

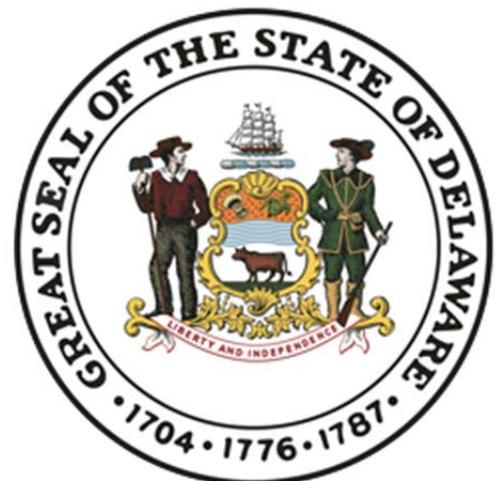
**State of Delaware
Office of Auditor of Accounts**

**School District Local Tax Collection and
Debt Service Management
Agreed-Upon Procedures Report**

Fiscal Year Ended June 30, 2011

**Fieldwork End Date: March 7, 2013
Issuance Date: March 8, 2013**

R. Thomas Wagner, Jr., CFE, CGFM, CICA
Auditor of Accounts



Background

This engagement focuses on whether Delaware school districts deposit their tax revenues as advertised to the taxpayers. We also look at how school districts manage the debt used to pay for school construction, focusing on whether the debt is paid according to the bond amortization schedule and if the school district has a reasonable amount of funds set aside to meet their bond obligations. All of these activities, including the collection and use of local tax receipts, are State funds and activities, as reflected in the State's Comprehensive Annual Financial Report as primary government.

Debt Service Management¹

Once approved by a taxpayer referendum, the General Assembly will approve a bond issuance to cover a school's construction cost. The school district is responsible for using county tax receipts to repay the local share of the bond, which is typically between 20% and 40%. The remainder of the bond is covered by other sources of funds. Most school districts have payment obligations for multiple debt service bonds that have accumulated over recent decades.

The debt service appropriation must be carefully monitored to ensure that the school has sufficient tax receipts to cover its debt service obligations without accruing an excessive fund balance. This analysis is a good indicator of whether the district's tax rates need adjustment. A sufficient balance means that the district has adequate funds to cover the debt service principal and interest payments for the first four months of the fiscal year, which is the Department of Education's recommendation. This four month window ensures that school districts can meet their debt obligations while waiting for the bulk of their county tax receipts that arrive in the fall. The current Attorney General's Opinion suggests that an excessive balance is greater than 110% of the annual debt service principal and interest payments.

Local Tax Collections

On a monthly basis, the school districts receive a lump sum amount of revenues collected from the three Delaware counties through real estate and capitation taxes.² These revenues are commonly referred to as local funds.

To receive local funds, each school district's local school board approves and sends an annual tax warrant to their respective county, which authorizes the levy and collection of taxes. The tax warrant shows a separate tax rate for a combination of the following categories:

- **Current Expense:** costs associated with the general operation of the district as well as specific programs approved by voter referenda. This tax rate can only be increased with taxpayer approval through future referenda.
- **Debt Service:** the principal and interest payments on capital improvement bonds used to pay for new construction, additions, and renovations. Voters must authorize the issue of bonds through a referendum. Thereafter, the district's local school board annually sets the debt service tax rate.
- **Tuition:** the cost of providing in- and out-of-district placements for students with special educational needs. The local school board sets this tax rate annually based upon anticipated needs of the student body.
- **Match:** provides a local match to State appropriations where required or allowed by law. According to the Fiscal Year 2011 State Budget Bill, examples of matching programs include

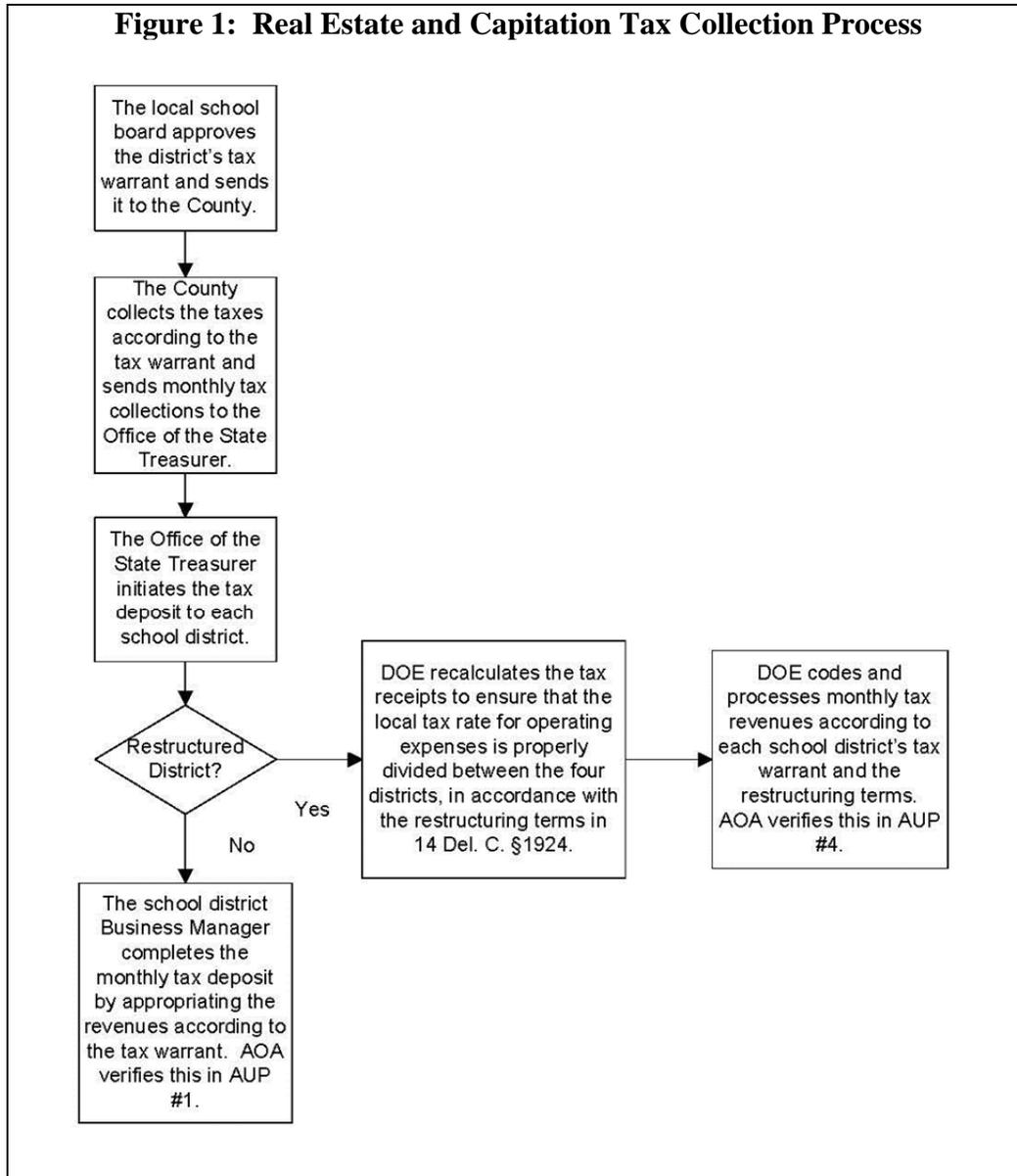
¹ Debt Service is the series of principal and interest payments required on debt over a given time period.

² Capitation taxes are collected based on the number of adult residents in a school district.

minor capital improvements, technology maintenance, reading resource teachers, mathematic resource teachers, and the extra time program. Although the State no longer provides its portion of most match funds, school districts are still permitted to collect taxes for their local portion.

The Department of Education (DOE) is responsible for appropriating tax revenues to the four restructured districts: Brandywine, Christina, Colonial, and Red Clay.³ Although these four districts operate separately, they all share a current expense tax rate as part of the restructuring plan. Each districts' student enrollment unit count is used as the basis for dividing the current expense tax revenue.

The tax collection process is summarized in Figure 1 below.



³ These four districts were formerly the New Castle County School District but were divided in 1981 in accordance with 14 Del. C. §1924. Each of the four districts shares a local tax rate for the current expense appropriation, which is distributed by DOE to ensure the funds are disbursed objectively.

The following statement was constructed as a result of the procedures performed:

Statement of School District Funds

School District	Total Tax Receipts ¹	Debt Service Expenditures ²	June 30, 2011
			Debt Service Reserve Fund Balance ³
Appoquinmink	\$ 25,877,060	\$ 6,088,882	\$ 3,418,281
Brandywine	61,370,248	8,637,731	2,812,497
Caesar Rodney	8,735,159	1,643,262	740,158
Cape Henlopen	24,443,221	3,722,906	3,141,371
Capital	20,910,757	3,581,682	3,712,856
Christina	88,464,670	8,620,813	4,777,888
Colonial	40,587,835	5,930,436	3,654,546
Delmar	1,459,913	354,844	160,248
Indian River	34,440,898	4,773,331	2,352,794
Lake Forest	4,913,873	667,509	169,936
Laurel	3,068,960	141,463	41,807
Milford	8,142,879	1,954,808	997,205
NCC Vo-Tech	25,252,476	1,529,367	719,353
Polytech	4,297,592	241,942	151,379
Red Clay	81,578,255	7,649,467	3,562,142
Seaford	6,603,457	701,319	437,348
Smyrna	7,782,559	2,565,322	2,247,210
Sussex Technical	7,872,360	720,106	366,960
Woodbridge	3,891,431	548,076	192,355
Totals	\$ 459,693,603	\$ 60,073,266	\$ 33,656,334

¹ The figures represented in the Tax Receipts column are the local tax revenues that each district received from the counties for the fiscal year.

² The debt service expenditures represent the principal and interest payments made on each school district's long-term debt obligations.

³ The debt service reserve balance represents the prior year debt service reserve balance plus the debt service tax receipts, and is reduced by the debt service expenditures for the fiscal year.

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STATE OF DELAWARE
OFFICE OF AUDITOR OF ACCOUNTS

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Independent Accountant's Report
on Applying Agreed-Upon Procedures

To the Specified Users of the Report:

The Honorable Mark Murphy
Secretary
Department of Education
401 Federal Street, Suite 2
Dover, DE 19901

Superintendents, All School Districts

We have performed the procedures described below, which were agreed to by you, solely to assist the specified parties in evaluating compliance with the applicable sections of the Delaware Code and the legal opinions listed after each procedure below. Management of each school district is responsible for their school district's compliance with those requirements for the period July 1, 2010 through June 30, 2011 (Fiscal Year 2011).

This agreed-upon procedures engagement was performed in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States, the attestation standards established by the American Institute of Certified Public Accountants, and *Quality Standards for Investigations*, issued by the President's Council on Integrity and Efficiency. The sufficiency of these procedures is solely the responsibility of the Department of Education (DOE). Consequently, we make no representation regarding the sufficiency of the procedures described below either for the purpose for which this report has been requested or for any other purpose.

A description of the procedures and any associated findings are as follows:

Procedure 1: For all districts, except for the four restructured districts within New Castle County, recalculated the real estate tax allocations to verify whether tax receipts were properly recorded in First State Financials (FSF). [14 Del. C. §1917 (a) and (b), 14 Del. C., § 2118 (d), and 14 Del. C., § 2119]

For each school district, we used the Fiscal Year 2011 tax warrant and the tax revenues reported by each County to calculate the amount of tax receipts that should have been deposited into each appropriation. We then compared this number to the amounts reported in FSF, taking any payments in lieu of taxes (e.g. Senior Property Tax Credit) into consideration. Any significant variances were researched further. We also reconciled the tax receipts to the local tax revenue received by the school districts as reported in the State's Comprehensive Annual Financial Report.

Results: The following school districts coded tax revenues that were levied as minor capital improvements into various match funds:

- Appoquinimink School District
- Capital School District

Both school districts explained that, although the proceeds were intended for both minor capital improvements and other match taxes, the tax warrants were simply mislabeled as minor capital improvements. Nevertheless, the tax warrant should be accurate and reflective of the school district's intended use.

In addition, the Laurel school district could not provide AOA with an official, signed Fiscal Year 2011 tax warrant.

Procedure 2: Verified that the debt service expenditures (principal and interest payments) were proper and in accordance with the amortization schedule provided by the Office of the State Treasurer. [14 Del. C., § 2108]

We obtained the school districts' amortization schedules from the Office of the State Treasurer and compared the actual principal and interest expenditures per FSF to determine if they agreed.

Results: One Lake Forest school district payment was \$27 less than the amount in the amortization schedule. The school district's 16 bond principal and interest payments totaled \$667,509 in Fiscal Year 2011.

Procedure 3: Analyzed the June 30, 2011 debt service reserve balance to determine if the balance is sufficient without being excessive.⁴ [Attorney General's Opinions 1W-024 and 89-I017]

We compared each school district's debt service reserve fund balance as of June 30, 2011, to the total required debt service payments for July 1, 2011 through October 31, 2011, to determine whether the debt service reserve was sufficient. If the balance was sufficient, it was compared to 110% of the debt service obligations from July 1, 2011 through June 30, 2012 (Fiscal Year 2012), to determine whether the balance was excessive. The Statement of School District Funds in the Background section lists each school district's debt service reserve fund balance.

Results: Our procedures disclosed the following:

⁴ Per Attorney General Opinion 1W-024, an excessive balance is defined as 110 % of total principal and interest payments for the following fiscal year. A minimum 4-month reserve is recommended by the Department of Education for a sufficient balance, according to Attorney General Opinion 89-I017.

**School District Local Tax Collection and Debt Service
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The five school districts listed in Table 1 below did not have a debt service reserve sufficient to cover the first four months of their Fiscal Year 2012 debt service obligations. They are as follows:

School District	Ending Fund Balance	Recommended Reserve Amount	Surplus/(Deficit)
Brandywine	2,812,497	4,177,463	(1,364,966)
Caesar Rodney	740,158	1,075,479	(335,321)
Lake Forest	169,936	268,275	(98,339)
New Castle County Vo Tech	719,353	798,557	(79,204)
Red Clay	3,562,142	3,601,289	(39,147)

All districts were aware of the insufficient balance. Three of the districts met their debt service obligations by borrowing funds from another appropriation in Fiscal Year 2012. The other two districts used subsequent tax revenues to meet obligations as they came due.

Procedure 4: In accordance with 14 Del. C. §1924, reviewed DOE’s Fiscal Year 2011 calculations to verify proper allocation of tax revenues for the four restructured districts within New Castle County. [14 Del. C. §1917 (a) and (b), 14 Del. C. §1924, 14 Del. C., § 2118 (d), and 14 Del. C., § 2119]

For each restructured school district, we used the Fiscal Year 2011 tax warrant and the tax revenues reported by each County to verify DOE’s calculation of the amount of tax receipts that were deposited into each appropriation. We then compared DOE’s revenue allocations to the amounts received by each school district in FSF, taking any payments in lieu of taxes into consideration.

Results: No exceptions were found as a result of applying the procedures above.

This report is intended solely for the information and use of the Department of Education and the management of school districts. It is not intended to be, and should not be, used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited. This report, as required by statute, was provided to the Office of the Governor, Office of the Controller General, Office of the Attorney General, and Office of Management and Budget.

We were not engaged to, and did not conduct an audit, the objective of which would be the expression of an opinion on compliance with specified laws. 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.

R. Thomas Wagner, Jr., CFE, CGFM, CICA
Auditor of Accounts

March 8, 2013