ST. LOUIS PUBLIC SCHOOL DISTRICT
REVIEW OF FINANCIAL CONDITION AND PROJECTIONS

From The Office Of State Auditor
Claire McCaskill

Report No. 2004-09
February 2, 2004
www.auditor.mo.gov

AUDIT REPORT

YELLOW SHEET

Office Of The
State Auditor Of Missouri
Claire McCaskill

February 2004

St. Louis Public School District is facing a severe budget deficit for fiscal year 2004 and must make additional cuts to balance its budget

This audit is the first of two reports related to the St. Louis Public School District's financial viability. For this report, auditors reviewed the factors causing the district's current financial hardship. Prior to the audit, the district underwent a leadership change from a traditional superintendent to a management consultant team. The management team took over the district after a May 2003 school board vote. Shortly thereafter, district officials learned more about the severity of the cuts in state funding to the district.

Audit sorts out differing budget projections

Before the prior Superintendent left the district, he and his staff projected the district would suffer a budget deficit of $55 million as of June 30, 2004 (if no cuts were made to the budget). They prepared the projection before the end of fiscal year 2003. In July 2003, the management team conducted their own analysis and figured a $73 million deficit as of June 30, 2004 (if no cuts were made to the budget). The management team prepared this projection using similar methods as the prior Superintendent, but were able to use updated information from the Department of Elementary and Secondary Education and end of the fiscal year figures. Auditors found the $73 million projection more accurate of the district's actual financial status, and detailed the differences in the two figures in the report. (See page 6)

Cash flow deficiencies

In addition to the year-end deficit, the management team also evaluated the district's financial position by looking at cash flow projections. The district has experienced cash flow deficiencies since early fiscal year 2003, but no cash flow projections had been performed. The prior administration covered cash flow shortfalls with restricted funds. The management team projected a cash flow shortfall of $99 million in December 2003 (if no cuts were made in the budget). Although this cash flow shortfall is not comparable to the year-end budget deficit, auditors found this cash flow shortfall projection accurate and an issue the district should monitor. After reducing some expenditures and receiving local property taxes earlier, the actual cash flow shortfall in December came to $37.6 million, which the district covered using desegregation funds. (See page 8)

State funding decrease and limited expense reductions led to deficits

Significant decreases in state funding, inadequate budgetary procedures and limited reductions in expenditures all led to the district's current financial difficulties. The substantial decrease in state funding was the most significant factor in the district's financial decline. Prior administration officials said they could not have anticipated this sharp decrease in state funding, and contractual obligations made quick, radical cost cuts impossible. The district has operated with expenditures exceeding revenues since fiscal year 2002, auditors found. In addition, budgetary procedures were insufficient to monitor the budget. For example, had the district stayed within their original budgeted expenditures for fiscal year 2003, the year-end balance would have been positive, even with the state cuts. Instead, the unrestricted operating funds reserve dropped from $55.4 million in June 2001 to a $12.3 million deficit in June 2003, which made the district "financially stressed," according to state law. (See page 9 and 10)

Current budget has deficit, violates state law

The budget approved in August 2003 included a projected deficit of $14.7 million at June 30, 2004, which violated state laws prohibiting unbalanced budgets. This budget is a projection and will be revised by the management team to more accurately reflect actual activity and project the year-end deficit. (See page 11)

The State Auditor's Office is continuing to audit the operations of the district and any findings and recommendations will be included in a subsequent report.

ST. LOUIS PUBLIC SCHOOL DISTRICT

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STATE AUDITOR'S REPORT

CLAIRE C. McCASKILL
Missouri State Auditor

Honorable Bob Holden, Governor
and
Board of Education of St. Louis Public School District
801 Locust Street
St. Louis, Missouri

The State Auditor was requested by the Honorable Bob Holden, Governor, under Section 26.060, RSMo 2000, to audit the St. Louis Public School District. The district has engaged Rubin, Brown, Gornstein and Company LLP (RBG), Certified Public Accountants (CPAs), to audit the district's financial statements for the year ended June 30, 2003. The scope of our audit of the district included, but was not necessarily limited to, the year ended June 30, 2003. The objectives of this audit were to:

1. Review the fiscal year 2003 financial information and the fiscal year 2004 budget projections for the general operating funds.

2. Identify any factors that may have led to the district's declining financial condition in the general operating funds.

To accomplish these objectives, we reviewed minutes of meetings, written policies, financial records, and other pertinent documents; and interviewed various personnel of the district including members of the School Board. Our methodology included, but was not necessarily limited to, the following:

1. We gained an understanding of the methodologies and assumptions used during the development of budget projections. We also verified applicable data from which various assumptions were based.

2. We reviewed detailed historical budget and actual financial data for fiscal years 2001 through 2003. This data was reviewed analytically to identify and explain significant fluctuations in revenues and expenditures.

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Our audit was conducted in accordance with applicable standards contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and included such procedures as we considered necessary in the circumstances.

The accompanying report presents information obtained during our audit regarding the financial condition of the district and the development of budget projections. While this report contains no specific recommendations to the Board at this time, district operations are still being audited and any findings and recommendations will be included in a subsequent report.

Appendixes I and II are included for informational purposes. This information was obtained from the district's accounting records and Comprehensive Annual Financial Reports and was not subjected to the procedures applied in the audit of the district. Appendix III includes responses obtained from the district's current and prior management.

Claire McCaskill
State Auditor

December 5, 2003 (fieldwork completion date)

The following auditors participated in the preparation of this report:

Director of Audits:	Thomas J. Kremer, CPA
Audit Manager:	Alice M. Fast, CPA
In-Charge Auditor:	Robert E. Showers, CPA
Audit Staff:	A. Dailey
	Kenneth M. Allman

RESULTS AND COMMENTS

ST. LOUIS PUBLIC SCHOOL DISTRICT
RESULTS AND COMMENTS

Results

Budget projections developed by the St. Louis Public School District's management consultant firm (the management team) for fiscal year 2004 were prepared using a methodology consistent with prior years' budgets. The assumptions used appear reasonable based on the information available to the management team at the time the projections were prepared. The Prior Superintendent's projections were prepared prior to the end of the fiscal year and were less accurate. The Prior Superintendent projected a $55 million general operating funds[1] deficit at June 30, 2004 (if no cuts were made in the budget). The management team projected a $73 million general operating funds deficit at June 30, 2004 (if no cuts were made in the budget). In addition, because the timing of the receipt and disbursement of transactions varies throughout the year, to further evaluate the financial position of the district, the management team prepared cash flow projections based on the budgeted revenues and expenditures and projected cash flow shortfalls throughout the year including a cash flow shortfall of $99 million in December 2003 (if no cuts were made in the budget).

Significant decreases in state funding combined with inadequate budgetary procedures and a lack of significant reductions in expenditures have lead to the district's current financial difficulties. General operating funds expenditures significantly exceeded revenues during fiscal years 2002 and 2003 resulting in the depletion of all district reserves and a negative general operating funds balance at the end of fiscal year 2003. This required the district to make reductions in expenditures to attempt to balance the budget for fiscal year 2004. The district's actual fiscal year 2004 budget, as approved by the current Board in August 2003, projected a deficit balance of $14.7 million at June 30, 2004, in the general operating funds and was in violation of Section 67.010 (2), RSMo 2000. In addition, Section 161.520, RSMo 2000, considers a district to be "financially stressed" if the year end operating funds balance is less than three percent of expenditures or is negative.

The district must continue to monitor the budget and make any additional reductions necessary to balance the budget in fiscal years 2004 and 2005.

[1] The district defines general operating funds as the General, Teachers, Free Textbook, Student Health, and Reimbursable Operating Expenses Funds. The district also maintains the School Lunchroom Fund, Debt Service Fund, various capital improvement funds, and various federal funds.

Background

The St. Louis Public School District encompasses the entire city of St. Louis, Missouri, approximately 61 square miles, and serves a population of approximately 339,000 citizens. With a total average daily attendance of approximately 39,000 students in school year 2002-2003 and total budgeted general operating expenditures historically exceeding $380 million per year, the district operates as the largest public school system in the State of Missouri. As of June 30, 2003, the district employed approximately 6,570 individuals, including approximately 4,100 full-time teachers and certified personnel.

The seven-member Board of Education is responsible for setting policy for the district to ensure efficient operations, overseeing the Superintendent of Schools, and adopting an annual budget and its supporting tax rate. Board members are elected by the voters of the city and serve without compensation. Four new members were elected to the Board in April 2003, while two of the remaining three members have served since 2001 and one has served since April 1997.

In January 2003, the Prior Superintendent, Dr. Cleveland Hammonds, announced his retirement effective at the end of fiscal year 2003. After the April 2003 election, the new Board voted to hire a management consultant firm in May 2003 to take over district operations starting in July 2003. The Prior Superintendent notified the Board in May 2003 of the impending projected operating funds budget deficit of approximately $55 million at June 30, 2004, and included a list of proposed programmatic reductions to possibly reduce the deficit. The management team later estimated the 2004 operating funds budget deficit to be approximately $73 million. The management team implemented measures to reduce the amount of the operating funds deficit. A total of 16 school facilities were closed with the students and teachers moved to other facilities prior to the start of the 2003-2004 school year. Additional measures are being discussed in an attempt to reduce the operating deficit, such as reductions in force in non-classroom related positions, privatizing a number of non-classroom related positions, and the elimination of nonessential costs.

Differences between management team and Prior Superintendent projections

In May 2003, the Prior Superintendent presented the Board with a preliminary fiscal year 2004 financial projection outlining an anticipated general operating funds deficit balance of $55 million at June 30, 2004. In July 2003, the management team created a "status quo" projection in an attempt to more accurately quantify the budget deficit that would result if the district continued to operate at previous year levels. This projection estimated a $73 million deficit general operating funds balance at June 30, 2004. The Prior Superintendent projections and the management team "status quo" projections are compared in Table 1.1.

Table 1.1: General Operating Funds Projection Differences

	Prior Superintendent 2004 Projections	Management Team "Status Quo" 2004 Projections	Differences in Projections
Beginning Balance	$ 7,666,412	(3,497,426)	(11,163,838)
Local Revenue	195,309,078	195,873,282	564,204
State Revenue	140,092,961	135,710,769	(4,382,192)
Federal Revenue	5,325,115	5,315,115	(10,000)
Total Revenue	340,727,154	336,899,166	(3,827,988)
Payroll and Benefits	(306,402,184)	(303,430,640)	2,971,544
Other	(97,292,261)	(103,142,940)	(5,850,679)
Total Expenditures	(403,694,445)	(406,573,580)	(2,879,135)
Ending Balance	$ (55,300,879)	(73,171,840)	(17,870,961)

Source: Prior administration and management team budget planning documents

As Table 1.1 indicates, the primary difference between the two sets of projections is $(11.1) million in the beginning balances assumed. This difference was due in part to a $(6.5) million restricted funds amount included in the Prior Superintendent's beginning balance figure and not included in the management teams amount. The remaining $(4.6) difference was due to the Prior Superintendent preparing his budget before the end of the fiscal year and using estimated revenues and expenditures for the remainder of fiscal year 2003.

There were also differences noted between the revenue and expenditure projections. The difference of $(3.8) million in revenues is primarily due to the management team's use of more conservative state revenue estimates based on updated information from the Department of Elementary and Secondary Education (DESE). The difference in "payroll and benefits" is because the management team projected a higher benefit figure than the prior administration, but also assumed lower staffing levels. In addition, the Prior Superintendent's "payroll and benefits" figure was overstated due to double counting summer school salary expenses. These differences netted to the $2.9 million difference. **The difference of $(5.8) million in the "other" expenditures projection is due primarily to the inclusion of the management team's fees, totaling approximately $5 million.** The remaining difference in "other" expenditures is due to the net effects of the inclusion of additional textbook expenditures by the management team, certain capital expenditures mistakenly included by the Prior Superintendent, and other miscellaneous differences. Both sets of expenditure projections are comparable to actual fiscal year 2003 expenditure levels.

While the beginning balance assumed by the management team was initially a negative $3.5 million, the final unrestricted beginning operating funds balance was negative $12.3 million. The majority of this change was caused by a $10.6 million adjustment made by the independent auditor to reverse a transaction made by the prior administration where it was thought that desegregation funds could be used to fund a general operating fund capital expense obligation.

Cash flow deficiencies

While the district's fiscal year budget reflects annual revenues and expenditures and a projected year end balance, the timing of the receipt and disbursement of transactions varies throughout the year. The timing of such cash flow may produce month end cash balances throughout the fiscal year that are either greater or are less than year end projections. Historically, the district experiences its lowest cash balance at December 31 as payments that month are especially high due to the district's annual employee retirement contribution payment[2] which is statutorily due by January 1. The district's cash balance has traditionally improved during the month of January when property tax revenues are received from the city.

To further evaluate the financial position of the district, the management team prepared cash flow projections based on the budgeted revenues and expenditures. In addition to their projected budget deficit of $73 million in the general operating funds at June 30, 2004, they also projected a cash flow shortfall in these funds of $99 million in December of 2003. So while the district had to focus on the projected fiscal year end budget deficit of $73 million, the interim cash flow shortfalls also had to be monitored.

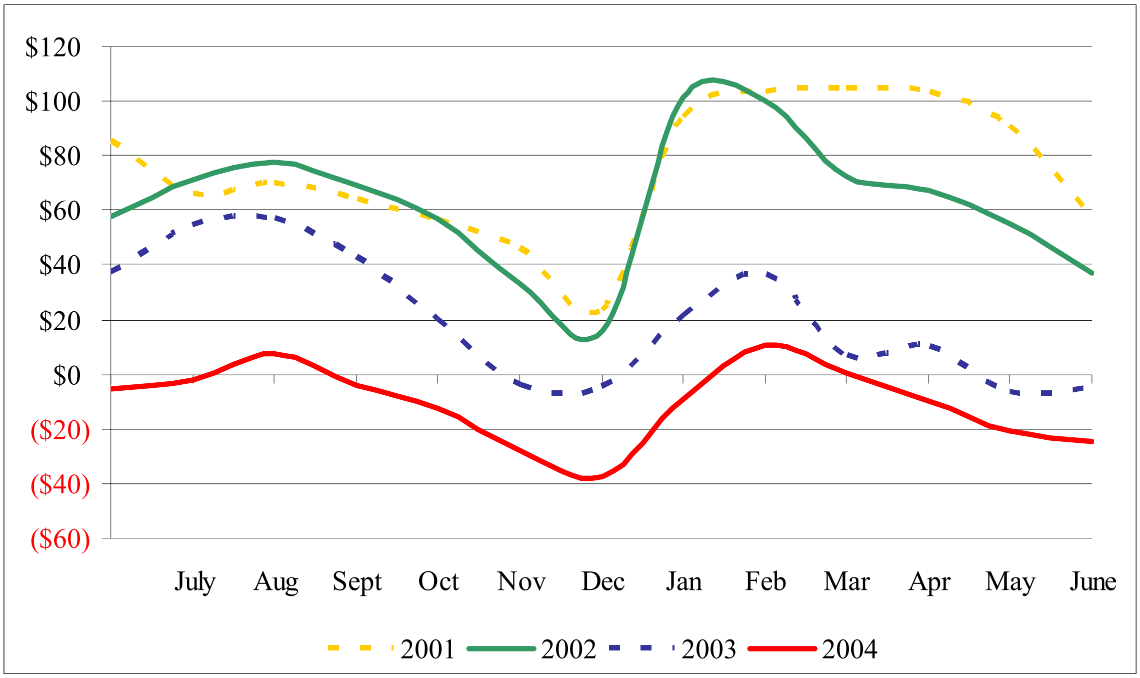
While the district's general operating funds have been experiencing cash flow deficiencies since early in fiscal year 2003, there was no evidence of cash flow projections being performed. For cash flow purposes, the prior administration used other restricted funds held in the combined bank account to cover negative cash operating funds balances during fiscal year 2003. This combined bank account includes the general operating funds, desegregation, federal, and other restricted funds. In November and December 2002, the prior administration needed up to $4.8 million in these funds to cover negative cash operating funds balances. In May and June 2003, the district again needed up to $6.8 million. In July 2003, the management team realized that the district would not have enough general operating cash to fund operations for the coming school year and that a cash shortfall would still exist at fiscal year end. The management team sought court approval to borrow monies from the desegregation funds to fund district operations. In August 2003, the United States District Court for the Eastern District of Missouri and the original plaintiffs in the desegregation litigation agreed to allow the district to borrow up to $49.5 million in desegregation funding for operating purposes. The court agreement requires any desegregation funds not repaid by June 30, 2004, be repaid, interest free, in six annual installments beginning in fiscal year 2005.

After taking measures to reduce expenditures and receive local property taxes earlier, the district's cash flow shortfall at December 31, 2003, was $37.6 million. The district covered this cash flow shortfall using desegregation funds.

Figure 1.1 depicts the district's general operating funds cash balances, by month, for fiscal years 2001 through 2003. Actual fiscal year 2004 month end cash balances are presented through December 2003, while balances through the end of fiscal year 2004 are projected.

[2] Historically this annual payment has been approximately $20 million.

Figure 1.1: General Operating Monthly Cash Balances By Year
In Millions



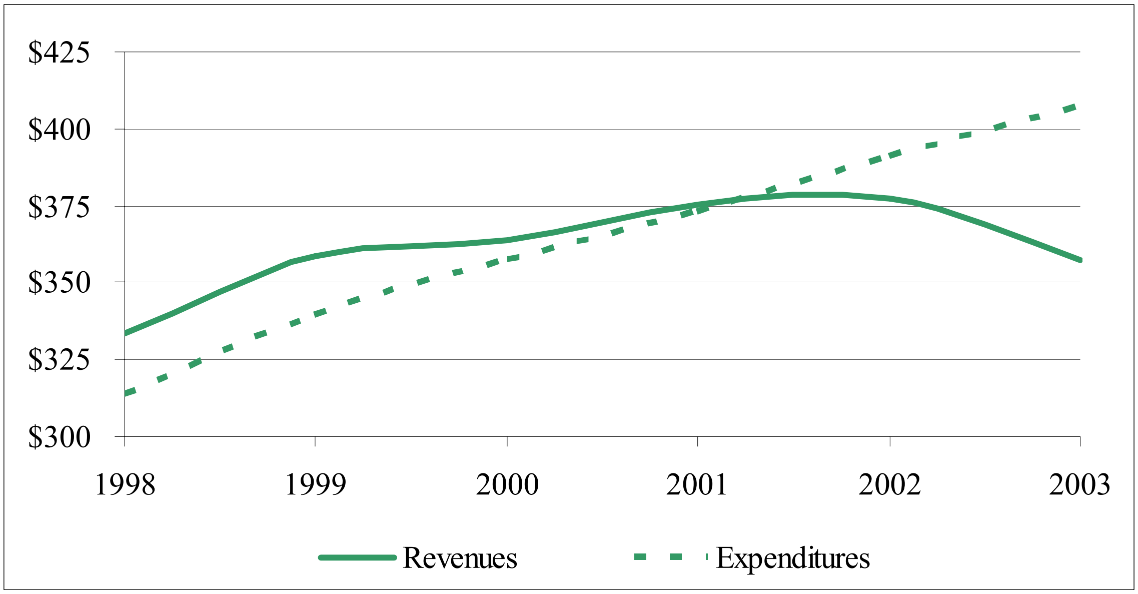
Source: District accounting records

As depicted in Figure 1.1, cash balances have been decreasing significantly each year since fiscal year 2001.

Factors leading to financial difficulties

Several factors have contributed to the decline in the district's financial condition, with the most significant being a substantial decrease in state revenues. As a result of state budget shortfalls, state revenues declined slightly in fiscal year 2002 (approximately $5 million or 3 percent) and declined substantially (approximately $21 million or 11.5 percent) in fiscal year 2003. A portion of this decline each year was due to increasing charter school payments (approximately a $4 million increase per year in 2001, 2002, and 2003.) The district's other significant revenue source, local tax revenues, remained relatively constant over the same time period. Overall, general operating funds revenues declined 5.1 percent from fiscal year 2001 through 2003. In contrast, operating funds expenditures increased 8.8 percent over the same time period. The increase is almost exclusively due to a $22.8 million (11 percent) increase in salaries and a $13.7 million (25 percent) increase in benefits. These increases were a result of a three year salary increase agreement with teachers and other staff and increasing health insurance costs. Other expenditures, which comprise only 27 percent of total expenditures, decreased 3.4 percent overall from 2001 to 2003. See Appendix I for a schedule of revenues, expenditures, and change in operating funds balance for fiscal years 2001 through 2003. Figure 1.2 depicts general operating funds total revenues and expenditures from fiscal year 1998 through 2003.

Figure 1.2: General Operating Revenues and Expenditures
In Millions



Source: Comprehensive Annual Financial Reports 1998 – 2000, District accounting records 2001 – 2003.

The district has been operating with expenditures exceeding revenues since fiscal year 2002. The disparity in operating funds revenues and expenditures in recent years has resulted in the unrestricted operating funds balance, or reserve, declining from $55.4 million in June 2001 to a deficit balance of $12.3 million in June 2003. Section 161.520, RSMo 2000, considers a district to be "financially stressed" if the year end operating funds balance is less than three percent of expenditures or is negative.

Inadequate budgetary procedures and follow through

Inadequate budgetary procedures and a lack of significant reductions in expenditures also contributed to the district's recent financial difficulties. Budgetary procedures were not sufficient to provide the Board with the information they needed to adequately monitor the budget. In addition to amendments to the budget decreasing overall revenues by $15 million, the Board also approved amendments increasing budgeted expenditures by $12 million during fiscal year 2003. Budget amendments approved by the Board did not include projections of the effect of the amendments on the operating funds ending balance. There is no documentation that indicates the Board received monthly updates on the status of the general operating funds balance or reserve. Furthermore, amendments were not prepared for additional revenue reductions and the amended budget was exceeded. The combination of revenues not meeting initial expectations and increases and overspending in expenditures resulted in a substantial depletion of the general operating funds reserve.

Although the general operating funds balance decreased in fiscal year 2002, and internal budget documents indicate that as early as December 2002 the Prior Superintendent was made aware that projections indicated the general operating funds balance would be negative by the end of fiscal year 2003, no significant reductions in expenditures were made for fiscal year 2003.

According to prior administration officials, the reductions in state revenue experienced in fiscal year 2003 could not be anticipated, and, by the time the district became aware of the reductions, significant cost cuts for fiscal year 2003 were not possible because of contractual obligations. However, some action was taken to mitigate the effects of the state revenue cuts and reduce expenditures, such as a freeze on hiring, the elimination of nonessential travel and other non-payroll expenditures, and the elimination of the extended school year program. The district used reserves to cover the state budget cuts and to honor the third year of the salary agreement. The district also promoted and passed a bond issue in April 2003 which could provide additional funds for capital improvements and debt service.

In addition, the district initiated a lawsuit regarding the state funding. In the lawsuit, the district has claimed that the state cannot reduce a portion of the district's state funding due to the desegregation agreement. This case was originally ruled in the district's favor but has been appealed and is currently pending. If the court rules in favor of the district, the state could owe money to the district.

Given the historical trends in financial information and declining balances of the district, it is unclear why there were not more documented communications between the board and the administration regarding the budgetary issues and possible solutions.

Current budget calls for general operating funds deficit

After the management team's projected cost reductions, the budget approved by the Board in August 2003 for fiscal year 2004 included a projected deficit general operating funds balance of $14.7 million at June 30, 2004. By approving a budget that includes a projected deficit fund balance, the Board has violated Section 67.010 (2), RSMo 2000, which states "in no event shall the total proposed expenditures from any fund exceed the estimated revenues to be received plus any unencumbered balance".

Future issues

The 2004 budget is a projection and assumes certain events, activities, revenues, and costs during the fiscal year. The management team is in the process of revising the fiscal year 2004 budget to more accurately reflect actual activity to date and project the year end deficit. As changes continue to be made at the district, the actual results will differ from these projections. As such, it is imperative that the district continue monitoring the budget and cash flow projections and make any reductions in expenditures necessary to balance the budget and carry the district into fiscal year 2005.

The State Auditor's Office is continuing to audit the operations of the district and any findings and recommendations will be included in a subsequent report.

APPENDIXES

APPENDIX I

ST. LOUIS PUBLIC SCHOOL DISTRICT
SCHEDULE OF REVENUES, EXPENDITURES, AND CHANGE IN GENERAL OPERATING FUNDS BALANCE

		Year Ended June 30,		
		2001	2002	2003
Beginning Balance	$	57,092,145	59,720,639	46,190,556
Revenues				
Local		185,356,983	189,843,031	186,640,506
State		185,240,287	179,788,428	159,174,982
Federal		4,913,567	7,775,574	10,516,889
Total Revenues		375,510,837	377,407,033	356,332,377
Expenditures and Transfers				
Payroll		209,287,529	223,870,733	232,138,289
Benefits		54,400,285	60,648,987	68,154,012
Transportation		23,932,492	30,322,351	30,823,789
Professional Services		14,582,638	14,679,662	11,529,286
Property Services		19,161,086	14,402,592	15,900,724
Supplies		18,770,217	21,504,387	18,664,842
Tuition		7,877,527	8,476,013	14,707,760
Capital Expense		15,509,823	7,789,271	11,641,981
Other		9,360,746	9,243,120	2,202,468
Total Expenditures and Transfers		372,882,343	390,937,116	405,763,152
Revenues Over (Under) Expenditures		2,628,494	(13,530,083)	(49,430,774)
Ending Balance	$	59,720,639	46,190,556	(3,240,218)
Restricted Balance		4,296,237	6,485,697	9,089,715
Unrestricted Balance		55,424,402	39,704,859	(12,329,933)
Total Balance	$	59,720,639	46,190,556	(3,240,218)

Source: District accounting records and Comprehensive Annual Financial Reports

APPENDIX II

ST. LOUIS PUBLIC SCHOOL DISTRICT
BUDGET VERSUS ACTUAL COMPARISON, GENERAL OPERATING FUNDS

	Year Ended June 30,								
	2001			2002			2003		
	Original Budget	Amended Budget	Actual	Original Budget	Amended Budget	Actual	Original Budget	Amended Budget	Actual
Revenues									
Local	$ 184,013,576	184,013,576	185,356,983	186,965,851	191,811,162	189,843,031	193,437,711	197,829,329	186,640,506
State	183,156,652	183,156,652	185,240,287	192,715,751	183,592,822	179,788,428	177,308,560	152,921,265	159,174,982
Federal	2,900,894	2,900,894	4,913,567	2,694,663	8,572,794	7,775,574	4,381,525	8,989,043	10,516,889
Total Revenues	370,071,122	370,071,122	375,510,837	382,376,265	383,976,778	377,407,033	375,127,796	359,739,637	356,332,377
Expenditures and Transfers									
Payroll	222,181,016	211,743,634	209,287,529	226,852,981	226,460,948	223,870,733	232,710,547	232,116,004	232,138,289
Benefits	53,738,851	58,041,191	54,400,285	59,531,215	60,769,430	60,648,987	67,048,264	68,126,160	68,154,012
Transportation	23,865,965	24,481,275	23,932,492	26,204,926	26,735,449	30,322,351	27,014,817	30,624,919	30,823,789
Professional Services	13,910,349	17,314,046	14,582,638	8,033,710	14,060,213	14,679,662	9,357,963	11,782,346	11,529,286
Maintenance	16,305,531	21,547,918	19,161,086	15,898,994	14,349,335	14,402,592	14,201,318	15,965,771	15,900,724
Supplies	24,930,523	22,771,539	18,770,217	25,087,222	21,649,122	21,504,387	17,372,975	18,686,483	18,664,842
Tuition	7,379,692	8,064,108	7,877,527	8,365,896	8,476,838	8,476,013	6,949,604	9,335,538	14,707,760
Capital Expenses	23,860,179	23,860,179	15,509,823	7,565,381	7,565,381	7,789,271	8,104,616	8,104,616	11,641,981
Other	10,615,699	10,616,353	9,360,746	9,015,642	7,697,757	9,243,120	6,811,588	7,129,625	2,202,468
Total Expenditures and Transfers	$ 396,787,805	398,440,243	372,882,343	386,555,967	387,764,473	390,937,116	389,571,692	401,871,462	405,763,152

Source: District accounting records

APPENDIX III

3222 Hawthorne Blvd.
St. Louis, MO 63104
January 20, 2004

Honorable Claire C. McCaskill
Missouri State Auditor
P.O. Box 869
Jefferson City, MO 65102

RE: Response to State Auditor's Report of St. Louis Public Schools

Dear Honorable McCaskill:

Thank you for allowing George Byron, Bill Purdy and me the opportunity to review your report on the finances of the St. Louis Public Schools.

We agree that the major reason for the financial difficulties that faced the school district for FY 2003 was the major revenue reductions by the State. The auditors also have agreed that the full impact of these revenue reductions was not known until late in June (the end of fiscal year 2003).

Contrary to the obvious public relations efforts, the auditors and I agree that there was never a projected deficit of $90 million plus for June, 2004.

We disagree with the statement that the lack of budgetary oversight and lack of significant action to reduce expenditures lead to the current financial difficulties. Monthly budgetary reporting to the board has been in the format that the board has requested, and has been that way for many years. A current board member requested the most recent change in the reporting format. The request was that all contracts submitted to the board indicate whether the appropriations to cover the contract were coming from a transfer, a new grant or new and additional appropriations (fund balance).

The monthly reports to the board included budget transfers, new and additional appropriations from either a new grant or from fund balance, new appropriations for additional personnel and a report by fund on total appropriations, year-to-date expenditures, outstanding encumbrances and remaining appropriations. Also included, but not as part of the financial reporting were all personnel transactions for the month.

If these reports are not adequate, then the board should address this issue and change their reporting requirements. The previous administration gave the board the reports in the format they (the board) had established years ago and there have never been any findings by the auditors that the board was not receiving sufficient information. It is easy to say after the fact that the board was not receiving enough information, but they received the reports they wanted in the format they wanted.

Actions were taken to reduce expenditures as the auditors explained in their report, but the severity of the state revenue reductions was not fully known until late in June, 2003. When it became known that the State was not fulfilling its obligation regarding the Desegregation Settlement Agreement, the District brought suit against the State (early in calendar year 2003). It was also presented to the board and approved that the passing of the $125 million bond issue would bring in additional revenues to the District for both debt service and general operating funds. The voters approved the bond issue and the first bonds issued redeemed the Leasehold Revenue Bonds, thus reducing the General Operating expenditures over $5 million for FY 2004. The application to DESE to utilize $0.18 of the Debt Service Levy to generate additional 2004 revenue for the District from all indications has not been done. To address the financial condition, the lawyers were contacted about reversing the $10.6 million transfer that was made for the city vocational high school. They drafted a resolution to reverse the previous transfer, bringing the monies back into the General Fund. Mr. Brostron, of Lashly & Baer, presented this resolution to the current board and it was approved and the transfer was reversed prior to the end of fiscal year 2003.

There were intense budget discussions before the board filed suit against the State over the Desegregation Agreement. There were extensive discussions about state cuts before the board approved the $125 million bond issue. Finally, on more than one occasion the superintendent and some board members went to Jefferson City to lobby against budget cuts.

In summary, four years ago when we entered into the salary agreement with our employees, we had no idea that the economy would cause state budget cuts. We certainly expected the State to live up to the Desegregation Agreement. We never expected the cost of charter schools to exceed $20 million. It is not true that the previous administration and board took no significant actions to avoid the current financial condition.

Sincerely,

Cleveland Hammonds

Cleveland Hammonds
Retired Supt. St. Louis Public Schools

Cc: George Byron & Bill Purdy

William V. Roberti
Acting Superintendent of Schools

St. Louis Public Schools Response to the Audit by the State Auditor's Office

The State Auditor's Report on St. Louis Public Schools confirms what the current Management Team and current Administration have been reporting:

- That the District's $90 million cash flow deficit was based on reasonable assumptions and standard methodologies; in other words, it was real.
- That the District's financial problems should have been recognized as early as the 2001-2002 school year, before any significant reduction in state aid had occurred.
- That the financial crisis was known by the prior Administration of the District as early as December 2002, but that few significant steps were taken to address it.
- That all District reserves were depleted by the prior Administration.
- That the prior Administration did present a plan to the Board of Education in June 2003 calling for some $55 million in program cost reductions, including school closings, teacher layoffs and elimination of athletic programs.

The report also notes that the prior Administration had inadequate budgetary procedures and did not take significant actions (cost reductions) to address the District's financial crisis. Since that time, the current Administration has implemented regular financial statements, monthly operating budget reports, and weekly cash flow reports, among other changes.

The report states that the District must continue to monitor the budget and make additional reductions necessary to balance the budget in 2004 and 2005, as required by state law, and that the District's unbalanced budget for the current fiscal year means that the District is still in violation of state law. In the dramatic cost reductions taken to date by the current Administration, there has been an effort to keep reductions away from the classroom, which is the District's core purpose. As we reported to the Board of Education and the public on Jan. 13, we have to reduce costs by an additional $23 million to balance the budget for 2004-2005. We will work diligently to ensure that the core purpose of the District remains whole, but we must closely consider all District operations.

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