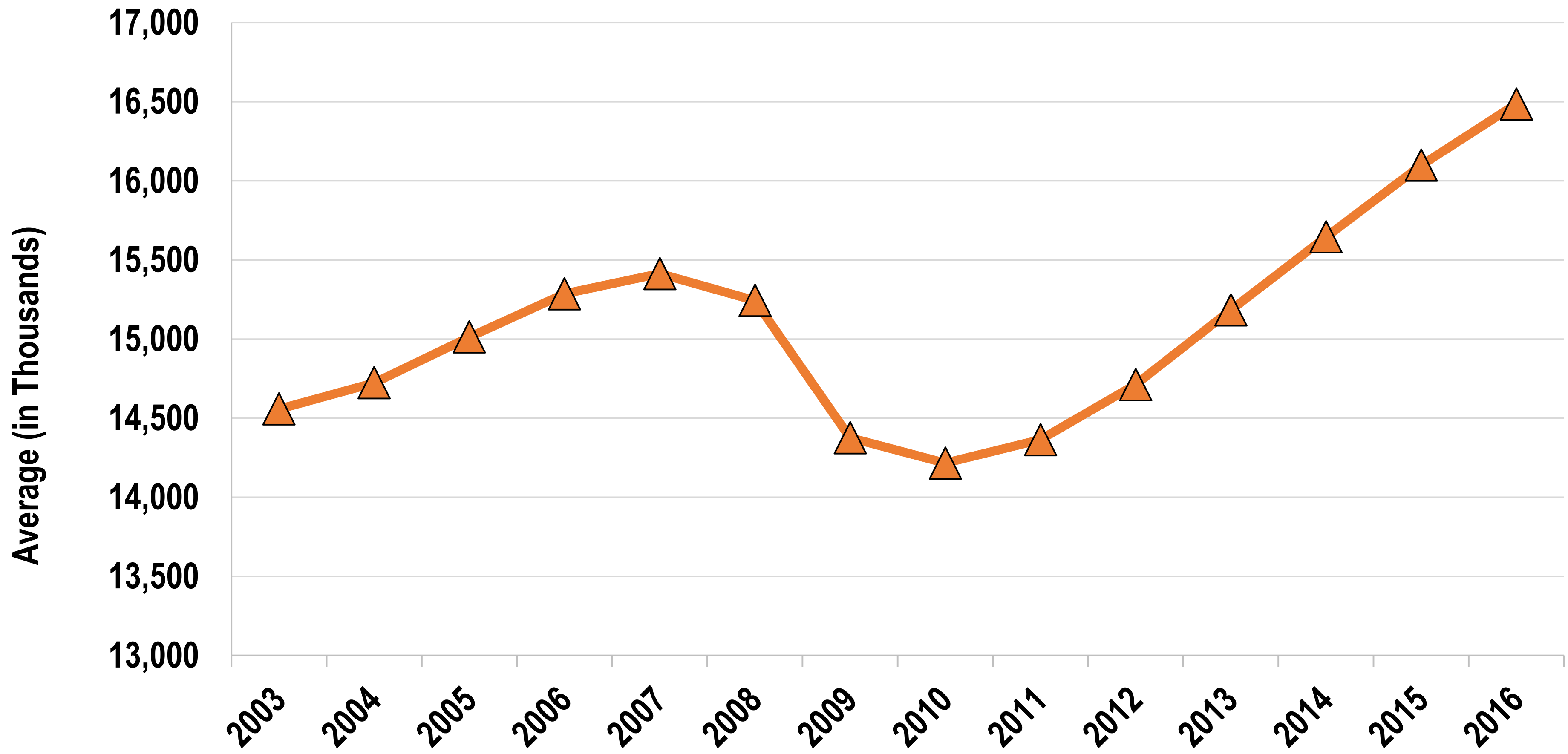
excerpts from School Services of California budget presentation

Preparing for the Slowdown

- The growth in education funding has been fueled by three major factors, all of which could change during 2016-17:
  - The Proposition 30 temporary taxes
  - Growth in the economy
  - Repayment of the Maintenance Factor
- At full implementation, each district will receive only cost-of-living adjustment (COLA) increases to its LCFF funding each year
  - COLAs over the next few years are estimated to be in the 2% to 3% range
  - If those COLA projections come to pass, most districts would again be making significant budget reductions
- We need to prepare for a slowdown while at the same time advocate for higher funding to continue to move toward at least the national average

Nonfarm Employment

B-5



Source: California DOF, Employment Development Department, Board of Equalization, U.S. Department of Commerce. Construction Industry Research Board, California Homebuilding Foundation: Estimates and Forecasts by the Los Angeles County Economic Development Corporation (LAEDC)

Risks to the Economy

- We think Governor Brown is right to worry about what we see as an overdue economic correction or recession

- The California economy is particularly vulnerable to the effects of the continued drought, volatile energy prices, a recovering labor market, and anti-business policies that continue to drive businesses and jobs out of the state

- California is a “high-beta state” – ups and downs are accelerated, as we have seen in the past and will see in the future

Multiyear Projections

- The cause of most school district insolvencies can be traced to a bad financial decision made during prosperous times that came back to bite the district during lean financial times, so caution is key
  - Resist using future revenue projection dollars to justify paying for ongoing expenditures in the current year
  - A future recession is predicted – the timing is unknown
  - Proposition 30 temporary taxes will expire

The Next Recession

- Governor Brown warns of the effects of a recession on the State Budget:
  - Capital gains tax revenues are volatile and will plummet at the next downturn
    - 69.5% of state revenues come from the personal income tax, with the top 1% of taxpayers accounting for half of these revenues
  - No one forecasts recessions, but they inevitably come
    - The current recovery is about six and a half years old; the average recovery lasts five years
  - Adding to ongoing spending at the peak of a recovery will only force painful cuts later
  - Economists have tried to eliminate the business cycle, but they have not figured out how to do it
- The Governor's solution: Build the state's Rainy Day Fund

The Long & Short Of It

deficits and the reality of the business cycle

Long-Term Fiscal Structural Concerns

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Although much-needed and well-deserved, recent increases to employee compensation were NOT fully covered by corresponding increases to funding, resulting in deficit spending for each of the past 4 years**.

	11-12	12-13	13-14	14-15
Revenue	**$56,419**	**$55,315**	**$62,231**	**$68,828**
Labor Costs	$48,186	$50,923	$53,631	$59,383
Non Labor Costs	$8,772	$8,764	$9,539	$10,266
****Total Expenses**	**$56,958**	**$59,688**	**$63,170**	**$69,649**
****Surplus/Deficit**	**($539)**	**($4,373)**	**($939)**	**($821)**

The deficit spending of these years was not reflective of poor financial stewardship, since it was explicitly the result of a deliberate, planned strategy to restore our educational programs and our salary schedule competitiveness by tapping into the substantial General Fund balance that had accumulated as a result of prudent cash-flow management strategies designed to maintain payroll solvency during the Great Recession.

Beg. Fund Bal.

$19,711

End. Fund Bal.

$13,038

*** Historical data from corresponding WUSD Certified Audited Financial Statements. Fund Balance will be marginally different from Audit Report because for Revenue/Expense analysis purposes these figures do not include Other Financing Sources/Uses, since OFSU not reflective of operating income/expense.*

Long-Term Fiscal Structural Concerns

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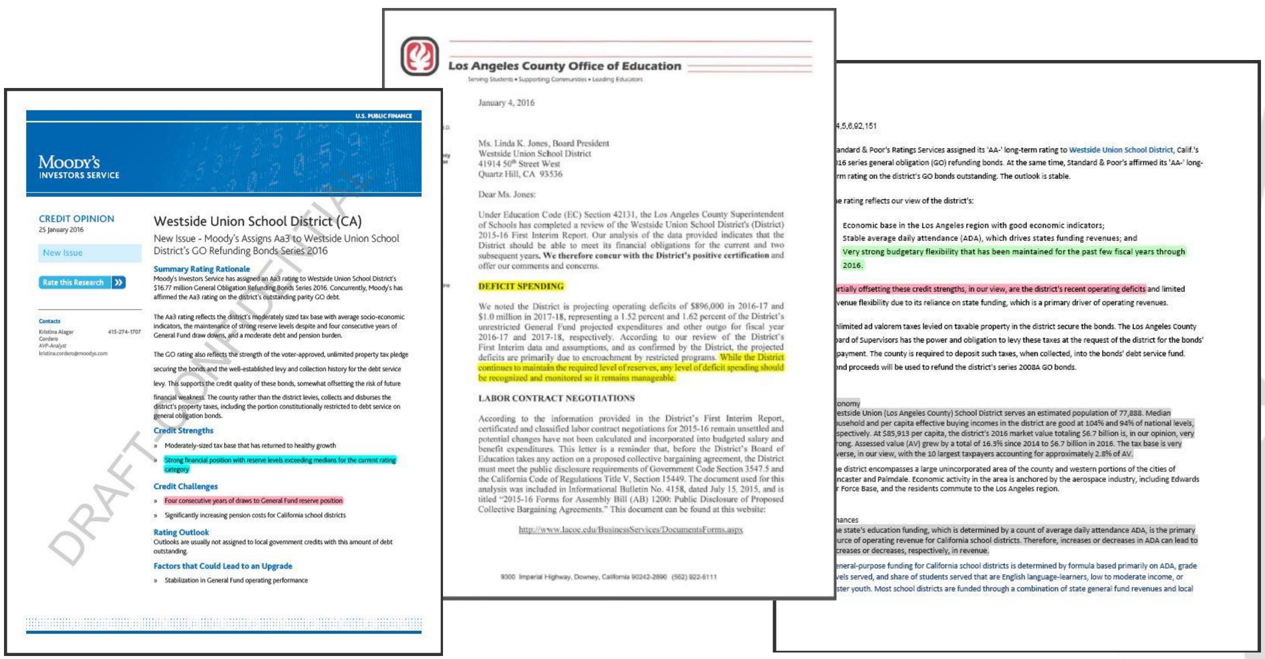
Although the past few years' deficit spending has been part of a strategy to use the General Fund balance to restore educational programs, compensation, and services we are rapidly approaching the point where further deficit spending could be cause for significant concern. The reasons for these concerns were outlined in the Management Discussion & Analysis in both the 2014 and the 2015 Certified Audited Financial Statements, and were later echoed by various independent agencies including Moody's Investor Service, the Los Angeles County Office of Education, and Standard & Poor's.



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Since the independent audited certified financial statements provide the accounting basis for these analyses, there can be no question of whether or not in expressing these concerns the District, as well as the concurring external financial experts, are crying ‘wolf’.

The concerns identified are based on concrete data and actual, historical spending patterns.

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The Short Term

Fiscal Year	11-12	12-13	13-14	14-15	15-16	16-17	17-18	18-19
Revenue Increases	-0.13%	-1.96%	12.50%	10.60%	20.27%	-2.29%	1.73%	0.68%
Labor Increases	2.14%	5.68%	5.32%	10.72%	12.53%	-0.47%	3.21%	2.56%
Non-Labor Increase	10.39%	-0.09%	8.84%	7.62%	55.60%	-14.12%	1.38%	-4.16%
Total Increase	**12.53%**	**5.59%**	**14.16%**	**18.34%**	**68.13%**	**-14.58%**	**4.59%**	**-1.60%**
Revenue	**$56,419**	**$55,315**	**$62,231**	**$68,828**	**$82,779**	**$80,884**	**$82,280**	**$82,837**
Labor Costs	$48,186	$50,923	$53,631	$59,383	$66,826	$66,514	$68,651	$70,408
Non Labor Costs	$8,772	$8,764	$9,539	$10,266	$15,974	$13,719	$13,908	$13,329
****Total Expenses**	**$56,958**	**$59,688**	**$63,170**	**$69,649**	***$82,799***	***$80,232***	***$82,559***	***$83,737***
****Surplus/Deficit**	**($539)**	**($4,373)**	**($939)**	**($821)**	**($20)**	**$651**	**($278)**	**($900)**
**Beginning FB	$19,711	$19,171	$14,798	$13,859	$13,038	$13,018	$13,670	$13,391
**Ending FB	$19,171	$14,798	$13,859	$13,038	$13,018	$13,670	$13,391	$12,491

AB1200 Perspective:
California economy cheats the business cycle in that over the future period in question funding remains essentially flat. Energy costs/inflation are capped at 1% or less, labor cost increases are limited to projected Health/Welfare increases, Step & Column movements, known increases to STRS/PERS, etc.

Outcome:
In the short term the projected Surplus/Deficit is net positive for the current and 2 future out-years ($358K). Even the signs of trouble in 18/19 (-$900K) are well within the District's historical margin of error with respect to deficit projection (more on that later in this presentation).

2011/12 to 2014/15 REPRESENTS ACTUAL, AUDITED FINANCIAL DATA.
2015/16 FORWARD IS FOR ILLUSTRATIVE PURPOSES ONLY.

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The Long Term: No Economic Cycles

Fiscal Year	11-12	12-13	13-14	14-15	15-16	16-17	17-18	18-19	19-20	20-21	21-22	22-23
Revenue Increases	-0.13%	-1.96%	12.50%	10.60%	20.27%	-2.29%	1.73%	0.68%	1.20%	1.20%	1.20%	1.20%
Labor Increases	2.14%	5.68%	5.32%	10.72%	12.53%	-0.47%	3.21%	2.56%	2.65%	2.65%	2.65%	2.65%
Non-Labor Increase	10.39%	-0.09%	8.84%	7.62%	55.60%	-14.12%	1.38%	-4.16%	1.00%	1.00%	1.00%	1.00%
Total Increase	**12.53%**	**5.59%**	**14.16%**	**18.34%**	**68.13%**	**-14.58%**	**4.59%**	**-1.60%**	**3.65%**	**3.65%**	**3.65%**	**3.65%**
Revenue	**$56,419**	**$55,315**	**$62,231**	**$68,828**	**$82,779**	**$80,884**	**$82,280**	**$82,837**	**$83,831**	**$84,837**	**$85,855**	**$86,886**
Labor Costs	$48,186	$50,923	$53,631	$59,383	$66,826	$66,514	$68,651	$70,408	$72,274	$74,189	$76,155	$78,173
Non Labor Costs	$8,772	$8,764	$9,539	$10,266	$15,974	$13,719	$13,908	$13,329	$13,463	$13,597	$13,733	$13,871
****Total Expenses**	**$56,958**	**$59,688**	**$63,170**	**$69,649**	***$82,799***	***$80,232***	***$82,559***	***$83,737***	***$85,736***	***$87,786***	***$89,888***	***$92,044***
****Surplus/Deficit**	**($539)**	**($4,373)**	**($939)**	**($821)**	**($20)**	**$651**	**($278)**	**($900)**	**($1,905)**	**($2,949)**	**($4,033)**	**($5,158)**
**Beginning FB	$19,711	$19,171	$14,798	$13,859	$13,038	$13,018	$13,670	$13,391	$12,491	$10,586	$7,637	$3,604
**Ending FB	$19,171	$14,798	$13,859	$13,038	$13,018	$13,670	$13,391	$12,491	$10,586	$7,637	$3,604	($1,554)

**Historical data from corresponding WUSD Certified Audited Financial Statements. **Does not include Other Financing Sources/Uses, since OFSU not reflective of operating income/expense.*

Best Case Scenario:
California economy cheats the business cycle, education funding increases at a steady rate adininitum, energy costs/inflation are capped at 1% or less, labor cost increases are limited to Health/Welfare increases, Step & Column movements, STRS/PERS, etc.

Outcome:
Even despite steady, continuous increases to funding, the short-term surplus nevertheless eventually gives way to persistent deficits, due to the inability of the rate of revenue increases to keep pace with the rate of expenses increases.

2011/12 to 2014/15 REPRESENTS ACTUAL, AUDITED FINANCIAL DATA.
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The Long-Term: History As A Guide

	11-12	12-13	13-14	14-15	15-16	16-17	17-18	18-19	19-20	20-21	21-22	22-23
Revenue Increases	-0.13%	-1.96%	12.50%	10.60%	20.27%	-2.29%	1.73%	0.68%	1.70%	-0.13%	-1.96%	12.50%
Labor Increases	2.14%	5.68%	5.32%	10.72%	12.53%	-0.47%	3.21%	2.56%	2.65%	2.65%	2.65%	2.65%
Non-Labor Increase	10.39%	-0.09%	8.84%	7.62%	55.60%	-14.12%	1.38%	-4.16%	1.00%	1.00%	1.00%	1.00%
Total Increase	**12.53%**	**5.59%**	**14.16%**	**18.34%**	**68.13%**	**-14.58%**	**4.59%**	**-1.60%**	**3.65%**	**3.65%**	**3.65%**	**3.65%**
Revenue	**$56,419**	**$55,315**	**$62,231**	**$68,828**	**$82,779**	**$80,884**	**$82,280**	**$82,837**	**$84,246**	**$84,136**	**$82,487**	**$92,798**
Labor Costs	$48,186	$50,923	$53,631	$59,383	$66,826	$66,514	$68,651	$70,408	$72,274	$74,189	$76,155	$78,173
Non Labor Costs	$8,772	$8,764	$9,539	$10,266	$15,974	$13,719	$13,908	$13,329	$13,463	$13,597	$13,733	$13,871
****Total Expenses**	**$56,958**	**$59,688**	**$63,170**	**$69,649**	***$82,799***	***$80,232***	***$82,559***	***$83,737***	***$85,736***	***$87,786***	***$89,888***	***$92,044***
****Surplus/Deficit**	**($539)**	**($4,373)**	**($939)**	**($821)**	**($20)**	**$651**	**($278)**	**($900)**	**($1,491)**	**($3,650)**	**($7,401)**	**$754**
**Beginning FB	$19,711	$19,171	$14,798	$13,859	$13,038	$13,018	$13,670	$13,391	$12,491	$11,000	$7,350	($51)
**Ending FB	$19,171	$14,798	$13,859	$13,038	$13,018	$13,670	$13,391	$12,491	$11,000	$7,350	($51)	$703

**Historical data from corresponding WUSD Certified Audited Financial Statements. **Does not include Other Financing Sources/Uses, since OFSU not reflective of operating income/expense.*

Business Cycle Scenario:
California economy experiences effect of typical business cycle *(to reflect actual historical business cycle impact, projected changes in % Revenue from 19/20 forward were taken from historical WUSD data from 2010/11 to 13/14)*. Education funding experiences volatility. In this scenario I have maintained long-term projected energy costs/inflation capped at 1% or less, labor cost increases are limited to Health/Welfare increases, Step & Column movements, etc.

Outcome:
Short-term surplus is quickly followed by major deficits. Fund balance eventually gives way to insolvency. Please note that the 'doom and gloom' of this scenario **does not take into account any action on the part of the Board or the employee associates to respond to the economic cycle's impact on revenue**. In the past the Board and the associations have worked together to find solutions to reduce expenses, which would of course has a significant effect on the District's ability to survive the downturn in the business cycle.

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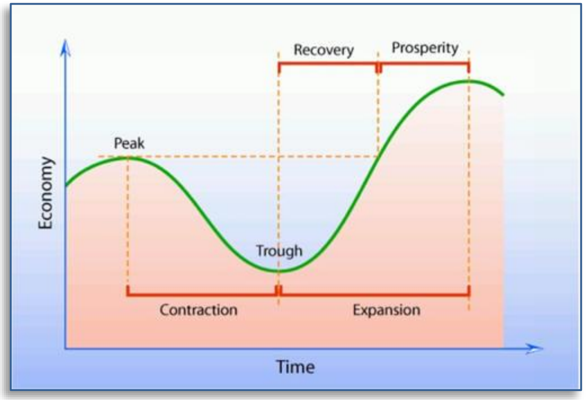
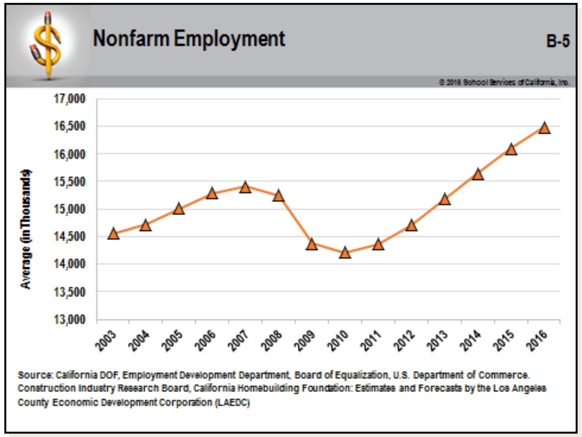
Economic Cycles & Probability Curves

Business Cycle Model

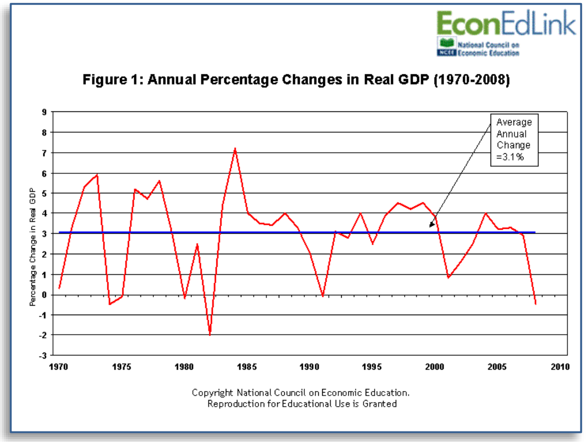


School Services of California, 2016

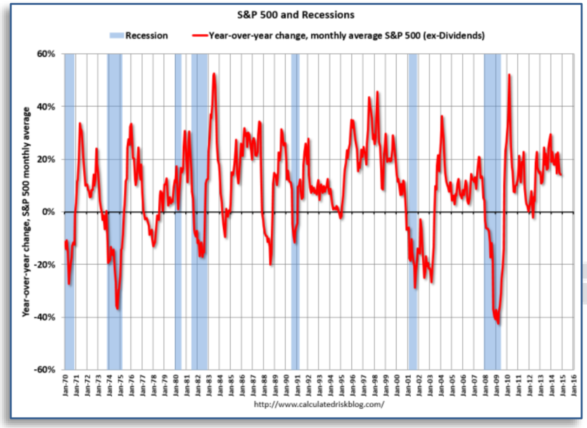


Unemployment Rate

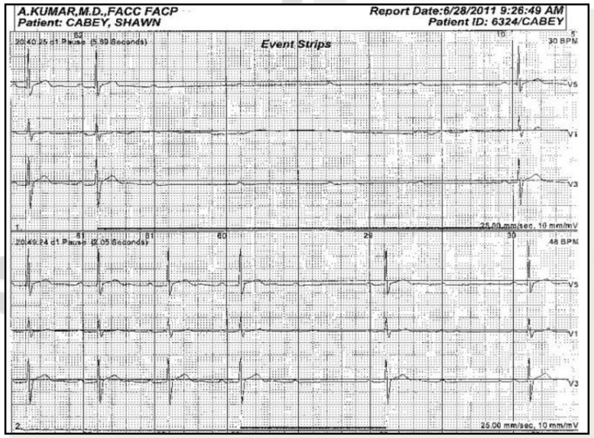
Real Gross Domestic Product



Stock Market Performance



Shawn's Heartbeat



The Fallout From Fallout

the practical meaning of “fallout” in budgeting

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fall·out

[fôl' out] n., pl.

1. revenue remaining in excess of that which was anticipated in the budget to be expended [the for-profit business enterprise equivalent of "Net Income"]

	"Fallout"		"No Fallout"	
	Budget	**Actual**	**Budget**	**Actual**
Revenues	$1,000.00	$1,100.00	$800.00	$900.00
Expenses	$900.00	$800.00	$1,100.00	$1,000.00
Surplus/(Deficit)	**$100.00**	**$300.00**	**($300.00)**	**($100.00)**

"Fallout" = $200

($200 additional dollars more than previously anticipated)

"Fallout" = $0

(No additional dollars, only less severe loss than previously anticipated)

fall·out

[fôl’ out] n., pl.

2. any variance in year-end closing position that deviates positively from the closing position anticipated in the previous budget. [includes losses not as large as projected]

	"Fallout"		"Also Fallout"	
	Budget	**Actual**	**Budget**	**Actual**
Revenues	$1,000.00	$1,100.00	$800.00	$900.00
Expenses	$900.00	$800.00	$1,100.00	$1,000.00
Surplus/(Deficit)	**$100.00**	**$300.00**	**($300.00)**	**($100.00)**
	“Fallout” = $200		**“Fallout” = $200**	
	($200 additional dollars more than previously anticipated)		($200 “additional dollars”, because **loss is less severe** than originally anticipated)	

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WUSD Historical Variance: Adopted Budget vs. Certified Audited Financial Statement

General Fund	Surplus/Deficit @ Adopted Budget	Surplus/Deficit @ Year-End Audit	Difference	Revenue (Audit Rpt)	% of Revenue	Expenses (Audit Rpt)	% of Expenses
2006-2007	$ 3,813,376	$5,632,042	$1,818,666	$61,879,315	2.9%	$56,247,273	3.2%
2007-2008	$ (215,976)	$950,569	$1,166,545	$63,217,678	1.8%	$62,267,109	1.9%
2008-2009	$ 25,292	$2,577,273	$2,551,981	$61,353,545	4.2%	$58,776,272	4.3%
2009-2010	$ (4,867,487)	-$995,527	$3,871,960	$55,544,953	7.0%	$56,540,480	6.8%
2010-2011	$ (3,565,532)	$1,367,812	$4,933,344	$56,491,412	8.7%	$55,123,600	8.9%
2011-2012	$ (5,327,991)	-$539,114	$4,788,877	$56,418,668	8.5%	$56,957,812	8.4%
2012-2013	$ (7,888,050)	-$4,372,928	$3,515,122	$55,314,856	6.4%	$59,687,784	5.9%
2013-2014	$ (3,595,829)	-$939,204	$2,656,625	$62,231,226	4.3%	$63,170,430	4.2%
2014-2015	$ (4,334,723)	-$820,832	$3,513,891	$68,828,190	5.1%	$69,649,022	5.0%

$2,860,091 **$28,817,011**

fall·out
[fôl' out] n., pl.
1. revenue remaining in excess of that which was anticipated in the budget to be expended [the for-profit business enterprise equivalent of "Net Income"]

fall·out
[fôl' out] n., pl.
2. any variance in year-end closing position that deviates positively from the closing position anticipated in the previous budget. [includes losses not as large as projected]

Sum of Surpluses/Deficits: $2,860,091

Average $ Variance: $317,788

% of Average Expenses: 0.5%

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Final Thoughts

Administrative Services believes that if fiscal policy were based solely upon economic factors aligned with a rational expectations macro-economic probability curve, decisions involving financial commitments that affect the long-term solvency of the District would most appropriately be evaluated with an **8-12 year Multi-Year Projection that incorporated anticipated fluctuations in the business cycle**.

TRANSLATION: A less-than-36-month look ahead (AB1200 MYP) that completely ignores the wild (but nevertheless largely predictable) ups & downs of business cycles, State revenues and funding is not only not good planning, it's not even good gambling!

That said, the District understands that mathematics and economics do not account for the social and political considerations that appropriately must also be factored into decisions regarding the District's expenditures.

Thank You.