

**ANNUAL REPORT TO THE LEGISLATURE
ON THE SCHOOL EMPLOYEES FUND
FOR STATE FISCAL YEAR 2011-12**

**Prepared by
California Employment Development Department
School Employees Fund Unit
March 2013**

**ANNUAL REPORT TO THE LEGISLATURE ON THE
SCHOOL EMPLOYEES FUND**

(State Fiscal Year Ending June 30, 2012)

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EXECUTIVE SUMMARY

In accordance with Section 832, Division 1, Part 1, Chapter 3, Article 6 of the California Unemployment Insurance Code (CUIC), the Employment Development Department (EDD) is pleased to provide the Annual Report to the Legislature regarding the School Employees Fund (SEF) for the State Fiscal Year (SFY) that ended June 30, 2012. The SEF is a special reimbursable financing method available to school employers to pay their Unemployment Insurance (UI) costs. It is a joint, pooled-risk fund administered by the EDD, which collects contributions from school employers participating in the SEF. Money deposited in the SEF is used to reimburse the California UI Trust Fund for the cost of UI benefits paid to former employees of those school employers. This report provides a financial summary for SFY July 1, 2011 through June 30, 2012, economic activities that affected SEF during the SFY, and recommendations to ensure the adequacy of funds.

The highlights of this report are:

- As of June 30, 2012, the SEF ended with a fund balance of \$414.6 million. This represents an increase in the fund balance of \$407.9 million when compared to SFY 2010-11, which ended with a fund balance of \$6.7 million. The increase in the fund balance in SFY 2011-12 is attributed to the rise in the contribution rate from 0.72 percent to 1.61 percent and a decrease in former employees collecting UI benefits. For a definition of UI contribution rate, refer to the Glossary, Appendix C.
- The SEF revenue during SFY 2011-12 totaled \$670.0 million, which represents an increase of \$348.0 million (108 percent) when compared to the \$322.0 million in total revenue collected during SFY 2010-11. This increase in revenue is due to the contribution rate of 1.61 percent which helped generate more UI contributions paid into the SEF.
- The Local Experience Charge (LEC) generated revenue during SFY 2011-12 of \$25.8 million, which represents an increase of 6.8 million (36.0 percent) compared to \$19.0 million in SFY 2010-11. The increase is a result of the school employee layoffs during the recession. For a definition of LEC, refer to the Glossary, Appendix C.
- Additional revenue is generated from penalties and interest paid by school employers, and Surplus Money Investment Fund interest earned on deposits made into the SEF. The revenue received from penalty and interest charges assessed to the school employers totaled \$0.4 million during SFY 2011-12, a decrease of \$0.1 million (20 percent) compared to \$0.5 million earned in SFY 2010-11. The interest revenue from the Surplus Money Investment Fund increased by \$0.3 million (300 percent) to total \$0.4 million in SFY 2011-12, compared to \$0.1 million in SFY 2010-11. The average Surplus Money Investment Fund apportionment yield during the SFY 2011-12 was 0.372 percent compared to 0.487 percent in the prior SFY 2010-11. For a definition of penalty and interest and the Surplus Money Investment Fund, refer to the Glossary, Appendix C.

- The SEF's total disbursements were \$262.2 million in SFY 2011-12 compared to \$313.2 million in SFY 2010-11, a decrease of \$51.0 million (16 percent) from the prior fiscal year. The SEF's major disbursement is to reimburse California's UI Trust Fund for benefits paid to former school employees.
- During SFY 2011-12, a total of \$259.7 million in UI benefits were paid to former school employees compared to the total of \$310.8 million in UI benefits paid during the SFY 2010-11, a decrease of \$51.1 million (16 percent). The high unemployment rate triggered the Federal-State Extended Duration Benefits Program (FED-ED) in February 2009. However, the U.S. Department of Labor has determined that California's Unemployment rate is no longer at the required level to continue filing and paying FED-ED benefits after May 12, 2012. Since school employers paid 100 percent of the FED-ED benefits paid to former school employees, UI benefit charges will continue to decline.
- Other expenses include SEF's administrative and operational costs and claims management fees. Administrative cost to operate the SEF totaled \$0.7 million during SFY 2011-12, an increase of \$0.1 million (17 percent) compared to \$0.6 million in SFY 2010-11. The claims management fees paid amounted to \$1.8 million. The claims management fees remain the same as last year. For a definition of the claims management fees, refer to the Glossary, Appendix C.
- The SEF UI contribution rate for SFY 2012-13 was calculated at 1.31 percent. If the rate was set at 1.31 percent, there would have been an excess of an adequate reserve. The Director has the statutory discretion to decrease the calculated UI contribution rate as mandated in CUIC, 823(c) and adjusted the rate down to 1.10 percent. This lower UI contribution rate will provide sufficient revenue for the SEF to meet its estimated financial obligations for SFY 2012-13.

INTRODUCTION

The Annual Report to the Legislature provides comments and recommendations on the administration of the SEF as of June 30, 2012, and includes the SEF operations and financial condition for the SFY 2011-12 as mandated by the CUIIC, Division 1, Part 1, Chapter 3, Article 6, Section 832.

In 1978, the UI coverage was extended to all public entities. Public school employers, kindergarten through 12th grades and community colleges were given the option to finance their UI costs by participating in the SEF, as authorized in the CUIIC, Section 821. The method to finance the UI costs under the SEF program is traditionally less costly for school employers than electing to finance the UI costs under the tax-rated method, which is required for private-sector employers, or the direct reimbursable method that other public and nonprofit entities may select to pay their UI costs. The direct reimbursable method that public entities may opt to use requires repayment of all UI benefits paid to former employees on a dollar-for-dollar basis.

The SEF is a pooled-risk fund administered by the State of California's Employment Development Department (EDD). The EDD collects quarterly contributions from all school employers participating in the SEF. The quarterly contributions are based upon the total wages paid to school employees by each school employer multiplied by the statutorily set UI contribution rate.

The SEF employer may also have to pay a quarterly LEC on the UI benefits paid to former school employees. All monies collected are deposited into the SEF and are used to reimburse California's UI Trust Fund for the cost of UI benefits paid to former school employees. Additional revenues to the SEF are generated from penalties and interest collected from employers and interest earned on the SEF deposits.

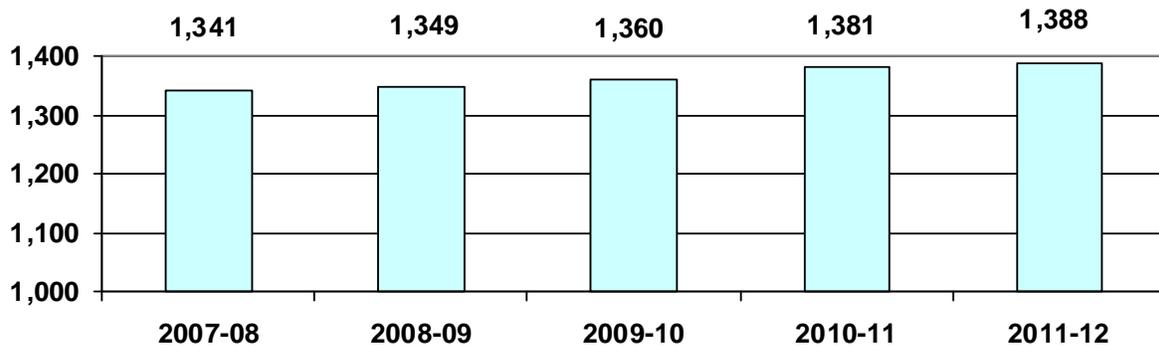
The SEF includes California's 72 community college districts and 1,316 public schools, which include County Offices of Education and charter schools, that choose to participate in the SEF. In SFY 2011-12, participating school employers paid wages in excess of \$39.2 billion. This represents an increase of \$1.3 billion from the \$37.9 billion in total wages paid during SFY 2010-11.

During SFY 2011-12, the participating school employers had a total of 898,896 school employees compared to 888,500 school employees in the prior fiscal year. This represents an increase of 10,396 employees (1.2 percent).

Participating School Employers

Figure 1 displays the SEF participant's growth over the past five SFYs.

Figure 1



SCHOOL EMPLOYER ADVISORY COMMITTEE

The School Employer Advisory Committee (SEAC) was created pursuant to the CUI, Section 831. The SEAC consists of five members who meet at least semi-annually with the EDD administrator to consider and recommend improvements in the administration of the SEF. The State Superintendent of Public Instruction, the Chancellor of the California Community Colleges, the Association of California School Administrators, the California Association of School Business Officials, and the California School Boards Association each appoint one member to the SEAC. For a listing of the names and addresses of current SEAC representatives, see Appendix B.

Serving under the direction of the SEAC is the UI Technical Subcommittee. Its membership consists of representatives from the school employer community throughout the State and representatives from EDD. The UI Technical Subcommittee works in conjunction with the SEAC to discuss the condition of the SEF and provides outreach and assists school employers in managing UI costs.

UNEMPLOYMENT INSURANCE SEMINARS FOR SCHOOL EMPLOYERS

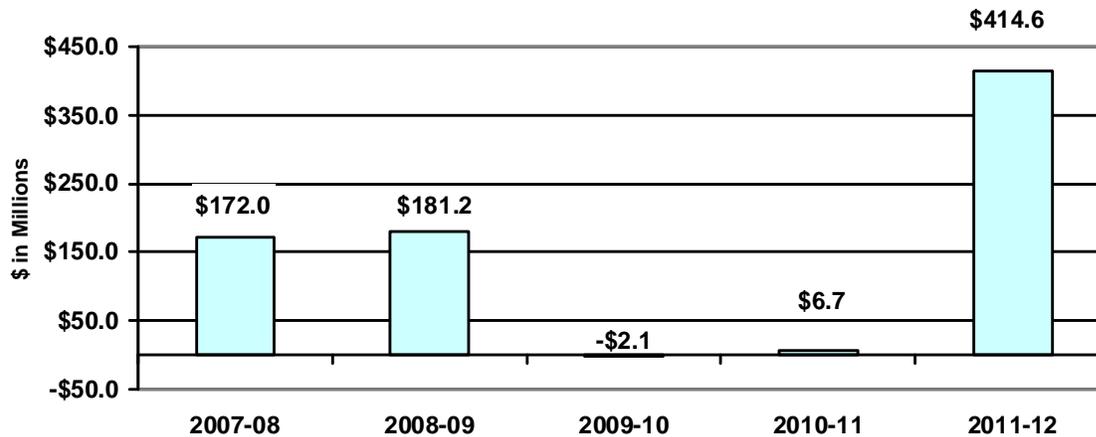
During SFY 2011-12, the SEAC and UI Technical Subcommittee planned the seminars held in Ontario and Los Angeles on October 23 and 24, 2012. Another seminar will be offered in Sacramento on March 5, 2013. The seminars focus on UI claims management practices for the school employers to help control their UI costs.

FINANCIAL CONDITION OF THE SCHOOL EMPLOYEES FUND

School Employees Fund Balance

On June 30, 2012, the SEF ended the SFY 2011-12 with a fund balance of \$414.6 million. This represents an increase in the fund balance of \$407.9 million when compared to SFY 2010-11, which ended with a fund balance of \$6.7 million. Figure 2 reflects the SEF's ending fund balances as of June 30th for the past five SFYs.

Figure 2



Total Fund Revenue

Total SEF revenue is generated from the quarterly UI contributions, LEC, penalties and interest assessed on school employers, interest income received from the Surplus Money Investment Fund, and prior year adjustments. For a definition of UI contributions, LEC, penalties and interest and prior year adjustment, refer to the Glossary, Appendix C.

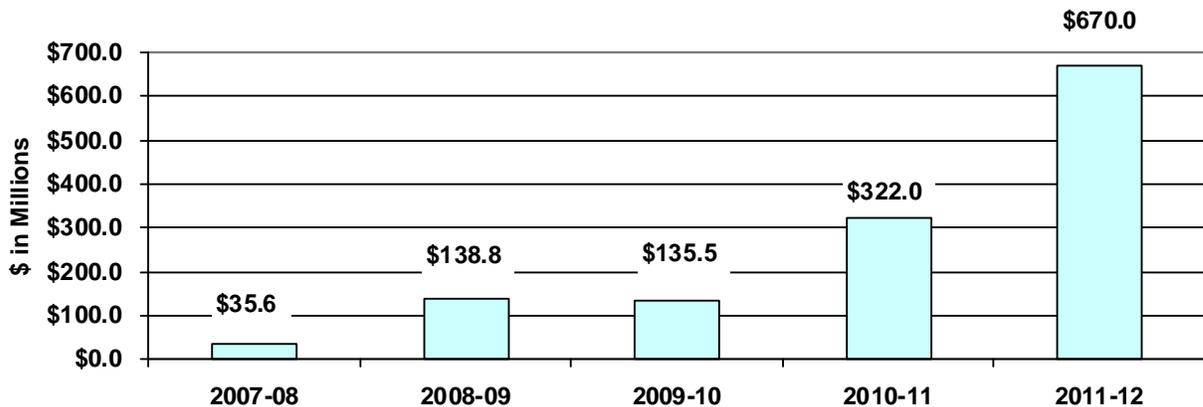
The revenue generated from UI contributions totaled \$619.1 million in SFY 2011-12, and reflects an increase of \$341.2 million (123 percent), compared to \$277.9 million in SFY 2010-11. The LEC revenue collected from school employers totaled \$25.8 million in SFY 2011-12, compared to \$19.0 million collected during SFY 2010-11 (see Appendix A3), which is an increase of \$6.8 million (36 percent). As UI benefits paid over the last several years have increased, many participants' LEC ranks have shifted to a higher LEC rate, contributing to the increase in LEC revenue.

The revenue received from penalty and interest charges assessed to SEF employers totaled \$0.4 million (see Appendix A3), during SFY 2011-12. This is a decrease of \$0.1 million (20 percent) compared to \$0.5 million earned in SFY 2010-11.

The interest income from the Surplus Money Investment Fund increased by \$0.3 million (300 percent) to total \$0.4 million in SFY 2011-12, compared to \$0.1 million in SFY 2010-11. The average Surplus Money Investment Fund apportionment yield during the SFY 2011-12 was 0.372 percent compared to 0.487 percent in the prior SFY 2010-11.

The SEF's total revenue was \$670.0 million for SFY 2011-12. This is an increase of \$348.0 million (108 percent) compared to the total revenue of \$322.0 million for the SFY 2010-11 (see Appendix A3). Figure 3 displays the total SEF revenue collected during the past five SFYs.

Figure 3



Unemployment Insurance Contribution Rates

Regarding the Contribution Rate, the CUIIC, Section 823(b)(2), states:

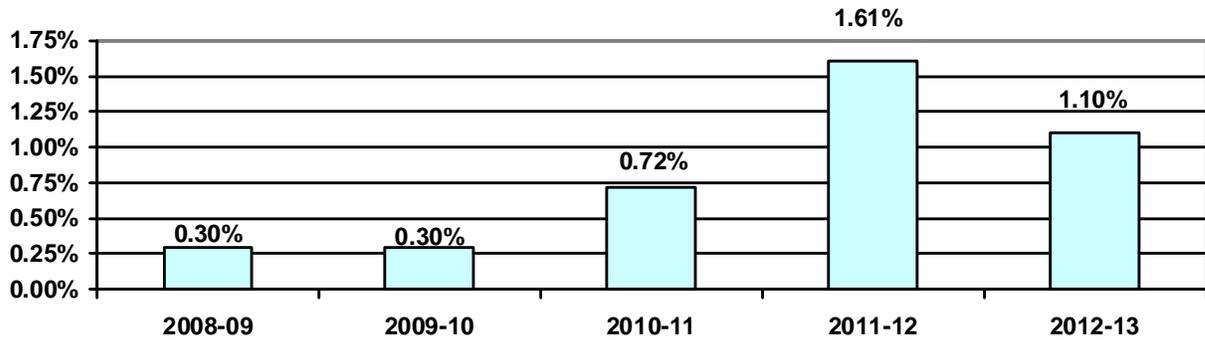
“The contribution rate for the fiscal year beginning July 1, 1988, and for each subsequent fiscal year shall be two times the amount disbursed for claims management fees, unemployment insurance benefit charges, and School Employees Fund administrative expenditures from the School Employees Fund during the 12-month period ending December 31 and immediately preceding the fiscal year for which the rate is to be effective, less the amount in the School Employees Fund on that December 31, with the resulting figure divided by total wages as described in paragraph (1) for the 12-month period ending June 30 and immediately preceding that December 31, and then rounded to the nearest one-hundredth of 1 percent. In no event shall the contribution rate be less than five one-hundredths of 1 percent.”

The UI contribution rate for school employers was calculated at 1.31 percent for SFY 2012-13. This rate would have generated an excess of an adequate reserve. Therefore, the Director, using the statutory discretion as mandated in CUIIC, Section 823(c), set the adjusted rate at 1.10 percent. This lower UI contribution rate will provide sufficient revenue for the SEF to meet its estimated financial obligations for SFY 2012-13.

The UI contribution rate is set annually for the subsequent SFY. Each SEF participant is notified of the rate by March 31.

Figure 4 displays the contribution rates for the last five SFYs.

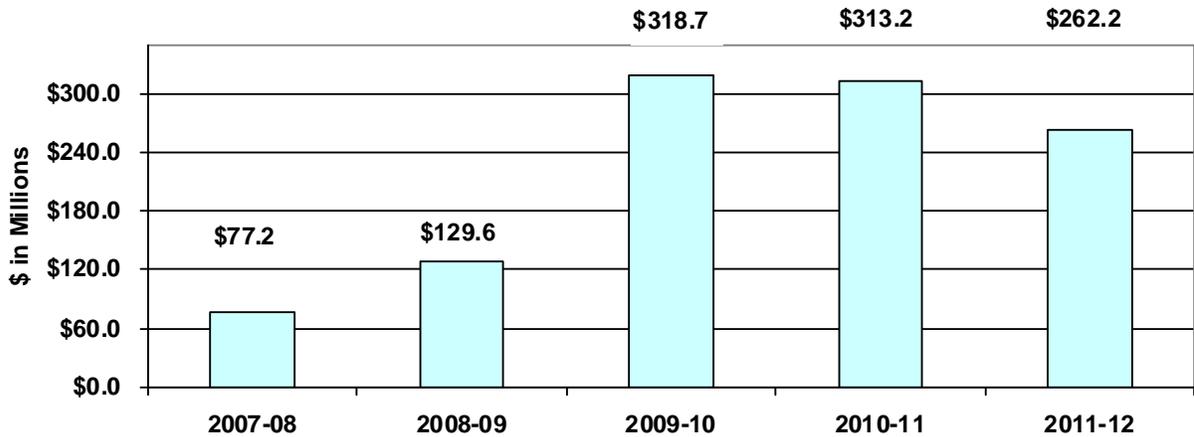
Figure 4



Total Fund Disbursements

The SEF's total disbursements were \$262.2 million during SFY 2011-12. This is a decrease of \$51.0 million (16 percent) compared to \$313.2 million in SFY 2010-11 (see Appendix A3). The expenditures include repayment to California's UI Trust Fund for UI benefits paid to former school employees, administrative costs, claims management fees, and prior year adjustments. Figure 5 displays the total disbursements for the last five SFYs.

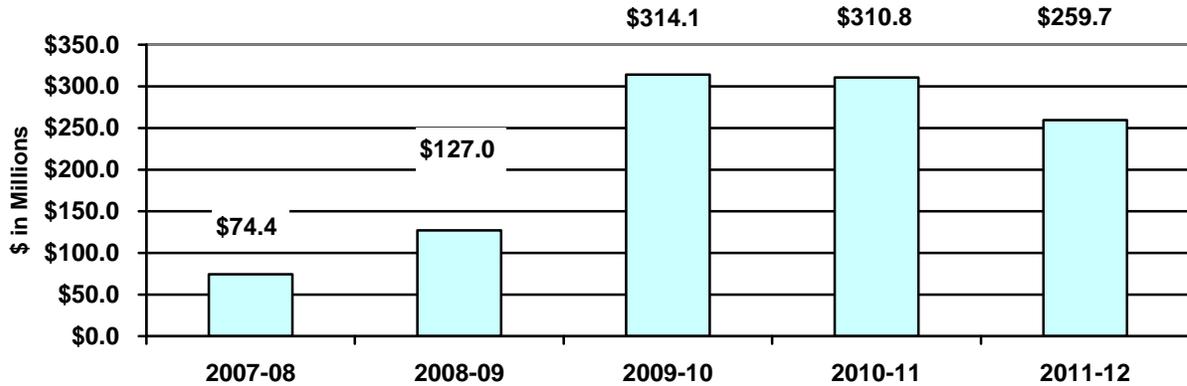
Figure 5



Total Benefits Paid

The total UI benefits paid to former school employees was \$259.7 million during SFY 2011-12. This represents a decrease of \$51.1 million (16 percent) when compared to \$310.8 million in SFY 2010-11 (see Appendix A3). The decrease in benefits paid is attributed to an increased number of school employees exhausting their UI benefits. In an effort to reduce layoffs, there were more furloughs, program eliminations, larger class sizes, and shortening of the school year. On May 12, 2012, the FED-ED program was terminated and as a result, UI benefit charges should continue to decline. Figure 6 displays the total UI benefits paid to former school employees during the past five SFYs.

Figure 6



LEGISLATION

The school employer community closely monitors legislative bills which may impact the UI program with the possible enactment of new laws, provisions, and policies. During SFY 2011-12, the school employers focused on several key bills.

- On December 23, 2011, President Obama signed the “*Temporary Payroll Tax Cut Continuation Act of 2011*” (House of Representatives Bill 3765, 112th Congress). This bill extended the effective date for filing the four federal Emergency Unemployment Compensation (EUC) extensions. It also extended the last effective date the 20 week FED-ED benefits could be filed to March 4, 2012.
- On February 22, 2012, President Obama signed the “*Middle Class Tax Relief and Job Creation Act of 2012*” (House of Representatives Bill 3630, 112th Congress). This legislation extended the filing deadlines for the EUC extended benefits for eligible unemployed workers to collect benefits while trying to secure a new job until late December. It modified potential maximum weeks of benefits provided for extensions after September 1, 2012. It also extended the last effective date a FED-ED claim could be filed to December 30, 2012 and the last payable week to January 5, 2013. However, it also modified the total potential maximum weeks of benefits provided for extensions filed with effective dates from February 19, 2012 through August 26, 2012 if California’s unemployment rate does not meet the legal threshold to continue filing and paying FED-ED extensions.
- The United States Department of Labor determined that California’s unemployment rate is no longer at the required level to continue paying FED-ED benefits after May 12, 2012. As a result of the FED-ED no longer being available, the fourth federal extension was temporarily modified from 6 to 16 weeks. As of June 30, 2012, the EUC extension filing and paying deadlines did not change. For claims filed on or after May 13, 2012, the maximum weeks of benefits paid will be reduced from 99 weeks to 89 weeks, and then to 73 weeks by December 23, 2012. However, the potential maximum weeks of benefits available to claimants for each extension will depend on many factors.

To summarize, the FED-ED program is separate from the EUC program and they are governed by a different set of laws. The FED-ED program has a direct impact to school employers as, by law, school employers must bear 100 percent of the costs for benefits paid under this program. Benefits paid under the EUC program are funded entirely by the federal government for all employers. Claimants cannot qualify for the FED-ED benefits until they have exhausted their regular UI benefits and exhausted benefits under the EUC program.

RECOMMENDATION

For SFY 2012-13, the SEF UI contribution rate was calculated at 1.31 percent. After consultation with the SEAC, the EDD Director approved the recommendation to reduce the calculated rate and set the SEF UI adjusted contribution rate at 1.10 percent. The new rate will generate sufficient revenue to meet the estimated financial obligations for SFY 2012-13.

QUESTIONS AND COMMENTS

Any questions, comments, or suggestions concerning the administration of the SEF should be directed to the SEF staff at (916) 653-5380.

APPENDIX A

FINANCIAL STATEMENTS

FINANCIAL STATEMENTS

Statement 1

**STATEMENT OF ACTIVITY
STATE FISCAL YEAR 2011-12**

ACCRUAL BASIS

Revenue

| | | |
|--------------------------------------|------------------|------------------|
| Contributions | \$619,129,090.13 | |
| Local Experience Charges | \$25,775,877.60 | |
| Penalty and Interest | \$432,189.56 | |
| Other Revenue | \$9.89 | |
| Interest Income | \$441,044.73 | |
| Prior Year Appropriation Adjustment* | \$11,499,530.70 | |
| Prior Year Adjustment* | \$12,769,553.83 | |
| Total Revenue | | \$670,047,296.44 |

Disbursements

| | | |
|--|------------------|------------------|
| Benefit Charges Repaid To UI Fund | \$259,668,589.40 | |
| SEF Administrative Costs | \$684,387.41 | |
| Claims Management Fees | \$1,797,791.00 | |
| Prior Year Adjustment* | \$0.00 | |
| Prior Year Benefit Appropriation Adjustment* | \$0.00 | |
| Total Disbursements | | \$262,150,767.81 |

Net Increase In Fund \$407,896,528.63

* Entry required at the end of the fiscal year for accrual of revenue and disbursement items.

Amounts Repaid to the Unemployment Insurance Fund

| <u>Quarters</u> | <u>Cost of Benefits</u> |
|--------------------|-------------------------|
| 3rd Quarter 2011 | \$114,062,466 |
| 4th Quarter 2011 | \$58,744,390 |
| 1st Quarter 2012 | \$45,861,734 |
| 2nd Quarter 2012** | \$41,000,000 |
| | <u>\$259,668,590</u> |

** Estimated Data

**STATEMENT OF RECEIPTS
AND DISBURSEMENTS
SEPTEMBER 1972 THROUGH JUNE 2012**

Revenue

| | | |
|--------------------------|--------------------|--------------------|
| Contributions | \$2,495,756,817.66 | |
| Local Experience Charges | \$143,162,106.77 | |
| Penalty and Interest | \$2,405,278.45 | |
| Interest Income | \$117,878,446.75 | |
| Total Revenue | | \$2,759,202,649.63 |

Disbursements

| | | |
|-----------------------------------|--------------------|--------------------|
| Benefit Charges Repaid To UI Fund | \$2,168,880,639.65 | |
| Local Assistance Special Pro-Rata | \$343,794.00 | |
| Accrued Penalty and Interest | \$2,007,962.97 | |
| Court-Ordered Interest Payments | \$1,764.27 | |
| SEF Administrative Costs | \$20,241,809.80 | |
| Fund Transfer* | \$98,800,000.00 | |
| Claims Management Fees | \$54,297,982.00 | |
| Total Disbursements | | \$2,344,573,952.69 |

Net Fund Balance

\$414,628,696.94

*Transferred to General Fund through Budget Acts of 1986 and 1988.

The Statement of Receipts and Disbursements is prepared on the accrual basis. As of June 30, 2012, outstanding liabilities for local assistance (benefits) totaled \$41 million.

| | |
|--|-----------------|
| | Accrued |
| | Disbursements |
| Second Quarter of 2012 Estimated Benefit Charges for year-end. | \$41,000,000.00 |

Statement 3

**COMPARATIVE STATEMENT OF FUND CONDITION
FOR THREE FISCAL YEARS ENDING JUNE 30, 2012
ACCRUAL BASIS (\$ in thousands)**

| | 2009-10 | 2010-11 | 2011-12 |
|------------------------------|------------------|------------------|------------------|
| Beginning Fund Balance | \$181,150 | (\$2,067) | \$6,732 |
| <u>Revenue</u> | | | |
| Contributions | \$120,960 | \$277,926 | \$619,129 |
| Local Experience Charge | \$13,478 | \$19,031 | \$25,776 |
| Penalty and Interest | \$165 | \$479 | \$432 |
| Interest Income | \$876 | \$127 | \$441 |
| Prior Year Adjustment | \$0 | \$24,439 | \$24,269 |
| Total Revenue | <u>\$135,479</u> | <u>\$322,002</u> | <u>\$670,047</u> |
| <u>Disbursements</u> | | | |
| Benefit Charges Repaid | \$314,053 | \$310,836 | \$259,669 |
| Pro-Rata | \$0 | \$0 | \$0 |
| SEF Administrative Costs | \$614 | \$590 | \$684 |
| Claims Management Fees | \$1,895 | \$1,777 | \$1,798 |
| Prior Year Adjustments | \$83 | \$0 | \$0 |
| Prior Year Benefit | | | |
| Appropriation Adjustment | \$2,051 | \$0 | \$0 |
| Total Disbursements | <u>\$318,696</u> | <u>\$313,203</u> | <u>\$262,151</u> |
| <u>Ending Fund Balance *</u> | <u>(\$2,067)</u> | <u>\$6,732</u> | <u>\$414,628</u> |

* Components may not add up to totals, due to rounding.

APPENDIX B

SCHOOL EMPLOYER ADVISORY COMMITTEE

SCHOOL EMPLOYER ADVISORY COMMITTEE

Members

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ACSA Ontario Office
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Ontario, CA 91784

California School Board Association
(CSBA)

State Superintendent of Public Instruction
(SSPI)

Chancellor of the California
Community Colleges (CCCC)

California Association of School Business
Officials (CASBO)

APPENDIX C

GLOSSARY

GLOSSARY

Benefits: The UI compensation payable to a former school employee, with respect to his or her unemployment, under the unemployment compensation law of any state or federal government.

Benefit Charges: The UI benefit charges reflected in the financial statements are the UI benefits paid during the period of July 1 through June 30 that is repaid to the California UI Trust Fund. All benefit charges paid from the SEF are considered a disbursement (expense).

Claims Management Fees: Two dollars (\$2) per covered employee, provided from available interest earnings from the SEF investments (less State administrative costs), is annually apportioned to the State Superintendent of Public Instruction (SSPI) or the Chancellor of the California Community Colleges (CCCC) for the administration of the UI management system.

Contributions: Each fund participant files documents and pays quarterly contributions which are deposited into the SEF as required by the CUIIC, Section 823(b)(1). The quarterly amount owed is calculated by multiplying the total wages times the contribution rate which is set for the SFY (see Contribution Rate definition below). The contributions paid by the fund participants are considered revenue and are deposited in the SEF to reimburse the California UI Trust Fund for UI benefits paid to former school employees.

Contribution Rate: The contribution rate is calculated annually for the SFY July 1 through June 30. The contribution rate is the same for all fund participants. As required by the CUIIC, Section 823(b)(1), all fund participants are notified by March 31 of the set contribution rate for the succeeding fiscal year.

Experience: A SEF participant must be in the Fund for more than three full SFYs to increase his or her reserve account in the SEF, so that in the fourth SFY, the LEC rate is calculated based on the experience of the school employer's relative usage of the UI fund (UI benefit charges). All fund participants are notified by March 31 of their LEC rate as required by the CUIIC, Section 828(c).

Fund Participants: This term is used to refer to the school employers who have elected to participate in the SEF to finance their UI taxes.

Interest Income: Interest is deposited quarterly into the SEF based on the SEF balance with the State Treasury, times the rate set by the Surplus Money Investment Fund.

Local Assistance Pro Rata: The Local Assistance Pro Rata is charged by the Department of Finance. Pro Rata is the recovery of central service administrative costs from special and non-governmental cost funds. The State of California provides certain services (central administrative agencies), such as accounting, computing, payroll services, banking, etc., to operating agencies (departments) on a centralized basis. Pro Rata is a process that identifies these central service administrative costs and assigns them to benefited activities (functions) on a reasonable and consistent basis.

Local Experience Charge (LEC): As mandated in the CUIC, Section 828, each school employer in the SEF shall be responsible for a quarterly LEC based on their LEC rate. The LEC is *in addition* to the quarterly contributions paid by the fund participants. The participant's individual LEC amount due is calculated by multiplying the employer's quarterly UI benefit charges times the fund participant's LEC rate. The LEC payment is due to the EDD 30 days after the mail date of the form, Notice of Amount Due (DE 6601).

Local Experience Charge (LEC) Rate: The LEC rate is calculated annually for a SFY July 1 through June 30. The LEC percentage is varied for each fund participant as listed below:

- 15 percent (ratio = negative < 1.00)
- 10 percent (ratio = 1.00 < 2.00)
- 5 percent (ratio = 2.00 < 3.00)
- 0 percent (ratio = 3.00 or more)

The LEC ratio is calculated by the fund participant's ending cumulative balance divided by the UI benefit charges. All fund participants are notified by March 31 of their individual LEC rates for the succeeding fiscal year as required by the CUIC, Section 828(c). Additionally, Section 828(a) mandates that new SEF participants are subject to a 10 percent LEC rate for the first three complete fiscal years.

Penalty and Interest: Penalty and interest are assessed to fund participants by the administrator of the SEF for delinquent payments and/or forms and errors. Interest is calculated daily until paid. The funds collected for penalty and interest are deposited in the SEF and are considered revenue.

Prior Year Adjustment: The Prior Year Adjustment is an entry to the account at the end of the fiscal year for financial statement preparation purposes required for accrual of revenue and expense items. The Prior Year Adjustment is any revenue collected or disbursed in the current SFY and tied to a prior period other than the current SFY.

School Employees Fund (SEF) Administrative Costs: The SEF Administrative Costs are the cost of resources and tools necessary to effectively operate the SEF program.

Surplus Money Investment Fund: Interest on investments of the Surplus Money Investment Fund is apportioned to other funds quarterly by the State Controller's Office per the Government Code Section 16475. The administering agency for the funds receiving interest will receive the State Controller's Office Notice of Transfer posting the interest in the month following the end of the quarter. Agencies will account for the interest as revenue or operating revenue in the applicable funds.