



CALIFORNIA  
DEPARTMENT OF  
EDUCATION

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STATE SUPERINTENDENT OF PUBLIC INSTRUCTION

April 17, 2009

Dear County and District Chief Business Officials and Charter School Administrators:

### **FISCAL ISSUES RELATING TO BUDGET REDUCTIONS AND FLEXIBILITY PROVISIONS**

This letter expands upon guidance in the California Department of Education's (CDE) letter of February 25, 2009, regarding the CDE's understanding and implementation of education trailer bill Senate Bill 4 of the 2009-10 Third Extraordinary Session (SBX3 4) (Chapter 12, Statutes of 2009). SBX3 4 enacts numerous significant changes to law, which include funding reductions to certain Kindergarten through Grade Twelve education programs and, to mitigate the effects of these reductions, unprecedented budgeting flexibility to local educational agencies (LEAs). The February 25 letter is available on the Web at <http://www.cde.ca.gov/fq/fr/eb/yr09budgetacts.asp>.

Following the enactment of SBX3 4, the CDE has worked extensively with Department of Finance, Legislative Analyst's Office, and legislative staff to clarify the intent and meaning of numerous provisions in the bill. This letter describes the clarifications achieved to date, gives fiscal and accounting guidance relating to the budget reductions and flexibility provisions, and notes anticipated changes to be enacted through cleanup legislation. The CDE is continuing to pursue those issues still requiring clarification.

### **BUDGETING FLEXIBILITY**

Sections 5, 15, and 42 of SBX3 4 provide budgeting flexibility for LEAs through the following measures:

- LEAs may use 100% of General Fund or Cafeteria Fund restricted balances as of June 30, 2008, for any educational purpose (but note caution below on use of Cafeteria Fund balances).
- For 2008-09 through 2012-13, LEAs may use funding formerly restricted for 39 specified categorical programs for any educational purpose.
- For 2008-09 through 2012-13, the required contribution to the routine restricted maintenance account (RRMA) is reduced from 3% to 1% of an LEA's total general fund expenditures and other financing uses.

- For 2008-09 through 2012-13, the local match requirement for Deferred Maintenance Program eligibility is eliminated.

These flexibility provisions are discussed in depth in the following sections.

In contrast to similar flexibility provisions in the 2002-03 state budget, SBX3 4 does not limit an LEA's budgeting flexibility to the amount of revenue limit and categorical funding reductions the LEA sustains. SBX3 4 also does not reduce the level of an LEA's required reserve for economic uncertainties.

### **Restricted Balance Flexibility**

Section 42 of SBX3 4 provides that, with the following specific exceptions, 100% of General Fund and Cafeteria Fund restricted account balances as of June 30, 2008, may be used for any educational purpose.

The exceptions are restricted reserves committed for capital outlay, bond or sinking funds, federal funds, and balances in the following programs:

- California High School Exit Exam Intensive Intervention Program
- Economic Impact Aid (EIA)
- Home-to-School Transportation (including Special Education and School Bus Replacement)
- Instructional Materials
- Quality Education Investment Act (QEIA)
- Special Education
- Targeted Instructional Improvement Grant

Note that SBX3 4 makes specific statutory reference to the original Targeted Instructional Improvement Grant, which ended in 2004-05, rather than to the current Targeted Instructional Improvement Block Grant, which replaced it.

The bill stipulates that balances of restricted accounts do not include appropriations deferred from 2006-07 to 2007-08 or appropriations deferred from 2007-08 to 2008-09. Attachment A lists the appropriation deferrals excluded from the provisions of SBX3 4. The bill also stipulates that restricted ending balances may not be used if that use would violate federal maintenance of effort requirements. Please see discussion of the effects on maintenance of effort requirements later in this letter.

It is the intent of the Legislature to allow LEAs to access surplus balances in the Cafeteria Fund. However, for districts participating in federal food programs, flexibility may be limited. Federal law requires school food authorities to establish a nonprofit school food service, and further requires that federal, state and local revenues received by the school food service be used only for the operation or improvement of such service. Therefore, you should exercise caution if your district receives federal funds and has established a school food service in accordance with federal guidelines, so as to ensure program compliance and avoid a federal audit exception.

The calculation of restricted balances eligible for flexibility and the accounting for transfers of restricted balances are discussed in the section titled "Accounting for Flexible Uses of Funds," later in this letter.

### **Categorical Program Flexibility**

Section 15 of SBX3 4 (*California Education Code (EC) Section 42605*) authorizes complete flexibility in the use of funds appropriated in 39 budget act items. For 2008-09 through 2012-13, school districts, county offices of education, and charter schools may use funds from these 39 items for any educational purpose. The funds are therefore unrestricted; program or funding requirements, as otherwise provided in statute, regulation, and budget act provisional language associated with the funding, are not in effect. Note that although *EC 42605(e)* describes certain continuing requirements with which LEAs must comply relating to the provision of instructional materials and the delivery of CalWORKS services, the existence of these requirements does not alter the newly unrestricted nature of the funding.

An LEA may choose to use funds from one or more of the 39 items in a manner completely different from how the funds could be used in years prior to 2008-09. Conversely, an LEA may choose to use the funds to continue to operate a program in the same manner as in the past. Both of these scenarios reflect a local decision as allowed by the flexibility provisions; any restrictions imposed on the funds from these 39 items are therefore local restrictions. There are no state restrictions or requirements, such as expenditure reports or compliance reviews, associated with the funding.

The accounting for categorical program flexibility is discussed in the section titled "Accounting for Flexible Uses of Funds," later in this letter.

Attachment B lists the programs specified in *EC 42605*.

## **Public Hearing**

There is ambiguity in SBX3 4 with regard to the public hearing requirement. The CDE has received clarification from the bill's authors that a public hearing as provided in *EC 42605(c)(2)* is a condition for receipt of funds from the 39 budget items made flexible by the bill, but is not a condition of the funds being flexible as is suggested in *EC 42605(e)(4)*. To receive funds, the governing board, at a regularly scheduled open public hearing, shall take testimony from the public and shall discuss and approve or disapprove the proposed use of funding. It is the intent of the authors that the annual governing board budget adoption may satisfy this requirement.

Action by the governing board to transfer funds from one use to another is not necessary for the funds to be flexible. Accordingly, there is no requirement for a public hearing on the proposed transfer of funds for the funds to be deemed flexible. The funds are deemed flexible upon receipt and retroactively to July 1, 2008.

Consistent with past practice, funds will be allocated to LEAs prior to any determination as to whether a public hearing occurred. If a subsequent compliance review were conducted and a determination made that the public hearing requirement was not met, the LEA would be subject to potential return of the funds. Due to the statutory timelines of the 2008-09 audit guide development, the CDE anticipates no audit of the public hearing requirement in 2008-09.

## **Base Year Funding Provisions**

SBX3 4 provides that amounts appropriated in the "flexed" 39 budget act items in 2009-10 through 2012-13 shall be apportioned to an LEA in the same relative statewide proportion as the LEA received those items for 2008-09. In other words, if an LEA received 2% of the funds allocated in a budget act item in 2008-09, that LEA will receive 2% of the amount appropriated in that same budget act item in each of 2009-10 through 2012-13.

This base year relative percentage formula supersedes all previous funding formulas, and is consistent with the concept of flexible funding. Accordingly, through 2012-13, the CDE will not require applications, will not monitor participation levels such as hourly attendance and average daily attendance, and will not collect other documents or data previously required for funding. All funding and program requirements are deemed satisfied.

Of concern is using 2008-09 as the base year when there are no provisions of law in effect by which an LEA could report meaningful participation in 2008-09, such as average daily attendance or hours. As such, for a relatively small number of the 39 budget items, representatives of the Administration and Legislature anticipate

legislation that will change the base year to 2007-08. At this time, the budget items that appear to be candidates for a legislative change to the base year are:

- Item 6110-104-0001 Remedial Supplemental Instruction Programs
- Item 6110-105-0001 Regional Occupational Centers and Programs
- Item 6110-156-0001 Adult Education
- Item 6110-190-0001 Community Day Schools
- Item 6110-193-0001 (Schedule 3) Reader Services for Blind Teachers
- Item 6110-198-0001 Cal-SAFE
- Item 6110-232-0001 Class Size Reduction Grade 9
- Item 6110-240-0001 (Schedule 2) Advanced Placement Fee Waiver Program

LEAs will see changes to apportionments in 2008-09 to reflect funding reductions resulting from SBX3 4 (see the CDE's February 25, 2009 letter). Apportionments for those items whose base year will likely change to 2007-08 will be adjusted when that change is enacted into law. In the interim, 2008-09 will be treated as the base year.

### **Charter Schools**

As currently written, the SBX3 4 requirement that an LEA's receipt of budget act item funds in 2009-10 through 2012-13 be based on the amount that the LEA received from that item in 2008-09 prevents charter schools established after 2008-09 from receiving funds from the 39 flexed budget act items, including the charter school categorical block grant. The CDE anticipates legislation to address this and other unintended consequences.

### **K-3 Class Size Reduction**

SBX3 4 changed the budget item source of appropriations, but not the total state support, for the Kindergarten and Grades One Through Three (K-3 CSR) Program in 2008-09, and also closed the program in 2009-10 through 2011-12 to participants that did not apply for 2008-09 funds. In addition, SBX3 4 established a new schedule of funding reduction percentages in *EC 52124.3* for classes exceeding 20.44 pupils. This new schedule replaces, for the four-year period from 2008-09 through 2011-12, the schedule of funding reduction percentages established previously in *EC 52124*. The new schedule provides for funding reductions as follows:

- 5% for classes ranging from 20.45 to 21.44, inclusive
- 10% for classes ranging from 21.45 to 22.44, inclusive
- 15% for classes ranging from 22.45 to 22.94, inclusive
- 20% for classes ranging from 22.95 to 24.94, inclusive, and
- 30% for classes ranging from 24.95 and more.

Like the previous schedule, funding for classes in excess of 20.44 pupils will be calculated based on a count of 20 pupils multiplied by the funding rate, less the funding reduction percentage multiplied by 20 times the funding rate.

As currently written, SBX3 4 also limits any funding to classes in the grade level or levels for which the LEA applied for 2008-09 funds, with this limit to be in effect for the four-year period from 2008-09 through 2011-12. It is our understanding, however, that clean-up legislation will be enacted to limit any funding to the number of classes, instead of the number of grades, for which LEAs applied for 2008-09 funds. The grade level implementation priorities remain in effect; at each school, grade one must be implemented first, followed by grade two. Once all classes in grades one and two at the school have been reduced, the classes in grade three or kindergarten may be reduced. However, if an LEA implementing grades one through three later chose to implement kindergarten instead of grade three, this would be allowed; the LEA's claim to funds would only be limited to the number of classes for which it applied for funds in 2008-09. We also anticipate that the clean-up legislation will change the date by which 2008-09 applications must have been received from December 10, 2008, to January 31, 2009.

### **Average Daily Attendance**

Discussions are underway among state agencies, the Administration, and the Legislature regarding the impact of the change in average daily attendance reporting on other areas and entitlement formulas such as Proposition 98, lottery, and county office other purpose funding.

### **Repeal of Budget Act Section 12.40**

SBX3 4 repealed Section 12.40 of the 2008 Budget Act, which allowed limited flexibility for transfers of funds among certain categorical programs. Any Section 12.40 transfers made in 2008-09 should be reversed.

## **Deferred Maintenance Program**

The local matching contribution normally required as a condition of eligibility for Deferred Maintenance basic grant funding is eliminated for 2008-09 through 2012-13. In response to many questions from LEAs about this provision, the CDE gives the following clarification.

To preface, the Deferred Maintenance Program is funded by the state one year in arrears. Funding for which LEAs apply in 2007-08 is appropriated by the state and apportioned to LEAs in 2008-09, and so on.

Procedure 510 of the California School Accounting Manual, Recognition of Common Revenue Sources, provides (page 510-3):

The Deferred Maintenance Apportionment is recognized in the year it is appropriated in the State Budget Act and apportioned to LEAs. The LEA's matching transfer to the deferred maintenance fund is recognized in the year that it is made or accrued.

The funding appropriated by the state and apportioned to LEAs in 2008-09 is therefore recognized in 2008-09, regardless of the fact that the LEA applied for it in 2007-08 and regardless of the year in which the LEA made its qualifying local match.

The funding apportioned to LEAs in 2008-09 is the first year of funding for which the local match is not required. The CDE is aware that by the time that SBX3 4 was enacted, LEAs may have already transferred their local match to the Deferred Maintenance Fund. Accordingly, the CDE believes that if an LEA already transferred its local match to the Deferred Maintenance Fund to be eligible for funds appropriated in the 2008-09 Budget Act, the LEA may reverse that transfer because the match is not required.

In addition to the elimination of the local match requirement, deferred maintenance program funding is one of the 39 budget items made flexible by *EC 42605* for 2008-09 through 2012-13. Funding related to this budget item is therefore unrestricted for this five-year period and may be used for any educational purpose. Please see discussion in the section titled "Accounting for Flexible Uses of Funds," later in this letter.

## **Routine Restricted Maintenance Account Contribution**

The contribution to the routine restricted maintenance account (RRMA), required for LEAs participating in the School Facility Program, is reduced from 3% to 1% of an

LEA's total general fund expenditures and other financing uses for 2008-09 through 2012-13. The accounting for RRMA contributions is discussed in the *California School Accounting Manual (CSAM)*, Procedure 650, Facility Maintenance Program—Coding Examples.

## **2008-09 Audit Guide**

The Office of the State Controller is issuing guidance on the changes to the 2008-09 audit guide that reflect the new flexibility provisions.

### **ACCOUNTING FOR FLEXIBLE USES OF FUNDS**

The unprecedented flexibility provided by SBX3 4 means that eligible balances and funds can be used for any educational purpose, whether that purpose was originally intended for that program or not.

This has some sweeping implications for accounting in the Standardized Account Code Structure. Given the now-unrestricted character of these balances and funds, in most instances the restricted resource codes formerly assigned to them are no longer meaningful and the continued use of restricted resource codes would be misleading.

The following sections provide accounting guidance for the flexibility provisions of SBX3 4.

#### **Accounting for Transfers of Restricted Balances Pursuant to Section 42**

The restricted balance flexibility pursuant to SBX3 4 effectively transforms the June 30, 2008, restricted account balances eligible for flexibility from restricted to unrestricted retroactively to July 1, 2008, and, with certain exceptions discussed below, the balances should be accounted for accordingly.

Transfers of restricted balances eligible for flexibility should be reported in Object 8997, Transfers of Restricted Balances, as a debit to the restricted resource from which the balance is being transferred and as a credit to Resource 0000, Unrestricted. This accounting reflects the change in the character of these formerly restricted balances to unrestricted pursuant to SBX3 4.

For purposes of identifying the restricted account balances available for transfer, include amounts in the restricted ending fund balance account as well as amounts in the deferred revenue account. This is consistent with the intent that "restricted account balances" is synonymous with "carryover," that is, the difference between the amount of

a program award available for expenditure and the amount of the award that the LEA has actually expended so far, without regard to how that carryover is treated for purposes of accounting.

In very few instances, it is also appropriate to include amounts that were not in any account on the LEA's books as of June 30, 2008, but that still meet the above definition of "carryover." An example would be an expenditure-driven grant in which only 75% of the funding was advanced to the LEA. If by June 30, 2008, the LEA had not expended more than the 75% advanced, the remaining 25% of the grant funds would not be part of either the LEA's restricted ending fund balance account or its deferred revenue account. However, since the LEA would have been entitled to expend the remaining 25% by June 30, 2008, the 25% would be considered in the LEA's calculation of restricted balances available for transfer.

The CDE notes that for multi-year grants such as Healthy Start, LEA balances as of June 30, 2008, are eligible for restricted balance flexibility, but amounts not yet allocated to the LEA and not allowable for expenditure by the LEA until a future year should not be recognized by the LEA and are not considered "balances" for this purpose.

Although SBX3 4 allows that available restricted account balances as of June 30, 2008, may be transferred at any time prior to closing the books for either 2008-09 or 2009-10, the CDE emphasizes that LEAs should complete all transfers as of 2008-09 to accurately portray in the 2008-09 financial reports that the balances are no longer subject to external restrictions. The CDE emphasizes that, except as discussed below, given the removal of external restrictions on these balances, use of the original restricted program resource, or even a locally defined restricted program resource, for these balances after June 30, 2008, is not appropriate regardless of whether the LEA has yet decided how it intends to use the balances.

The CDE will close the restricted standardized account code structure (SACS) resource codes associated with balances eligible for transfer using the following approach. These codes will not be available in the Budget release of the CDE's 2009-10 financial reporting software being released in the next few weeks.

- Restricted resource codes for programs whose restricted balance is eligible for transfer, and whose ongoing funding is unrestricted pursuant to Section 15 of SBX3 4 or for which there is no ongoing funding, will be closed as of the end of 2008-09. LEAs should transfer all restricted balances in these accounts by the end of 2008-09.
- Restricted resource codes for programs whose restricted balance is eligible for transfer, but whose ongoing funding is not unrestricted pursuant to

Section 15 of SBX3 4, will be left open. LEAs that elect not to transfer these balances should continue to report them in the original restricted resource.

- Restricted resource codes for programs that do not have either of the above characteristics will be considered on a case by case basis.

### **Accounting for Categorical Program Flexibility Pursuant to Section 15**

Section 15 of SBX3 4 states that LEAs using the categorical program flexibility provisions “shall be deemed to be in compliance with the program and funding requirements contained in statutory, regulatory, and provisional language associated with the items.”

This freedom from reporting and spending restrictions effectively transforms the ongoing funding allocated for the 39 budget items specified in the bill from restricted to unrestricted retroactively to July 1, 2008. The funding should therefore be accounted for accordingly. The transformation of these funds to unrestricted is not conditional on the required public hearing about the intended use of the funds; the public hearing is a condition of receipt of the funds, but is not a condition of the funds’ newly unrestricted character.

**Accounting for 2008-09 through 2012-13:** Except as discussed in “Accounting Issues Unique to 2008-09” below, LEAs must account for all revenues and expenditures relating to funding from the 39 budget act items enumerated in Education Code Section 42605 as unrestricted. Apportionment letters from the CDE will reflect this effective immediately.

Although LEAs that choose to use funds from one or more of these 39 items to operate a program in the same manner as in the past must now account for the program as unrestricted, they may use a locally defined unrestricted resource code in the range 0001-0999 to identify the program if they wish. Locally defined unrestricted resource codes must be rolled up to Resource 0000, Unrestricted, when reporting year-end financial data to the CDE. The CDE emphasizes that given the removal of external restrictions on these funds, use of the original restricted program resource, or even a locally defined restricted program resource, is not appropriate.

Note that the statutes requiring that state funding formerly restricted to the Deferred Maintenance and Adult Education programs be deposited into the Deferred Maintenance and Adult Education funds are made inoperable by SBX3 4. Revenues relating to these budget items should now be deposited to the General Fund. The CDE is researching statutory and accounting requirements relating to the continued use of

the Deferred Maintenance Fund and the Adult Education Fund, and will issue further guidance when that research is complete.

**Accounting Issues Unique to 2008-09:** Because SBX3 4 was not enacted until nearly three quarters of the way through 2008-09, accounting accurately for funds made flexible in 2008-09 is almost certain to be problematic. Most LEAs have operated the original programs relating to these 39 items for most of the year in accordance with the restrictions formerly applicable to the funds. Although the restrictions were removed retroactive to July 1, the CDE recognizes that it may not be practicable or preferable for LEAs to adjust their accounting this late in the year to portray these funds as unrestricted.

The CDE acknowledges that inconsistencies in the SACS data collected for 2008-09 will be inevitable due to the authorization of funding flexibility so late in the fiscal year. Nevertheless, the CDE encourages LEAs to report their 2008-09 uses of these funds in as meaningful a manner as possible within practical constraints. Possible accounting approaches include:

- Report activities relating to these funds as unrestricted for the entire year by reclassifying year-to-date activity from a restricted resource to an unrestricted resource, and by accounting for the remainder of the year's activity as unrestricted. The CDE believes this is the most accurate portrayal, but recognizes that it is the most time intensive.
- Report activities relating to these funds as restricted until February 20, 2009 (the date that SBX3 4 was enacted) or until the date that the LEA began to use funds flexibly. After that date use Object 8998, Categorical Flexibility Transfers, to transfer unspent balances in the formerly restricted resources to an unrestricted resource, and account for the remainder of the year's activity as unrestricted.
- Report activities relating to these funds as restricted for the entire year. At the end of the year use Object 8998, Categorical Flexibility Transfers, to transfer unspent balances in the formerly restricted resources to an unrestricted resource and account for the ending balances as unrestricted.

The CDE believes this approach involves the least effort, but in the interest of making accounting data as meaningful as possible, the CDE suggests that an LEA should use this approach only if its uses of the funds following enactment of SBX3 4 were largely consistent with the former restrictions relating to those funds. If the LEA's uses of the funds following enactment of SBX3 4 differed significantly from the original restrictions, the CDE encourages the LEA to report the use of the funds in an unrestricted resource rather than in the original restricted resource.

Regardless of which approach an LEA takes to report its 2008-09 activities relating to these 39 budget items, at the end of 2008-09 all LEAs, without exception, should use Object 8998, Categorical Flexibility Transfers, to show the transfer of any unspent balances in these formerly restricted program resources to unrestricted and to accurately portray in the 2008-09 financial reports that the balances are not subject to external restrictions.

The CDE will close most of the restricted resource codes associated with the 39 budget items as of the end of 2008-09. These codes will not be available in the Budget release of the CDE's 2009-10 financial reporting software being released in the next few weeks.

As noted previously, SBX3 4 repealed Section 12.40 of the 2008 Budget Act. Any Section 12.40 transfers made previously in 2008-09 should be reversed. The title of Object 8998, Categorical Flexibility Transfers, has been changed to remove mention of Budget Act Section 12.40.

## **IMPORTANT CONSIDERATIONS RELATING TO TRANSFERS OF RESTRICTED BALANCES**

### **Effect on Federal Maintenance of Effort Requirements**

As mentioned previously, SBX3 4 stipulates that “[an LEA] governing board shall not use the ending balance in any restricted account if that use would violate a federal maintenance of effort requirement.”

The CDE notes that the transfer of formerly restricted balances from a restricted resource to an unrestricted resource is unlikely to have an effect on LEA-level MOE requirements. Rather, it is the *use* of the balances, once transferred, that might potentially impact an LEA's MOE. However, the CDE believes that the likelihood of an LEA compromising an MOE requirement by expending its formerly restricted balances “for any educational purposes” as allowed by SBX3 4 is remote.

To illustrate:

- No Child Left Behind (NCLB) MOE: Generally, all of an LEA's expenditures of non-federal funds for educational purposes, whether restricted or unrestricted, are counted for purposes of the NCLB MOE requirement. Transfers of formerly restricted balances to unrestricted, as long as the resulting expenditures are “for any educational purpose,” would have no effect on the NCLB MOE.

- Special Education MOE: If Special Education balances were used for an educational purpose not relating to Special Education, the Special Education MOE might be compromised. However, Special Education balances are not eligible for flexibility.

LEAs should be aware that waiver provisions exist for when MOE requirements are not met. For example, NCLB regulations provide that if there is an unprecedented decline in state revenues, individual LEAs may apply directly to the federal government for a waiver of the MOE requirements. If you are unsure whether a particular federal program has a required MOE or whether an MOE requirement can be waived, you should contact the appropriate CDE program office.

### **Voter-approved initiatives**

Because the Legislature generally has no authority to amend a voter-approved initiative unless the measure itself so provides, balances generated as a result of a voter-approved initiative are not available for flexibility purposes. Examples of such programs include:

After School Education and Safety – Proposition 49  
Lottery Instructional Materials - Proposition 20  
Tobacco Use & Prevention Education (TUPE) - Proposition 10

### **Contractual obligations with external parties**

We also recommend that you use caution when applying SBX3 4 flexibility so that you do not violate contractual obligations with external parties. The Legislature's authority to abrogate contractual obligations is limited, and legal issues may arise if you unilaterally cancel contracts with external parties. The Legislature's authority does extend, however, to contracts and grants between state and local governmental agencies, where state funds are involved.

### **CASH FLOW ISSUES**

The state's current year budget cuts and appropriation deferrals may result in cash flow management problems for LEAs in the current year. To alleviate cash shortfalls, you may wish to consider the following options.

## **Interfund Borrowings**

EC 42603 provides that moneys held in any fund or account may be temporarily transferred to another fund or account for payment of obligations, with certain limitations.

- Amounts transferred shall be repaid either in the same fiscal year, or in the following fiscal year if the transfer takes place within the final 120 calendar days of a fiscal year.
- Borrowing shall occur only when the fund receiving the money will earn sufficient income during the current fiscal year to repay the amount transferred.
- No more than 75% of the maximum of moneys held in any fund during a current fiscal year may be transferred.

**Accounting for Interfund Borrowings:** EC 42603 provides that the transfer shall be accounted for as temporary borrowing between funds or accounts and shall not be available for appropriation or be considered income to the borrowing fund or account. The accounting is a debit to Object Code 9310, Due From Other Funds, with a credit to Cash in the lending fund, and a debit to Cash with a credit to Object Code 9610, Due To Other Funds, in the borrowing fund. These amounts are then carried on the balance sheet until the entry is reversed when the funds are repaid. Temporary borrowings are not accounted for as interfund transfers, and do not affect the fund balance for either the borrowing or lending fund.

If you are considering borrowing from restricted programs and are concerned about the legality of doing so, we suggest you discuss the issue with your legal counsel. Also note that borrowings from certain restricted funds should be repaid with interest, if there are interest requirements relating to those programs or funds.

## **Short-term Borrowings from External Sources**

If it is not possible to alleviate temporary cash shortfalls by interfund borrowing, it may be necessary for LEAs to borrow funds on a short-term basis from external sources. Following are some possible sources.

- Tax Revenue Anticipation Notes. Tax Revenue Anticipation Notes (TRANs) are short-term, interest bearing notes issued by a government in anticipation

of tax revenues that will be received at a later date. The notes are retired from the tax revenues to which they are related. Many LEAs issue TRANs for cash flow management purposes every year.

- County Office of Education. EC sections 42621 and 42622 authorize county offices of education to loan funds to school districts. The funds must be repaid either within the fiscal year or within the next fiscal year, depending on the type of loan that is granted. Certain other restrictions apply, as indicated in the applicable statutes. Such loans are discretionary and are subject to availability of funds at the county office level.
- County Treasurer. EC 42620 requires the county board of supervisors to loan money to school districts when certain conditions exist. However, Section 6 of Article XVI of the Constitution of the State of California requires that such loans must be made before the last Monday in April. Loan and repayment terms vary by county, so you may wish to coordinate with your county office of education.

#### **FUTURE CDE EFFORTS REGARDING SBX3 4**

The CDE will continue working with other agency staff to clarify remaining issues relating to implementation of SBX3 4 and will communicate these issues as they are identified.

The CDE anticipates posting Frequently Asked Questions in the near future on the Web at <http://www.cde.ca.gov/fg/fr/eb/yr09budgetacts.asp>. For now, we encourage LEAs to implement the budgetary and accounting guidance contained in this letter as they develop their 2009-10 budgets, revise their 2008-09 budgets, and prepare their 2008-09 year-end financial reports.

For questions relating to the applicability of SBX3 4 to a particular program, please contact the program office directly. Program contact information can be found on the SACS Query page at <http://www.cde.ca.gov/fg/ac/ac> or by using the Search CDE Funding Web page at <http://www.cde.ca.gov/fg/gp/sf>.

For accounting questions relating to the flexibility provisions of SBX3 4, please contact the Office of Financial Accountability and Information Services at 916-322-1770 or [sacsinfo@cde.ca.gov](mailto:sacsinfo@cde.ca.gov).

For questions regarding the state education budget overall, please contact the Fiscal Policy Division at 916-324-4728. You may also contact Carol Bingham, Director, Fiscal Policy Division, by e-mail at [cbingham@cde.ca.gov](mailto:cbingham@cde.ca.gov).

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All other questions may be directed to Scott Hannan, Director of the School Fiscal Services Division, at 916-322-3024.

These are challenging fiscal times for the state and for LEAs and we hope that the guidance in this letter is helpful. We appreciate your patience as we have worked to get clarification on some of the extraordinary provisions of SBX3 4 and as we continue to work to resolve the remaining issues.

Sincerely,

Scott Hannan, Director  
School Fiscal Services Division

SH:pwo  
Attachments  
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