



November 6, 2009

**ORANGE COUNTY  
DEPARTMENT  
OF EDUCATION**

200 KALMUS DRIVE  
P.O. BOX 9050  
COSTA MESA, CA  
92628-9050  
(714) 966-4000  
FAX (714) 662-3570  
[www.ocde.us](http://www.ocde.us)

**WILLIAM M. HABERMEHL**  
County Superintendent  
of Schools

LYNN APRIL HARTLINE  
Deputy Superintendent

JOHN L. NELSON  
Associate Superintendent

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To: Assistant Superintendents, Business Services  
Directors, Business Services  
ROC/Ps

From: Wendy Benkert, Ed.D., Assistant Superintendent  
Business Services

Subject: **2009-10 First Interim Report**

Since May 2008, County Office Chief Business Officials have been working with various statewide educational organizations to craft common messages to advise school districts on assumptions for budget and interim reports. The attached common message provides guidance for the 2009-10 First Interim Report and is based upon the July Enacted Budget and any changes that have occurred since the August 5, 2009 Common Message.

If you have any questions or concerns regarding this information, please contact me at (714) 966-4229.

cc: Superintendents  
Dari Barzel, Moody's Investors Services  
Jean Buckley, Tamalpais Advisors, Inc.

**CCSESA BASIC DISTRICT FISCAL OVERSIGHT COMMON  
MESSAGE TALKING POINTS TO  
COUNTY OFFICE OF EDUCATION CBOs  
2009-10 FIRST INTERIM REPORT AND RELATED MYPS  
NOVEMBER 4, 2009**

**BACKGROUND**

Since May 2008, County Office Chief Business Officials have been working with various statewide educational organizations to craft common messages and advice to school districts on assumptions for budget and interim reports. Our goal is to have as consistent a county office message as possible to school districts. This edition provides guidance for the 2009-10 First Interim Report and reflects changes since the August 5, 2009 Common Message which incorporated the July Enacted Budget for 2009-10 that was signed by Governor Schwarzenegger on July 28, 2009.

**2008-09 YEAR-END CLOSING**

Based upon the best available information and lack of clear direction from state agencies, the August 5, 2009 Common Message provided guidance to accrue accounts receivables for categorical programs relative to GASB 33 requirements.

Currently, the State Controller's Office (SCO) and audit firms are in the process of finalizing their interpretation of GASB 33 requirements for the 2008-09 audit reports. This could result in an audit adjustment for local education agencies (LEAs). It is anticipated that the SCO will soon issue an advisory to auditors and LEAs.

**2009-10 FIRST INTERIM REPORT**

**Revenue Limit and Categorical Reversion**

The revised Enacted Budget, ABX4 2, specifies the deficit factor for 2009-10 as defined in the following table. In addition, pursuant to ABX4 3 (Chapter 3/2009/10) LEAs must make a one-time reduction to the 2009-10 revenue limit income of \$252.83 per ADA. This \$252.83 per ADA reduction in 2009-10 is for the \$1.516 billion needed to restore the categorical reductions taken in 2008-09.<sup>1</sup>

	<b>2009-10</b>
Statutory Cost of Living Adjustment (COLA)	4.25%
K-12 Deficit	18.355% (0.81645)
County Office Deficit	18.621% (0.81379)

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<sup>1</sup> In order to reduce the Proposition 98 funding level without having to suspend Proposition 98, the Legislature captured \$1.6 billion in categorical funds unallocated, unexpended, or not liquidated in 2008-09. With the exception of High Priority Schools Grant, which is eliminated in 2008-09, \$1.5 billion is restored in 2009-10. Per Section 5 of ABX4 3, apportionments for school districts, county offices, and charter schools are reduced on a one time basis in 2009-10 by an equivalent amount to fund the \$1.5 billion categorical restoration.

**We recommend that school districts use the SSC dartboard, which was updated September 14, 2009, in the development of the 2009-10 First Interim Report.**

As an additional note of caution, school districts should carefully review their revenue limit projections. Due to the deficits and changes in both property taxes and state aid, it is possible that a school district might temporarily shift in or out of basic aid status. Basic aid districts are also subject to the estimated \$252.83 per ADA one time reduction from their categorical funding in 2009-10. This amount shall be deducted from a basic aid district's state categorical aid in 2009-10, exclusive of Special Education, After School Education and Safety Program (ASES), Quality Education Investment Act (QEIA), and child care and development funding (CCDF). The deduction cannot violate the California Constitution (Section 6 of Article IX) requirement that the state provide at least \$120 per ADA, or \$2,400 per school agency, whichever is greater (Education Code Section 41975). Thus this creates in essence a floor in which a basic aid district would always be left with at least the \$120/\$2400 constitutionally protected funding under this calculation and would not have to lose additional funding once that level is reached.

## **State Fiscal Stabilization Funds**

K-12 schools and colleges are entitled to \$4.9 billion under the SFSF, with \$3.2 billion already distributed.

Another \$1.3 billion will soon be available, with approximately \$300 million going to K-12 schools, for a total phase 1 allocation of \$2.9 billion (approximately \$500 per student). \$1 billion in new funds is designated for community colleges and state universities, for a phase 1 total of \$1.5 billion.

The remaining 10 percent (\$488 million) is pending approval of California's compliance with SFSF phase 2 requirements.

However, due to the Governor's support for using these funds to backfill the QEIA revenue limit reduction, **school districts should not budget either the remaining Phase I (\$300m) or the Phase II (\$488m) additional SFSF allocations until the actual cash apportionment is received.**

## **Quality Education Investment Act of 2006 (QEIA)**

Section 39 of ABX4 2 allocates \$402 million from Proposition 98 to K-12 and \$48 million to community colleges to fund selected school sites that participate in the Quality Education Investment Act program in 2009-10. The bill also contains specific instructions to reduce the revenue limit funding of local educational agencies (LEAs) receiving QEIA funds by an equivalent amount. Originally, the Legislature intended to backfill for this reduction to the revenue limit by allowing LEAs that participated in QEIA to, on behalf of eligible school sites, apply for Title I grants. However, it quickly became clear that the Title I funds were unlikely to fit, and QEIA districts were at risk of losing revenue limit funds with no assured restoration from another funding source. Therefore, SB 84 was enrolled in the last days of the session to prohibit the QEIA revenue limit reduction until the Superintendent of Public Instruction and the Director of Finance both certify that offsetting funds are available. However, the Governor vetoed SB 84 but stated that he intended to use ARRA-Fiscal Stabilization Funds to backfill the revenue limit reduction. Currently ABX3 56 is the vehicle to enact the "fix". The bill was signed by the Governor on November 6, 2009. Therefore, **it is acceptable for school districts to budget for a backfill to the revenue limit cut corresponding to the 2009-10 QEIA revenue amount.**

QEIA is also extended one more year to 2014-15 to fully meet the State's obligation for QEIA. At this point in time, we are still waiting for clarification from the California Department of Education on whether or not LEAs can opt out of receiving QEIA funds for 2009-10.

## K-3 Class Size Reduction

Previously, K-3 Class Size Reduction (CSR) funding was based on grade levels included in the District's application. ABX4 2 caps the funding for eligible K-3 CSR at the total number of classes rather than grade levels on the application as of January 31, 2009. Local educational agencies (LEAs) may claim an Option One (full-day) class in lieu of an Option Two (half-day) class. The district wide cap is calculated based on the total number of Option One and Option Two classes, making no distinction in type. In other words, **LEAs may choose to have an Option One class in place of a previous Option Two class.**

## Transportation

Home-to-School Transportation and Special Education Transportation funding is **reduced by 19.84% in 2009-10** as compared to the 2007-08 funding level.

## Instructional Materials

ABX4 2 extends the suspension of the Instructional Materials requirement from 2009-10 through 2012-13 and postpones the State Board of Education's adoption cycle for an equivalent time-frame. Therefore, **districts will not be required to purchase materials under the adoption schedule for 2009-10 through 2012-13. However, if new adoption materials are purchased, they must be made available to all pupils for whom they are intended.** Please note that school districts **must hold a public hearing** and adopt a resolution certifying sufficiency of textbooks per Education Code (EC) Section 60119 as in previous years.

## Lottery

Please note that Lottery funding will be calculated in the same manner as in prior years, with the exception that through 2012-13, some of that ADA (such as ROC/P, Community Day Schools, and Adult Education) is based upon the 2007-08 ADA<sup>2</sup>.

**The current projection for 2009-10 is \$111.00 per ADA (unrestricted) and \$13.25 per ADA (Prop. 20).**

## Property Taxes

The latest countywide projections provided by the Office of the Orange County Auditor-Controller indicate that Secured assessed values decreased by 1.32% and that Unsecured assessed values increased by 0.37% for 2009-10. However, a 40% decline continues to be projected in Supplemental taxes due to a slowing housing market for 2009-10. Not included at this time are the rates for homeowner's exemption subvention and the State-assessed property roll.

For the basic-aid districts, the secured taxes are expected to increase by 4.06% for Laguna Beach Unified, 1.00% for Newport-Mesa Unified, and 0.60% for Irvine Unified. These projections do not factor in any refund activity, home-owners subvention, or any unitary related revenue. In addition, the estimates are based on the initial current year secured property tax levy; hence any roll changes during the year can affect the levy.

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<sup>2</sup> For fiscal years 2008-09 through 2012-13, the programs funded based on 2007-08 ADA include Adult Education, Advanced Placement Fee Waiver Program (schedule 2), Reader Services for Blind Teachers (schedule 3), Cal-SAFE Academic and Supportive Services, Class Size Reduction, Grade 9, Community Day Schools, Regional Occupational Center and Programs (ROC/P), and Supplemental Hourly Instructional Programs.

## **Community Redevelopment Funds**

Assembly Bill (AB) 1389 requires redevelopment agencies and county auditors to annually report information to the State Controller's Office (SCO) regarding payments that the redevelopment agencies made to school districts. The 2008-09 audit focused solely on the payments made during fiscal years 2003-04 through 2007-08. If a school district did not report the appropriate revenue limit offset for community redevelopment funds during that time frame, an adjustment will be made in a future apportionment period.

On October 1, 2009, the California Department of Education (CDE) notified school districts via letter that the CDE will either add or deduct an amount as a prior year adjustment from the 2009-10 First Principal Apportionment based upon the data in the SCO's AB 1389 report (published in June 2009). School districts have 30 days to request a summary review and 60 days to file a formal appeal on any one or more of the grounds set forth in Education Code Section 41344(d).

School districts may want to include an appropriate budget entry in the 2009-10 First Interim to reflect the prior year adjustment outlined in the October 1, 2009 letter from the CDE. However, if you submitted a request for a summary review to the Education Audit Appeals Panel (EAAP) within the 30 day time frame, your P-1 adjustment will be put on hold.

## **Interest Yield Projection**

The current interest yield projection for fiscal year 2009-10 is 1.35%. This projection is provided by the Orange County Treasurer and is based on the current yield environment taking into account any possible action from the Federal Open Market Committee. This information is updated throughout the year in the Orange County Treasurer's Monthly Management Reports. Given the financial market instability and tightening credit market, this interest rate projection is likely to be reduced.

## **Routine Restricted Maintenance**

The contribution requirement for the routine restricted maintenance account has been reduced to zero percent for five years (2008-09 through 2012-13) for school districts that meet the facility requirements of the *Williams* settlement.

## **BASIC AID FAIR SHARE BUDGET REDUCTIONS**

To implement the 2009-10 "Fair Share" reduction, Section 37 of ABX4 2 reduces categorical funding for basic aid districts in 2010-11 by the amount that is proportionate to the revenue limit reductions implemented for non-basic aid districts as described earlier. The amount of categorical reduction is equal to the basic aid district's 2009–10 fiscal year total revenue limit, subject to the deficit factor, calculated as of the 2009–10 fiscal year certified second principal apportionment, multiplied by 5.81 percent. This amount shall be deducted from a basic aid district's state categorical aid in 2010-11, exclusive of Special Education, After School Education and Safety Program, QEIA, and CCDF. The deduction cannot violate the California Constitution (Section 6 of Article IX) requirement that the state provide at least \$120 per ADA, or \$2,400 per school agency, whichever is greater (Education Code Section 41975).

## **PUBLIC HEARING ON TIER III FLEXIBILITY**

ABX4 2, Education Code Section, 42605, paragraph (c) (2) and (3) requires a public hearing on the proposed use of funds for the Tier III Categorical Programs. Paragraph 2 was amended to read,

*(2) As a condition of receipt of funds, the governing board of the school district or board of the county office of education, as appropriate, at a regularly scheduled open public hearing shall take testimony from the public, discuss, approve or disapprove the proposed use of funding, and make explicit for each of the budget items in paragraph (2) of subdivision (a) the purpose for which the funds will be used.*

The term “explicit” has now been added to the code, but is not defined in code! We recommend that school districts review the board agenda and minutes from their public hearing to ensure compliance with the new language. If necessary, school districts may want to hold another public hearing on the Tier III categorical flexibility. Attachment A provides a sample board resolution.

## **CASH MANAGEMENT**

### **Apportionment Deferrals**

The Revised Enacted Budget defers an additional \$1 billion in revenue limit apportionment from November 2009 to January 2010. The \$1 billion that was originally deferred from July 2009 to October 2009 has been extended to December 2009. Please refer to the table below for a complete list of deferral amounts. Note that approximately \$5 billion in payments is being delayed from one fiscal year to the next. Attachment B provides a graphical illustration of the apportionment deferrals.

<b>K-12 Deferral Amount</b>	<b>Timeframe</b>
\$1.0 Billion	July 2009 to December 2009
\$1.5 Billion	August 2009 to October 2009
\$1.0 Billion	November 2009 to January 2010
\$2.0 Billion	February 2010 to July 2010
\$679 Million	April 2010 to August 2010
\$1.0 Billion	May 2010 to August 2010
\$1.4 Billion <sup>3</sup>	June 2010 to July 2010
<b>Total: \$8.6 Billion (\$5 Billion across fiscal years)</b>	

### **Apportionment Schedule**

In addition to deferrals, ABX4 16 has significantly changed the schedule for the principal apportionment and the special purpose apportionment and added a schedule for Education Code Section 42605 budget items (Tier III Categorical Programs). Please refer to the following table for an example of the change in

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<sup>3</sup> 100% of the June P-2 Principal Apportionment is deferred to July (estimated to be \$1.4 billion).

apportionment schedule<sup>4</sup> with the deferrals described in the section above (note that a negative amount includes funds being deferred to a different timeframe, a positive amount shows funds being restored from a prior deferral). ABX4 16 Section 3 also specifies an apportionment schedule for EC 42605 budget items (Tier III categorical programs). We are waiting for additional clarification from the CDE as to the implementation details. In light of the reduced and deferred apportionments and change in timing of distribution of funds from the State, **a great deal of emphasis must be placed on cash flow analysis and monitoring.**

Principal Apportionment Monthly Payment Schedule Comparison						
<u>Month</u>		Old Monthly Payment Schedule*	New (SBX4 -16) Monthly Payment Schedule	Monthly Payment Schedule with Deferrals**	Monthly % Shortfall/ Excess	Cumulative % Shortfall/ Excess
July	**	6.0%	5.0%	1.0%	-4.0%	-4.0%
August		12.0%	5.0%	0.0%	-5.0%	-9.0%
September		8.0%	9.0%	9.0%	0.0%	-9.0%
October	**	8.0%	9.0%	14.0%	5.0%	-4.0%
November		8.0%	9.0%	4.5%	-4.5%	-8.5%
December	**	8.0%	9.0%	13.0%	4.0%	-4.5%
January		8.0%	9.0%	13.5%	4.5%	0.0%
February		14.0%	9.0%	0.5%	-8.5%	-8.5%
March		7.0%	9.0%	9.0%	0.0%	-8.5%
April		7.0%	9.0%	6.0%	-3.0%	-11.5%
May		7.0%	9.0%	4.5%	-4.5%	-16.0%
June		7.0%	9.0%	0.0%	-9.0%	-25.0%
<u>Subsequent Year</u>						
July				17.5%		-7.5%
August				7.5%		0.0%

\* Does not include past deferrals  
\*\*Does not include July 09 overpayment % and subsequent adjustments in Oct. and Dec.

We have always stressed the importance of maintaining appropriate reserves. These cash management challenges make it even more imperative that **we consider reserve levels greater than the minimums required within the State's Criteria and Standards.** Reserves are especially critical in order to meet cash flow needs that guarantee the ability to adequately meet payrolls and other obligations.

<sup>4</sup> Please note that the new 5-5-9 apportionment schedule does not apply to EC Section 14041(a)(7) school districts (Buena Park School District, Brea-Olinda Unified School District, and Laguna Beach Unified School District).

## MULTI-YEAR PROJECTIONS

Our office recommends using the assumptions set forth by the School Services of California dartboard (see table below for an excerpt of the Dartboard) in the preparation of multi-year projections.

	2009-10	2010-11	2011-12
Statutory COLA	4.25%	0.50%	2.30%
Revenue Limit Deficit	18.355%	18.355%	18.355%
<b>Effective COLA</b>	<b>-7.95%</b>	<b>0.50%</b>	<b>2.30%</b>
<b>Other Revenue Limit Adjustments</b>	<b>-\$252.83 per ADA</b>		
Special Education COLA	0.00%	0.00%	0.50%
State Categorical Funding			
Tier 1	0.00%	0.5%	2.3%
Tier 2	-4.46%	0.5%	2.3%
Tier 3	-4.46%	0.5%	2.3%

## RESERVE FOR ECONOMIC UNCERTAINTIES

The revised Enacted Budget lowers the minimum reserve requirement levels for economic uncertainties to 1/3 the percentage level adopted by the State Board as of May 1, 2009. However, school districts are required to make progress in the 2010-11 fiscal year to return to compliance with the specified standards and criteria adopted by the State Board. ABX4 2 also restores the requirement for the 2011-12 fiscal year to the percentage adopted by the State Board as of May 1, 2009. We believe that the percentages established in the Criteria and Standards for reserves prior to the current Enacted Budget are the BARE MINIMUM. Moreover, once the minimum reserve levels are reduced, it would take budget reductions of twice the amount of the lowered reserve levels to fully restore the reserve by 2011-12.

Basic aid school districts are also advised to maintain reserves much greater than the State required minimum because they do not have the prior year ADA protection provided to school districts under Education Code 42238.5, whereby revenue limit funding is based on ADA for either the current or prior fiscal year, whichever is greater.

## NEGOTIATIONS

When considering a multi-year contract, school districts need to be very flexible and have appropriate contingency language, such as basing compensation increases on “funded COLA” or “effective COLA”. Also recognize that there may be different COLAs and deficits for revenue limits versus categorical programs and this should be considered during negotiations.

## **FIRST INTERIM CERTIFICATIONS**

A new AB 1200 provision is in effect for fiscal year 2009-10 only. The Education Budget Trailer Bill ABX4 2 (Chapter 2/2009) specifies that COEs do not have the authority to assign a qualified certification *if* the problem in the third year is substantially due to the loss of ARRA funds. However, this is only one of many indicators of fiscal stability. We will continue to consider all tools available such as the FCMAT Predictors of School Agencies Needing Intervention.

## **2010-11 BUDGET REDUCTIONS**

For school districts that took board action to make ongoing budget reductions for 2010-11 during the 2009-10 budget adoption process, it is our understanding that an itemized list of Board approved reductions will be submitted with the First Interim Report. We are expecting to see a contingency plan for items on the list that are pending negotiations.

## **SUMMARY**

We recognize that these are extraordinary economic times and it is difficult to gauge the future. School district budgets should be managed with a great degree of conservatism over the next few years. In these times of great economic and budgetary uncertainty, school districts need reserves that are much greater than the minimum.

We understand how difficult it is for school districts to deal with the increased pressures, significantly reduced funding, apportionment deferrals, and the uncertainty associated with a volatile economy. It is important that school districts be proactive through developing contingency plans that allow the most flexibility possible. School districts are advised to follow through with planned budget reductions for 2009-10 and begin planning now for necessary reductions for 2010-11 and 2011-12. While planning necessary budget reductions for 2010-11 and 2011-12, school districts can also develop program or expenditure restoration priorities if more revenues become available.

We recommend and strongly encourage that all school districts use these guidelines to assist in the preparation of the 2009-10 First Interim Report and associated multi-year projection. If you have any questions or concerns regarding this information, please contact me at (714) 966-4229.

# ATTACHMENT A



September 23, 2009

To: Assistant Superintendents, Business Services  
Directors, Business Services

From: Wendy Benkert, Ed.D, Assistant Superintendent, Business Services

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## **Subject: Tier 3 Categorical Flexibility Requirements**

As you know, the Budget Act of 2009 granted categorical flexibility to local educational agencies (LEAs) for fiscal years 2008-09 through 2012-13. There are two requirements that LEAs should be aware of regarding the flexibility provisions. The first requirement is that the governing board of each LEA is to hold a public hearing as a condition of the receipt of funds. The second requirement is that LEAs must report the flexibility expenditures with the appropriate Standardized Account Code Structure (SACS) function codes. Please see below for additional information about the two requirements listed above.

### **Public Hearing Requirement**

As a condition of receipt of funds, the governing board of the school district or board of the county office of education, as appropriate, at a regularly scheduled open public hearing shall take testimony from the public, discuss, approve or disapprove the proposed use of funding, and make *explicit* for each of the budget items in Education Code Section 42605(a)(2) the purposes for which the funds will be used. We have attached a sample Board resolution for the categorical flexibility public hearing and a template that lists Tier 3 categorical programs, amounts, and uses of funds.

It is important to note that the public hearing requirement has been included in the proposed 2009-10 Audit Guide regulations. For 2009-10, your independent auditor will review minutes or other records of the governing board that document that the governing board held such a public hearing or hearings before determining the use of each flexible funding source. The public hearing may have been held in the prior year.

### **SACS Reporting Requirement**

Using the SACS reporting process, a local educational agency shall report expenditures of funds pursuant Education Code Section 42605(a)(2) by using the appropriate function codes to indicate the activities for which these funds are expended. The California Department of Education shall collect and provide this information to the Department of Finance and the appropriate policy and budget committees of the Legislature by April 15, 2010, and annually thereafter on April 15 until, and including, April 15, 2014.

If you have any questions or concerns about this information, please call me at (714) 966-4229.

**RESOLUTION #** \_\_\_\_\_

**RESOLUTION OF THE GOVERNING BOARD OF THE  
SCHOOL DISTRICT  
CATEGORICAL FLEXIBILITY FUNDS**

On motion of member \_\_\_\_\_, seconded by member \_\_\_\_\_, the following resolution is adopted.

**WHEREAS**, the State Adopted Budgets of 2008-09 and 2009-10 (SBX3 4) provides "Flexibility" for the use of certain Categorical Program Funds to be used in responses to the State fiscal crisis, and

**WHEREAS**, the Flexibility legislation requires the Governing Board, at a regularly scheduled open public hearing to take testimony from the public and shall discuss and approve or disapprove the proposed use of funding, and

**WHEREAS**, the attached schedule reflects the estimated amount of Flexibility funds to be used in the General Fund for educational purpose as reflected in the various budgets which has been adopted by the Board for the 2009-10 fiscal year,

**NOW THEREFORE, BE IT RESOLVED AND ORDERED**, the Board approves the use of the Flexibility Funds as required by the Budget Act of 2009.

**PASSED AND ADOPTED** by the Governing Board of the \_\_\_\_\_ School District, County of Orange, State of California, this \_\_\_\_\_ day of \_\_\_\_\_ 2009, by the following vote:

AYES:

NOES:

ABSENT:

ABSTAIN:

STATE OF CALIFORNIA)  
COUNTY OF ORANGE )

I, \_\_\_\_\_, Secretary of the \_\_\_\_\_ School District Governing Board, do hereby certify that the foregoing is a full, true, and correct copy of a resolution passed and adopted by the Board at a regularly scheduled and conducted meeting held on said date, which resolution is on file in office of said Board.

\_\_\_\_\_  
(Name of Secretary)  
Secretary of Governing Board  
\_\_\_\_\_  
School District

**SCHOOL DISTRICT**  
**CATEGORICAL FLEXIBILITY FUNDS**  
**FY 2009-10**

**2008-09 Categorical Program Budget Flexibility**

<b><u>Tier 3 Categorical Programs</u></b>	<b><u>Amounts</u></b>	<b><u>Use of Funds</u></b>
<b>Total Flexibility Transfers</b>		

# Apportionment Deferrals

Attachment B

