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# REPORT ON SIGNIFICANT FINANCIAL TRENDS AND FINDINGS IN 2012-13 FISCAL YEAR AUDITS OF DISTRICT SCHOOL BOARDS

STATE OF FLORIDA
AUDITOR GENERAL
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# REPORT ON SIGNIFICANT FINANCIAL TRENDS AND FINDINGS IN 2012-13 FISCAL YEAR AUDITS OF DISTRICT SCHOOL BOARDS

## SUMMARY

**This report provides a summary of significant financial trends and findings identified in the audits of the 67 district school boards. For the 2012-13 fiscal year, audits of 47 school districts were performed by our office and audits of 20 school districts were performed by other independent certified public accountants (CPAs). The audit reports prepared by the other independent CPAs were required to be filed with us no later than March 31, 2014.**

**Significant Financial Trends**

- **At June 30, 2013, school districts Statewide had an average level of general fund total assigned and unassigned fund balance that was 10.62 percent of general fund revenues (financial condition ratio), which represents a 1.62 percentage point decrease compared to the average financial condition ratio for the previous fiscal year. Of the 67 school districts, 5 had ratios that were below 3 percent at June 30, 2013. In these circumstances, these school districts had significantly less resources available for emergencies and unforeseen situations than other school districts.**

**Significant Findings**

- **The audit reports for 61 of 67 school districts included audit findings addressing weaknesses in internal control; instances of noncompliance with applicable laws, rules, or regulations; or additional matters. Audit reports of four school districts included one or more findings considered to be material weaknesses, which represents a decrease compared to the eight audit reports that included material weaknesses for the previous fiscal year. Of the four audit reports, one also cited an instance of material noncompliance.**

## BACKGROUND

Sections 11.45 and 218.39, Florida Statutes, provide for audits of district school boards to be performed annually by the Auditor General or by other independent CPAs. The scope of these audits includes an examination of the financial statements, the issuance of a report on compliance and internal control in accordance with generally accepted government auditing standards, and the issuance of a report on compliance and internal control for each major Federal program in accordance with United States Office of Management and Budget Circular A-133.

Section 11.45(7)(f), Florida Statutes, requires that we annually compile a summary of significant financial trends and findings identified in school district audit reports.

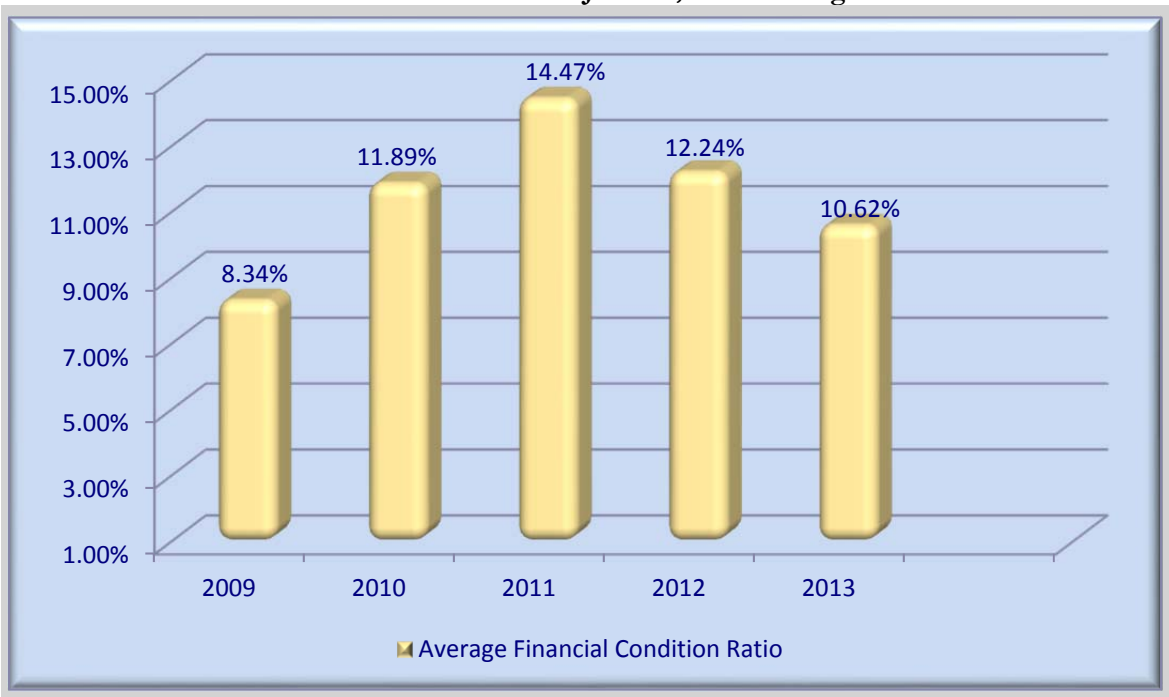
## FINANCIAL TRENDS

Section 11.45(7)(f), Florida Statutes, along with other inquiries, evidences that critical interest exists to understand and address factors that affect the financial condition of school districts. The financial condition of school districts can be assessed by a review of the general fund balances and activities, which account for the majority of the operating resources and expenditures for K-12 educational programs. Consequently, the general fund is used as the primary basis for measurement of financial condition.

## Financial Condition Trends

The financial condition measure used in this report is the financial condition ratio[1] of the general fund total assigned and unassigned fund balance, or unreserved fund balance, to the general fund total revenues (see Exhibits 12 and 13). Exhibit 1 shows the average financial condition ratios for the fiscal years ended June 30, 2009 through 2013. The average financial condition ratio was 10.62 percent at June 30, 2013, which represents a 1.62 percentage point decrease compared to the average financial condition ratio for the previous fiscal year. The notable financial condition ratio increases for the 2009-10 and 2010-11 fiscal years were primarily due to the school districts' receipt and use of American Recovery and Reinvestment Act (ARRA) and other Federal economic stimulus funds for certain allowable operating expenditures. The Florida Department of Education (FDOE) required school districts to account for these funds in special revenue funds, rather than the general fund. As discussed in the **American Recovery and Reinvestment Act and Other Federal Funding** section, with the exception of the Race-to-the-Top and School Improvement grants, most ARRA funding terminated during the 2010-11 fiscal year.

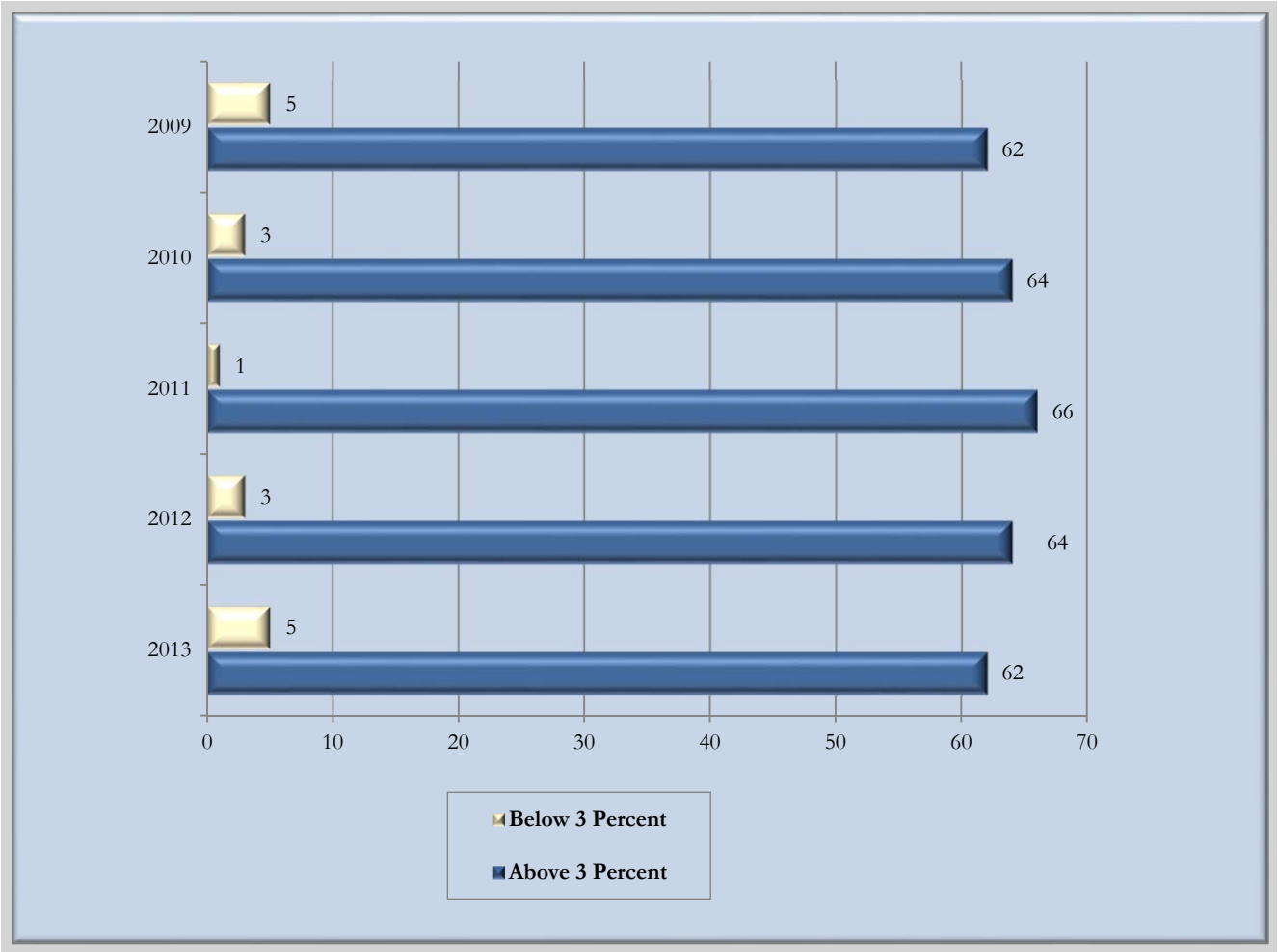
**Exhibit 1**
**Average Financial Condition Ratios of School Districts**
**for the Fiscal Years Ended June 30, 2009 Through 2013**




Section 1011.051, Florida Statutes, requires that each school district maintain a general fund ending fund balance that is sufficient to address normal contingencies. If at any time the financial condition ratio determined from the school district's approved operating budget is projected to fall below 3 percent during the current fiscal year, school district superintendents must notify the Commissioner of Education and respective school board. Exhibit 2 shows the number of school districts with ratios below and above 3 percent for the fiscal years ended June 30, 2009 through 2013.

[1] Governmental Accounting Standards Board (GASB) Statement No. 54 established the assigned/unassigned fund balance classifications, effective for the 2010-11 fiscal year, which is similar to the unreserved fund balance classification required for prior fiscal years. For comparison purposes, financial condition ratios are calculated using the applicable assigned/unassigned or unreserved fund balances. See Exhibits 12 and 13.

**Exhibit 2**
**Number of School Districts with Financial Condition Ratios**
**Below and Above 3 Percent for the Fiscal Years Ended June 30, 2009 Through 2013**




As indicated on Exhibit 2, the number of school districts with financial condition ratios below 3 percent at fiscal year end increased from one to five school districts over the past three fiscal years, including two school districts that had deficit ratios at fiscal year ended June 30, 2013. These school districts have significantly less resources available for emergencies and unforeseen situations than other school districts. In addition, Exhibit 3 identifies the financial condition of these school districts and the number of consecutive fiscal year ends that their financial condition ratio was below 3 percent.

**Exhibit 3**
**School Districts with Financial Condition**
**Ratios Below 3 Percent**

| School Districts | Financial Condition Ratios - Fiscal Year Ended June 30, 2013 | Number of Consecutive Years Ratio Below 3% |
|---|---|---|
| Clay | 2.12% | 1 |
| Columbia | 0.70% | 2 |
| Franklin | -2.43% | 2 |
| Manatee | -2.80% | 6 |
| Martin | 2.45% | 1 |

The financial condition ratios of several other school districts were below the above-noted threshold at certain times during the 2008-09 through 2012-13 fiscal years, but not at June 30, 2013. Historically, school districts that experience weak financial conditions implement measures that generally restore their financial conditions to favorable positions within one or two fiscal years.

If at any time a school district's financial condition ratio, determined from the school district's approved operating budget, is projected to fall below 2 percent, Section 1011.051(2), Florida Statutes, requires the school board to have a reasonable plan to avoid a financial emergency, or the FDOE will appoint a financial emergency board to implement measures to assist the school board in resolving the financial emergency. Pursuant to Section 218.503(3), Florida Statutes, a school district is considered to be in a state of financial emergency if the FDOE determines that the school board needs State assistance to resolve or prevent a financial emergency condition. As noted in Exhibit 3, three school districts had financial condition ratios below 2 percent at June 30, 2013; however, the FDOE determined that financial emergency boards were not necessary to assist these school boards and the school districts needed no State assistance to resolve or prevent a financial emergency condition.

## Factors Impacting Financial Condition

As previously discussed, the financial condition ratios for the fiscal year ended June 30, 2010 and 2011 were significantly impacted by the receipt and use of ARRA and other Federal economic stimulus funding, most of which terminated during the 2010-11 fiscal year. Further analyses of school district financial trend data identified other factors that impact the financial condition of school districts and may increase the risk of weak financial condition. While no single factor is identified as a guaranteed predictor of financial condition, factors such as declining property values, increasing or declining enrollment, and school and class sizes require the exercise of effective financial management to limit the impact on the school districts' financial condition.

**Declining Property Taxes**. Property taxes are the primary source of local revenues for school districts, and as part of the overall general economic decline, property values have decreased Statewide. According to the Florida Department of Revenue, Statewide property values declined from $1.6 trillion in the 2009 calendar year to $1.4 trillion in the 2013 calendar year, a decrease of 12.5 percent. Due in part to this decline, Statewide property tax levies for school district operations declined from $12.1 billion for the 2009-10 fiscal year to $10.6 billion for the 2012-13 fiscal year, a decrease of 12.4 percent.

**Increasing Enrollment**. Statewide enrollment increased slightly from 2,598,617 for the 2008-09 fiscal year to 2,656,450 for the 2012-13 fiscal year. A total of 28 school districts experienced enrollment growth during this period, including 12 school districts that had enrollment growth of 1,000 or more unweighted full-time equivalent (FTE) students, as shown on Exhibit 4. Although these school districts experienced an increase in FTE-based revenue for the increased enrollment, revenue increases can lag behind school district expenditures when staffing new schools and paying initial start-up costs. Also, there is a risk that rapidly growing school districts may overestimate FTE when making FTE projections. Not only are these overestimates costly when FTE-based revenues are adjusted (reduced), but school districts may have made costly hiring and other expenditure decisions based on the estimated enrollment projections.

**Exhibit 4**
**School Districts with Enrollment Growth**
**From 2008-09 to 2012-13 Fiscal Years**

| Number of School Districts | | Unweighted FTE | | |
|---|---|---|---|---|
| | | 2008-09 | 2012-13 | Increase |
| 1 | Orange | 170,093 | 182,438 | 12,345 |
| 2 | Hillsborough | 190,090 | 199,085 | 8,995 |
| 3 | Palm Beach | 169,613 | 177,797 | 8,184 |
| 4 | Miami-Dade | 342,775 | 350,817 | 8,042 |
| 5 | Lee | 78,281 | 84,576 | 6,295 |
| 6 | Osceola | 51,071 | 55,881 | 4,810 |
| 7 | Broward | 255,058 | 259,405 | 4,347 |
| 8 | St. Johns | 28,834 | 32,351 | 3,517 |
| 9 | Manatee | 42,084 | 45,150 | 3,066 |
| 10 | Duval | 123,716 | 126,763 | 3,047 |
| 11 | Polk | 93,104 | 95,634 | 2,530 |
| 12 | Collier | 41,985 | 43,400 | 1,415 |

**Declining Enrollment**. While enrollment slightly increased in total for all school districts from the 2008-09 fiscal year to the 2012-13 fiscal year, 39 school districts experienced enrollment declines during this period, including 4 school districts with declines of 1,000 or more unweighted FTE students, as shown on Exhibit 5. Variations in student enrollment and the related impact on funding from year to year can make school district planning and budgeting decisions for staffing and other activities more challenging. In particular, smaller school districts may experience difficulty with gradual enrollment declines, as it is difficult to reduce the number of instructional staff because often no one grade or class within an individual school may be affected enough to justify the reduction.

**Exhibit 5**
**School Districts with Declining Enrollment**
**From 2008-09 to 2012-13 Fiscal Years**

| Number of School Districts | | Unweighted FTE | | |
|---|---|---|---|---|
| | | 2008-09 | 2012-13 | Decrease |
| 1 | Pinellas | 105,461 | 102,764 | (2,697) |
| 2 | Volusia | 62,965 | 61,056 | (1,909) |
| 3 | Brevard | 72,197 | 70,529 | (1,668) |
| 4 | Charlotte | 16,992 | 15,992 | (1,000) |

**Number and Size of Schools**. Considerable variation exists in the number and size of schools. Some school districts have a predominantly larger number of schools, and some have a predominantly smaller number of schools. Additionally, some have varying combinations of large, medium, and small school sizes. Logically, larger schools cost less per student than smaller schools because the salary, benefits, and fixed costs are spread over a larger number of students. The number and size of schools are relevant factors that impact financial condition among school districts.

## Future Financial Trends Considerations

**State Funding**. For the 2012-13 fiscal year, the base Florida Education Finance Program (FEFP) allocation was $3,582.98 per weighted FTE student, which represents an increase of $103.76 from the base FEFP allocation of $3,479.22 for the 2011-12 fiscal year. Also, based on the 2013-14 fiscal year FEFP Fourth Calculation released by the FDOE in April 2014, the base FEFP allocation for the 2013-14 fiscal year is expected to increase by $169.32, from the 2012-13 fiscal year final allocation, to $3,752.30. The weighted FTE in school districts increased by approximately 41,000 from the 2011-12 fiscal year to the 2012-13 fiscal year, and based on the 2013-14 FEFP Fourth Calculation, the weighted FTE increased further, by approximately 21,000, in the 2013-14 fiscal year. While these are relatively significant increases compared to previous fiscal years, effective financial monitoring and timely and appropriate adjustments to operations are critical to school districts to ensure that the costs of operations remain within available financial resources.

**Debt and Other Long-Term Financing**. School districts may finance capital outlay projects by issuing long-term debt such as general obligation bonds and school district revenue bonds and by entering into long-term lease finance arrangements generally referred to as certificates of participation. The long-term debt and other financing obligations reported as outstanding as of June 30, 2013, consisted primarily of: Certificates of Participation (COPs) totaling $13 billion; Qualified School Construction Bonds (QSCBs), Qualified Zone Academy Bonds (QZABs), and Build America Bonds (BABs) totaling $943 million, $247 million, and $101 million, respectively; and school district revenue, State Board of Education, and general obligation bonds totaling $803 million, $416 million, and $125 million, respectively. Also, school districts had $117 million in long-term debt notes. Generally, school districts extinguish their debt through various pledged resources such as capital outlay millage, discretionary sales surtax, pari-mutuel distributions, and other tax proceeds. As of June 30, 2013, pledged resources were generally sufficient to cover the required debt service by school districts. However, given the impact of the decreases in certain revenue sources, such as property taxes, school districts will need to closely monitor the impact on required debt service payments.

Further, eight school districts that had variable interest rate COPs at June 30, 2013, had entered into 22 interest rate swap agreements to reduce overall borrowing costs. The objective of an interest rate swap agreement, a type of hedging derivative, is to achieve lower borrowing costs by synthetically fixing interest rates on the debt as compared

to issuing regular fixed-rate debt. Debt service payments fluctuate, depending on changes in the underlying interest rates linked to the interest rate swap agreements, and accounting standards require that hedging derivatives be disclosed at fair value as of the financial reporting date.

The fair value of an interest rate swap agreement is the estimated amount the school district would have received or paid if the swap agreement was terminated. As of June 30, 2013, total fair values of the interest rate swap agreements for each of the eight school districts ranged from negative $626 thousand to negative $95 million. However, the interest rate swap agreements are associated with COPs with remaining terms that exceeded 20 years, and the actual benefit or additional costs of the swap agreements generally will not be known until the COPs have been paid off.

Depending on the fair value of the swap agreements upon termination, there is a risk that the debt service costs of these school districts may exceed the costs that could have been experienced from regular fixed-rate debt. As of June 30, 2013, each of these school districts had sufficient available resources to meet their respective debt service requirements.

**American Recovery and Reinvestment Act and Other Federal Funding**. The distribution of $5 billion dollars of ARRA funds to the Florida school districts' K-12 programs began in the 2008-09 fiscal year to improve schools and achieve and produce better results for students. ARRA had a significant financial impact for the 2009-10 and 2010-11 fiscal years on school districts with funding amounts for State stabilization, Federal Special Education, and Federal Title I programs of $2.7 billion, $647 million, and $491 million, respectively. Further, ARRA competitive grants have been made available to school districts, the largest being Race-to-the-Top Incentive grants. With the exception of the Race-to-the-Top Incentive and School Improvement grants, ARRA funding generally terminated during the 2011-12 fiscal year. For the 2012-13 fiscal year, school districts incurred ARRA and other Federal economic stimulus expenditures totaling $152 million, a significant decrease compared to the $229 million expended for the 2011-12 fiscal year, and the $1.9 billion expended for the 2010-11 fiscal year.

## School District Trends

**Funding Trends.** School district governmental funds include the general fund, special revenue funds, debt service funds, and capital projects funds. School districts frequently have fiduciary funds (agency and trust funds) and proprietary funds (primarily internal service funds that account for such activities as self-insurance programs). However, substantially all of a school district's resources are accounted for in the governmental funds. Exhibit 6 shows that school districts reported revenues of $24.5 billion in the governmental funds for the 2012-13 fiscal year, an increase of $534 million from the previous fiscal year.

**Exhibit 6**
**Statewide Revenues – All Governmental Funds**
**2011-12 and 2012-13 Fiscal Years**

| Governmental Fund Type | 2011-12 Amount | 2011-12 Percent of Total | 2012-13 Amount | 2012-13 Percent of Total | Increase/ (Decrease) | Percent Increase/ (Decrease) |
|---|---|---|---|---|---|---|
| General Fund | $ 17,822,854,462 | 74.24% | $ 18,383,370,949 | 74.91% | $ 560,516,487 | 3.14% |
| Other Funds | 6,182,920,817 | 25.76% | 6,155,977,370 | 25.09% | (26,943,447) | (0.44)% |
| | | | | | | |
| **Total** | **$ 24,005,775,279** | **100.00%** | **$ 24,539,348,319** | **100.00%** | **$ 533,573,040** | **2.22%** |

Exhibit 7 shows total governmental fund type revenues reported by school districts for the 2012-13 and 2011-12 fiscal years by revenue source.

**Exhibit 7**
**Revenues by Source - All Governmental Funds**
**2011-12 and 2012-13 Fiscal Years**

| Sources | 2011-12 Amount | 2011-12 Percent of Total | 2012-13 Amount | 2012-13 Percent of Total | Increase/ (Decrease) | Percent Increase/ (Decrease) |
|---|---|---|---|---|---|---|
| Federal | $ 3,157,525,877 | 13.15% | $ 3,116,588,736 | 12.70% | $ (40,937,141) | (1.30%) |
| State | 9,079,185,050 | 37.82% | 9,838,227,146 | 40.09% | 759,042,096 | 8.36% |
| Local | 11,769,064,352 | 49.03% | 11,584,532,437 | 47.21% | (184,531,915) | (1.57%) |
| **Total** | **$ 24,005,775,279** | **100.00%** | **$ 24,539,348,319** | **100.00%** | **$ 533,573,040** | **2.22%** |

The $534 million increase in total revenues for the 2012-13 fiscal year consisted of a net decrease in Federal revenues of $41 million, an increase in State revenues of $759 million, and a decrease in local revenues of $185 million. Total State revenues increased by 8.36 percent, and the Federal and local revenues decreased by 1.30 percent and 1.57 percent, respectively. The increase in State revenues consists of increases of $709 million in State FEFP revenues and $50 million in restricted State revenues. The decrease in local revenues is due primarily to a decrease in the local effort required by the State to be levied by school districts, which decreased from $6.9 billion for the 2011-12 fiscal year to $6.7 billion for the 2012-13 fiscal year.

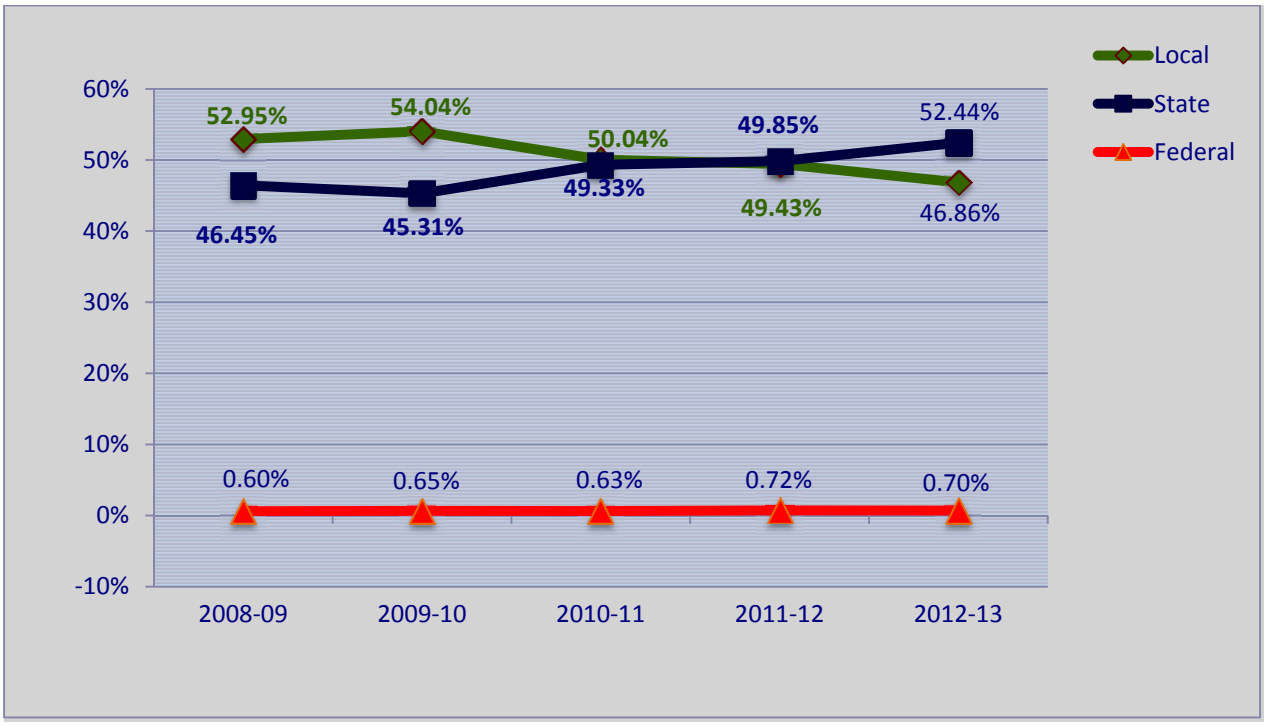
Exhibit 8 shows Federal, State, and local sources reported in the general fund (operating fund) of school districts for the 2012-13 and 2011-12 fiscal years.

**Exhibit 8**
**General Fund Revenues by Source**
**2011-12 and 2012-13 Fiscal Years**

| General Fund | 2011-12 Amount | 2011-12 Percent of Total | 2012-13 Amount | 2012-13 Percent of Total | Increase/ (Decrease) | Percent Increase/ (Decrease) |
|---|---|---|---|---|---|---|
| Federal | $ 127,531,840 | 0.72% | $ 128,605,676 | 0.70% | $ 1,073,836 | 0.84% |
| State | 8,886,112,029 | 49.85% | 9,640,457,591 | 52.44% | 754,345,562 | 8.49% |
| Local | 8,809,210,593 | 49.43% | 8,614,307,682 | 46.86% | (194,902,911) | (2.21%) |
| **Total** | **$ 17,822,854,462** | **100.00%** | **$ 18,383,370,949** | **100.00%** | **$ 560,516,487** | **3.14%** |

As shown on Exhibit 8, the State provided 52.44 percent of general fund resources during the 2012-13 fiscal year, while local revenue sources provided 46.86 percent of general fund resources. As discussed later in this section, Federal funds are restricted and most of those funds are reported in the school districts' special revenue funds. The percentage of revenues from Federal, State, and local sources in the general fund over the last five fiscal years can be seen on Exhibit 9:

**Exhibit 9**
**Percentage of General Fund Revenues from Federal, State, and Local Sources for 2008-09 Through 2012-13 Fiscal Years**




**FEFP – State and Local Revenues.** The majority of the State and local revenues for school district operations are derived from FEFP, which is designed to provide a base level of educational resources per FTE for all school districts. FEFP moneys are primarily generated by multiplying the number of FTE students in funded educational programs by various weights and cost factors determined by the Legislature. Each school district receiving State FEFP moneys must levy the required local effort millage in its local property taxes.

State and local FEFP revenue for school district operations totaled $12.97 billion for the 2012-13 fiscal year, comprised of $6.25 billion in State revenues and $6.72 billion in local revenues. In addition to the $6.25 billion in State revenues for operations as part of the FEFP, the school districts reported $3.59 billion in restricted State revenues. These restricted State revenues were for Class Size Reduction, Workforce Development, School Recognition, and other specific programs.

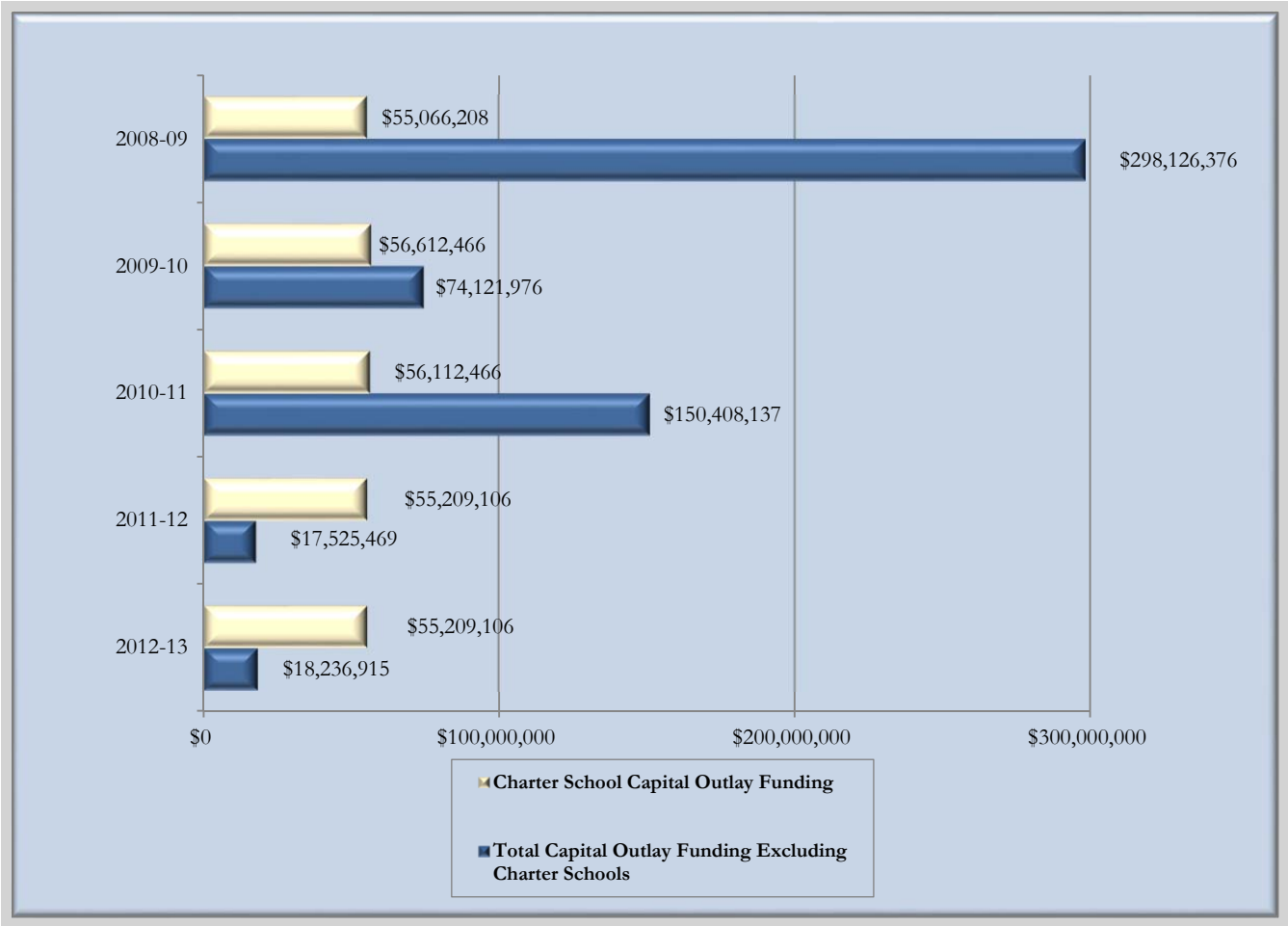
**Other Local Revenues.** In addition to the $6.72 billion in local revenues for funding operations as part of the FEFP, the school districts reported $4.87 billion in other local revenues. These local revenues included, but were not limited to, $1.79 billion from capital outlay millage levies for advertised construction, facility maintenance, and equipment; $889 million from discretionary local effort millage levies for operations; $235 million from special voter levies; $52 million from debt service millage levies for servicing debt; and $28 million from critical needs operation levies. Because of discounts for early payments, property tax revenues are approximately 96 percent of the tax levy. Additional sources of local revenue included sales taxes, impact fees, charges for services, investment income, and other local sources. Twenty-two school districts reported local sales tax revenue totaling $467 million for the 2012-13 fiscal year, while the same number of school districts reported $445 million for the previous fiscal year. Twenty-six school districts reported impact fee revenues totaling $162 million for the 2012-13 fiscal year compared to 29 school districts that reported $102 million for the previous fiscal year. Ten school districts assessed impact fees but reported no revenue for the 2012-13 fiscal year, compared to seven districts in the previous fiscal year.

**Federal Revenues.** Resources of the special revenue funds consist of moneys restricted by Federal and State grantors to be used for specific program purposes, such as Federal Title I and National School Lunch Act revenues. Because these resources are restricted, school districts can use them only for those specific activities that meet the purposes of the granting agency, and such resources are not available for general appropriation for operating activities or for unexpected events or emergencies.

**Debt Issuance Proceeds.** The issuance of long-term debt is a significant source of capital funding for school districts. Proceeds associated with the issuance of debt (net of refundings) for the 2012-13 fiscal year totaled $129 million as compared to $40 million for the 2011-12 fiscal year. Within the governmental funds, debt service and capital projects funds are used to account for resources restricted specifically for the payment of debt and for the acquisition of real property and the construction, renovation, remodeling, and maintenance of school district facilities. These resources are generally not available to finance the operating activities of a school district.

**State Capital Outlay Appropriations.** Until recently, certain statutory appropriations, such as Public Education Capital Outlay (PECO) appropriations authorized by Section 1013.65, Florida Statutes, constituted significant State funding for school district new construction and facilities maintenance projects. These statutory appropriations included, but were not limited to, PECO, Classrooms First, Classrooms for Kids, and Capital Outlay and Debt Service (CO&DS), which were predominantly funded using proceeds from the gross receipts tax established by Sections 9(a)(2) and 9(d), Article XII of the State Constitution. As shown on Exhibit 10, these appropriations to school districts, excluding charter schools, have decreased from $298.1 million for the 2008-09 fiscal year to $18.2 million for the 2012-13 fiscal year. During the same time period, capital outlay funding for charter schools has remained relatively constant, increasing slightly from $55.1 million for the 2008-09 fiscal year to $55.2 million for the 2012-13 fiscal year.

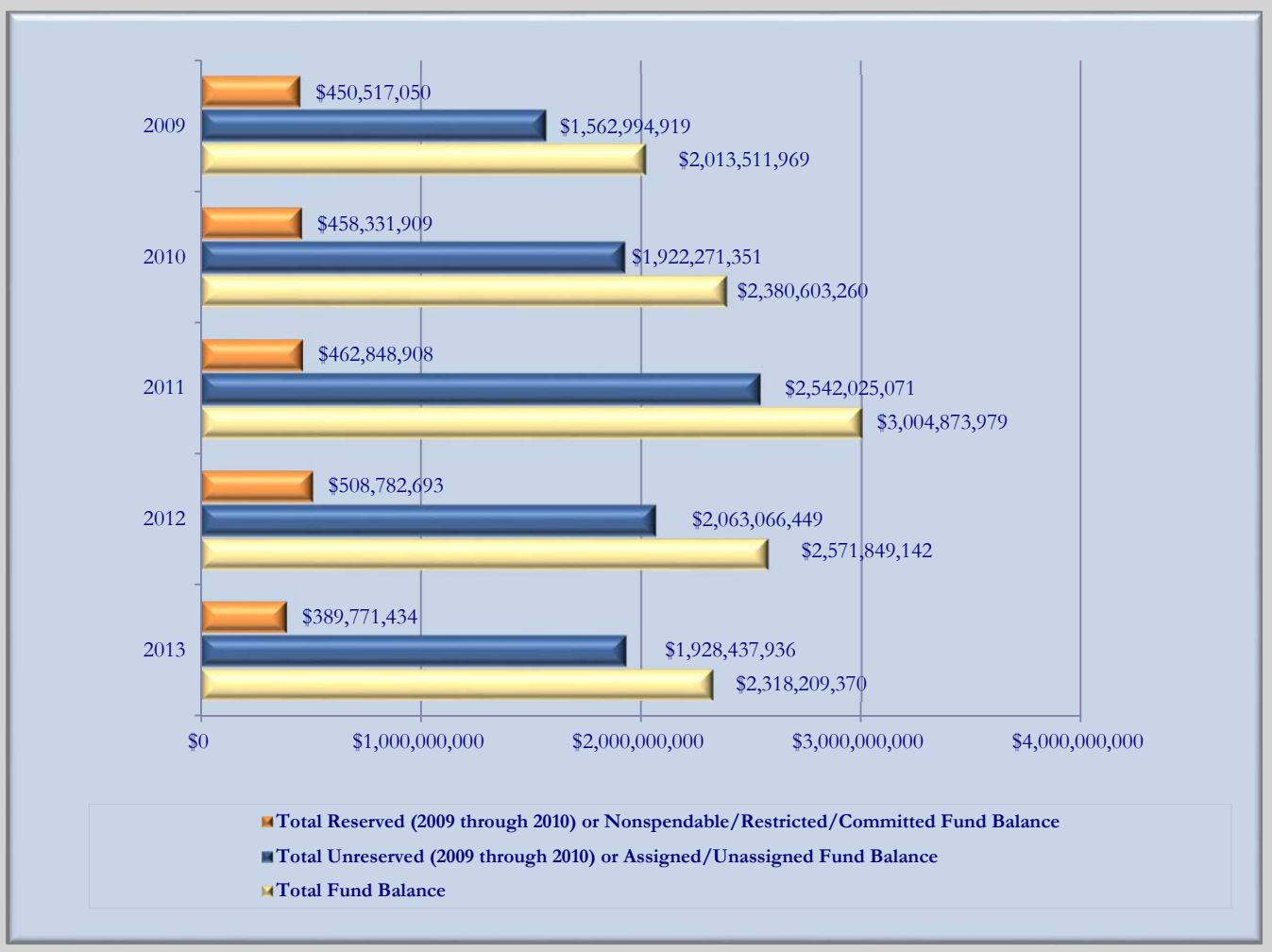
**Exhibit 10**
**State Capital Outlay Appropriations[2]**
**for 2008-09 Through 2012-13 Fiscal Years**




**Fund Balance Trends.** As shown below on Exhibit 11, the combined fund balances of the general funds (operating funds) of school districts Statewide increased from $2.01 billion for the 2008-09 fiscal year to $2.32 billion for the 2012-13 fiscal year.

[2] State capital outlay appropriations include PECO, Classrooms First, Classrooms for Kids, and CO&DS (excluding interest earnings on undistributed CO&DS).

**Exhibit 11**
**Fund Balances of the General Fund[3]**
**for the Fiscal Years Ended June 30 2009 Through 2013**




The percentage of unreserved or assigned/unassigned fund balance to total fund balance ranged from a low of 77.6 percent at June 30, 2009 to a high of 84.6 percent at June 30, 2011.

Total fund balance decreased by $254 million from fical year ended June 30, 2012 to June 30, 2013, due in part to reductions of local revenues discussed in the **Funding Trends** section and also increases in costs, such as salaries and benefits, for certain school districts. Also, in the 2009-10 and 2010-11 fiscal years, certain instructional costs were shifted to the special revenue funds where these costs were paid from Federal funds such as ARRA, as mentioned in the **Financial Condition Trends** section. However, as discussed in the **American Recovery and Reinvestment Act and Other Federal Funding** section, with the exception of the Race-to-the-Top Incentive and School Improvement grants, most ARRA funding terminated in the 2010-11 fiscal year. An expected increase in the per FTE FEFP allocation for the 2013-14 fiscal year may mitigate further fund balance decreases in the 2013-14 fiscal year.

[3] See Footnote 1. Also, GASB Statement No. 54 requires the nonspendable/restricted/committed fund balance classifications, beginning June 30, 2011, which are similar to the reserved fund balance classification required before that date.

## Financial Condition Background

**Financial Condition Measure**. There are several measures that may be used to evaluate the financial condition of governments. One widely used financial condition measure that is relevant to school districts compares the level of available equity in the operating fund to overall operating resources for that fund for a fiscal year. This measure shows the net accumulated resources at a point in time that is available for appropriation to meet the costs of unexpected and nonrecurring events. We used this measure in analyzing school district financial condition (see Exhibits 12 and 13).

**Exhibit 12**
**Financial Condition Measure**
**(Pre-Fiscal Year Ended June 30, 2011)**

| | | |
|---|---|---|
| General Fund Unreserved Fund Balance[4] / General Fund Total Revenues | = | Financial Condition Ratio (%) |

**Exhibit 13**
**Financial Condition Measure**
**(Fiscal Year Ended June 30, 2011 and Afterwards)**

| | | |
|---|---|---|
| General Fund Total Assigned and Unassigned Fund Balance[4] / General Fund Total Revenues | = | Financial Condition Ratio (%) |

Credit rating agencies generally look more favorably on financial condition ratios of at least 5 percent. Other literature suggests percentages ranging from 5 to 10 percent. However, often the guidance is not clear as to whether the percentage is derived from total fund balance or assigned and unassigned fund balance (previously reported as unreserved fund balance). We also considered revenue stream characteristics and expenditure practices for school districts. In view of the revenue and expenditure considerations of school districts, the established financial management practices followed by school districts, and the oversight by the FDOE, a lower total assigned and unassigned fund balance threshold may be reasonable with acceptable risks.

# AUDIT FINDINGS

## Classification of Audit Findings

Auditing standards require that auditors report material weaknesses in internal control and significant control deficiencies that are disclosed during the course of a financial statement audit. A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the financial statements would not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. Auditors must also report material noncompliance or abuse that has a material effect on the audit. The classification of an audit finding is

[4] See Footnote 1.

dependent upon its potential impact on the specific school district under audit. Therefore, the classification of an audit finding could vary from school district to school district.

The audit reports for 6 school districts contained no findings, while audit reports for the remaining 61 school districts included a total of 504 findings addressing weaknesses in internal control; instances of noncompliance with applicable laws, rules, or regulations; or additional matters. For purposes of this report, audit findings are generally classified in one of three categories. The first category consists of material weaknesses, as defined above, and instances of material noncompliance. Noncompliance with applicable laws or rules is considered material when it is determined that the noncompliance could have a direct and material effect on the determination of financial statement amounts. The second category consists of significant deficiencies as defined above, instances of noncompliance with applicable laws or rules, or additional matters that should be addressed by management. The third category includes instances of major Federal program noncompliance or internal control deficiencies.

In the audit reports issued by our office, all audit findings are included within the body of the audit report. In the audit reports issued by the other independent CPAs, material weaknesses and significant deficiencies are identified within the body of the report, and additional matters are generally included in a separate management letter within the audit report.

## Financial Statement Material Weakness and Material Noncompliance Findings

The audit reports for four school districts (Bay, Manatee, Pinellas, St. Lucie) included findings that were considered to be material weaknesses and for one of the school districts (Manatee), the material weakness was also considered to be an instance of material noncompliance. This represents a decrease from the eight audit reports in the previous fiscal year that included material weaknesses, one of which was also considered to be material noncompliance. Pursuant to Section 1003.621(1)(a)3., Florida Statutes, a school district cited with a material weakness or instance of material noncompliance in a financial audit is ineligible for recognition as an academically high-performing school district. Academically high-performing school districts are granted more flexibility than other school districts in meeting the specific requirements of Florida statutes and State Board of Education rules.

For one school district (Manatee), a material noncompliance and material weakness finding addressed control deficiencies over the budgetary process and financial monitoring that contributed to a continual decline in financial condition. The school district did not appropriately monitor the budget to actual revenues and expenditures throughout the fiscal year to assist in identifying budget deficits, resulting in overestimating State revenues by $4.4 million and overspending seven general fund expenditure budget categories totaling $5.4 million. Also, for two school districts (Bay, St. Lucie), material weaknesses addressed procedural enhancements needed to ensure the accuracy and completeness of the financial statements. In addition, for one school district (Pinellas), a material weakness addressed needed enhancements in internal controls over the investment program to strengthen accountability.

## Financial Statement Significant Deficiency and Additional Matter Findings

The following is a summary of findings included in 61 school district audit reports that addressed control deficiencies; instances of noncompliance with applicable laws, rules, and regulations; or additional matters.

**Financial Condition**. Five school districts had findings addressing the school districts' financial condition, as follows:

- Manatee County School District's general fund total assigned and unassigned fund balance declined 109 percent from a deficit of $4.1 million at June 30, 2012, to a deficit of $8.6 million at June 30, 2013, or a decline of $4.5 million. At June 30, 2013, the District's financial condition ratio (See Exhibit 13 for calculation) was negative 2.80 percent. Also, the general fund balance may be further reduced if the District is required to repay questioned costs and contribute to the District's self-insurance program fund.
- Franklin County School District's general fund total assigned and unassigned fund balance declined 203 percent from $222,496 at June 30, 2012, to a deficit of $230,053, at June 30, 2013, or a decline of $452,549. At June 30, 2013, the District's financial condition ratio was negative 2.43 percent. Also, the FDOE required the District to restore $97,928 from the general fund, representing unencumbered State Capital Outlay appropriation balances and questioned costs. In addition, the ending general fund balance could be further reduced if the District is required to repay additional questioned costs related to the Capital Projects – Local Capital Improvement Fund.
- Columbia County School District's general fund total assigned and unassigned fund balance declined by 56 percent from $1,034,850 at June 30, 2012, to $453,761 at June 30, 2013, or a decline of $581,089. At June 30, 2013, the District's financial condition ratio was 0.70 percent. Also, the general fund balance may be further reduced by Federal questioned costs.
- For two other school districts (Clay and Martin), the general fund total assigned and unassigned fund balances declined by $4.7 million and $2.1 million, respectively, for the 2012-13 fiscal year. At June 30, 2013, the financial condition ratios of these school districts were 2.12 and 2.45 percent, respectively.

Under these circumstances, these school districts have less resources available for emergencies and unforeseen situations than other school districts and were at a higher risk of experiencing financial difficulty.

**Information Technology**. For 39 school districts, various control deficiencies in information technology (IT) were noted, as discussed below:

- **Access Controls**. Twenty-three school districts had various deficiencies in IT access controls. For example, at certain school districts, inappropriate or unnecessary access privileges existed or documentation of user access authorization was not properly maintained.
- **Data Loss Prevention**. Twenty-two school districts needed improvements in security controls over data loss prevention. Effective data loss prevention helps ensure protection from unauthorized disclosure through the establishment of procedures to identify and classify confidential or sensitive data, locate the storage and pathways of confidential or sensitive data, and monitor the use and transmission of confidential or sensitive data.
- **User Authentication.** Twenty-one school districts needed improvements in security controls related to user authentication for IT applications, such as password setting controls.
- **Logging/Monitoring**. Sixteen school districts had inadequate logging or monitoring of data and IT resources.
- **Security Incident Response Plans**. Nine school districts lacked or needed enhancements in written security incident response plans. Computer security incident response plans are established by management to ensure an appropriate, effective, and timely response to computer security incidents. These written plans typically detail responsibilities and procedures for identifying, logging, and analyzing security violations and include a centralized reporting structure, provision for designated staff to be trained in incident response, and notification of the affected parties.
- **Disaster Plans**. Eight school districts needed improvements in disaster preparedness and recovery plans or the plans needed to be tested.

- **Written Policies**. Eight school districts lacked written IT policies and procedures for certain important IT control functions.
- **Risk Assessment**. Six school districts had not developed written, comprehensive IT risk assessments. IT risk assessments, including the identification of risks and the evaluation of the likelihood of threats and the severity of threat impact, help support management's decisions in establishing cost-effective measures to mitigate risk and, where appropriate, formally accept residual risk.

**Record Keeping/Records Management**. In addition to the material weaknesses in financial reporting procedures discussed previously for Bay and St. Lucie County School Districts, the audit reports for 32 school districts included findings addressing the need for improvements in certain record keeping and financial records management procedures. For 22 school districts, procedures needed improvement to ensure the accuracy and completeness of the financial statements. While many of these findings related to required audit adjustments for the accuracy of the financial statements, other instances included needed improvements in procedures to properly report major governmental funds or discretely presented component units in the financial statements.

For four school districts, deficiencies were noted in accountability over transportation and food service department inventories. Also, three school districts reported unrestricted resources ranging from $211,000 to $768,000 in capital projects funds, without evidencing the specific intended use of these funds. For three school districts, controls over journal entries needed improvements. Other findings and recommendations addressed the lack of an actuarial valuation to support a reported liability, enhancements needed in budget process monitoring, the lack of monthly financial reports to the school board, and school board minute procedures.

**Cash and Investment Controls**. Audit reports of 21 school districts included findings addressing the need for enhancements in controls over cash or investments. For 12 school districts, controls over electronic funds transfers (EFTs) needed improvements. Deficiencies noted in EFTs included the lack of school board-approved policies and procedures prescribing EFT accounting and controls, contrary to State Board of Education (SBE) Rule 6A-1.0012, Florida Administrative Code (FAC); EFT agreements with banks that omitted critical information, such as the names and signatures of employees authorized to initiate EFTs; EFT agreements that authorized former employees to make EFTs; and EFT agreements or school district procedures that did not provide for appropriate separation of duties. Funds available at the 12 school districts for EFTs ranged from approximately $1 million to $1.67 billion.

Audit reports also noted that improvements in bank reconciliation procedures for nine school districts were needed. At four of these school districts, improvements in controls were needed over decentralized collections, such as food service collections and school extended day program fee collections. In addition to the material weakness discussed previously for Pinellas County School District, one other school district had findings addressing control deficiencies over investments.

**Capital Assets Management**. For eight school districts, findings addressed deficiencies in the accountability for long-lived assets, including land, improvements other than buildings, buildings and fixed equipment, and tangible personal property. For three school districts, deficiencies were noted in tangible personal property accountability procedures, such as inadequately documenting or updating property records for acquisitions and the lack of adequate physical inventory procedures. Three school districts did not adequately maintain detailed subsidiary records for capital assets. In addition, two school districts needed improvements in controls over land or building contracts.

**Expenditures/Purchasing**. For 17 school districts, findings addressed the need to improve controls over purchasing practices and operating expenditures. For 11 school districts, controls needed to be enhanced over contract monitoring procedures to ensure that contracts clearly describe the nature and timing of deliverables and payments are consistent with contract terms and conditions. For seven school districts, improvements were needed in

controls over purchasing cards, such as monitoring of purchasing card credit limits, reviews and approvals of purchasing card charges prior to payment, and procedures for cancelling terminated employees' card accounts. Four school districts needed improvements in controls over procuring enterprise resource planning (ERP) software. These school district records did not clearly demonstrate the ERP software purchases were made at the lowest price consistent with desired quality, and also controls over payments for the ERP software and related services were not adequate. Three school districts did not comply with competitive selection requirements of SBE Rule 6A-1.012, FAC, for various contractual service contracts.

**Payroll and Personnel**. For 38 school districts, findings addressed the need to improve controls over payroll and personnel, as summarized below:

- **Compensation**. For 23 school districts, school boards had not established the documented process to identify certain school district personnel entitled to differentiated pay using the factors prescribed in Section 1012.22(1)(c)4.b., Florida Statutes.
- **Monitoring of Bus Drivers.** For 16 school districts, controls over monitoring school bus drivers needed enhancements. The findings addressed the lack of documented review of bus driver history records to comply with requirements under SBE Rule 6A-3.0141(6), FAC.
- **Personnel Administration.** For 11 school districts, improvements were needed in controls over various areas of personnel administration. For these school districts, procedures for performing background screenings or rescreening for employees and contracted vendors with direct student contact were not adequate. Other control deficiencies noted included procedures needed for properly classifying an employee as an independent contractor and policies and procedures needed to identify and prevent potential conflicts of interest to comply with Section 112.313, Florida Statutes.
- **Payroll Processing**. For eight school districts, controls over payroll processing could be enhanced. At four of these school districts, auditors noted that procedural enhancements could be made to sufficiently and appropriately evidence employee work time supporting salary and benefits costs. Three school districts made compensation payments that were not consistent with the board-approved salary schedules. Other control deficiencies noted included the lack of detailed supervisory review and approval of salary payments; untimely contributions to the Florida Retirement System; and the need for a payroll reconciliation process to ensure accurate reporting of payroll information to the Internal Revenue Service.
- **Other**. For three school districts, findings addressed noncompliance with severance pay provisions of Section 215.425, Florida Statutes. For example, at two of these school districts, employment agreements for superintendents included severance pay provisions that allowed for severance pay that exceeded 20 weeks of salary, contrary to the law. In addition, for two of these school districts, improvements were needed in school district policies and procedures related to accrued leave time and calculations of terminal leave payments to ensure consistency with Florida law.

**Insurance**. For four school districts, findings addressed the need to improve controls over the administration of self-insurance plans. For two of these school districts, the self-insurance plan funds had net position deficits of $1.7 million and $1.2 million, respectively, at June 30, 2013, resulting in significantly less resources for emergencies and unforeseen situations of the self-insurance plans. One school district needed improvements in controls over monitoring a third party administrator of the self-insurance plan, such as periodic reviews by the school district of insurance claims paid by the third party administrator. One other school district did not obtain initial approval from the Florida Department of Financial Services, Office of Insurance Regulation, to operate its employee health self-insurance program. In addition, one school district lacked procedures on health insurance premium payments, such as reconciliations of health insurance billings to payroll records, to ensure that board contributions toward health insurance premium payments were only for eligible participants and that contribution amounts were consistent with board-approved salary schedules.

**Capital Construction and Related Expenditures**. Findings addressed the need to improve controls over construction and capital outlay expenditures for 38 school districts, as summarized below:

- **Construction Planning**. For 36 school districts, procedural enhancements were needed related to construction planning, alternative construction methods and maintenance techniques, and accountability for facilities and maintenance departments' accountability. These school districts needed to establish long-range facilities planning committees comprised of various stakeholders to periodically meet and assist school district facilities personnel in identifying long-range construction needs; develop written policies and procedures requiring periodic evaluations of alternative facilities construction methods and techniques for performing significant maintenance-related jobs; or develop additional goals and objectives for the facilities planning and maintenance departments to identify efficiency or cost effectiveness outcomes for department personnel.
- **Construction Monitoring.** For five school districts, improvements were needed in controls over construction management entity (CME) and subcontractor contracts.
- **Acquiring Professional Services**. Two school districts had findings related to procurement of CME services. One school district lacked policies and procedures over awarding of CME contracts below $2 million to prequalified CMEs. The other school district did not comply with Section 287.055, Florida Statutes, when procuring CME services.
- **Restricted Capital Outlay Resources**. Audit reports for ten school districts addressed control deficiencies over restricted capital outlay resources as summarized below:
  - For eight school districts, school district records did not evidence that the use of ad valorem tax levy proceeds or other capital outlay moneys were consistent with applicable statutory provisions. Contrary to Section 1011.71, Florida Statutes, expenditures of ad valorem tax levy proceeds ranging from $9,181 to $1.4 million were used for unallowable purposes, such as premiums for property and casualty insurance that exceeded statutory limit, non-enterprise resources software purchases, groundskeeping services or supplies, gasoline, library books, and certain unallowable salaries and benefits. For one of these school districts, we also questioned $4.1 million of expenditures of sales surtax proceeds used for copier leases that appeared to be contrary to Section 212.055(6), Florida Statutes.
  - Four school districts needed to resolve certain Public Education Capital Outlay or other capital outlay resource questioned costs, ranging from $30,777 to $728,815, which were subject to reversion to the State pursuant to Section 216.301(2), Florida Statutes.

**Adult General Education Classes**. Chapter 2012-118, Laws of Florida, Specific Appropriation 106, provides that each school district shall report enrollment for adult general education programs identified in Section 1004.02, Florida Statutes, in accordance with the FDOE instructional hours reporting procedures. The audit reports for 22 school districts included findings that the school districts misreported enrollment data. Since future funding may be based, in part, on enrollment data reported to the FDOE, it is important that such data be reported correctly to the FDOE.

**Virtual Instructional Program**. Audit reports for 11 school districts addressed the administration and oversight of the school district virtual instruction programs (VIPs) and compliance with selected provisions in Section 1002.45, Florida Statutes, as summarized below:

- **Written Policies and Procedures**. Ten school districts needed enhancements in developing and maintaining comprehensive, written VIP policies and procedures.
- **Provider Background Screenings**. For eight school districts, procedures for performing required background screenings for VIP provider employees and contracted personnel were not adequate.
- **Written Parental Notification**. Eight school districts lacked timely notification to parents regarding student opportunities to participate in a VIP.
- **Computing resources and Instructional Materials**. Seven school districts needed to enhance procedures for notifying VIP students and their parents about the availability of computing resources and that qualified VIP students are provided computing resources.

- **Provider Contracts**. For six school districts, VIP provider contracts were deficient in that contracts did not include all provisions required by State law.
- **Student Compulsory Attendance**. For five school districts, procedures did not always require written documented verification that VIP students complied with compulsory attendance requirements.
- **VIP Options**. Four school districts could enhance their procedures to ensure that the required number of VIP options is offered.
- **Other**. Two school districts needed to enhance procedures to ensure that residual VIP funds are properly restricted for use as required by State law. Two school districts did not report certain contract and student cost information to the FDOE.

**Rebates**. Certain Federal and State resources are typically restricted by Federal or State law and rebates generated by expenditures of those funds may be subject to the same restrictions. Six school districts did not allocate e-Payable or purchasing card program rebates generated by restricted resources to appropriate school district funds. In these circumstances, there is an increased risk that rebates generated by restricted sources may be used for purposes inconsistent with the restrictions on these resources.

**Workforce Development Funds**. For five school districts, workforce development funds were sometimes used for purposes contrary to Chapter 2012-118, Laws of Florida, or school districts did not have a spending plan for the use of unspent funds.

**Miscellaneous Findings**. In addition to those findings described above, audit findings addressing various other matters, although not predominant, were included in the individual school district audit reports. These matters included, for example, deficiencies in monitoring of motor vehicle maintenance and fuel usages; the insufficiency of formal fraud policies; the need for improved controls over social security numbers to ensure compliance with Section 119.071(5)(a), Florida Statutes; noncompliance with educational facility safety standards; the need for enhancement over food service operations; deficiencies in monitoring of insurance for charter schools; and control deficiencies over school internal funds collections.

## Federal Awards Findings

For 32 school districts, findings addressed major Federal program noncompliance and control deficiencies. Major Federal program material noncompliance and material internal control weaknesses were noted at ten school districts (Calhoun, Clay, Columbia, DeSoto, Duval, Gadsden, Manatee, Monroe, Putnam, Union). These material Federal findings addressed noncompliance with the Federal compliance requirements of Allowable Costs/Cost Principles; Matching, Level of Effort, and Earmarking; and Eligibility; and related to major programs including the Special Education; Title I; Improving Teacher Quality; Teacher Incentive Fund; and Promoting Student Achievement programs. Other Federal findings that were not considered material noncompliance addressed various Federal compliance requirements for the Child Nutrition Cluster; Special Education; Race-to-the-Top; Title I; Pell Grant; School Improvement Grants, and other programs. As previously discussed in the **American Recovery and Reimbursement Act and Other Federal Funding** section of this report, ARRA mandates special accountability and transparency requirements regarding Federal economic stimulus funds, which requires additional record keeping for school districts and expanded audit procedures for auditors.

## OTHER MATTERS OF INTEREST

### Repeated Findings From Prior Fiscal Years

Section 218.39(8), Florida Statutes, requires the Auditor General to notify the Legislative Auditing committee of district school boards that failed to take full corrective action in response to one or more recommendations included in the two preceding financial audit reports. Of the 504 findings included in the 2012-13 fiscal year audit reports reviewed, 114 (23 percent) were repeated from previous audit reports for at least two consecutive fiscal years. The percentage of repeated findings indicates that some school districts did not take action to timely correct prior year deficiencies or noncompliance.

Pursuant to Section 218.39, Florida Statutes, on September 2, 2014, we notified the Legislative Auditing Committee of 43 district school boards that failed to take full corrective action in response to one or more recommendations included in the two preceding audit reports.

### School District Budget Transparency

Section 1011.035, Florida Statutes, requires each district school board to post on its Web site a plain language version of each proposed, tentative, and official budget describing each budget item in easily understandable terms. The statute includes a list of items recommended for inclusion on the Web sites, such as budget hearing information, contracts with teachers' unions and noninstructional staff, and contracts with vendors exceeding $35,000. This statutory requirement enables taxpayers, parents, and education advocates to obtain school district budget and related information in a manner simply explained and easily understandable. Budgetary transparency leads to more responsible spending, more citizen involvement, and improved accountability.

Pursuant to Section 11.45(7)(i), Florida Statutes, on July 14, 2014, we notified the President of the Senate, the Speaker of the House of Representatives, and the Chief Financial Officer of the Florida Department of Financial Services that five school districts (Columbia, Franklin, Gilchrist, Hamilton, Jefferson) were reported for noncompliance with Section 1011.035(2), Florida Statutes.

## OBJECTIVES, SCOPE, AND METHODOLOGY

The objective of this project was to identify significant financial trends and findings based on our review of school district audit reports.

The scope of this project included a review of the audit reports for the 47 school districts audited by our office and the 20 school districts audited by other independent CPAs for the fiscal year ended June 30, 2013.

Our audit methodology included a review of applicable audit reports and a compilation of significant financial trends and findings. We conducted this review in accordance with applicable generally accepted government auditing standards. We believe that the procedures performed provide a reasonable basis for the summaries of significant financial trends and findings included in this report.

## AUTHORITY

Pursuant to the provisions of Section 11.45(7)(f), Florida Statutes, I have directed that this report be prepared to present the summary of financial trends and significant findings identified in district school board audit reports for the fiscal year ended June 30, 2013.

David W. Martin, CPA
Auditor General