Comments

CALIFORNIA STATE AUDITOR'S COMMENTS ON THE RESPONSE FROM SACRAMENTO UNIFIED

To provide clarity and perspective, we are commenting on Sacramento Unified's response to our audit. The numbers below correspond to the numbers we have placed in the margin of Sacramento Unified's response.

Sacramento Unified implies it needed to cut services to pay for its 2017 labor agreement with its teachers union. However, it fails to note that it was warned before approving the contract that it could not afford this agreement and its board approved the agreement anyways. It relied on one-time funds to pay for the salary increases instead of proposing a plan to cover these ongoing costs. Further, the district could have negotiated additional cost savings since the 2017 agreement that did not reduce services, but it has not. Consequently, the district now faces insolvency and the potential for reduced funding for its teachers and students if it accepts a loan from the State due to the need to pay interest on the loan and other related costs that we discuss on pages 34 and 35. ①

Sacramento Unified overstates our conclusions. The report indicates that the district needs to address the three largest drivers of its costs, which are salaries, benefits, and special education costs, and we recommend on page 39 that the district develop a detailed plan that would address its costs. ②

We did not validate the district's budget data. We based our report on sufficient evidence, including audited financial statements. We also used information prepared by the district, such as budgets, and information from the district's accounting system and compared it to audited financial statements and trends from prior years to assess the reasonableness of the information. However, as we note on page 27, we identified significant variances between the district's budget and actual expenditures and on page 39 we recommend that the district develop a budget methodology using best practices. ③

In its attempt to summarize the findings of our audit, Sacramento Unified selectively presents our key findings. The summary fails to note where our report details the district's decisions that led to its current situation. For example, the district board approved the 2017 labor agreement despite being warned it could not afford it. ④

5 Our audit did not confirm that Sacramento Unified needs to make $27 million in cost reductions. As we state on page 35, the *district recommended to its board* $27 million as the amount of cost reductions needed to eliminate deficit spending by fiscal year 2021–22. As we note in Figure 9 on page 35, the district spends more than it receives in revenue and its costs are growing faster than its revenues. Consequently, as Figure 9 shows, these reductions alone would likely not be sufficient for it to avoid continued deficit spending in fiscal year 2022–23.

6 While preparing our draft audit report for publication, some of the text quoted by Sacramento Unified was changed to remove the term *state takeover*. Recent changes to state law have made the term inaccurate.

7 While preparing our draft audit report for publication, some of the figure and table numbers quoted by Sacramento Unified changed. Figure 7 is now Figure 9. Figure 8 is now Figure 10, and Table 5 is now Table 3.

8 Our audit did not confirm that the 2017 labor agreement cost $31 million. Rather, as we note on page 14, Sacramento Unified calculated in June 2017 that a 1 percent increase in salary and statutory benefits would cost about $2.1 million. Based on this calculation, we estimate that the 2017 contract's salary increases and adjustment to the salary schedule, which resulted in a 15 percent increase in salary and statutory benefits for teachers, would add about $31 million per year in ongoing spending.

9 We developed the decline in enrollment independent of Sacramento Unified based on the district's audited financial statements for fiscal years 2013–14 through 2017–18 and its unaudited financial report for fiscal year 2018–19.

10 Although Sacramento Unified states that it agrees with our recommendation, its response does not indicate how or when it will implement the recommendation. We look forward to seeing the district's progress at its 60-day update.

11 As we told Sacramento Unified several times during the audit, our report would not divulge ongoing, nonpublic negotiations between the district and its labor unions. Further, Figure 10 on page 37 does indicate the potential savings the district could incur if it revised its health care options for all employees.

Sacramento Unified's statement is disingenuous. As we note in the report on page 16, the county office superintendent warned the district before it approved its agreement with its teachers union that the district could not afford the agreement. Yet, its board approved the agreement anyway. In addition, the district's statement that it could have only made reductions by cutting programs is not accurate. The district board could have proposed offsetting cost reductions, such as to health care costs, before it approved the 2017 labor agreement, but it did not do so. As the district notes in its response, and as we note in our report on page 18, the district instead chose to rely on one-time funds rather than trying to solve its fiscal problems. As such, we stand by our statement that the district board failed to uphold its fiduciary duties because it approved this contract without making necessary cost reductions. ⑫

Sacramento Unified's quotation of a letter from the county office superintendent is misleading, as it does not fairly represent what the county office superintendent told the district at the time. As we note in our report on page 16, the county office superintendent warned the district before it approved its 2017 labor agreement that it needed to reduce its costs in other areas to afford the cost of the new agreement. Further, as we note on page 18, when the district ultimately decided to rely on one-time funds from the State, the county office superintendent warned the district that such an action was a poor business practice. ⑬

Sacramento Unified's statement regarding when its board recognized it needed to make cost reductions is misleading. The sentence seems to imply that the board did not realize it would need to make cost reductions until after it had approved the 2017 labor agreement. As we note on page 16, the county office superintendent informed the board before it approved the agreement that it could not afford the agreement without making cost reductions. In addition, as we discuss on pages 17 and 18, the district's former chief business officer also informed the board of the need to make budget adjustments before the board approved the agreement. ⑭

We did not report that the layoffs Sacramento Unified issued in 2019 were to "right-size" its staff. Rather, we note on page 9 that the district laid off staff in an effort to reduce its costs but that it subsequently rehired many of those it laid off. ⑮

Even though it has recently required some employees to begin contributing toward their retiree health benefits, the district has not developed a plan for how it will pay for these promises to its employees despite repeated requests from the county office superintendent, as we note on pages 21 and 22. ⑯

(17) Sacramento Unified's summary of the OPEB actuarial report (OPEB report) it mentions is misleading. At the time of our exit conference with the district in October 2019, the district's fiscal year 2018–19 independent financial audit that includes information from the referenced OPEB report had not been finalized. Therefore, we did not include this information in our audit. Nevertheless, the district's statement that its liability declined due to district actions is inaccurate. The actuary that prepared the OPEB report reduced the district's projected liability because of favorable changes in assumptions, the majority of which were due to health care premiums not increasing as fast as expected—a factor that had nothing to do with actions of the district. Further, the OPEB report still notes that the district has a $526 million liability and the district has no plan for how it will pay for it, as we note on page 21.

(18) Although, as we note on page 28, Sacramento Unified submits its budget in June and interim reports in December, March, and May, there is still a six-month gap between submission of its budget in June and the first interim report in December where the district could update its multiyear projections to increase transparency.

(19) We agree there are statewide issues concerning special education that may affect the district. Nonetheless, because the district's special education costs increased significantly over the last several years, we expected the district to have taken steps to control these costs—particularly in light of its deteriorating financial situation. However, as we note on page 23, Sacramento Unified has done little to control its special education costs.

(20) Although Sacramento Unified states that it agrees with many of our recommendations, we are concerned that it fails to address several of our recommendations in its response. Specifically, the district fails to discuss our recommendations regarding any efforts to reduce its executive management turnover, including developing a succession plan and a mentoring program. We look forward to seeing the district's progress in these areas in its 60-day update.