

Fiscal
& Crisis
Management
Assistance
Team

San Francisco Unified School District

*Comprehensive Fiscal
Assessment*

April 17, 2000

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San Francisco Unified School District

Comprehensive Fiscal Assessment

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Preface

The San Francisco Unified School District has a diverse student population of approximately 64,000 students attending 115 schools. The school district's budget serving that student population is nearly \$500 million.

During the last two fiscal years, there has been a growing lack of confidence expressed by state and local legislators regarding the district's financial condition and fiscal practices. As a result, the Fiscal Crisis and Management Assistance Team (FCMAT) was commissioned by the Superintendent of Public Instruction to conduct a comprehensive fiscal assessment of the district. Funding for the assessment was appropriated by the Governor as a part of the 1999 Budget Act.

FCMAT began the comprehensive assessment in July 1999 and ended in April 2000. The assessment represents a comprehensive view of the district's fiscal condition and practices during that period. Assisted by both private and public experts in financial management, FCMAT reviewed current district fiscal practices and the financial health of the district. Although the district is financially solvent for the current year, there are serious questions regarding the capability of the district to prudently manage its resources and hold true to its fiduciary responsibility to its citizens. Those most affected by this condition are the students and staff of the San Francisco Unified School District. The district's future as a viable, effective organization, charged with the education our youth, rests with its ability to address these issues.

FCMAT is optimistic that the report's recommendations will be embraced by both the administration and governing board. The Interim Superintendent and the Board's leadership have been supportive of FCMAT's assessment and have expressed a commitment to the report's recommendations. In the coming months, the Board and administration will need to prioritize the recommendations, redirect resources for implementation, and focus on accountability. Therein lies the greatest opportunity for success.

Introduction and Historical Background

The purpose of the following report is to provide the Superintendent of Public Instruction (SPI), the San Francisco Unified School District and other interested stakeholders with the findings and recommendations from the Fiscal Crisis and Management Assistance Team's (FCMAT) comprehensive independent external assessment. That assessment was based on existing legal and professional standards applicable to all California public school districts. The assessment focused on three major areas:

- Internal controls.
- District's use of technology.
- Multi-year projections to determine solvency for the current and two subsequent years.

Of primary importance to the Superintendent of Public Instruction was the district's fiscal condition. Stated concerns included the district's recent trend of deficit spending, its reliance on restricted funding to balance its books, and a growing lack of confidence expressed by legislators in regard to the district's financial condition. As a result, the SPI requested the FCMAT to assess the district's financial condition.

Additionally, the Governor, in his July 1999 budget language, requested FCMAT to conduct a comprehensive review of the district's financial condition and to submit this report to the Superintendent of Public Instruction, State's Director of Finance, Secretary for Education and the district. The Governor required that the review include an assessment of whether the district is capable of meeting its fiscal obligations for the current and two subsequent fiscal years. The Governor's language also required FCMAT to incorporate data from the closing of the 1998-99 fiscal books. This charge and responsibility set out by the Governor and the SPI provided for the scope of the FCMAT study.

Study Team

The study team was composed of the following members.

General Report

Thomas E. Henry, FCMAT Chief Administrative Officer

Internal Control Review

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Technology Review

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Multi-year Projection

Anthony Bridges, FCMAT Director of Management Assistance

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*As members of this study team, these consultants were not representing their respective employers but were working solely as independent contractors for FCMAT.

Executive Summary

During the course of the FCMAT study, the San Francisco Unified School District continued to experience fiscal uncertainty. The district's 1998-99 books should have been closed by October 1999. They were not officially closed until January 2000. The district's external audit report was due to the Superintendent of Public Instruction and the State Controller no later than December 15, 1999. The district requested from the State Controller an extension to March 31, 2000. The external audit was filed on that date. Due to the condition of the financial records and the inability to close the books in a reasonable time period, FCMAT believed that the district demonstrated a lack of "Going Concern." On November 19, 1999, FCMAT recommended that the SPI assign a fiscal expert to advise the county office/district of its financial condition. In December 1999, pursuant to Education Code Sections 1630 (a) and 42131 (f), the SPI appointed FCMAT as fiscal expert to advise and assist the district in the preparation of its fiscal reports. Among FCMAT's primary responsibilities was assisting the district in the closing of its 1998-99 books, conducting the multi-year projections, and the completion of the internal control review and management information system review.

The findings of the FCMAT report indicate that the district is having great difficulty in meeting basic industry and legal standards relative to the district's financial operations and that the district's management information system functions at an unacceptably low level. FCMAT believes that these circumstances require immediate attention from the district. The internal control weaknesses are particularly serious. The report includes a complete list of the specific findings and recommendations. The following is a summary of the general findings and recommendations.

Material Internal Control Weaknesses

A **Material Weakness** is a deficiency in an internal control so serious that errors or fraud may occur. Because of the weakness, employees in the normal course of business may not detect the errors within a timely period. A material weakness also may be a violation of laws or regulations. In the course of the study, FCMAT identified twenty-four areas as having material weaknesses.

A **Reportable Condition** is a significant deficiency in the design or operation of an internal control that could adversely affect the district's ability to record, process, summarize, and report financial data. FCMAT identified eighteen areas as having a reportable condition.

A **Management Improvement** is a suggestion for improving the operations of the district to conform to the best practices within the school district. FCMAT identified thirteen areas requiring management improvement. There are significant weaknesses in the internal control environment that increase the likelihood for fraud or abuse to occur.

Inadequately Trained District Office Accounting and Budgeting Support Staff

Staff members in key positions do not possess the necessary skills to perform competently at the level they are assigned. The Board of Education is not receiving adequate financial information and in some instances the staff has not submitted the legally required documents to the board for approval. The necessary skill level, training and leadership have not been demonstrated to ensure that the district's financial information will be accurate and timely. The district's books were not closed until January 2000 for the 1998-99 year. Most school districts in the state close by the middle of September. The budget office staff has not performed any significant monitoring for the 1999-00 budget.

Inadequate Documentation for Accounting Transactions

The district's fiscal year-end closing checklist used to monitor the closing did not have any entries on the checklist to indicate that any steps in the year-end closing had been completed. Records are not maintained in an orderly manner and it is often difficult to find support for the district's transactions. This pattern has led to numerous errors in the closing entries for federal and state programs.

A Minimally Functioning Management Information System

One of the more critical issues facing the district is the low functioning level of its management information system. The system's general ledger barely functions, with only one general ledger report available. Other necessary system functions either function at low levels or have never been implemented. The district needs timely, reliable, and accurate information in order to manage a nearly \$500 million operation. For the 1998-99 fiscal year, the district was late closing its books, completing its annual audit, and preparing state mandated reports for the 1999-2000 fiscal year. If the district does not improve the level at which its information system operates, it can anticipate similar difficulties in the future.

The district's external auditors noted problems with the internal system security in the 1998-99 audits. User access privileges to salary and budget information was not limited to key personnel in the Human Resources and Budget Departments. FCMAT also verified that staff in the payroll department could change the information on the pay screen for any employee without a checks and balance system in place. This breach in security increases the risk of generating fraudulent checks.

The district's current information systems are performing at levels far below what is needed to support the district's objectives and mission. There is a lack of continuity in district leadership and clarity of purpose. The lack of adequate staff development was encountered consistently during the review, and the district offered no clear path for training to raise the systems users' competence.

Multi-year Projections to Determine Solvency

One of the main components of FCMAT's assessment was to prepare a multi-year financial projection to evaluate the financial solvency of the district for the current and three subse-

quent fiscal years. There are inherent limitations with any forecasting model, and FCMAT has been careful to consider certain criteria and budget assumptions while preparing the projections.

The multi-year financial projection forecasts a positive ending balance that exceeds the district's required two percent reserve requirement. The projections do not reflect any salary increases. Any adjustments to the salary or benefit categories will compound the current expenditures projected and would have an impact on the free balance depicted in the bottom line of the projections. The enrollment trends demonstrate a slight decline in each year of the projections. This enrollment trend, coupled with any modest salary increase, could place the district in a precarious fiscal position. Accordingly, the district should update these projections at each Interim report or at any time the assumptions change.

