SUPPLEMENT #1 (2009)
INTRODUCTION TO FISCAL RESPONSIBILITIES

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Can California's Community Colleges Survive?

"Black Is the night against the back of my neck, red is the abyss coloring my face. The crash of falling walls are drowned out by the beat of my heart growing louder and faster as I draw nearer to the abyss."

Peering over the edge into the abyss of pending financial disasters for our California Community Colleges is scary but necessary. California's financial disaster added to the national economic recession has created a situation whereby many of the California community colleges face a financial disaster. The probable continued reduction in state and local funding compounded by increased costs for employee benefits, insurance, utilities, etc. and the demand by more students to enroll will place our colleges on the edge of the abyss if not already falling into the darkness. This paper is intended to assist Trustees in their understanding of their situation and to offer suggestions on how to create opportunities for improvement.

The problems affecting the major source of funding for community colleges in California include the following:

1. State Funding.

   The largest revenue source for most community colleges in California is state funding. The depressed economy and projected slow economic recovery will translate into reduced state funding into at least the next three to five years at a minimum. In addition, the political division and inability of the Governor and the State Legislature to agree on a common and effective budget resolution will also continue in the foreseeable future. The impact of these two factors will mean that budgets for most community colleges will continue to diminish.

2. Local Property Tax Revenues

   Another large revenue source for our colleges is Property Taxes. As we are all aware, the home mortgage meltdown and associated falling property values has resulted in either decreased or flat property tax revenues throughout the state. The full impact of this economic problem has not yet occurred and as such property tax revenues will not rise in the immediate future or if there is an increase it will not be sufficient to offset the lost state revenues or cover the increased costs of operation.

3. Increased Expenses

a. The cost of manpower will continue to rise due to wage agreements with employee organizations as well as step and column pay increases incorporated in many of our existing pay employee schedules. In addition, the costs for various employee benefits will continue to increase as examplified by the cost increases in the past few years for employee health insurance.
b. The cost of liability coverage (insurance) for unemployment, risk liability and workers compensation will continue to increase.
c. The burden on funding the unfunded liability of retirees' health insurance for many of our districts will continue to increase as we see an increase in the percentage of employees retiring at a younger age due to incentive buyouts and/or more stressful work conditions. Trustees can expect to be challenged with the request to terminate funding this liability due to the large cost (and the money being placed in a reserve) in place of keeping people working.

4. Local Funding Decisions

The commitment by some Boards to fund employee salaries and benefits in an amount greater than 85% (the 2007/08 statewide average) of the District's annual revenues has placed such Districts on thin financial ice. Preliminary data for 2008/09 and 2009/10 college budgets indicates that the statewide average is increasing with a number of colleges exceeding 90% of current revenues being allocated to staff salaries and benefits.

Potential Solutions:

1. Board of Trustees Reviews and Cost reduction Ideas:

Given the financial problems affecting all public sector agencies, it is necessary for Board of Trustees to not only be aware of the problems mentioned above, but to look at possible solutions to these problems. The following ideas are just that--ideas which Boards can pick and choose from as they peer into the abyss of how to continue with our core programs in a period of great fiscal constraint. Not all of these ideas will work in all situations or at all of our colleges. Some of these concepts and ideas are easy to implement while others are not and would require a great deal of analysis and consideration before they are implemented. It also needs to be recognized that the ideas regarding personnel are not easy to contemplate but may be necessary to do so if our core programs are to be kept intact.

While working with less money is never desirable, Districts need to use this as an opportunity to focus their District's funding on the core services associated with their institutions and needed by their communities. It will be necessary for Boards to identify and bring focus to the programs that are at the core of the College's mission. A review of the District's mission statement and clarification of which programs support the District's mission and which do not should be accomplished early on in the process. In addition, the Board may wish to review the associated Board policies regarding such issues as Board expenses, Board travel, any budget policies and align these with the Board's mission statement and budget prioritization. Other potential cost areas that could be reviewed are the District's level of legal expenditures and the District's administrative functions in order to determine if any may be privatized or in the case of insurance policies to determine which may be eliminated and/or reduced. Another administrative effort that could be undertaken is to establish a process mapping effort for all District functions in order to determine where cost savings may be able to occur.

Other cost savings ideas:

- A Two or three year look-ahead budgets: Too often Boards do not look beyond the year in which a given budget is adopted but we do have much information and data which can give us reasonable projections about the next two to three years and it behooves Boards to peer into the future, as it were, to make those preliminary decisions which will keep Districts from having to make drastic (and perhaps, unwise) decisions with regard to budgetary matters. Trustees can gain a better understanding of what the future may hold and thus better understand the types of financial decisions they need to make in the current year.

- Audit Reviews & Recommendations. The District's auditors are responsible to the Board of Trustees and as such, the Board can utilize their services to evaluate the financial impacts of past budget decisions.

- Employee reductions through incentives to retire employees rather than by layoffs of employees. Colleges can control their costs and the program areas to be reduced by offering employees either college wide or in specific programs an incentive to retire. As an example, offering employees a one time payment of $1,000 per year of service to a maximum of $25,000 to retire on or before the next fiscal year. The incentive for the College is that the cost can be made up quickly thru salary savings.

- Four day work week on a college wide basis. The reduction in the number of days the campus is operational will reduce utility costs among other operational expenses. Colleges that have other colleges nearby could consider staggering the days each is closed in order to allow students to take classes in both institutions on the days most convenient for them.

- Identify and implement new fees such as a student fee to audit classes as it may be feasible to charge fees to those students who take a class for self-satisfaction and not to earn a grade. Or consider an additional fee for late registration due to class sizes increasing it may be feasible to charge those who register late after a certain date. Another fee alternative is to increase charging for GED testing in those Districts which allow for the GEDs as it might be feasible to increase the charges which Districts presently use for such testing in order to recoup the real costs to the District.

- The statewide average in the 2007/08 fiscal year for salaries and benefits was close to 85% of the District's annual expenditures. As such, Boards need to consider various tactics on how to reduce such expenditures. One idea is to consider delaying the replacement of full-time faculty who retire or resign and hire full-time replacements only in rare circumstances and possibly for a limited contract period. Another alternative is to furnish substitute teachers only under certain conditions. Since our students need paid employment, Boards should consider using students rather than full-time employees whenever feasible.

- Enrollment management: increase average class size in order to improve efficiency of use of faculty per student. Smaller class sizes are not proven to positively affect student outcomes in all programs. Therefore, it is important for the District to determine if, in certain classes, the class size can be increased without diminishing learning to increase the Weekly Student Contact Hours generated by the faculty and thus increase productivity and revenues.

- Establish target enrollments by semester, involve faculty more in student recruitment.

- Additional acquisition of Federal and State Funds. Districts should pursue Title III funds if eligible and reward those individuals who secure such funds (the most recent Chronicle of Higher Education has an article about this). Also consider using a staff development day for grant-writing training to educate faculty members in how to apply for federal funding in their area of expertise. Another potential area is CAL-OSHA and Federal OSHA as their requirements may lend themselves to allocating Federal funding to carry out these requirements.

- Develop potential partnerships by asking faculty and staff to work with local businesses to see if they can help the District in any of way, or partner with your service area K -12 Districts, State and private universities in order to form coalitions to reduce costs or generate additional income, and finally to work with institutions and cities in foreign countries to increase the number of international students attending your local college.

2. Potential revenue sources requiring state legislation

a. Special fees. Our colleges are precluded from establishing fees for special services or for technological support. Colleges in other states are permitted to establish technology fees to help maintain and improve the technological infrastructure of their institutions. Colleges which provide free transit services for students to access the colleges are precluded from controlling their own fee structure in order to generate sufficient fees to cover such expenses.

b. Potential Parcel tax relief. Colleges could be allowed to establish specific parcel taxes for local revenue with a 55% majority vote if the State would approve such legislation changing the voter approval limit from 67% to 55%.

c. Contracting out for ancillary services such as food services and bookstore services. For those colleges that have traditionally utilized college staff to operate ancillary services such as cafeterias or bookstores, the colleges cannot contract out for such services and reduce their costs due to existing law.

3. FCMAT Assistance

In 1991 AB 1200 was signed into law and created a new State program, the Fiscal Crisis Management Assistant Team (FCMAT) to assist K -12 school districts which had financial and/or governance problems. In 2006 the law was amended to allow FCMAT to assist community college districts having such problems. Trustees have at this assistance at their disposal should the District's administration and the Board agree such assistance would be beneficial. The advice can include suggestions on how to improve cash flow, reserve commitments, accounting procedures and practices, and budget allocations. Boards can use such suggestions to improve their financial operations and to restructure their budgets in order to preserve more capital for education.

Potential Repercussions for failure to resolve financial matters:

4. **State Takeover**: In dire situations when a District is unable to resolve its financial problems and fails to retain a positive cash flow, the District could be taken over by the State Chancellor's Office. The questionnaire attached to this paper (see Exhibit A) is used by the Chancellor's Office to evaluate a District's financial situation. A Board can also use this questionnaire as part of their annual audit process and have a discussion with the administration to determine the vitality of the District's financial situation. The Chancellor, in accordance with California Code of Regulations Title 5 Sections 58312 et seq., has the authority to take any of the following actions at district expense:
    a. Conduct a comprehensive management review of the district and its educational programs and an audit of the financial condition of the district.
    b. Direct the district to amend and readopt the fiscal and educational plans prepared pursuant to CCR T5 Section 58310 based on the findings of the comprehensive audits.
    c. Direct outside fiscal crisis intervention assistance from FCMAT, other specialized external assistance and/or through the appointment of a Special Trustee to help address the fiscal concerns and to assist with the district's recovery.
    d. Assign a Special Trustee to assume management and fiscal control of the district to the extent deemed necessary in order to achieve fiscal stability or solvency and also implement the principles of sound fiscal management. Such a step removes the authority of the Board of Trustees and the District's Superintendent (President or Chancellor) to lead the District and instead focuses all such powers onto the Special trustee appointed by the state. Such a trustee can impose strict financial requirements and changes in order to try to restructure the financial program of the District. Additional state funding may be provided in the

form of a loan and must be repaid in the future by the District. Such a situation may also place the District on a warning status with WASC and the loss of accreditation is a possibility. For these reasons a state takeover should be avoided if at all possible.

5. District Mergers/J.P.A.'s

   As financially troubled Districts are taken over by the State, there may be an associated attempt to have more fiscally sound Districts "take over" or "merge" the District in trouble. There has been very limited experience in this situation and numerous operational problems arose and caused both Districts trouble. A more viable alternative may be for Districts close in proximity to each other to form Joint Powers Authorities to provide administrative functions such an accounting services, warehouse, or purchasing, etc. in order to reduce costs. Districts located in rural portions of the state may need to seek such agreements with local K-12 districts and/or university systems.

6. Bankruptcy

   Districts in our state do not have the legal authority to declare bankruptcy and restructure their debt and/or contractual obligations. The State prevents such an action by first stepping in and assuming control of the District.

Conclusions:

The State is near a financial disaster and is being drawn closer as local school districts and community college districts fail in their attempts to control their financial problems. Trustees need to acknowledge when their District is in financial trouble and seek assistance as early as practical. Once the Trustees have received recommendations on actions to be taken to resolve their financial problems, the trustees need to implement such changes as quickly as practical. Further, Trustees may need to reduce the broad scope of services the District is now providing and refocus its resources on the critical few programs that are at the core of their mission. Finally, it is time for Trustees to increase their political influence and hold the state legislators accountable to resolving the state's financial problems for the good of us all.

EXHIBIT "A"

California Community Colleges
Sound Fiscal Management
Self-Assessment Checklist

1. **Deficit Spending -** Is this area acceptable? **Yes / No**
Is the district spending within their revenue budget in the current year?
Has the district controlled deficit spending over multiple years?
Is deficit spending addressed by fund balance, ongoing revenue increases, or expenditure reductions?
Are district revenue estimates based upon past history?
Does the district automatically build in growth revenue estimates?

2. **Fund Balance** – Is this area acceptable? **Yes / No**
Is the district's fund balance stable or consistently increasing?
Is the fund balance increasing due to on-going revenue increases and/or expenditure reductions?

3. **Enrollment -** Is this area acceptable? **Yes / No**
Has the district's enrollment been increasing or stable for multiple years?
Are the district's enrollment projections updated at least semiannually?
Are staffing adjustments consistent with the enrollment trends?
Does the district analyze enrollment and full time equivalent students (FTES) data?
Does the district track historical data to establish future trends between P-1 and annual for projection purposes?
Has the district avoided stabilization funding?

4. **Unrestricted General Fund Balance** – Is this area acceptable? **Yes / No**
Is the district's unrestricted general fund balance consistently maintained at or above the recommended minimum prudent level (5% of the total unrestricted general fund expenditures)?
Is the district's unrestricted fund balance maintained throughout the year?

5. **Cash Flow Borrowing -** Is this area acceptable? **Yes / No**
Can the district manage its cash flow without interfund borrowing?
Is the district repaying TRANS and/or borrowed funds within the required statutory period?

6. **Bargaining Agreements -** Is this area acceptable? **Yes / No**
Has the district settled bargaining agreements within new revenue sources during the past three years?
Did the district conduct a pre-settlement analysis identifying an ongoing revenue source to support the agreement?
Did the district correctly identify the related costs?
Did the district address budget reductions necessary to sustain the total compensation increase?

7. **Unrestricted General Fund Staffing -** Is this area acceptable? **Yes / No**
Is the district ensuring it is not using one-time funds to pay for permanent staff or other ongoing expenses?
Is the percentage of district general fund budget allocated to salaries and benefits at or less than the statewide average (i.e. the statewide average for 2003-04 is 85%)?

8. **Internal Controls** - Is this area acceptable? **Yes / No**
Does the district have adequate internal controls to insure the integrity of the general ledger?
Does the district have adequate internal controls to safeguard the district's assets?

9. **Management Information Systems -** Is this area acceptable? **Yes / No**
Is the district data accurate and timely?
Are the county and state reports filed in a timely manner?
Are key fiscal reports readily available and understandable?

10. **Position Control** – Is this area acceptable? **Yes / No**
Is position control integrated with payroll?
Does the district control unauthorized hiring?
Does the district have controls over part-time academic staff hiring?

11. **Budget Monitoring** - Is this area acceptable? **Yes / No**
Is there sufficient consideration to the budget, related to long-term bargaining agreements?
Are budget revisions completed in a timely manner?
Does the district openly discuss the impact of budget revisions at the board level?
Are budget revisions made or confirmed by the board in a timely manner after the collective bargaining agreements are ratified?
Has the district's long-term debt decreased from the prior fiscal year?
Has the district identified the repayment sources for the long-term debt?
Does the district compile annualized revenue and expenditure projections throughout the year?

12. **Retiree Health Benefits -** Is this area acceptable? **Yes / No**
Has the district completed an actuarial calculation to determine the unfunded liability?
Does the district have a plan for addressing the retiree benefits liabilities?

13. **Leadership/Stability** - Is this area acceptable? **Yes / No**
Has the district experienced recent turnover in its management team (including the Chief Executive Officer, Chief Business Officer, and Board of Trustees)?

14. **District Liability** – Is this area acceptable? **Yes / No**
Has the district performed the proper legal analysis regarding potential lawsuits that may require the district to maintain increased reserve levels?
Has the district set up contingent liabilities for anticipated settlements, legal fees, etc?

15. **Reporting** – Is this area acceptable? **Yes / No**

Has the district filed the annual audit report with the System Office on a timely basis?

Has the district taken appropriate actions to address material findings cited in their annual audit report?

Has the district met the requirements of the 50 percent law?

Have the Quarterly Financial Status Reports (CCFS-311Q), Annual Financial and Budget Reports (CCFS-311), and Apportionment Attendance Reports (CCFS-320) been submitted to the System Office on or before the stated deadlines?