

The Fiscal Crisis and Management Assistance Team:

*Its Recommendations, if Implemented,
Should Help Financially Troubled
School Districts*



June 2004
2003-129

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June 16, 2004

2003-129

The Governor of California
President pro Tempore of the Senate
Speaker of the Assembly
State Capitol
Sacramento, California 95814

Dear Governor and Legislative Leaders:

As requested by the Joint Legislative Audit Committee, the Bureau of State Audits presents its audit report concerning the effectiveness of the Fiscal Crisis and Management Assistance Team (FCMAT).

This report concludes that FCMAT's recommendations, if implemented, should help financially troubled school districts improve their financial conditions. Although all of the school districts we reviewed appeared to have implemented or partially implemented some of the recommendations we selected to review, many of them continue to experience financial problems. Full recovery can take several years, depending on the nature and severity of a district's problems. Since its formation, FCMAT's scope of responsibilities has significantly expanded, primarily as a result of legislation, to include comprehensive reviews and periodic progress reports of specific school districts that received state emergency loans, and projects such as the California School Information Services system, which is an electronic statewide system that facilitates the exchange of student information. FCMAT's studies cost an average of \$3.1 million annually for fiscal years 2000-01 through 2002-03, including \$2.1 million per year for management assistance studies and \$1 million per year for comprehensive reviews as mandated by legislation. Its billing rate of \$400 per person per day spent working on site at school districts and county education offices is on the low end of what FCMAT pays its consultants, which is consistent with FCMAT's understanding that the Legislature intended it to assist financially troubled school districts to avert a financial crisis, such as bankruptcy. Finally, FCMAT's administrative costs appear reasonable and although FCMAT is not subject to competitive bidding rules, it uses a fair process for selecting consultants for its large comprehensive reviews of school districts.

Respectfully submitted,

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CONTENTS

<i>Summary</i>	1
<i>Introduction</i>	5
<i>Audit Results</i>	
The Fiscal Crisis and Management Assistance Team Provides Valuable Advice to Troubled School Districts	19
FCMAT's Consultant Selection Process Is Fair, but Improvements Can Be Made	31
FCMAT Has Good Reasons to Keep Its Billing Rate Artificially Low	33
FCMAT's Administrative Costs Appear Reasonable	34
Recommendations	37
<i>Response to the Audit</i>	
Kern County Superintendent of Schools	39

SUMMARY

Audit Highlights . . .

Our review of the Fiscal Crisis and Management Assistance Team (FCMAT) disclosed:

- FCMAT's reports include recommendations that are valuable and should help improve the financial health of school districts.*
 - Most of the school districts we reviewed have implemented or partially implemented many of FCMAT's recommendations.*
 - Fiscal recovery of a school district can take several years depending on the nature and severity of its problems.*
 - Since its formation, FCMAT's responsibilities have expanded, primarily as a result of legislation.*
 - FCMAT's process for selecting consultants to work on its large comprehensive reviews is fair, but FCMAT can improve by sending application packets to a larger group of consultants.*
 - FCMAT's governing board has good reasons to keep the rate FCMAT bills school districts low.*
 - The percentage of FCMAT's administrative and overhead costs seems reasonable.*
-

RESULTS IN BRIEF

The Fiscal Crisis and Management Assistance Team (FCMAT) provides fiscal and management assistance services to county offices of education (county offices) and school districts. The Legislature authorized the creation of FCMAT in 1991 when it passed Assembly Bill 1200 (Chapter 1213, Statutes of 1991). This law provided county offices with tools to oversee the fiscal health of the school districts under their purview. One of these tools was the ability to request FCMAT's assistance at troubled school districts.

Since FCMAT's inception, it has completed 369 school district studies and other services, including acting as a fiscal adviser to school districts and county offices and assisting the State Superintendent of Public Instruction. Although helping California's local educational agencies fulfill their financial and management responsibilities continues to be FCMAT's main purpose, its responsibilities have grown over the years, almost exclusively as the result of other legislation, to include preparing comprehensive assessments and recovery plans for four of the six school districts that received emergency loans from the State, facilitating fiscal training for county offices and school districts, and developing and maintaining two separate statewide information systems.

Our review of FCMAT's involvement at 10 school districts revealed that FCMAT provides findings and recommendations that are valuable and should help improve the financial health of school districts. All of the school districts we reviewed appeared to have implemented or partially implemented some of the recommendations we selected to review, although due to various factors, including the severity and nature of their problems, several of them continue to experience financial difficulties. Because FCMAT's recommendations are standards-based, they have resulted in improved practices, which can lead to improved overall fiscal health for the school districts that implemented them. However, FCMAT's recommendations can be effective only if school districts take action on them. School districts are not required to implement FCMAT's

recommendations and, except for those districts that received emergency loans, FCMAT is not required to report the progress the districts make in implementing its recommendations.

Additionally, staff at some of the school districts believe that having FCMAT as an independent, external consultant added credibility to the problems they faced and the solutions they proposed to their communities and governing boards. This credibility helped the districts make difficult but necessary decisions, such as reducing spending for transportation and special education programs.

FCMAT has a list of nearly 70 consultants it can use on any given request for management assistance services to school districts. Although it is not subject to state contracting laws, which would require it to use a competitive bid process to select its consultants, FCMAT requests bids when contracting for consultant services for its bigger comprehensive studies, such as for the Compton Unified School District and Oakland Unified School District. Generally, FCMAT's contracting process appears fair, although it could invite more consultants to bid on these jobs, providing it with a broader group of experts from which to choose.

To offset some of the costs of performing management assistance studies, the Legislature authorized FCMAT to charge school districts that are not declared as fiscal emergencies a daily rate for these services. Currently, FCMAT's governing board has approved a \$400 rate per team member for every day that FCMAT or its consultants are on site at the districts. This rate is on the low end of what FCMAT pays its consultants for these services, but it appears reasonable given FCMAT's understanding that the Legislature intended FCMAT to assist financially troubled school districts to head off financial crises, such as bankruptcy, thereby avoiding the need for emergency loans from the State. FCMAT generally does not bill school districts that have received state emergency loans or that FCMAT's board has designated as being in a fiscal emergency for its services. Rather, the State pays FCMAT's costs in such cases, either through FCMAT's annual appropriation for management assistance studies or through separate appropriations specific to particular school districts.

For the three fiscal years 2000–01 through 2002–03, FCMAT's studies cost an average of \$3.1 million annually, including \$2.1 million per year for management assistance studies and an average of \$1 million during each of the three fiscal years

for comprehensive studies of school districts as mandated by legislation. Of the \$2.1 million, it billed approximately \$632,000, or 31 percent of its average costs per year, to the school districts that received the services. Also during this period, FCMAT spent, on average, \$419,000 per year, or 13.5 percent of the \$3.1 million, on administrative costs, including costs for office space, utilities, office supplies and equipment, and other costs not directly associated with its studies.

We noted that the administrative costs do not include the portion of two managers' salaries that is related to administrative duties, such as approving staff time sheets and attending FCMAT's board meetings. However, it is not likely that including the portion of their salaries associated with performing those tasks would cause FCMAT's total administrative costs to exceed a reasonable proportion of the total costs. Further, given the small size of FCMAT, it is reasonable that its administrative costs, most of which would remain the same regardless of the number of studies it performs, represent a higher proportion of its total costs when compared to larger organizations because FCMAT cannot benefit from the economies of scale that large organizations enjoy.

Finally, according to its bylaws, the FCMAT governing board provides policy direction and broad operational guidance to the Kern County Superintendent of Schools (Kern superintendent's office), which houses and administers FCMAT. The FCMAT governing board meets quarterly to discuss topics including FCMAT's reports, to prioritize requests for FCMAT's assistance, and to oversee its projects.

As one of several divisions of the Kern superintendent's office, FCMAT is subject to the same administrative policies and procedures as other divisions within that office. Through its other divisions, the Kern superintendent's office handles certain administrative aspects of FCMAT's operations, such as providing personnel and information technology support services.

RECOMMENDATIONS

To obtain the broadest range of consultants to choose from, FCMAT should expand its list of consultants who receive request for application packets.

AGENCY COMMENTS

FCMAT agrees with our findings and recommendations and will develop, in coordination with its governing board, a corrective action plan for the two recommendations. ■

INTRODUCTION

BACKGROUND

In September 1991, the Legislature passed Assembly Bill 1200 (Chapter 1213, Statutes of 1991), which authorized the creation of the Fiscal Crisis and Management Assistance Team (FCMAT) and established its governing board. The legislation also expanded the responsibility and authority of the county offices of education (county offices) in monitoring their school districts' budgets and required county offices to intervene under certain circumstances to ensure that the districts meet their financial obligations. The Legislature passed this law in part to establish accountability standards, but also to address concerns arising from the bankruptcy of the Richmond Unified School District, now the West Contra Costa Unified School District (West Contra Costa), and the financial collapse of other school districts that were preparing to seek emergency loans from the State. The Legislature envisioned FCMAT as a service to help local educational agencies meet their fiscal accountability standards.

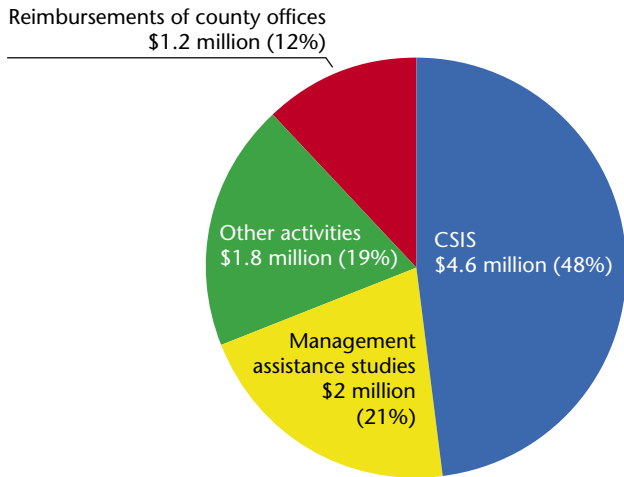
FCMAT's enabling legislation requires it to operate under the immediate direction of an appropriate county office selected jointly, through an application process, by the State Superintendent of Public Instruction (state superintendent) and the State Secretary of Child Development and Education (education secretary). According to FCMAT's annual report for fiscal year 2002–03, four county offices submitted applications, and the state superintendent and education secretary awarded the FCMAT contract to the Kern County Superintendent of Schools (Kern superintendent's office), which signed a contract in June 1992 with the Department of Education.

From FCMAT's inception through fiscal year 2003–04, the Legislature's annual appropriation to the Kern superintendent's office to fund FCMAT's management assistance has increased from \$500,000 to \$2 million. In total, the State allocated more than \$9.6 million to the Kern superintendent's office to fund all of FCMAT's operations in fiscal year 2003–04. Of that amount, the Legislature appropriated more than \$4.6 million for FCMAT's operation of the California School Information Services system (CSIS), \$2 million for FCMAT's provision of management assistance, nearly \$1.2 million for FCMAT to reimburse county offices for performing their enhanced responsibilities, and more

than \$1.8 million for FCMAT’s other responsibilities. These other responsibilities include the administration of the Education Data Partnership, which provides financial and demographic data and allows the sharing of that data among stakeholders; the professional development of district and county office business officials; and FCMAT’s ongoing studies at the Compton and Oakland unified school districts. Figure 1 shows the breakdown of FCMAT’s appropriations for fiscal year 2003–04.

FIGURE 1

**Breakdown of FCMAT’s Appropriations
Fiscal Year 2003–04**



Source: FCMAT.

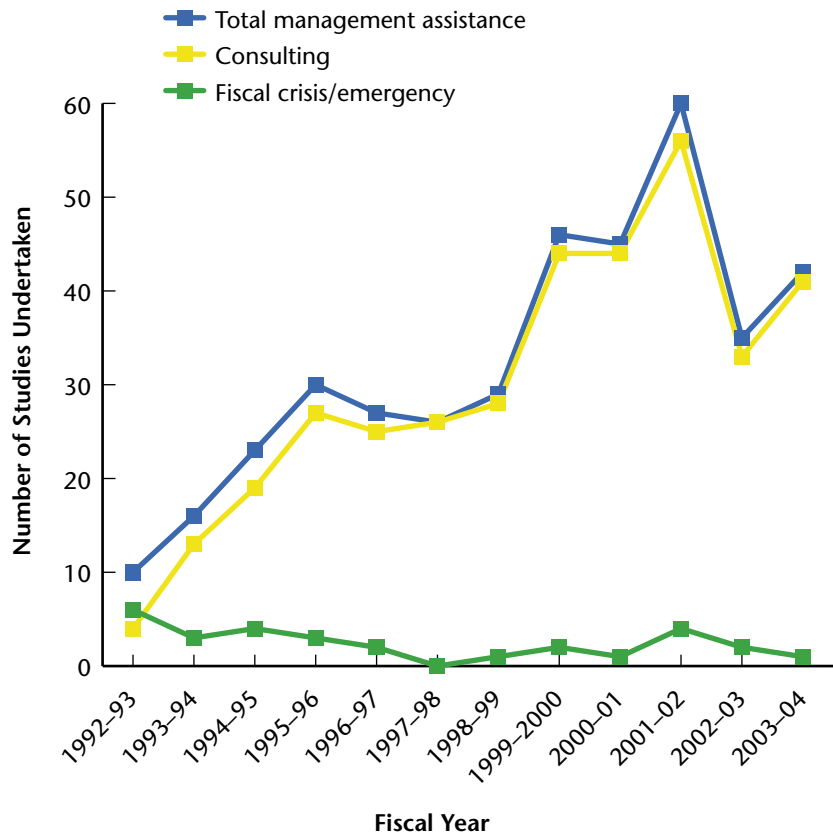
CSIS is a statewide electronic school information system that facilitates the exchange of student information within the California public school system for the purposes of state reporting and records transfer. It was created in 1997, when the Legislature required FCMAT to develop a plan to administer, coordinate, and manage the development and implementation of such a statewide system, and FCMAT has administered it since 1999.

FCMAT’s mission is to help California’s local educational agencies fulfill their financial and management responsibilities by providing fiscal advice, management assistance, training, and other related school business services. This mission is consistent with the mandate of its enabling legislation, which states that FCMAT shall provide management assistance at the request of any school district or county office and shall assist the state

superintendent with his or her statutory responsibilities. One way in which FCMAT accomplishes its mission is by issuing study reports to the school districts and county offices it assists. From its inception in June 1992 through March 10, 2004, FCMAT has completed 369 reports, and 29 more studies are pending completion. Most of these 398 studies are management assistance studies. Figure 2 shows the number of management assistance studies that FCMAT has completed or that are pending since its formation.

FIGURE 2

FCMAT’s Management Assistance Studies by Fiscal Year



Source: FCMAT.

FCMAT’s chief executive officer attributed the sharp increase in the number of management assistance studies from fiscal years 1999–2000 through 2001–02 to several causes. For example, many school districts and county offices used the deficit reduction payments they received from the State in fiscal year

1999–2000, a one-time source of funds, to finance recurring costs, such as employees’ salaries. During this same time period, many school districts experienced flat or declining enrollment; habitual deficit spending; and continual encroachment by categorical programs, like special education, on their general funds. As a result, many districts and county offices requested FCMAT’s management assistance and fiscal crisis intervention in the years immediately after the deficit reduction payments. Furthermore, some school districts and county offices asked FCMAT to help them develop implementation plans for a statewide accounting code structure.

FCMAT’s governing board helps FCMAT fulfill its mission by exercising its own statutory authority and overseeing FCMAT’s operations. (We discuss the governing board’s oversight of FCMAT in another section of this Introduction.) The education code establishes FCMAT’s 23-member governing board, consisting of one representative chosen by the California County Superintendents Educational Services Association (CCSESA) from each of its 11 county service regions; 11 superintendents of school districts chosen by the Association of California School Administrators (ACSA), one from each of the county service regions; and one representative from the Department of Education, chosen by the state superintendent. To choose its representatives, CCSESA requires the county superintendents in each region to select a peer to serve on FCMAT’s governing board. ACSA’s executive director recommends school district superintendents from its membership to serve on the governing board; the ACSA board must then approve the recommendations. Generally, county superintendents serve two-year terms and district superintendents serve three-year terms.

FCMAT’S ENABLING LEGISLATION ALSO EXPANDED THE FISCAL OVERSIGHT RESPONSIBILITIES OF COUNTY OFFICES OVER SCHOOL DISTRICTS

The law that created FCMAT also gave county offices greater responsibilities for the fiscal oversight of the school districts within their boundaries. A different law provides reimbursement through FCMAT of a portion of the costs the county offices incur in carrying out these responsibilities. These expanded responsibilities include the following:

- If, based on the recommendations of a budget review committee, with input from the district's governing board, the state superintendent disapproves a school district's budget, the county office must monitor and review the operation of the school district, develop and adopt a fiscal plan and budget for the district, and stay or rescind actions that are inconsistent with that budget.
- The county office must monitor the operation of each school district pursuant to each district's adopted budget and, if the county office determines that a school district will be unable to meet its financial obligations, it may assign a fiscal adviser to assist the district. It may also conduct a study of the district's finances and recommend actions to the district that will help it meet its obligations.
- After notifying the state superintendent that a school district will be unable to meet its financial obligations, the county office may request additional information from the district regarding its budget or operations, revise the district's budget, and stay or rescind any district action that is inconsistent with those revisions. The county office may take similar actions for any school district that has a negative certification of its financial and budgetary status.
- The county office may permit a school district having a qualified or negative certification to issue debt instruments that do not require the approval of the voters of the district, which the law otherwise prohibits, if the county office determines that repayment of the indebtedness is probable.

All of the activities just described relate to a county office's responsibility to certify the financial and budgetary status of a school district. The education code defines the process that leads to the certification of a school district's financial and budgetary status, which is based on the school district's interim reports. To begin the certification process, the superintendent of each school district must submit two reports to the governing board of the district during each fiscal year. The first report must cover the financial and budgetary status of the district for the period ending October 31, and the second report covers the period ending January 31. For each report, the district's governing board must certify the school district's financial and budgetary status as positive, qualified, or negative. Definitions of the three types of certifications are shown in the text box on the following page.

Three types of certifications for a local educational agency's interim reports:

Positive—the local educational agency will be able to meet its financial obligations for the current fiscal year and subsequent two fiscal years.

Qualified—the local educational agency may not be able to meet its financial obligations for the current fiscal year or subsequent two fiscal years.

Negative—the local educational agency will not be able to meet its financial obligations for the remainder of the current fiscal year or the subsequent fiscal year.

According to the education code, the certifications are based on current financial projections.

Source: California Education Code, sections 1240(l) and 42131(a)(1).

By law, each district's governing board must submit its interim reports to its county office. A county office may change a certification to negative or qualified, and the school district may appeal the change. The appeals process ends with the state superintendent's determination of the school district's certification.

Any school district that has a qualified or negative certification on its second interim report must submit a third interim report to its county office, the state superintendent, and the state controller by June 1. The report must provide financial statements that project the school district's fund and cash balances through June 30. The education code contains similar provisions that cover the certification of the financial and budgetary status of county offices.

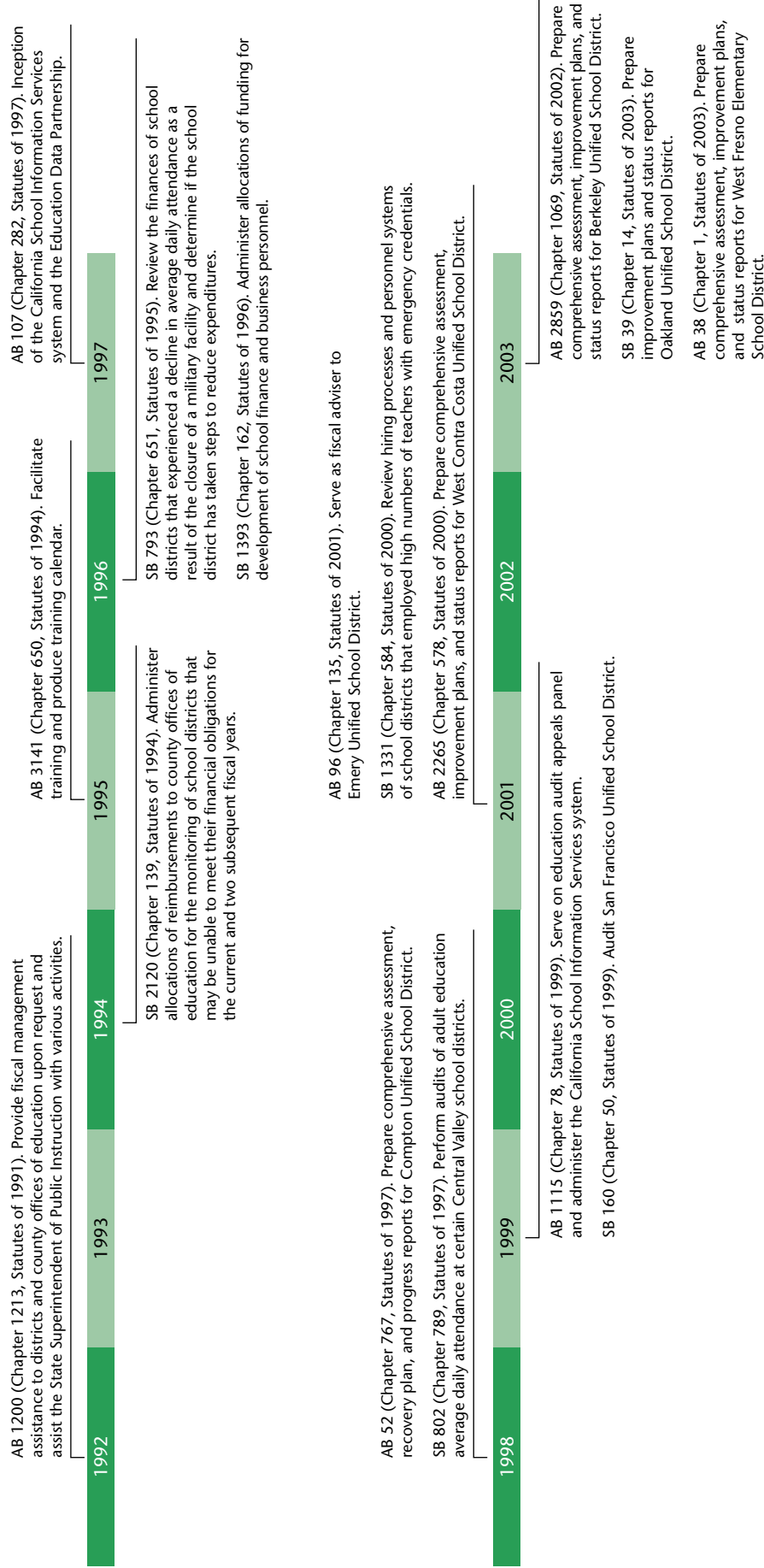
LEGISLATION IS THE PRIMARY CAUSE OF FCMAT'S EXPANDED RESPONSIBILITIES

In addition to authorizing the creation of FCMAT, the law also described FCMAT's original responsibilities, which include assisting county offices with their obligation to oversee the fiscal condition of school districts at the request of the state superintendent, reviewing a school district's budget as part of a budget approval process as requested by the state superintendent, and providing management assistance at the request of school districts or county offices. Subsequent legislation has given FCMAT other responsibilities that complement its original responsibilities, such as facilitating fiscal management training for the staffs of county offices; facilitating training on fiscal matters for school district governing board members, district and county superintendents, and some of their employees; and producing a training calendar for fiscal training services that are being offered at the local, regional, and state levels. Figure 3 shows the legislation that expanded the scope of FCMAT's responsibilities since its formation.

Among FCMAT's legislated responsibilities are assignments to perform studies of certain school districts. For five of these studies—those for the Berkeley, Compton, Oakland, West Contra Costa, and West Fresno school districts—the Legislature assigned FCMAT to prepare comprehensive assessments and

FIGURE 3

Legislation Expanding FCMAT's Responsibilities



Note: Laws are shown by the year in which each took effect.

improvement plans. Except for Berkeley, these school districts had received or would receive a state emergency loan at the time of FCMAT's legislative assignment. The subject of another legislated study, Emery Unified School District (Emery), also received a state emergency loan, but the Legislature did not require FCMAT to prepare a comprehensive assessment and improvement plan for it. Instead, the Legislature required the state superintendent to appoint FCMAT as Emery's fiscal adviser. In addition, the Legislature required FCMAT to perform audits of the average daily attendance data for adult education at certain school districts in the Central Valley that requested one, and an audit of the San Francisco Unified School District.

The Legislature has also expanded FCMAT's scope of responsibilities beyond providing management assistance to school districts and county offices to administering allocations of funds to reimburse county offices for some of the costs of their oversight responsibilities and to help pay for development of school finance and business personnel. However, according to FCMAT, in fiscal year 1994-95 reimbursements were distributed to only nine county offices. As a result, the Department of Finance reduced the amount of funding available for these reimbursements and FCMAT, the Department of Education, and the steering committee of CCSESA developed a proposal wherein, on a onetime-only basis, FCMAT would use the unused reimbursement funds to provide teleconferencing capabilities in all county offices. In 1999, FCMAT completed facilitating the installation of satellite dishes and the necessary downlink capabilities at each county office in the State to receive training workshops and other educational staff development.

Furthermore, FCMAT administers or helps administer two separate statewide information systems: CSIS and the Education Data Partnership. As mentioned earlier, in 1997 the Legislature required FCMAT to develop plans for administering and managing CSIS, and in 1999 it gave FCMAT full responsibility for administering CSIS. CSIS's inception in 1997 coincided with the establishment of the Education Data Partnership, which provides financial and demographic data to local educational agencies and allows those agencies, other governmental agencies, and the broader educational community (including parents) to share that data. FCMAT's partners in the project are the Department of Education, the Alameda County Office of Education (Alameda county office), and EdSource, which is a not-for-profit organization.

FCMAT has also performed two types of studies that legislation authorizes certain entities to perform, but which the law does not specifically require FCMAT to perform. Specifically, FCMAT assumed the role of an external evaluator under the Public Schools Accountability Act of 1999 (act), a role it no longer performs. According to FCMAT's chief executive officer, the Department of Education and the education secretary encouraged FCMAT to become an external evaluator so that it could establish a protocol for evaluations under the act. By October 1999 FCMAT had established the protocol, and it released the last of its five studies as an external evaluator in February 2001. In addition, FCMAT has performed fraud audits under legislation that took effect in 2002. FCMAT's deputy executive officer told us that if the audit specifications fall within FCMAT's scope and the expertise of its staff, FCMAT may perform the audit. Since the law took effect in January 2002, FCMAT has completed five such audits and is working on another.

Finally, according to FCMAT, its expertise and familiarity with the Compton Unified School District (Compton) resulted in FCMAT being designated for a court-ordered responsibility resulting from a lawsuit against the State. On February 7, 2000, the court approved a consent decree in the *Serna v. Eastin*¹ case, in which the plaintiffs claimed that children attending public schools in Compton were deprived of basic educational opportunities available to children elsewhere in California. The consent decree requires continued improvement in Compton's school facilities and sites and in its classroom environment, and it appointed FCMAT to oversee compliance with the decree. From the date of the consent decree's approval through December 11, 2001, when the state superintendent officially returned governing authority to Compton's school board, FCMAT had both statutory and court-ordered responsibilities at the district. Since December 11, 2001, FCMAT's sole responsibilities to Compton have been under the consent decree. FCMAT reported in its February 2004 progress report that Compton has made significant progress under the consent decree and that all consent decree stipulations but one have been met.

¹ *Roxanne Serna, et al., v. Delaine Eastin, State Superintendent of Public Instruction, et al.* Los Angeles County Superior Court, Case No. BC174282.

OVERSIGHT OF FCMAT COMES PRIMARILY FROM ITS GOVERNING BOARD AND THE KERN SUPERINTENDENT'S OFFICE

FCMAT's governing board and the Kern superintendent's office oversee different aspects of FCMAT's operations. According to the bylaws of the FCMAT governing board, the board provides policy direction and broad operational guidance to the Kern superintendent's office, which houses and administers FCMAT. The governing board also oversees the operations involving FCMAT's core mission, which is to provide fiscal advice and management assistance, and its other projects. The Kern superintendent's office oversees FCMAT's administrative operations.

In its role of providing oversight, the governing board performs several functions. For example, the education code requires the governing board to establish the rates that FCMAT charges school districts and county offices for the on-site personnel and travel costs it incurs in providing management assistance. Since October 1999, the rate has been \$400 per FCMAT team member per day, plus travel costs. Another way in which the governing board oversees FCMAT's core operations is through its statutory authority to declare fiscal emergencies at local educational agencies. For example, at the request of the state superintendent and the Alameda county office, the governing board declared on October 22, 2000, that a fiscal emergency existed at Emery. This situation eventually led to the district's receiving a state emergency loan.

The governing board's bylaws note other significant oversight responsibilities. For example, the bylaws state that the governing board is to develop criteria and prioritize requests for assistance, including requests from the state superintendent, and that it must ensure that FCMAT is kept free from real or perceived interference or conflicts of interest that might impair its independence and objectivity. Furthermore, the governing board meets quarterly to discuss FCMAT's reports, prioritize requests for its assistance, and oversee its projects. The governing board's authority prevents FCMAT's staff from undertaking significant projects without the board's knowledge and authorization.

The Kern superintendent's office oversees FCMAT's administrative operations. For example, the human resources divisions of the Kern superintendent's office handle the process of hiring some of FCMAT's staff. Other divisions assist FCMAT with its information technology needs, provide vehicles for its employees' use, and ensure that it has office space and furniture.

As a division of the Kern superintendent's office, FCMAT is subject to the same administrative policies and procedures as the other divisions and subunits of that office.

Except for having a representative on FCMAT's governing board, the Department of Education does not provide any oversight of FCMAT. In accordance with state law, the Department of Education has selected one of its deputy superintendents to serve on the governing board, and as a member of the board, that individual helps to oversee FCMAT's projects. According to the deputy superintendent who was appointed, she and other representatives of the Department of Education meet monthly with FCMAT's deputy executive officer to exchange mutually beneficial information, such as notes on troubled school districts and the CSIS project. However, she would not characterize these meetings as oversight.

Additionally, as one would expect, the Department of Finance's oversight of FCMAT is related to fiscal matters. As part of the State's annual budget process, the Department of Finance reviews FCMAT's budget and makes recommendations to the Legislature regarding its annual appropriations.

THE STATE SUPERINTENDENT APPOINTS ADMINISTRATORS AND TRUSTEES FOR SCHOOL DISTRICTS

When a school district receives an emergency loan from the State, the state superintendent may assume control of the district's operations. Under the education code, for larger loans, the state superintendent may appoint a state administrator to operate the district on his or her behalf. For smaller loans or after the state superintendent determines that a school district no longer needs an administrator, the state superintendent must appoint a state trustee to monitor and review the operation of the district. When we asked the Department of Education how the state superintendent selects administrators and trustees for districts that receive emergency loans, it told us that the state superintendent considers the needs and relevant unique circumstances of the district in question. The state superintendent also consults with the county superintendent of schools, as provided in statute. Table 1 on the following page shows the terms of service and contracted salaries for currently serving state administrators and trustees.

TABLE 1

**Salaries of State Trustees and Administrators Currently Serving
School Districts That Received State Emergency Loans**

School District	Trustee or Administrator	Dates of Assignment	Contracted Annual Base Salary
Emery Unified	Administrator	November 2003 to present	\$110,000
Oakland Unified	Administrator	June 2003 to present	233,025
Richmond/West Contra Costa Unified	Trustee	May 1992 to present	51,180
West Fresno Elementary	Administrator	March 2003 to present	120,000

Source: Department of Education and FCMAT.

SCOPE AND METHODOLOGY

The Joint Legislative Audit Committee (audit committee) requested that the Bureau of State Audits conduct a performance and financial audit of FCMAT, including a review of its prescribed roles and responsibilities in connection with school districts requesting emergency apportionment loans from the State. Specifically, we were asked to evaluate the mix of responsibilities that FCMAT has been asked to assume since its formation. This included assessing the level of involvement FCMAT has had with the various school districts receiving state emergency loans. In addition, we were asked to determine whether FCMAT can demonstrate that its involvement has improved the fiscal health of school districts, and to what extent its involvement has prevented the need for state emergency loans to school districts. We were also asked to examine the policies and procedures that FCMAT uses to acquire the services of contractors, including determining whether FCMAT reasonably justifies the use of noncompetitive personal services contracts and how FCMAT monitors and evaluates the performance of its contractors. The audit committee asked us to review FCMAT’s financial statements to determine the amount of administrative and overhead costs and, for a sample of school districts that received state emergency loans, to determine the amount FCMAT charged for its services.

Additionally, we were asked to determine the level of oversight other entities have over FCMAT, including FCMAT’s management of its annual budget. We were also asked to determine, where appropriate, the amounts received by the

trustees or administrators of the school districts. Finally, we were asked to review and evaluate the process for selecting FCMAT's board members and staff, including whether it has defined minimum qualifications for the various employment levels.

To determine the role FCMAT plays in connection with school districts that have requested state emergency loans, we researched relevant state laws and regulations. To assess FCMAT's level of involvement and effectiveness at these districts, we reviewed its work at five of the six school districts that had received state emergency loans. We did not include the Coachella Valley Unified School District (Coachella) in our sample because FCMAT was not involved with the district's recovery. Coachella received its state emergency loan on June 16, 1992, a week after the Kern superintendent's office signed the contract with the Department of Education to create FCMAT as one of its divisions, so FCMAT did not perform a study of Coachella at the time of the loan. Furthermore, FCMAT has not subsequently performed a comprehensive fiscal review of Coachella.

To assess the effectiveness of the assistance that FCMAT provides to its clients, we reviewed FCMAT's reports for the school districts that received state emergency loans and for five other districts we sampled. From those reports, we selected recommendations that have fiscal implications from the areas of internal controls, budget preparation and monitoring, attendance accounting, facilities improvements, and collective bargaining. We also interviewed staff at eight of the 10 school districts to determine the status of their implementation of the recommendations. We obtained documentation supporting the school districts' assertions that they had implemented the recommendations that we selected, and if they had not implemented a recommendation, we requested an explanation. We did not interview staff at Compton, because the district has repaid its loan and the State returned control of the district to its governing board. Instead, we reviewed several of FCMAT's six-month progress reports to determine whether FCMAT's involvement helped it recover from its fiscal crisis. In addition, we did not interview staff at the Oakland Unified School District (Oakland) because at the time of our fieldwork, FCMAT was in the process of completing its second progress review of the district. FCMAT focused its review on Oakland's progress toward implementing certain recommendations that Oakland's state administrator, FCMAT, and the Department of Education had previously identified as high priority. Therefore, rather than selecting other, lower-priority recommendations that the district

had not focused on, we selected some of the high-priority recommendations to review. Then, to avoid further burdening Oakland's staff by interviewing them about some of the same recommendations that FCMAT covered in its report, we reviewed FCMAT's report after it was completed to determine whether the district had implemented the recommendations we selected.

To determine whether the school districts improved fiscally after FCMAT's report, we compared each school district's fiscal status to certain criteria, including the type of certification the district received on its interim reports; the repayment of its state emergency loan, where applicable; the recovery of its school board powers from the State; the presence of a state-appointed adviser, administrator, or trustee at the district; and whether the districts implemented or partially implemented FCMAT's recommendations.

To understand whether FCMAT reasonably justifies the use of noncompetitive personal services contracts, we interviewed staff of both FCMAT and the Kern superintendent's office and reviewed the process that FCMAT used to award the contracts. To determine whether FCMAT's clients were satisfied with its services and to determine the steps FCMAT takes to address its clients' concerns, we reviewed a sample of evaluation forms that FCMAT's clients completed and interviewed FCMAT's staff to determine whether FCMAT followed up on the clients' concerns.

To determine FCMAT's administrative and overhead costs, we obtained the direct and indirect costs for its fiscal oversight activities for fiscal years 2000–01 through 2002–03. We also used this data to determine the costs of FCMAT's services for the Berkeley, Compton, Emery, Oakland, West Contra Costa, and West Fresno school districts.

To determine the level of oversight other entities have over FCMAT, we interviewed staff members of the departments of Finance and Education. We also reviewed some of the minutes from meetings of FCMAT's governing board and other relevant documents.

To understand the process of selecting FCMAT's board members, we reviewed FCMAT's enabling law and interviewed the executive directors of CCSESA and ACSA. We also determined whether FCMAT's current staff met established minimum qualifications. ■

AUDIT RESULTS

THE FISCAL CRISIS AND MANAGEMENT ASSISTANCE TEAM PROVIDES VALUABLE ADVICE TO TROUBLED SCHOOL DISTRICTS

The reports prepared by the Fiscal Crisis and Management Assistance Team (FCMAT) provide findings and recommendations that are valuable and, if implemented effectively, should improve the fiscal health of school districts. However, FCMAT's effectiveness in assisting school districts is contingent upon the districts' willingness and ability to implement its recommendations, which depends on various factors, including the severity and nature of the districts' financial problems.

For example, in its July 2003 report on the West Fresno Elementary School District (West Fresno), FCMAT stated that the conflict and controversy surrounding the board and the district's administration during the prior two years had left West Fresno in the position of having to reestablish virtually all of its financial management policies, procedures, systems, and controls. Until these basic structural improvements are in place, West Fresno cannot be expected to recover its financial health as quickly as a district with less severe problems.

Because FCMAT's recommendations appear sound and are based on standards it developed, implementation of the recommendations should result in improved business practices for the districts, which in turn can lead to fiscal recovery or improvement. However, school districts are not required to implement FCMAT's recommendations, and for most of its studies, the law does not require FCMAT to report on the progress the districts make in implementing the recommendations. Therefore, the decision to implement FCMAT's recommendations is left to the discretion of the school districts and county offices that receive its services.

Most School Districts That Received State Emergency Loans Show Improvement in Their Financial Condition After Receiving FCMAT's Assistance

We reviewed five of the six school districts that received emergency loans from the State and FCMAT's assistance. We did not review one school district, Coachella Valley Unified School District, because it received its loan just one week after FCMAT was formed, and so FCMAT was not involved with its recovery. One of the five school districts, West Contra Costa Unified School District (West Contra Costa), formerly Richmond Unified School District, received its loan before the Legislature formed FCMAT; however, in 2000, as a condition of West Contra Costa receiving other funding, the Legislature required FCMAT to conduct a comprehensive assessment and develop improvement plans for the school district.

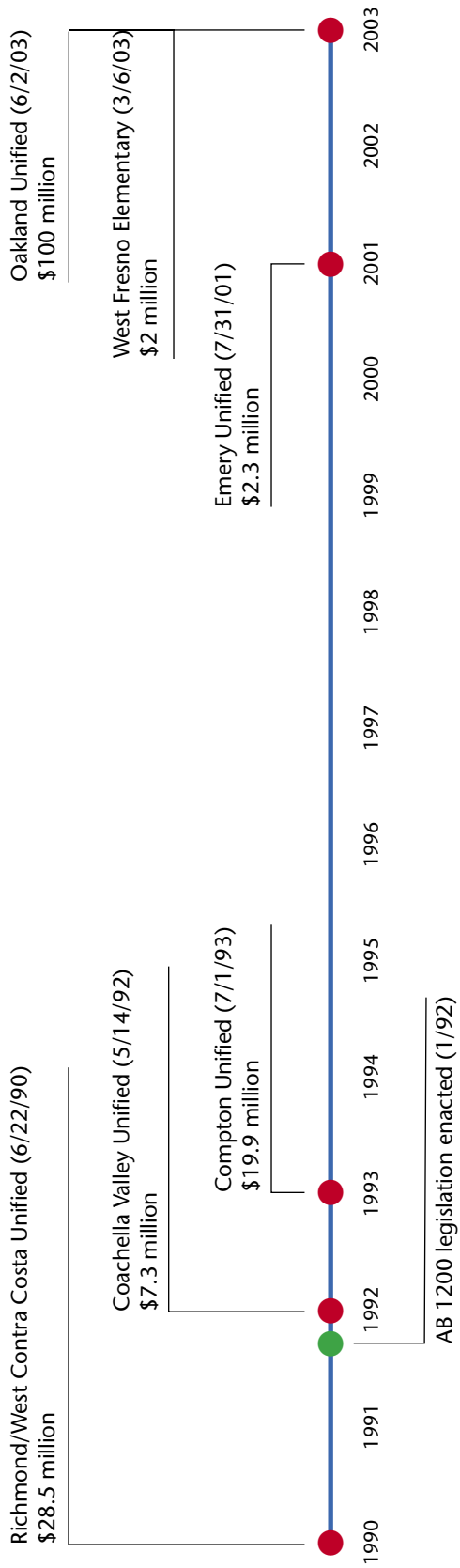
Figure 4 shows the six school districts that received state emergency loans. Three of the five school districts we reviewed either implemented or took meaningful steps toward implementing most of the recommendations we reviewed. These actions, over time, should help improve the districts' financial condition. The Compton Unified School District (Compton) has repaid its loan, and the State has returned control of the district to its governing board. The governing board of the Emery Unified School District (Emery) has regained partial control of the district's operation. Also, according to FCMAT, West Contra Costa has made significant improvements in the area of financial management in the two years since it was reviewed. The other two districts, West Fresno and Oakland Unified School District (Oakland), continue to experience financial difficulties and may not fully recover for several years. We discuss each of these districts in more detail next.

Compton Took Eight Years to Achieve Substantial Recovery

As the first district for which FCMAT performed a comprehensive review, Compton provides an example of how long it can take for a district to achieve substantial recovery. Its financial recovery process spanned more than eight years. Compton received an emergency loan amounting to \$10.5 million in July 1993 after Compton and the Los Angeles County Office of Education (Los Angeles county office) became concerned that the district would not be able to meet its immediate fiscal obligations. According to FCMAT's initial report in February 1999, the Department of Education and the Los Angeles county office had previously developed recovery plans clearly indicating that Compton was virtually near collapse. Specifically, Compton's

FIGURE 4

**California State Loans to School Districts
(1990 to Present)**



Source: FCMAT.

educational programs lacked direction and focus, its fiscal systems were unreliable, its management and governance structure was ill-defined, and the facilities were aging and showing signs of neglect.

As a result of these issues, for Compton to receive the loan, the Legislature required that it meet certain conditions, including submitting a progress report on its implementation of recommendations made in a May 1993 recovery plan developed by the Department of Education and the Los Angeles county office. The loan also required that the State Superintendent of Public Instruction (state superintendent) appoint a state administrator who would exercise the powers and responsibilities of the district's governing board. Soon after the state administrator assumed the governance responsibilities for the district, a more detailed analysis of the district's financial position revealed that for the district to be solvent by the end of fiscal year 1993–94, it needed another \$9.5 million in addition to the original loan. In October 1993, Compton received a second emergency loan of \$9.45 million.

In 1997, the Legislature passed Assembly Bill 52 (Chapter 767, Statutes of 1997), stating its intention to incrementally return control of Compton to its governing board, contingent upon Compton's improvement in five major functional areas: pupil achievement, financial management, facilities management, personnel management, and community relations. This legislation also required FCMAT and Compton's state administrator to conduct comprehensive assessments and develop recovery plans in these five areas and to report at six-month intervals on whether Compton had made substantial and sustained progress in those areas, until the state superintendent returned full control of the school district to its governing board. Specifically, FCMAT was required to make recommendations regarding when to return control over specified areas of the school district's operations to the district's board.

In February 1999, FCMAT published its comprehensive assessment and recovery plan for Compton. In the report, FCMAT noted that Compton had made progress over the six years since it had received its first emergency loan, but that deficiencies still existed. Specifically, in the area of financial management, FCMAT found significant deficiencies:

At Compton, part of FCMAT's role was to recommend when to return control of specific operations to the district's board.

- A number of weaknesses existed in its internal controls.
- The organizational structure of the business and operational departments provided inadequate supervision and ineffective lines of communication.
- A high number of entry-level job classifications existed, causing some departments to be overstaffed but underskilled for the requirements of their positions.
- Salary schedules within the departments were not competitive.

FCMAT's subsequent reports on Compton's progress indicated that it was clear to FCMAT that Compton had implemented some of FCMAT's recommendations and was moving toward recovery. For example, FCMAT recommended that Compton reconfigure its organizational structure, establish supervisory functions, revise job descriptions for supervisors and managers, implement formal staff training and development plans, and evaluate salaries for competitiveness with other districts. By the end of August 1999, Compton had completely reorganized its business and administrative services division, improved staff supervision, evaluated the skills of each employee, provided appropriate training and individual counseling, and was in the process of evaluating salaries for competitiveness with other districts. On other recommendations, such as establishing an internal audit function to ensure compliance with laws, regulations, internal controls, and district policies, Compton had made little progress. However, by February 2000, FCMAT reported that Compton had established an internal audit function and that the internal audit staff had performed reviews of areas at high risk for monetary loss or noncompliance with laws and regulations.

Table 2 on the following page shows that since FCMAT conducted its initial study, Compton has received positive certifications on its interim reports. Additionally, our review of Compton revealed that the district has implemented or partially implemented all of the recommendations we selected. We selected recommendations that have fiscal implications in the areas of internal controls, budget development processes, attendance accounting, and adherence to legal and professional standards. Moreover, in June 2001, Compton paid back its state loan, and in December 2001, the state superintendent returned full control of the district to the governing board, which is further evidence of the district's improvement.

TABLE 2

Status of School Districts That Received State Emergency Loans and FCMAT’s Assistance

	Compton Unified	Emery Unified	Oakland Unified	West Contra Costa Unified	West Fresno Elementary
Date of FCMAT’s initial study	February 1999	July 2001	January 2000	July 2001	July 2003
Number of interim reports filed since FCMAT’s initial study*	10	5	8	5	3
Number of positive certifications	10	0	4 [†]	5	0
Number of recommendations from FCMAT’s study that we selected for follow-up	13	8	10	7	10
Number of selected recommendations the district implemented or partially implemented	13	8	5	6	5

* As of first interim report certification for fiscal year 2003–04.

† The fiscal year 2002–03 Alameda County Grand Jury reported that, although the Alameda County Office of Education (Alameda county office) raised concerns about Oakland’s fiscal year 2001–02 budget and interim reports, questioning Oakland’s enrollment projections and its ability to cover the mandated reserve requirement, it approved the budget and gave positive certifications to both interim reports. Further, in the grand jury report, the Alameda county office stated that it did everything it could under the law, and that districts are ultimately responsible for keeping their financial houses in order.

Emery Will Soon Regain Control Over Its Fiscal Affairs

Emery has also made progress toward improving its financial condition since FCMAT’s involvement. According to FCMAT, Emery identified financial difficulties early in fiscal year 1999–2000, and in March 2000 submitted a qualified certification on its second interim report, projecting a negative fund balance of approximately \$93,000. A qualified certification indicates that a district may not be able to meet its financial obligations in the current or next two subsequent fiscal years. Because of Emery’s qualified status and the departure of its business manager, the Alameda county office required Emery to prepare a third interim report, and with the assistance of Alameda county office fiscal staff, Emery reported a projected negative ending fund balance of \$638,000. As a result, the Alameda county office made a \$650,000 emergency loan to Emery.

In early October 2000, the state superintendent and the Alameda county office requested that FCMAT’s board declare a fiscal emergency at Emery, which it did later that month. According to FCMAT, under Education Code Section 42127.8(e), this provided for immediate assistance from FCMAT. Subsequently, the Alameda county office appointed FCMAT as the district’s fiscal adviser with authority to rescind any actions of the district’s governing board that were inconsistent with the district’s revised budget. Furthermore, the Legislature passed Assembly Bill 96 (Chapter 135, Statutes of 2001), giving Emery a \$1.3 million

emergency loan from the State and a \$1 million line of credit. This legislation also required the state superintendent to appoint an administrator to manage the district and FCMAT to act as fiscal adviser to the district until it became financially solvent.

Our visit to Emery revealed that the district implemented or partially implemented most of the recommendations we selected for review. For instance, FCMAT recommended that Emery reflect in its financial reports not only the actual expenditures it incurred, but also amounts not yet paid, such as purchase orders, so that it could properly monitor its budget. Also, Emery implemented new budgeting software that automatically reserves a portion of the available budgeted funds as the district staff enters purchase orders into the system.

Because of Emery's improved financial condition, the state superintendent anticipates returning all fiscal responsibilities and powers to the district's governing board by July 1, 2004.

In April 2004, the state superintendent announced that Emery is expected to end the fiscal year with a positive fund balance of approximately \$1.1 million and will meet the state-recommended reserve levels. Furthermore, because of the district's improved financial condition, the state superintendent returned control over facilities to Emery's governing board and anticipates returning all fiscal responsibilities and powers to the governing board by July 1, 2004, three years after the State took over control of the district.

Despite such improvements, Table 2 shows that Emery has not received a positive certification on its recent interim reports since receiving assistance from FCMAT. According to Emery's chief business officer, the school district could have filed a positive certification for its second interim report for fiscal year 2003-04; however, it decided that filing a qualified certification was prudent in light of the fact that it cannot confidently project whether it will maintain its current enrollment level. Between 40 percent and 45 percent of Emery's students are transfers from neighboring school districts that are also experiencing financial difficulties, and these districts may be reluctant to grant such transfers as readily as they did in the past. As a result, Emery is unable to quantify the number of students who will transfer in from other school districts in the next few years, and it has therefore based its fiscal year 2003-04 budget and future projections on a flat enrollment figure. However, upon consulting with the Department of Education about this matter, Emery intends to file a positive certification for its third interim report of fiscal year 2003-04.

Neither West Fresno nor Oakland Has Made Much Progress Toward Financial Recovery

Our reviews of West Fresno and Oakland revealed that neither has made significant progress toward implementing the recommendations we selected. Furthermore, they have shown almost no measurable improvement in their financial conditions, and because the extent and severity of their problems are similar to those Compton experienced, these districts may not fully recover for several years. According to FCMAT, West Fresno, which has drawn \$1.3 million of the \$2 million emergency loan authorized in March 2003, must reestablish virtually all of its financial management policies, procedures, systems, and controls. According to West Fresno, the district staff is currently attempting to reestablish internal controls and governing board policies and procedures, and it has already re-created job descriptions and is in the process of developing job manuals for the district employees.

Both West Fresno and Oakland have significant deficiencies in their financial management policies and procedures, indicating that these districts may not fully recover for several years.

FCMAT reviewed Oakland in 1999, noting significant deficiencies in the school district's financial management policies and procedures. In April 1999, Oakland's board voted to ask for a comprehensive review from FCMAT. The vote was contingent upon acquiring funds from the Legislature to conduct the study. Assembly Bill 1115 (Chapter 78, Statutes of 1999) allocated \$750,000 to FCMAT to conduct a comprehensive assessment and complete a recovery plan for the district. FCMAT issued its report to Oakland's board in January 2000, indicating that the district was having great difficulty and emphasizing that Oakland's financial solvency was in serious question. FCMAT reported that Oakland had challenges that are more serious and difficult to overcome than those faced by most districts. For example, the district's facilities were unsafe, it was unable to attract and retain high-quality professional staff, and it experienced inadequate communication and a pervasive perception that the district was mismanaged.

By October 2002, the district's fiscal health had worsened, and it clearly had not implemented most of FCMAT's recommendations. Consequently, the Alameda county office disapproved Oakland's budget for fiscal year 2002-03 and appointed FCMAT as the district's fiscal adviser. In June 2003, the Legislature granted the school district a \$100 million loan for which funds could be disbursed only if the state administrator and FCMAT determined it was necessary. According to FCMAT, in June 2003, the district requested \$65 million of the loan to cover its June payroll and severe negative cash position. According to the state administrator for Oakland, the district plans to request another \$25 million

in June 2004 for bond repayment and a new student information system. The remaining balance of the loan is available to the district as a line of credit, which FCMAT expects the district to use.

Although it is too early to expect significant improvement, Oakland has made progress in implementing five of the 10 recommendations we reviewed.

As a condition of Oakland receiving the state loan, the Legislature required that the state superintendent appoint an administrator to manage the district. Because of the severity of Oakland's financial problems, and since the district received its loan less than a year ago, it is too early to expect significant improvement. The district has fully implemented one and partially implemented another four of the 10 recommendations we selected; however, because a state administrator is working with Oakland, it is reasonable to assume that the district will continue to make progress over time.

West Contra Costa Has Made Significant Improvements

West Contra Costa received a \$28.5 million emergency loan from the State in 1990, but it received FCMAT's assistance for a different reason than did the other districts receiving state emergency loans. Specifically, the State Allocation Board allocates to school districts, on a per student basis, funding for new construction and modernization of school facilities. However, under the Education Code, Section 17017.1, West Contra Costa was generally ineligible for any state school facilities funding until June 1998 or until it paid off its emergency loan, whichever was later. Nevertheless, in 2000, Assembly Bill 2265 (Chapter 578, Statutes of 2000) authorized the state superintendent to allocate up to \$800,000 annually for fiscal years 2000–01 through 2004–05 to the district for projects that would otherwise have been eligible for state funding between 1993 and 1998. The Legislature did this because it believed that the matter of the loan repayment was separate from the issue of providing access to adequate school facilities for the district's pupils. This legislation authorized the district to use the funds for any discretionary school purpose. As a condition of receiving the funding, the legislation required West Contra Costa to allow FCMAT to conduct an assessment of the district. In addition, it required FCMAT to complete improvement plans in the areas of instruction, finance, facilities, personnel management, and community relations, and to report on West Contra Costa's progress in implementing FCMAT's recommendations.

From our review of FCMAT's final progress report, published in July 2003, it appears that West Contra Costa's largest financial problem is an unfunded liability amounting to approximately \$275 million for lifetime health benefits for its employees.

According to West Contra Costa's assistant superintendent of fiscal services, during contract negotiations 30 years ago the district's employees struck a bargain wherein, in exchange for accepting lower salaries, employees who worked for the district at the time and who were hired afterward, and their spouses, would receive health coverage paid in full by the district for the rest of the employees' lives. After the death of the employee, spouses were eligible to continue coverage at their own expense, but this benefit was later changed to allow the surviving spouse to continue receiving health care coverage at the district's expense. This type of retirement benefit is rare among California's school districts. In fact, most school districts that offer their employees coverage for health benefits offer it only until age 65, when the retiree enrolls in Medicare. West Contra Costa's assistant superintendent of fiscal services told us that the district has approached its bargaining units to discuss employee health benefits and will continue to raise this issue until the school district and the unions reach a satisfactory alternative.

In addition, in its final report, FCMAT commended West Contra Costa for its efforts and stated that the district had made significant improvements in its finances, particularly in its board policies on fraud and its detection, and in its budget projections, adoption, reporting, filing, and monitoring. As shown in Table 2 on page 24, we found that West Contra Costa implemented six of the seven recommendations we selected and has received positive certifications on all of its interim reports since FCMAT became involved with the district.

School Districts Can Improve by Implementing FCMAT's Recommendations

Although FCMAT's management assistance studies are narrower in scope, implementing its recommendations should, over time, help a school district improve its financial condition.

Most of FCMAT's management assistance studies are much narrower in scope than those that were mandated by statute, such as those for districts that received state emergency loans. Nevertheless, some of the school districts and county offices that request the studies experience financial problems that may take time to overcome. Although several of the school districts we reviewed have shown little improvement in their fiscal health, implementing FCMAT's recommendations has helped these districts make important improvements in areas such as internal controls, budget monitoring, and attendance accounting, which can ultimately lead to the districts' fiscal recovery. However, as with the districts that received state emergency loans, the fiscal recovery of these school districts may be gradual because

many of FCMAT's recommendations take time to implement. Moreover, the implementation of certain recommendations may be contingent upon longer-term improvements occurring first.

Table 3 shows that the five school districts we reviewed that requested FCMAT's assistance implemented or partially implemented at least some of FCMAT's recommendations, and three of them received positive certifications after FCMAT completed its study. It may be too soon to determine the recovery status of the other two districts, Berkeley Unified School District (Berkeley) and Orchard School District (Orchard), because of the severity of their problems in comparison with other districts we reviewed. For example, Orchard and Victor Valley Union High School District (Victor Valley) received FCMAT's assistance within a couple of months of each other; however, Victor Valley has improved significantly, while Orchard still has not received a positive certification on its interim financial reports. FCMAT reviewed Victor Valley in November 2002, after the district's county office rejected its budget twice. Although the school district had previously received positive certifications on its interim reports, it was showing a deficit of \$1.5 million and needed help in reducing its expenditures. Our testing at Victor Valley revealed that the district has implemented all of FCMAT's recommendations and has continued to receive positive certifications on its interim reports since FCMAT's study.

TABLE 3

Status of Sampled School Districts That Received Management Assistance Studies From FCMAT

	Antioch Unified	Berkeley Unified	Monterey Peninsula Unified	Orchard	Victor Valley Union High
Initiator of FCMAT's study	Contra Costa COE*	Legislature	Monterey COE	Santa Clara COE	San Bernardino COE
Date of FCMAT's study	August 1998	July 2003	March 2000	September 2002	November 2002
Number interim reports filed since FCMAT's study	12 [†]	2 [†]	8 [‡]	4 [‡]	4 [‡]
Number of positive certifications	8	0	4	0	3
Number of recommendations from FCMAT's report that we selected for follow-up	5	12	10	10	6
Number of selected recommendations the district implemented or partially implemented	4	11	9	8	6

* County Office of Education.

[†] As of the second interim report certification for fiscal year 2003–04.

[‡] As of the first interim report certification for fiscal year 2003–04. The second interim certification for fiscal year 2003–04 was not available.

According to FCMAT's review of Orchard, the school district not only had a \$2 million budget deficit, but many of its records were missing or incomplete, its board policies and procedures were not complete or did not exist, and the district's staff did not follow proper business procedures. FCMAT's recommendations addressed issues such as the district's fiscal solvency, inadequate monitoring, overspending of funds, and application of internal controls. In its report, FCMAT projected that the recovery process for Orchard would take approximately three years.

Our review of Orchard revealed that, although it has not filed positive certifications on its interim reports since FCMAT's study, it has addressed many of FCMAT's recommendations. For instance, upon beginning fieldwork in December 2001, FCMAT found that Orchard's business staff entered dollar amounts into the computer system for salaries and benefits with no logic or supporting documentation while developing a budget. Similarly, revenues were not calculated correctly and program budgets did not reflect the current level of anticipated revenues or expenditures. FCMAT recommended that Orchard develop and monitor its budgets for accuracy on a regular basis. Although implementing this recommendation may not correct the district's financial problems immediately, it can help the district to develop an accurate budget, which should ultimately lead to an improvement in the district's fiscal status.

Some school districts believed that FCMAT's credibility drew the public's attention to key issues and helped governing boards make critical decisions about the districts' business management.

Staff at some of the school districts we visited believed they had benefited from FCMAT's assistance. Specifically, some school districts felt that FCMAT's credibility drew the public's attention to key issues and helped governing boards make critical decisions about the districts' business management in areas such as cuts to transportation and special education. For example, the business services department at Victor Valley told us that although the San Bernardino County Superintendent of Schools disapproved the district's budget, the governing board was resistant to making certain budget reductions that the district recommended until FCMAT made recommendations for similar reductions to the district. In another example, Berkeley staff commented that they sometimes had trouble convincing their board to agree to make important changes, and having FCMAT as an independent reviewer gave district staff the credibility they needed to convince the board to make the necessary changes. Berkeley added that it cites FCMAT's standards at board meetings to bolster its credibility when proposing certain changes.

FCMAT'S CONSULTANT SELECTION PROCESS IS FAIR, BUT IMPROVEMENTS CAN BE MADE

FCMAT uses a fair process to identify and select consultants for its studies, but it does not solicit a sufficiently large number of consultants to bid on its comprehensive reviews. FCMAT is not subject to state contracting laws, but it does follow some best practices, such as putting its more extensive, comprehensive review work out to bid and requesting that its clients evaluate its performance on each job. Although most of its clients who completed an evaluation form are pleased with its performance, FCMAT does not keep records of its resolution of complaints and thus cannot ensure that it addresses the concerns they raise. Using this information from its customers, FCMAT should be able to improve its service over time and continue using consultants that its customers have found helpful and professional.

Due to its small number of core staff, FCMAT uses consultants to assist in performing the work at the school districts and county offices.

Due to its small number of core staff, FCMAT uses consultants to assist in performing the work at the school districts and county offices but uses its own staff to supervise the consultants' work and write final reports. Through its professional network, FCMAT's staff recommend qualified consultants to the chief administrative officer, who gives the final approval to add a consultant to the list. Currently, FCMAT has compiled a list of 68 consultants with expertise in the fields of accounting, budget development, curriculum and instruction, human resources, maintenance and operations, special education, technology, and transportation, among other areas. These consultants include county office and school district employees on leave from their jobs, retirees, and independent consultants. The rates they charge FCMAT range from \$240 to \$1,000 per day, with an average rate of \$475 per day; the highest rates are charged by information technology consultants. To ensure the quality of their work, FCMAT consultants sign a protocol agreement requiring them to follow the scope and objectives of the study and to support their findings and recommendations. In addition, FCMAT requires its consultants to be independent during their assignments and to maintain confidentiality about their findings and recommendations. According to FCMAT, its policy is that if a consultant does not follow the protocol or meet performance expectations, FCMAT will not ask the consultant to work on future studies. Although we did not see evidence of this in practice, with only a small number of negative evaluations, FCMAT has had limited opportunity to apply this policy.

FCMAT is exempt from competitive bidding rules for its contracts, but has used a formal request for application process to select consultants for its larger comprehensive studies.

Although FCMAT is not subject to state contracting laws, which would require it to follow competitive bidding rules for its contracts, beginning with the Compton comprehensive review in 1998, FCMAT has used a formal request for application (RFA) process to select consultants for its larger studies. As part of the selection process, FCMAT's managers rank and review applications based on the criteria in the RFA. Based on the RFAs and responses for Compton, Oakland, West Contra Costa, West Fresno, and Berkeley, we determined that FCMAT's selections appeared reasonable, although it used the same consultants multiple times. For the first comprehensive study of Compton, FCMAT published an open RFA and received numerous responses. However, for the first Oakland study in 1999 and the subsequent studies in West Contra Costa and Berkeley, FCMAT did not publish an open RFA; instead, it mailed invitations to bid to only a short list of applicants. FCMAT may have received more bids from qualified applicants if it had sent invitations to bid to a larger group. By not soliciting bids from a larger group of consultants, FCMAT did not ensure that it had a sufficiently broad pool of experts from which to choose.

FCMAT uses another prudent business practice by soliciting feedback from its clients at the end of each job. From its formation in 1992 through January 15, 2004, FCMAT completed 357 management assistance studies and received 207 client evaluations representing 190 jobs, a 53 percent response rate. In 176, or 85 percent, of the evaluations received, the client rated FCMAT's performance a 4 or 5, meaning the client believed that FCMAT had provided a great deal of assistance or excellent assistance. Of the remaining 31 evaluations, 29, or 14 percent, ranked its assistance a 3 or below, and two did not give a rank.

According to FCMAT, the deputy executive officer will discuss with the client any evaluation that is rated a 3 or less to determine the strengths and weaknesses of the study and how FCMAT might improve its services. However, we reviewed five of the 29 evaluations receiving a 3 or below, and for four of them we were unable to determine how FCMAT had handled them and whether it addressed the concerns raised. The percentage of FCMAT's clients who expressed dissatisfaction is low, but almost half of its clients did not return their evaluation forms, and some of these clients may also be dissatisfied. Although FCMAT cannot be expected to address concerns it does not know about, it can be more effective in addressing those concerns that are brought to its attention.

FCMAT HAS GOOD REASONS TO KEEP ITS BILLING RATE ARTIFICIALLY LOW

By law, FCMAT charges its daily rate of \$400 per team member only for days that its staff or consultants spend at a school district or county office.

To offset some of the costs of performing the management assistance studies, the Legislature authorized FCMAT to charge school districts that are not declared as fiscal emergencies a daily rate for these services. In October 1999, FCMAT's governing board approved the current rate of \$400 per team member per day. The law allows FCMAT to charge this rate only for days that its staff or consultants spend at a school district or county office. As a result, the time spent on activities away from the school districts, such as report writing, is paid for from FCMAT's annual appropriation for management assistance studies.

As we discussed earlier, FCMAT's consultants charge FCMAT rates ranging from \$240 to \$1,000 per day, with an average rate of \$475 per day. Thus, the \$400 rate FCMAT charges school districts and county offices is on the low end of this scale but appears reasonable given that it is FCMAT's understanding that the Legislature intended for it to assist financially troubled school districts to avert financial crises, such as bankruptcy, and avoid the need for emergency loans from the State. Keeping the rate low affords these entities a lower-cost alternative to contracting for consulting services on the open market.

In January 2004, FCMAT's governing board reviewed the \$400 per day rate and agreed that FCMAT's services should be cost-effective for school districts to use. It also indicated that although the rate does not fully cover FCMAT's actual costs, the current amount of its annual management assistance appropriation is sufficient to make up the difference. Therefore, the board approved keeping the rate at \$400 per day but agreed to review it again should the appropriation for management assistance activities be insufficient to cover the difference in FCMAT's actual costs.

School districts that have received state emergency loans or that FCMAT's board determines to be in a fiscal emergency are generally not billed for FCMAT's services. Rather, the State pays the costs for these services, either through an annual appropriation or through separate, one-time appropriations for specific school districts. State law requires FCMAT's governing board to reserve at least 25 percent but not more than 50 percent of its revenues for management assistance studies for school districts it deems as being in a fiscal emergency. Over the last four fiscal years, FCMAT's governing board has designated

four school districts as being in a fiscal emergency. As a result of this designation, FCMAT can, at its discretion, choose not to charge these districts for the days its teams spent on-site.

Given FCMAT's understanding that the Legislature intended for it to assist troubled school districts to avert financial crises, it is reasonable that the State subsidizes the management assistance studies.

For fiscal years 2000–01 through 2002–03, FCMAT spent an average of \$2.1 million per year to provide management assistance studies and billed an average of \$632,000, or 30 percent of its average costs per year, to the school districts or county offices that requested FCMAT's management assistance services. Given FCMAT's understanding that the Legislature intended for it to assist troubled school districts to avert financial crises, it is reasonable that the State subsidizes the management assistance studies.

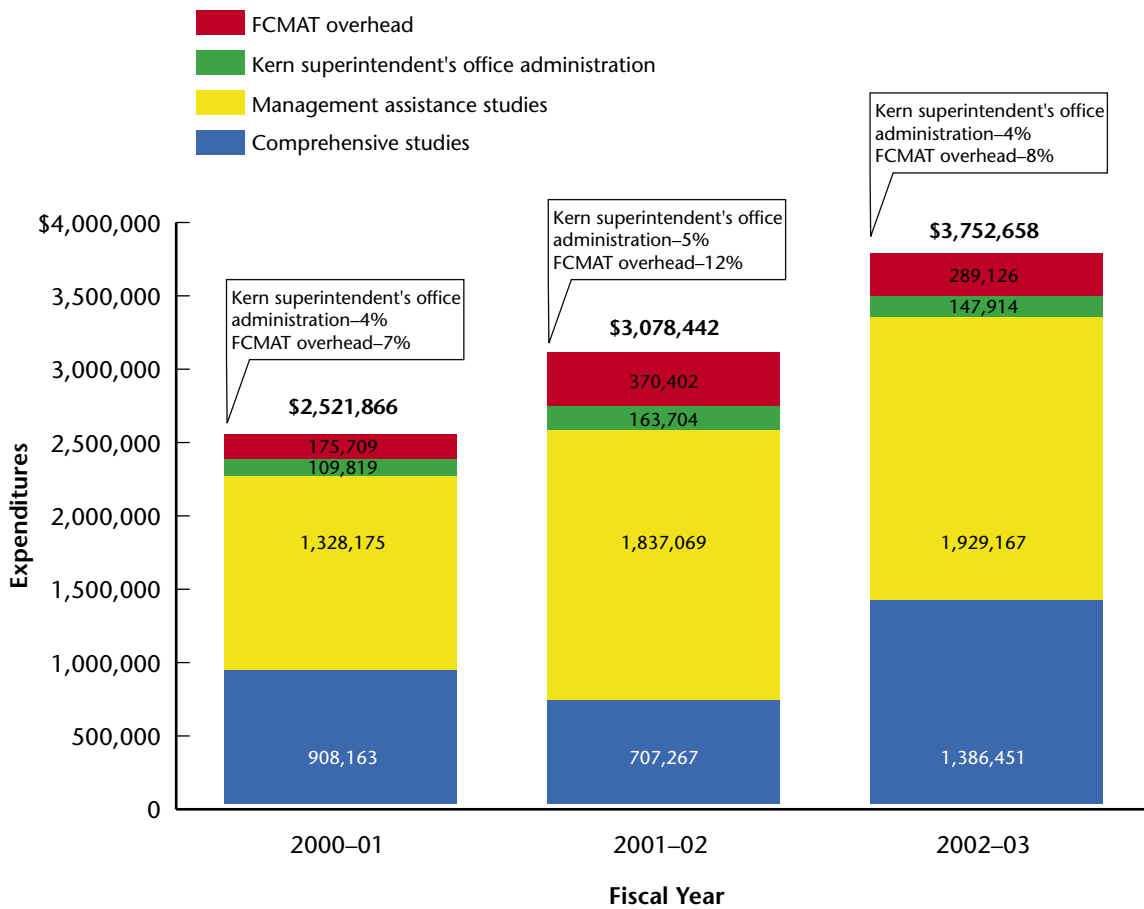
To help control the costs of these studies, FCMAT typically develops a study agreement. In the study agreement, FCMAT describes the scope and objectives of the study, indicates the services it will provide, and includes a list of documents and other information that it will need the school district to provide for the study. In addition, as part of its consultant contracts for these studies, FCMAT prohibits consultants from altering the scope and objectives defined in the study agreement without its approval. FCMAT also limits to seven days the amount of time consultants may spend finalizing their work before providing it to FCMAT after they conclude their work at the district site.

FCMAT'S ADMINISTRATIVE COSTS APPEAR REASONABLE

As we discussed in the Introduction, FCMAT's studies cost an average of \$3.1 million annually for fiscal years 2000–01 through 2002–03, including \$2.1 million per year for management assistance studies. For the larger comprehensive studies it worked on during that time period, which were funded under other school district-specific appropriations, it spent an average of about \$1 million per year. Figure 5 shows that FCMAT's administrative costs related to both types of studies are composed of two components: (1) costs incurred for services performed by the Kern County Superintendent of Schools (Kern superintendent's office), such as information technology and human resources; and (2) overhead costs for office space, utilities, office supplies, and equipment that are not directly related to school district studies but are necessary costs of FCMAT's operations. From fiscal years 2000–01 through 2002–03, FCMAT spent, on average, \$419,000, or 13.5 percent of its budget, per year on administrative costs.

FIGURE 5

FCMAT's Costs of Studies for Fiscal Years 2000-01 Through 2002-03



Source: FCMAT.

The overhead portion of FCMAT's total administrative costs was approximately \$195,000 higher for fiscal year 2001-02 than for fiscal year 2000-01. This difference is due primarily to increased computer equipment purchases and a shift in the mix of FCMAT's work. FCMAT's chief executive officer explained that a significant portion of the increase in overhead costs in fiscal year 2001-02 is because FCMAT purchased more computer equipment than it did in fiscal year 2000-01. FCMAT's accounting records support this assertion, indicating that in fiscal year 2001-02 FCMAT spent more for computer equipment and other technology-related purchases. When compared with the overhead costs for fiscal year 2000-01, these purchases account for approximately \$51,000, or 26 percent, of the increase. The remaining \$144,000 difference is due primarily to the fact that in fiscal year 2000-01 FCMAT spent more of

its time working on projects, such as the California School Information Services system and the professional development program, that are not related to FCMAT's school district studies and for which costs are not shown in Figure 5. As was shown previously in Figure 2 on page 7, FCMAT worked on more school district studies in fiscal year 2001–02 than in fiscal year 2000–01, leaving less time to work on other projects. As a result, for fiscal year 2001–02, a higher percentage of FCMAT's costs related to school district studies.

Similarly, compared to fiscal year 2001–02, FCMAT's overhead costs were approximately \$81,000 lower in fiscal year 2002–03. Approximately \$29,000, or 36 percent, of this decrease can again be attributed to higher computer-related purchases in fiscal year 2001–02. Most of the remaining difference represents costs for a study for the Kern superintendent's office for which FCMAT was reimbursed in fiscal year 2002–03.

Not included in FCMAT's overhead cost component are the costs for its chief executive and deputy executive officers to perform administrative duties, such as approving staff time sheets and attending meetings of FCMAT's governing board. FCMAT accounts for the entire salaries of these two managers as being directly related to its school district studies and other projects because most of their time is spent in these areas. Although the portion of time the chief executive officer and deputy executive officer spend on administrative tasks is part of the overall cost of administering FCMAT, it is not likely that including the portion of their salaries associated with performing those tasks would cause FCMAT's total administrative costs to exceed a reasonable proportion of its total costs. Specifically, even if the total amount of the salaries for FCMAT's chief executive and deputy executive officers were included as administrative costs, the percentage of FCMAT's total administrative costs would not exceed 26 percent of its total expenditures. Given FCMAT's small size, it is reasonable that its administrative costs, most of which would remain the same regardless of the number of studies FCMAT performs, represent a higher proportion of its total costs when compared to larger organizations, because FCMAT cannot benefit from the economies of scale that large organizations enjoy. Also, in order to be responsive to school districts located in Northern and Southern California and so it can be close to Sacramento, FCMAT maintains its main office in the Kern superintendent's office in Bakersfield and a satellite office in Petaluma, which results in higher administrative costs.

The component of FCMAT's administrative costs related to the Kern superintendent's office is below the amount that the Department of Education allows. Specifically, the Department of Education annually specifies a percentage of the total administrative costs of a grant or program, such as FCMAT, that the costs of administrative agents, such as the Kern superintendent's office, may not exceed. For fiscal years 2000-01 through 2002-03, the established rate ranged from 7.65 percent to 7.33 percent, while the portion of FCMAT's costs for the services the Kern superintendent's office provided did not exceed 7.15 percent.

RECOMMENDATIONS

To obtain the broadest range of consultants to choose from, FCMAT should expand its list of consultants who receive request for application packets.

To improve its customer service, FCMAT should ensure that it adequately addresses the issues its customers raise in post-study evaluations by developing a process for tracking the concerns and documenting the steps it takes to resolve them.

We conducted this review under the authority vested in the California State Auditor by Section 8543 et seq. of the California Government Code and according to generally accepted government auditing standards. We limited our review to those areas specified in the audit scope section of this report.

Respectfully submitted,



ELAINE M. HOWLE
State Auditor

Date: June 16, 2004

Staff: Nancy C. Woodward, CPA, Audit Principal
Debra L. Maus, CPA
Phillip Burkholder, CPA
Michelle R. Ludwick
John J. Romero
Leonard Van Ryn
Lea Webb

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Agency's comments provided as text only.

Kern County Superintendent of Schools
Larry E. Reider, Superintendent
1300 17th Street - City Centre
Bakersfield, CA 93301-4533

May 27, 2004

Ms. Elaine Howle, State Auditor
Bureau of State Audits
555 Capitol Mall, Suite 300
Sacramento, CA 95814

Dear Ms. Howle:

As the Administrative Agent for the Fiscal Crisis and Management Assistance Team (FCMAT), I took receipt of the draft Bureau of State Audit (BSA) report of the Fiscal Crisis and Management Assistance Team on Tuesday May 25, 2004. This letter represents our formal response to the draft audit.

We embrace the audit findings and recommendations and will develop, in coordination with the FCMAT Governing Board on June 23, 2004, a corrective action plan for the two recommendations.

Recommendation 1:

To obtain the broadest range of consultants to choose from, FCMAT should expand its list of consultants who receive request for application packets.

FCMAT Response:

We appreciate the Bureau of State Audits acknowledging that FCMAT uses a fair process to identify and select consultants for its studies and that FCMAT follows some best practices, such as putting more extensive, comprehensive review work out to bid.

FCMAT supports the Bureau's recommendation and will expand its list of consultants who receive requests for application packets. The corrective action plan approved by the FCMAT Governing Board relative to this recommendation will be submitted to the Bureau of State Audits as documentation of follow-up by FCMAT.

Recommendation 2:

To improve its customer service, FCMAT should ensure that it adequately addresses the issues its customers raise in post-study evaluations by developing a process for tracking the concerns and documenting the steps it takes to resolve them.

FCMAT Response:

We appreciate the Bureau of State Audits acknowledging that FCMAT uses prudent business practices in this area by soliciting feedback from its clients at the end of each job. Thank you for providing an independent analysis verifying that 85% of FCMAT's clients responding to the client evaluation form rated FCMAT's performance as "a great deal of assistance" to "excellent assistance".

FCMAT supports the Bureau's recommendation and will track the concerns of any FCMAT client by documenting the steps taken to resolve the concerns expressed through the client evaluation form. The corrective action plan approved by the FCMAT Governing Board relative to this recommendation will be submitted to the Bureau of State Audits as documentation of follow-up by FCMAT.

Summary Comments:

Finally, we would like to extend our appreciation for the Bureau's professional staff throughout the audit. They were professional, objective, and thorough.

Sincerely,

(Signed by: Larry E. Reider)

Larry E. Reider
Kern County Superintendent of Schools
FCMAT's Administrative Agent

cc: Members of the Legislature
Office of the Lieutenant Governor
Milton Marks Commission on California State
Government Organization and Economy
Department of Finance
Attorney General
State Controller
State Treasurer
Legislative Analyst
Senate Office of Research
California Research Bureau
Capitol Press