

# Last Minute Memorandum

**To:** STATE BOARD MEMBERS

**Date:** August 29, 2003

**From:** Susan Lange

**Re:** ITEM # 16

**Subject** ANNUAL FINANCIAL REPORTING FOR ALL K-12 LOCAL EDUCATIONAL AGENCIES, INCLUDING CHARTER SCHOOLS, AS REQUIRED BY ASSEMBLY BILL 1994 (CHAPTER 1058, STATUTES OF 2002) – ADOPT PROPOSED TITLE 5 REGULATIONS

There were no comments during the public hearing held on August 25, 2003; however, two letters were received during the 45-day public comment period regarding the proposed regulations and the alternative form for charter school financial reporting. The letters are included as Attachments 2 and 3.

1. The Department of Finance (DOF) suggested an amendment to Section 15070 to clarify that the regulations proposed in Section 15070 do not impose a mandate on local educational agencies (LEAs) to use the standardized account code structure (SACS). Even though all school districts and county offices of education have voluntarily opted into the program by accepting the funding provided by Section 39 of Chapter 299, Statutes of 1997, the DOF was concerned that a section of the proposed regulations could be construed as imposing a State mandate on school districts. We have incorporated the language suggested by the DOF into Section 15070, although with their concurrence, we have rearranged the proposed sentence.

The wording of Section 15070 as proposed by DOF (and modified by CDE) is shown below with underlined and strikeout type to show the changes:

15070. Submission of Annual Financial Statements

Except as provided in Section 15071, every county office of education, school district, charter school, and educational joint powers agency (as defined in Education code Section 41023) that elects to use the standardized account code structure, subject to the provisions of Section 39 of Chapter 299, Statutes of 1997, shall submit an annual statement of receipts and expenditures in the format of the standardized account code structure, ~~subject to the provisions of Section 39 of Chapter 299, Statutes of 1997.~~

2. A letter expressing opposition to the proposed regulations was received from Eric Premack, an interested party.

Mr. Premack expressed various concerns about requiring charter schools to report using SACS and the level of detail contained in the alternative form for charter schools.

CDE response: The regulations allow, but do not require, charter schools to report in the SACS format. Also, as previously discussed, we believe the alternative form for charter schools is an appropriate level of detail, and is not onerous for charter schools. Therefore, we recommend no changes to the regulations or alternative form as a result of these comments.

Please note that an inadvertent error was made when the draft regulations were released for public comment, in that some last minute, non-substantive changes were not incorporated. We have already confirmed with the Office of Administrative Law (OAL) that these changes are non-substantive and may be included in the current package with no requirement for an additional public comment period. These changes, along with the change recommended by the Department of Finance, are included in the revised regulations in Attachment 1 (see ~~strikeout~~, **bold**, and double underlined type).

### **Recommendation**

We recommend that the State Board adopt the regulations with the understanding that if OAL finds that the changes are substantive, the proposed regulations will be immediately sent out for a 15-day public comment period and will be brought back to the State Board for approval in November.

1 Title 5. EDUCATION

2 Division 1. State Department of Education

3 Chapter 14. School Finance

4 Subchapter 2. Budgeting, Accounting and Reporting

5  
6 Add Article 2 (commencing with Section 15060) to read:

7 **Article 2. Standardized Account Code Structure**

8 **§ 15060. Standardized Account Code Structure**

9 (a) The California School Accounting Manual adopted by the State Board of Education pursuant  
10 to Education Code section 41010 shall incorporate a standardized account code structure which is a  
11 statewide, uniform financial reporting format (based on the definitions and comprehensive chart of  
12 accounts set forth in the California School Accounting Manual). The structure shall be designed to  
13 provide a flexible statewide accounting system for local educational agencies to use in budgeting and  
14 reporting their revenues and expenditures. The structure shall accommodate local, state, and federal  
15 reporting needs as determined by the State Board.

16 (b) The standardized account code structure shall include, but not be limited to, the following  
17 fields:

18 (1) Fund/Account Group. Each fund is a fiscal and accounting entity, with a self-balancing set of  
19 accounts recording cash and other resources, all related liabilities and residual equities and balances or  
20 changes therein. Fund types include, but are not limited to, Governmental Funds, Proprietary Funds,  
21 Fiduciary Funds, and Account Groups.

22 (2) Project Year. The project year field is used to distinguish the activities of the same grant with  
23 different project years within the fiscal year.

24 (3) Resource (Project/Reporting). The resource field identifies the source of funding and is used  
25 for accumulating revenues and expenditures to meet various specialized reporting requirements and  
26 tracking categorical activities, such as No Child Left Behind (NCLB) Act, Economic Impact Aid, and  
27 School Improvement Program.

28 (4) Goal (Program). The goal field defines the objective, such as the target population being  
29 served or the education mode (e.g., regular education, special education, or vocational education).

30 (5) Function. The function field describes the activity being performed for which a service or  
31 material object is acquired, for example, instructional services, pupil services, and general administration.

32 (6) Object. The object field describes the service or commodity obtained as a result of a specific  
33 expenditure (e.g., salaries, books, and capital outlay).

34 (7) Site. The site field is optional, providing local educational agencies the ability to designate  
35 specific school sites within their individual accounting systems.

1 NOTE: Authority cited: Section 33031, Education Code. Reference: Section 41010, Education Code.

2  
3 Add Article 3 (commencing with Section 15070) to read:

4 **Article 3. Annual Financial Statements**

5 **§15070. Submission of Annual Financial Statements.**

6 Except as provided in Section 15071, every county office of education, school district, charter  
7 school, and educational joint powers agency (as defined in Education Code section 41023) **that elects to**  
8 **use the standardized account code structure, subject to the provisions of Section 39 of Chapter 299,**  
9 **Statutes of 1997,** shall submit an annual statement of receipts and expenditures in the format of the  
10 standardized account code structure, ~~subject to the provisions of Section 39 of Chapter 299, Statutes of~~  
11 1997. The form for the annual statement shall be prescribed and amended periodically (to accommodate  
12 changes in statute or generally accepted accounting principles for government agencies) pursuant to  
13 Education Code sections 1628 and 42100 and shall reflect Section 15060.

14 NOTE: Authority cited: Section 33031, Education Code. Reference: **Assembly Bill 1578, Section 39,**  
15 **Chapter 299, Statutes of 1977, and** Sections 1628, 41010, 41023, and 42100, Education Code.

16 **§15071. Alternative Form for Submission of Annual Financial Statements by Charter Schools.**

17 (a) Charter schools have the option of reporting their annual financial statements using an  
18 alternative form prescribed and amended periodically (to accommodate changes in statute or generally  
19 accepted accounting principles for government agencies) pursuant to Education Code section 42100. The  
20 alternative form shall be structured for electronic submission of data and shall include the following  
21 information:

22 (1) Revenues. An accounting of all funds received during the preceding fiscal year, including  
23 identification of specific details within the major revenue categories of revenue limit sources, federal  
24 ~~sources~~**revenues**, other state ~~sources~~**revenues**, and other local ~~sources~~**revenues.**

25 (2) Expenditures. An accounting of all funds expended during the preceding fiscal year, including  
26 identification of specific details within the major expenditure categories of certificated salaries, ~~classified~~  
27 **non-certificated** salaries, employee benefits, books and supplies, services and other operating expenses,  
28 capital outlay, and other outgo.

29 (3) Other information. An accounting of additional information including beginning and ending  
30 fund balances, other sources and uses, assets, liabilities, and reserves.

31 (b)(1) The reporting of financial data by charter schools that are established as governmental  
32 accounting entities shall reflect the definitions, and to the extent necessary for accurate financial  
33 reporting, the guidance provided in the California School Accounting Manual.

34 (b)(2) The reporting of financial data by charter schools that are established as nongovernmental  
35 accounting entities shall reflect the definitions, and to the extent necessary for accurate financial

1 reporting, the guidance provided in the California School Accounting Manual, except for accounting  
2 differences required due to their nonprofit status.

3 NOTE: Authority cited: Section 33031, Education Code. Reference: Sections 1628, 41010, and 42100,  
4 Education Code.

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DEPARTMENT OF  
**FINANCE**

GRAY DAVIS, GOVERNOR

915 L STREET ■ SACRAMENTO, CA ■ 95814-3706 ■ WWW.DOF.CA.GOV

August 20, 2003



Debra Strain, Regulations Adoption Coordinator  
Department of Education  
Legal Division  
1430 N Street, Room 5319  
Sacramento, CA 95814

Dear Ms. Strain:

The Department of Finance has reviewed the proposed regulations regarding forms for annual financial statements, as published July 4, 2003, and recommends amendments as outlined below.

While we support full implementation of the Standardized Account Code Structure (SACS), we are concerned that a section of the proposed regulations could be construed as imposing a State mandate on school districts. Our understanding is that all school districts have received funding for conversion to SACS and have voluntarily opted into the program. However, we are concerned that the proposed language could potentially be interpreted as now requiring all districts to follow the provisions of the enabling legislation and participate in SACS. This could potentially lead to a mandate claim, even if districts are already voluntarily completing these activities.

Our understanding is that no mandate is intended. To clarify that these regulations do not impose a mandate, we recommend that proposed section 15070 be amended as follows:

§15070. Submission of Annual Financial Statements

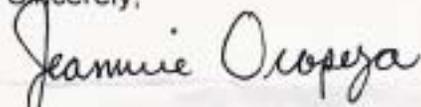
Except as provided in Section 15071, every county office of education, school district, charter school, and educational joint powers agency (as defined in Education Code Section 41023) **that elects to participate in the standardized account code structure program** shall submit an annual statement of receipts and expenditures in the format of the standardized account code structure, subject to the provisions of Section 39 of Chapter 299, Statutes of 1997. The form for the annual statement shall be prescribed and amended periodically (to accommodate changes in statute or generally accepted accounting principles for government agencies) pursuant to Education Code Sections 1628 and 42100 and shall reflect Section 15060.

We believe that this amended language would eliminate potential mandate issues and still provide for the desired financial reporting, as all school districts have voluntarily decided to participate in SACS.

Ms. Debra Strain  
August 20, 2003  
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If you have any questions regarding this matter, please feel free to contact Dan Troy, Principal Program Budget Analyst, or Phillip Dean, Finance Budget Analyst, at (916) 445-0328.

Sincerely,



Jeannie Oropeza  
Program Budget Manager

cc: Ms. Caryn Becker, Department of Education  
Mr. Eric Skinner, Office of the Secretary for Education  
Ms. Rae Belisle, State Board of Education

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**MEMORANDUM**

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**TO:** DEBRA STRAIN, CDE REGULATIONS ADOPTION COORDINATOR  
**FROM:** ERIC PREMACK  
**SUBJECT:** PROPOSED REGULATIONS CONCERNING CHARTER SCHOOL FINANCIAL REPORTING  
**DATE:** 9/16/2003

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I am writing to express opposition to proposed California Administrative Code of Regulations, Title V, Sections 15060, 15070, and 15071. These proposed regulations are in violation of the California Administrative Procedure Act (APA) and should be rejected.

Assembly Bill 1994 of the 2002 legislative session contained narrow authorization for requiring limited reporting of annual receipts and expenditures by charter schools. Prior to the enactment of AB 1994, charter schools were not required to submit such reports, in alignment with the general goals of the Charter Schools Act to avoid unnecessary administrative paperwork and shift from a rule-based accountability system to a performance-based one. AB 1994's provisions were narrowly tailored and amended at the urging of the charter school community to require a regulatory review to ensure that the burden imposed by the new law was held to an absolute minimum. They should be rejected for the reasons summarized below.

**Initial Statement of Reasons is Incomplete**

While school districts and county offices were provided incentive funding to implement the SACS system, charter schools were not and are not required by law to use the complex and costly SACS system. The Statement fails to note these key facts and uses the mere existence of the SACS system as the primary justification for imposing conformity to the system on charter schools. Since charter schools are not subject to these requirements, the Statement does not clearly state either the necessity or a sound rationale for imposing the SACS system, in whole or in part, on charter schools.

**Excessive Burden**

The regulations illegally and inappropriately incorporate and mandate either a full or partial implementation of the SACS system for charter schools.

The SACS system is unique to California's public education system. Though the SACS system is certainly elegant and powerful, it is also very burdensome and complex. The system specifies a very lengthy and complex account code string (19+ digits in 6 fields) and compliance with a complex SACS manual.<sup>1</sup> Though the alternative format prescribed in the regulations and form employ only a part of the SACS system (the object field), the proposed regulations would require charter schools to

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<sup>1</sup> The massive manual for this system is available on line: [www.cde.ca.gov/fiscal/sacs/csam/](http://www.cde.ca.gov/fiscal/sacs/csam/)

adopt a substantial part of SACS. Though some charter schools are able to do this, especially those who procure accounting services from school districts or county offices of education, others would be very challenged. Many would need to re-program their existing accounting systems to conform to SACS (either in whole or in part) and/or would need to add complexity to their current system to track in both the existing and SACS formats, in effect mandating keeping of a dual set of books. Though the SACS system may be "so familiar" to school districts and county offices, it is quite foreign to many charter school operators.<sup>2</sup>

SACS is burdensome and costly for schools to implement in many respects. First, there are very few electronic accounting systems available to support SACS and the few that are available are extremely complex and costly. Software licenses can cost in the hundreds of thousands of dollars and generally require substantial annual maintenance and upgrade support.<sup>3</sup> Second, implementing such a complex system requires more sophisticated and costly accounting and bookkeeping staff. Third, most also require a sophisticated mainframe, mini-mainframe, or high-powered file server computer and network to run and (fifth) these must be supported by costly information technology staff. For these and other reasons, many school districts now regret having committed to the SACS system for the modest incentive funds provided. Some charter schools enjoy cooperative relationships with school districts or county offices of education can procure access to such systems economically by sharing the cost. Many other charter schools, however, have less cooperative and supportive relations with districts and county offices, have invested heavily in their own independent systems, and procure accounting services on their own. Still others function as an arm of a pre-existing nonprofit corporation and the corporation's accounting systems rarely are programmed to support SACS.

For the many charter schools that are incorporates as nonprofit public benefit corporations, imposing SACS is to impose a fundamentally incompatible system. Generally accepted accounting principles for governmental agencies (which underpin the SACS system) are fundamentally different from those governing nonprofit corporations. Nonprofit accounting standards, for example, generally call for "full accrual" accounting practices which are fundamentally different from the "modified accrual" practices used by governmental agencies and which underpin SACS. The two systems also book assets under very different rules. SACS also mandates the establishment of several different accounting "funds" whereas nonprofit accounting standards permit a high degree of flexibility in fund structure. For these and other reasons, SACS is largely incompatible with many charter schools accounting standards.

The level of detail demanded by the proposed regulations and forms is also unnecessarily high and burdensome. Though the Statement of Reasons characterizes the alternative format as requesting "very basic summary" data, it actually requests an unnecessarily high level of detail (over 130 lines worth!). There is no apparent public purpose or need for the 130-line level of detail mandated here. Is there, for example, a compelling legal mandate or "need" to distinguish between a school's expenses on "non-certificated instructional aides" versus "non-certificated support?" In many

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<sup>2</sup> The California Department of Education maintains a large web site to explain and support the complex SACS system ([www.cde.ca.gov/fiscal/sacs/index.asp](http://www.cde.ca.gov/fiscal/sacs/index.asp)). This site contains a list of "frequently asked questions." It includes dozens of questions spread across over 20 topic areas—proof positive of the system's complexity ([www.cde.ca.gov/fiscal/sacs/sacsfaqs/default.asp](http://www.cde.ca.gov/fiscal/sacs/sacsfaqs/default.asp)).

<sup>3</sup> We have contacted most of the vendors of such systems ([www.cde.ca.gov/fiscal/sacs/provider.htm](http://www.cde.ca.gov/fiscal/sacs/provider.htm)). None expressed a willingness or had the capacity to sell such systems to individual charter schools, fearing that charter schools lacked the very sophisticated hardware, staff, and expertise to load and operate their software.

charter schools, especially small ones, staff "wear many hats" and do not fit into traditional job classifications or neat boxes.

The statutes (Education Code Section 42100(b)) calls for charter schools to report only a "statement of all receipts and expenditures." The proposed form, however, calls for extensive additional data beyond receipts and expenditures, including (1) other financing sources and uses (section "D"), (2) net fund balance change (section "E"), (3) fund balance information "(section F), (4) a detailed enumeration of assets and liabilities (sections "G" and "H"), (5) net fund balance (section "I"), and (6) additional data regarding federal funds expended on capital outlay, debt service, and community services. These several sets of additional data are clearly beyond the scope of the statute.

In lay terms, the level of detail requested here is akin to a full Form 1040 on a federal income tax return when "very basic summary" data, which should suffice and be the goal here according to the Statement of Reasons, would be more akin to a "1040-EZ" form. The form should be condensed to truly summary data (e.g., a one page "EZ" form or less) and should provide charter schools with a high and reasonable degree of flexibility in their account code structure.

### **Sneaking SACS Past APA Review**

SACS itself was adopted without regulatory review and should have been. Though many school districts and county offices of education were lured in to implementing SACS with modest financial incentives, these proposed regulations attempt to "formalize" and mandate SACS without enumerating a specific necessity or rationale and without consideration of any alternatives, in direct violation of the APA. Specifically, proposed Section 15060 mandates the imposition of a SACS-like structure as a minimum ("not limited to"). Instead of glibly sneaking the SACS mandate into regulations, the State Board and Department should instead engage in a full review of alternatives, especially less burdensome and costly ones. It is a virtual certainty that a system that is less complex and burdensome could be devised and meet the requirements of applicable laws.

I would be pleased to discuss these and other concerns regarding these regulations.

Eric Premack

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