

**Sachem Central School District**  
**Independent Accountant's Report On**  
**Applying Agreed-Upon Procedures**  
March 10, 2013

**INDEPENDENT ACCOUNTANT'S REPORT ON  
APPLYING AGREED-UPON PROCEDURES**

Board of Education and Audit Committee  
Sachem Central School District  
Holbrook, New York

We have performed the procedures described in the following pages, which were agreed to by the Sachem Central School District (District), solely to review the financial projections for the 2012-2013 fiscal year and to review the preliminary 2013-2014 budget.

The District's management is responsible for administering this area.

This engagement to apply agreed-upon procedures was performed in accordance with attestation standards established by the American Institute of Certified Public Accountants. The sufficiency of the procedures is solely the responsibility of the District. Consequently, we make no representation regarding the sufficiency of the procedures either for the purpose for which this report has been requested or for any other purpose.

Our procedures and findings are described in the following pages.

We were not engaged to and did not conduct an audit, the objective of which would be the expression of an opinion on the District's financial projections and budget. Accordingly, we do not express such an opinion. Had we performed additional procedures, other matters might have come to our attention that would have been reported to you.

We would like to express our appreciation for the cooperation and assistance that we received from the District's administration and other employees during our engagement.

This report is intended solely for the information and use of the District and is not intended to be and should not be used by those who have not agreed to the procedures and taken responsibility for the sufficiency of the procedures for their purpose.

*Cullen & Danowski, LLP*  
March 10, 2013

**SACHEM CENTRAL SCHOOL DISTRICT**  
**Report on Applying Agreed-Upon Procedures**  
For the Period Ended March 10, 2013

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**Introduction:**

This report is organized as follows:

- Background information
- Summary of the engagement
- Procedures performed during our detailed testwork
- Findings as a result of our review
- Recommendations to further strengthen internal controls or improve operational efficiency.

Some of the recommendations may require a reassignment of personnel duties within the District and/or a monetary investment. However, any enhancement of controls should be done after a careful cost-benefit analysis.

**SACHEM CENTRAL DISTRICT**  
**Report on Applying Agreed-Upon Procedures (Continued)**  
For the Period Ended March 10, 2013

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**Background:**

We have been engaged to review the 2012-2013 financial projections and the 2013-2014 proposed budget for the Sachem Central School District (Sachem). The District has operated at a substantial deficit over the past several years, which has reduced the General Fund Total Fund Balance from \$41M as of June 30, 2010, to a projected balance of \$14M as of June 30, 2013. Based on continued reductions of fund balance available to appropriate, restrictions on state aid and increases in mandated costs the District will need to reduce expenditures and/or increase taxes significantly to balance the budget for the 2013-2014 fiscal year. This may substantially impact the programs provided by the District.

Sachem is one of the largest school districts in New York State with annual expenditures near \$300M. As with any budget, the assumptions and calculations used to develop the budget can have a significant impact on the budget. As part of our review, we noted that the assumptions used to develop the budget are reasonable. It should be pointed out that with a total budget of \$300M, even a 1% variance from the budget would result in a \$3M variance.

Sachem has provided a significant amount of budget and actual cost information on the Sachem website. Audited financial reports are also included on the website. This indicates a level of transparency, which helps ensure that the Board of Education and the voting public are well informed.

The General Fund Budget consists of three major items: revenues, expenditures and fund balance appropriated to balance the budget. The budget for the year must be in balance based on this formula:

$$\text{Revenue} + \text{Appropriated Fund Balance} = \text{Expenditures}$$

By this definition, when a district budgets any Appropriated Fund Balance (either unassigned fund balance or reserves) to balance the budget, the inherent meaning is that the district is planning to operate at a deficit. In other words, the district is planning to spend more than it is receiving in revenue. It is using Fund Balance.

Districts (and Sachem is no different) have historically not spent the entire amount of the expenditure budget. This is due to several factors:

- The budget assumptions are conservative, and the actual results are less than the budget.
- Actual expenditures are less than preliminary estimates due to actual changes in conditions.
- The district does a good job of controlling costs and limits expenditures.

The difference between the budgeted expenditures and actual expenditures is a variance and the difference will impact Total Fund Balance.

Similarly, districts have historically, conservatively budgeted revenue. For example, state aid might be conservatively budgeted so that actual revenue exceeds the budget.

The annual financial results of the District's General Fund for the past 3 years along with the current projection for 2012-2013 and the proposed budget for 2013-2014 are as follows: (All amounts are in \$ millions)

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For the Period Ended March 10, 2013

	2009-2010 Actual	2010-2011 Actual	2011-2012 Actual	2012-2013 Projected	2013-2014 Budget
Revenue	271	265	262	274	297
Expenditures	266	270	277	286	304
Surplus(Deficit)	5	(5)	(15)	(12)	(7)

Please note that the amounts in the 2012-2013 projected column are the current projections provided by the District. We believe this projection is substantially accurate.

As you can see, from the 3 year period from 2010-2011 through the projection for the current 2012-2013 year, the District will have operated at a combined deficit of \$32M (\$5+\$15+\$12). (During the past three years the District has transferred approximately \$5M from other funds into the General Fund). During this period the District has maintained educational programs and limited tax increases, but as a result of operating at a deficit the District no longer has the funds available to appropriate as much fund balance for the 2013-2014 as had been appropriated and used over the past several years.

It is important to note that while the Total Fund Balance will be approximately \$14M at June 30, 2014, approximately \$6M of this Total Fund Balance is contained in "Reserves", which can only be utilized for certain purposes and may not be available in the short or medium term to help balance the budget.

In the findings section below we will analyze projected and budgeted revenues and then analyze projected and budgeted expenditures and provide an analysis of the total Fund Balance of the District.

**Summary:**

The District's preliminary budget is substantially accurate in all material respects. As is consistent with most school districts at this point of the annual budget process, it is a "roll-over" budget and to date does not consider potential areas to reduce costs.

Later, we will identify several areas in which we believe the budget could be adjusted. However, any adjustment to the budget without operational changes will impact the amount of spending variance experienced in the 2013-2014 year and must be considered in relation to the fund balance appropriated. Over the past 3 years the District has utilized the majority of its available fund balance and is in danger of having little or no fund balance to account for unforeseen issues.

The obvious concern is the amount of property taxes contained in the budget. For the past 3 years the District has appropriated very significant amounts of the available fund balance to maintain programs and limit the tax increases. However since the 2009-2010 school year (the last year that the District operated at a surplus), state aid has been reduced by \$12M and benefit costs have increased by \$24M. As a result, the District needs to plan for some combination of reduced costs and/or increased property taxes.

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**Report on Applying Agreed-Upon Procedures (Continued)**  
For the Period Ended March 10, 2013

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**Procedures:**

**Detailed Internal Control Testing**

We applied the agreed-upon procedures, which the Board of Education (Board) and the management of the District specified, listed below, to review the District's documentation related to the fiscal 2013-2014 annual budget.

**Detail Procedures**

- Reviewed Board policies and District procedures in detail related to budget preparation.
- Interviewed Business Office personnel and administrators to determine significant assumptions used to develop the budget and to discuss levels and risk associated with budgeted amounts.
- Reviewed the current financial projection for the 2012-2013 fiscal year. We analyzed assumptions made and traced amounts to supporting documentation as appropriate.
- Reviewed the most current budget for the 2013-2014 school year. Analyzed assumptions made in development of the budget for reasonableness. On a test basis, traced amounts to supporting documents. Prepared a listing of possible budget adjustments for consideration by the Board of Education.
- Reviewed other budget related presentations as prepared by the District. Traced amounts to supporting documentation as appropriate and considered the completeness and transparency of the presentation.

**Findings:**

***Revenue: Total Budget for Revenue is \$297.3M***

For our purposes, the term "revenue" refers to revenue from outside sources (it does not include appropriated fund balance or transfers from other funds). Revenues can be classified into three categories:

- State Aid – State Aid is budgeted to be \$105M. This is based on the Governor's proposal which historically has been increased by the legislature. Unfortunately, on March 1, the New York State Education Department advised that due to a technical adjustment of interest rates used to calculate Building Aid that the aid to Sachem for 2013-2014 would be reduced by \$1.5M. This has not been considered in the budget we reviewed. However, considering that historically there have been increases to the state aid budget from the Governor's budget proposal to the actual budget, and there has been some effort for increased state aid for 2013-2014, we believe that for now, the budget appears to be substantially accurate.
- Other – Other is budgeted at a total of \$5M. This is made up of various relatively small amounts. All of these items appear to be budgeted appropriately.
- Property Tax – Property Tax is budgeted at a total of \$186M. This amount is based on the result of the expenditure budget, less all other revenue and based on using appropriated fund balance of \$7M. This will result in a 16.5% increase from the prior year and the public vote will require a 60% favorable vote for this to be in effect.

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***Expenditures: Total Expenditure Budget is \$305M***

- General Support – General Support is budgeted at a total of \$27M and appears to be budgeted appropriately. There is little change from prior years, and the majority of the costs are salary and we performed detail testing of the proposed 2013-2014 salary budget without exception.
- Instruction – Instruction is budgeted at a total of \$162M and appears to be budgeted appropriately. The current year's budget is \$158M and the projection for the current year reflects a small positive variance (projected actual costs will be somewhat below budget in 2012-2013). As in general support, the majority of costs are salaries and we performed detailed testing of the proposed salaries without any exceptions.
- Pupil Transportation – Pupil Transportation is budgeted at a total of \$21M. This is 10.7% higher than the actual transportation costs in the 2011-2012 fiscal year. The District has reviewed the situation, and believes it would not be productive to open the contract to bid at this time.
- Community Services – Community Services are budgeted at a total of \$1M and appears to be budgeted appropriately. It is our understanding that these costs are supported by charges for services.
- Employee Benefits – Employee Benefits are budgeted at a total of \$73M. The more significant accounts are outlined below:
  - Employees Retirement System (ERS) – ERS is budgeted at a total of \$4M and appears to be budgeted appropriately. ERS expenditures are budgeted to remain relatively flat from 2012-2013 projected actual expenses since the District has elected to amortize certain costs.
  - Teachers Retirement System (TRS) – TRS is budgeted at a total of \$21M and appears to be budgeted appropriately. TRS rates will increase substantially in 2013-2014 (from 11.84 % to 16.25%, for a total change of 37.25%) and this is reflected in the budget, which is increasing from \$15M in 2012-2013 to \$21M in 2013-2014.
  - Social Security – Social Security is budgeted at a total of \$12M and appears to be budgeted appropriately.
  - Workers' Compensation – Workers' Compensation is budgeted at a total of \$2M and appears to be budgeted appropriately. Actual costs from 2009-2010 to projected 2012-2013 have been approximately \$2M per year.
  - Unemployment Insurance – Unemployment Insurance is budgeted at a total of \$1.45M. It appears that the actual 2012-2013 costs for unemployment insurance will be below the budget by approximately \$1M dollars. Based on the 2013-2014 budget assumption, of limited layoffs occurring, and the anticipated budget surplus for the 2012-13 fiscal year, the 2013-2014 budget appears to be overstated by \$1M.
  - Medical Insurance – Medical Insurance is budgeted at a total of \$32M and appears to be budgeted appropriately. The budget includes an increase in January 2014 at an estimate of 7.75%.
- Debt Service – Debt Service is budgeted at a total of \$21M and appears to be budgeted appropriately.

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**Appropriated Fund Balance: Planned use of \$7.3M of fund balance**

As noted earlier in this report, school districts can appropriate all or some of the year end fund balance to reduce the tax levy. When a district appropriates fund balance, it is implicitly acknowledging that the district plans to operate at a deficit. In other words, actual expenditures are budgeted to exceed actual revenue and the plan is to utilize fund balance to balance the budget.

As of June 30, 2013, the current projection for fund balance can be estimated as follows (all amounts are in \$ millions):

Total General Fund Fund Balance July 1, 2012		24.4
Budget Revenue	273.8	
Current Variance	<u>0.0</u>	
Current Forecast		273.8
Budget Expenditure	291.4	
Current Variance	<u>-5.1</u>	
Current Forecast		<u>286.2</u>
Forecasted Operating Surplus (Deficit)		-12.5
Planned Surplus (Deficit)	-17.6	
Current Variance	<u>5.1</u>	
Forecasted Operating Surplus (Deficit)	-12.5	
Transfer Unused Funds from Capital Fund to General Fund		<u>2.0</u>
Projected Fund Balance June 30, 2013		<u>13.9</u>
The Projected Fund Balance at June 30, 2013 is comprised of:		
Restricted for workers' compensation		1.6
Restricted for employee benefit accrued liability		4.4
Unassigned		<u>8.0</u>
Projected Fund Balance June 30, 2013		<u>13.9</u>

Fund balance is comprised of two major categories. The first is unassigned funds and the other is reserved funds. Reserve funds can only be used under certain circumstances as allowed by law. Unassigned fund balance can be appropriated to reduce taxes related to any expenditure. For the 2013-2014 budget, the District intends to appropriate \$0.3M from the workers' compensation reserves, and \$7M of the unassigned balance. As you can see, appropriating \$7M of the \$8M unassigned fund balance means that the District is using substantially all of the unassigned balance. The effect is that unless the District has a favorable budget variance in 2013-2014, there will be very limited funds left in fund balance, which could be used to reduce the 2014-2015 tax levy. In other words for the 2014-2015 fiscal year the District will need to either reduce costs or increase revenues to make up for the loss of appropriated fund balance.

**Subsequent Events**

Subsequent to the date of this report the Board of Education and administration worked to address the issues raised. There were several significant adjustments to the budget, and on April 17, 2013, the Board voted to adapt a tax increase of 7.49%. Cullen & Danowski provided no services related to these adjustments.