



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

**Annual Financial Statements**

**June 30, 2003**

**(With Independent Auditors' Report Thereon)**

Prepared by

Office of School Site Support  
Financial Operations

4100 Normal Street  
San Diego, CA 92103

# SAN DIEGO UNIFIED SCHOOL DISTRICT

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## **INTRODUCTORY SECTION**



## SAN DIEGO CITY SCHOOLS

EUGENE BRUCKER EDUCATION CENTER  
4100 Normal St., Room 2244, San Diego, CA 92103-2682

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### FINANCIAL OPERATIONS DIVISION

**Scott H. Patterson**  
Chief Financial Officer

Members of the Board of Education  
San Diego Unified School District  
San Diego, California 92103

#### Members of the Board:

Attached are the annual financial statements of the San Diego Unified School District (the District) for the fiscal year ended June 30, 2003, and the Independent Auditors' Reports on those financial statements and on the Federal and State Compliance audits. These financial statements confirm that the District is a fiscally sound district, as defined by the State Controller's Office, with a general fund unreserved fund balance of \$5,020,016.

The auditors' reports cite no material internal control weaknesses. One material instance of non-compliance on federal programs is reported related to bi-annual certifications for employees working on federal awards. The district is currently taking steps to ensure that mandatory certifications are completed as required on an on-going basis.

The California Education Code requires that the governing board provide for an annual audit made by certified public accountants licensed by the State Board of Accountancy. The licensed firm of KPMG LLP rendered the attached auditors' reports. It is my opinion that the audit satisfies all of the requirements of the Education Code.

The annual financial statements for the fiscal year 2002-2003, also include financial statements in the format required under the Government Accounting Standards Board Statement 34 (GASB 34). These financial statements are explained in more detail in the Management's Discussion and Analysis that accompanies the GASB 34 compliant financial statements. This is now the second year of such reporting.

The auditors also provided a list of findings and recommendations and an analysis of the District's response to the findings and recommendations contained in the prior year's audit. District administration has reviewed the findings and recommendations and has positively responded to each of the recommendations.

May 11, 2004

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*"The mission of San Diego City Schools is to improve student achievement by supporting teaching and learning in the classroom."*

## SAN DIEGO UNIFIED SCHOOL DISTRICT

Organization

June 30, 2003

The San Diego Unified School District (the District) was incorporated in 1889 and is comprised of an area of approximately 210.9 square miles located in San Diego County. There were no material changes in the boundaries of the District during the current year. The District is currently operating the following facilities:

### Number of Educational Facilities

Elementary Schools, Grades K-6	116
Middle Schools, Grades 6-8	20
Junior High Schools, Grades 7-9	3
Senior High Schools, Grades 9-12	16
School of Creative and Performing Arts, Grades 7-12	1
Secondary Center of Science/Math/Computers, Grades 7-12	1
Connections	1
Continuation High Schools, Grades 7-12	3
Alternative School	1
Schools for the Handicapped	4
Community Day School	1
Community Home School	1
<b>Total</b>	<b>168</b>
Children's Centers	25
<b>Grand total</b>	<b>193</b>

The District operates preschool centers for three and four year olds at 41 school sites.

Fifty-three elementary schools, five middle schools, and one junior high school conduct year-round multiple or single-track programs.

The Board of Education was comprised of the following members as of June 30, 2003:

<u>Name</u>	<u>Office</u>	<u>Term expires</u>
Ron Ottinger	President	December 2004
Katherine Nakamura	Vice President	December 2006
John de Beck	Member	December 2006
Frances Zimmerman	Member	December 2004
Ed Lopez	Member	December 2004

The Superintendent of Schools for fiscal year 2003-2003 is Alan D. Bersin. Alan D. Bersin was appointed Superintendent of Schools effective July 1, 1998.

**FINANCIAL SECTION**



KPMG LLP  
Suite 1500  
750 B Street  
San Diego, CA 92101

## Independent Auditors' Report

The Honorable Board of Education  
San Diego Unified School District:

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the San Diego Unified School District (the District) as of and for the year ended June 30, 2003, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the District as of June 30, 2003, and the respective changes in financial position and the respective budgetary comparison for the General Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

Management's discussion and analysis on pages 3 through 13 is not a required part of the basic financial statements but is supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming an opinion on the financial statements that collectively comprise the District's basic financial statements. The introductory section and the combining nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards for the year



ended June 30, 2003 is presented for the purpose of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements. The supplementary information on pages 42 through 79 is presented for the purpose of additional analysis as required by the California State Controller's Office. The combining nonmajor fund financial statements, the schedule of expenditures of federal awards, and the supplementary information on pages 42 through 79 have been subjected to the auditing procedures applied in the audit of the basic financial statements, and, in our opinion, are fairly stated, in all material respects, in relation to the basic financial statements taken as a whole. The information in the introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we express no opinion on it.

In accordance with *Government Auditing Standards*, we have also issued a report dated April 15, 2004 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

KPMG LLP

April 15, 2004



**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
 Management's Discussion and Analysis (Unaudited)  
 Year ended June 30, 2003

This section of the San Diego Unified School District's (the District's) annual financial report presents our discussion and analysis of the District's financial performance during the fiscal year ended June 30, 2003. Please read it in conjunction with the District's basic financial statements, which follow this section.

**Financial Highlights**

- The District's total net assets were \$544.4 million at June 30, 2003.
- During the year, the District's expenses were \$120.3 million less than the \$1,554.2 million generated in taxes and other revenues for governmental activities.
- The General Fund reported a fund balance this year of \$126.1 million.
- The District issued approximately \$275.0 million in bonds during fiscal year 2003.

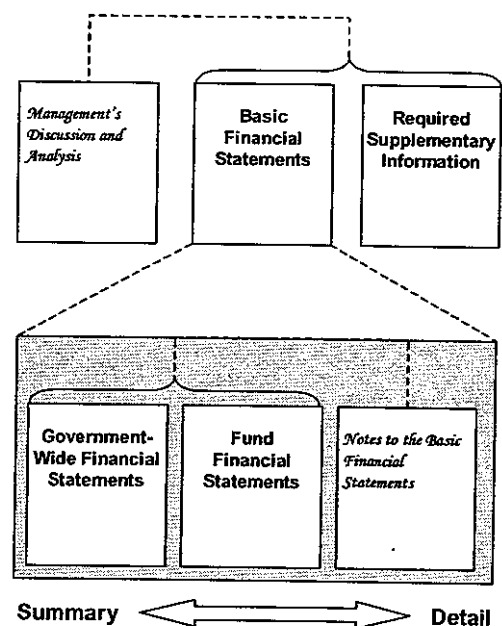
**Overview of the Basic Financial Statements**

This annual report consists of three parts – *management's discussion and analysis* (this section), the *basic financial statements*, and *required supplementary information*. The basic financial statements include two kinds of statements that present different views of the District:

- The first two statements are government-wide financial statements that provide both long-term and short-term information about the District's overall financial status.
- The remaining statements are fund financial statements that focus on individual parts of the District, reporting the District's operations in more detail than the government-wide statements.
  - The *governmental funds* statements tell how *general government* services were financed in the *short-term* as well as what remains for future spending.
  - *Fiduciary fund* statements provide information about the financial relationships in which the District acts solely as a trustee or agent for the benefit of others, to whom the resources in question belong.

The financial statements also include *notes* that explain some of the information in the basic financial statements and provide more detailed data. Generally accepted accounting principles prescribe that certain information be presented as required supplementary information (RSI). The District has met that requirement by including the management's discussion and analysis, as part of the basic financial statements. Figure A-1 shows how the required parts of this annual report are arranged and related to one another.

**Figure A-1. Required Components of the District's Annual Financial Report**



**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
**Management's Discussion and Analysis (Unaudited)**

Year ended June 30, 2003

Figure A-2 summarizes the major features of the District's basic financial statements, including the portion of the District government they cover and the types of information they contain. The remainder of this overview section of management's discussion and analysis explains the structure and contents of each of the statements.

**Government-Wide Statements**

The government-wide statements report information about the District as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes *all* of the government's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two government-wide statements report the District's *net assets* and how they have changed. Net assets – the difference between the District's assets and liabilities – are one way to measure the District's financial health or position.

- Over time, increases or decreases in the District's net assets are an indicator of whether its financial health is improving or deteriorating, respectively.
- To assess the overall health of the District, you need to consider additional nonfinancial factors such as changes in the District's tax base and changes in composition and amounts of external funding.

The government-wide financial statements of the District include the *Governmental activities*. Most of the District's basic services are included here, such as instruction, extracurricular activities, curriculum and staff development, health services, and general administration. Property taxes and grants finance most of these activities.

Figure A-2. Major Features of the District's Government-wide and Fund Financial Statements

Type of Statements	Government-wide Statements	Fund Statements	
		Governmental Funds	Fiduciary Funds
Scope	Entire District's government (except fiduciary funds) and the District's component units	The activities of the District that are not proprietary or fiduciary	The District is the trustee or agent for someone else's resources
Required financial statements	<ul style="list-style-type: none"> <li>* Statement of net assets</li> <li>* Statement of activities</li> </ul>	<ul style="list-style-type: none"> <li>* Balance sheet</li> <li>* Statement of revenues, expenditures and changes in fund balances</li> </ul>	<ul style="list-style-type: none"> <li>* Statement of fiduciary net assets</li> <li>* Statement of changes in fiduciary net assets</li> </ul>
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus
Type of asset/liability information	All assets and liabilities, both financial and capital, and short-term and long-term	Only assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets included	All assets and liabilities, both short-term and long-term; District funds do not currently have capital assets, although they can
Type of inflow/outflow information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and payment is due during the year or soon thereafter	All revenues and expenses during year, regardless of when cash is received or paid

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
Management's Discussion and Analysis (Unaudited)  
Year ended June 30, 2003

***Fund Financial Statements***

The fund financial statements provide more detailed information about the District's most significant *funds* – not the District as a whole. Funds are accounting devices that the District uses to keep track of specific sources of funding and spending for particular purposes.

- Some funds are required by state law and by bond covenants.
- The Board of Trustees establishes other funds to control and manage money for particular purposes or to show that it is properly using certain taxes and grants.

The District has two kinds of funds:

- *Governmental funds* – Most of the District's basic services are included in governmental funds, which focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the District's programs. Because this information does not encompass the additional long-term focus of the government-wide statements, we provide additional information at the bottom of the governmental funds statement, or on the subsequent page, that explain the relationship (or differences) between them.
- *Fiduciary funds* – The District is the trustee, or fiduciary, for certain funds. It is also responsible for other assets that – because of a trust arrangement – can be used only for the trust beneficiaries. The District is responsible for ensuring that the assets reported in these funds are used for their intended purposes. All of the District's fiduciary activities are reported in a separate statement of fiduciary net assets and a statement of changes in fiduciary net assets. We exclude these activities from the District's government-wide financial statements because the District cannot use these assets to finance its operations.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
Management's Discussion and Analysis (Unaudited)  
Year ended June 30, 2003

**Financial Analysis of the District as a Whole**

**Net Assets.** The District's net assets were approximately \$544.4 million at June 30, 2003 (See Table A-1).

**Table A-1**  
**The District's Net Assets**  
(In millions of dollars)

	<b>Governmental activities</b>		<b>Percentage change</b>
	<b>2003</b>	<b>2002</b>	
Current and other assets	\$ 595.0	633.8	(6.1)%
Capital and noncurrent assets	927.8	653.8	41.9%
Total assets	\$ 1,522.8	1,287.6	18.3%
Current liabilities	121.4	197.5	(38.5)%
Long-term liabilities	857.0	666.1	28.7%
Total liabilities	\$ 978.4	863.6	13.3%
Net assets:			
Invested in capital assets net of related debt	441.8	270.8	63.1%
Restricted	35.5	110.7	(67.9)%
Unrestricted	67.1	42.5	57.9%
Total net assets	\$ 544.4	424.0	28.4%

The 2002-2003 increase in capital and noncurrent assets of \$274.0 million was primarily due to a purchase of land for six new schools for \$56.0 million, building improvements under Proposition MM for \$44.0 million, and construction in progress of \$173.0 million. Current liabilities decreased by \$76.1; \$65.0 million for defeasance of short-term certificates of participation and \$19.0 million in deferred revenue. Long-term liabilities increased by \$191.0 million as a result of the issuance of \$275.0 million of Series D bonds under Proposition MM and the defeasance of \$98.0 million of long-term certificates of participation. As a result, net assets increased by \$120.0 million.

The \$67.1 million of unrestricted net assets represents resources available to fund the programs of the District next year.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
 Management's Discussion and Analysis (Unaudited)  
 Year ended June 30, 2003

**Changes in Net Assets.** The District's total revenues were \$1,554.2 million. The largest portion, 54%, of the District's revenue comes from operating grants and contributions (See Figure A-3). A significant portion, 28%, comes from property taxes. 14% comes from state apportionment, 1% from nonrestricted lottery, 2% from other revenues, while only 1% relates to charges for services.

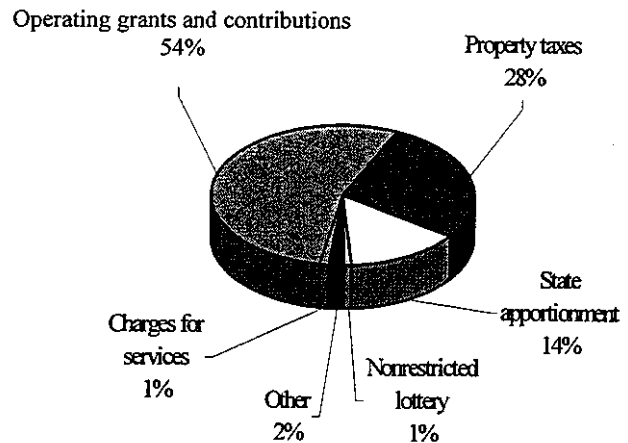
The total cost of all programs and services was \$1,433.9 million; 75% of these costs are for instructional and student services.

**Governmental Activities**

- The District sold capital bonds of \$275.0 million. These bonds were authorized under Proposition MM for school construction and capital improvements.
- The District completed the site acquisition for one new elementary school (Cherokee Point) this year as well as completed construction on 38 Whole Site Modernization Projects. Of these 38 projects, 22 were the last Whole Site Modernization Phase at that school. These projects included work in the following categories:
 

<ul style="list-style-type: none"> <li>- Ceiling tile repair/replacement</li> <li>- Roofing repair/replacement</li> <li>- Plumbing repair</li> <li>- Door and window replacements</li> <li>- ADA compliance upgrades</li> <li>- Electrical system repair/replacement</li> <li>- Interior and exterior painting</li> </ul>	<ul style="list-style-type: none"> <li>- HVAC repair</li> <li>- Flooring replacements</li> <li>- Upgrade of Fire security and alarm systems</li> <li>- Asphalt/paving</li> <li>- Lunch court shelter construction</li> <li>- New/expanded libraries</li> <li>- New/upgraded science classrooms</li> </ul>
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**Figure A-3. District Sources of Revenue for Fiscal Year 2003**



**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
Management's Discussion and Analysis (Unaudited)  
Year ended June 30, 2003

**Table A-2**  
**Changes in the District's Net Assets**  
(In millions of dollars)

	Governmental activities		Percentage change
	2003	2002	
Revenues:			
Program revenues:			
Charges for services	\$ 11.3	11.6	(2.6)%
Operating grants and contributions	839.6	564.3	48.8%
General revenues:			
Property taxes	430.2	397.2	8.3%
State apportionment	219.0	256.2	(14.5)%
Lottery apportionment – nonrestricted	14.6	16.4	(11.0)%
Mandated cost reimbursement	0.2	18.1	(98.9)%
Other	40.0	40.1	(0.2)%
Total revenues	<u>1,554.9</u>	<u>1,303.9</u>	<u>19.2%</u>
Expenses:			
Instruction	707.3	695.2	1.7%
Instruction related services	201.0	198.7	1.2%
Pupil services	162.5	164.0	(0.9)%
Ancillary services	1.0	—	100.0%
Community services	0.3	0.4	(25.0)%
General administration	41.8	14.1	196.5%
Plant services	112.6	123.0	(8.5)%
Other outgo	143.8	44.2	225.3%
Interest expense	63.6	32.3	96.9%
Total expenses	<u>1,433.9</u>	<u>1,271.9</u>	<u>12.7%</u>
Increase in net assets before special item	121.0	32.0	278.1%
Special item – loss on disposal of equipment	(0.7)	(0.1)	600.0%
Increase in net assets	120.3	31.9	277.1%
Beginning net assets (1)	<u>424.1</u>	<u>392.1</u>	8.2%
Ending net assets	<u>\$ 544.4</u>	<u>424.0</u>	28.4%

(1) Beginning net assets does not match ending net assets from previous year due to the decision not to blend the 501(c)(3) charter schools this year.

Operating grants and contributions increased by \$275.3 million in 2002-2003. Some of the more significant reasons for this were the County School Facilities apportionment of \$102.0 million, \$88.0 million received by the District's Public School Building Corporation for a combination of certificates of participation proceeds on a refunding bond; the one-time defeasance of debt, the recognition of previously deferred

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
Management's Discussion and Analysis (Unaudited)  
Year ended June 30, 2003

interest income; and the release of \$43.0 million related to the defeasance of all of the District's certificates of participation. Property tax revenues were up \$33.0 million, primarily from increased assessed valuation on property. State apportionment was down a total of \$37.2 million. \$26.0 million of this was due to a combination of a reduction in the factor that the state applies to the principal apportionment and a decrease in the PERS Reduction transfer. The other \$11.0 million of the decrease resulted from not doing School Based Coordination Program transfers in 2002-2003, in order for the District to be compliant with the State's Standardized Account Code Structure (SACS). Also, a \$17.9 million decrease in mandated cost reimbursement revenue was due to the full recognition in 2001-2002 of all deferred income per the guidelines set forth in GASB Statement No. 33.

Other outgo was up \$99.6 million due primarily to the early prepayment of Proposition O certificates of participation. The \$31.3 million increase in interest expense was related to the additional expense of the Proposition MM Series D bonds issuance.

Table A-3 presents the cost of each of the District's largest functions as well as each function's *net cost* (total cost less fees generated by the activities and intergovernmental aid). The net cost reflects what was funded by state and federal revenues as well as local tax dollars.

- The cost of all governmental activities this year was \$1,433.9 million.
- However, the amount that our taxpayers paid for these activities through property taxes was \$430.2 million.
- Some of the cost was paid by those who directly benefited from the programs (\$11.3 million), or
- By grants and contributions (\$839.6 million).

**Table A-3**  
**Net Cost of Selected District Functions**  
(In millions of dollars)

	Total cost of services		Percentage change	Net cost of services		Percentage change
	2003	2002		2003	2002	
Instruction	\$ 707.4	695.2	1.8%	\$ 423.8	433.7	(2.3)%
Instruction related services	201.0	198.7	1.2%	120.2	123.7	(2.8)%
Pupil services	162.5	164.0	(0.9)%	88.4	93.2	(5.2)%
Plant services	112.6	123.0	(8.5)%	(62.9)	(4.3)	1362.8%
Other	250.4	91.0	175.2%	13.6	49.7	(72.6)%
Total	\$ 1,433.9	1,271.9	12.7%	\$ 583.1	696.0	(16.2)%

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
Management's Discussion and Analysis (Unaudited)  
Year ended June 30, 2003

**Financial Analysis of the District's Funds**

Revenues from governmental fund types totaled \$1,436.2 million, while expenditures were \$1,711.6 million. When combined with the \$255.5 million in other financing sources, the governmental funds experienced a \$19.9 million decrease in fund balance during the year. This decrease was attributed to the following:

- The fund balance of the General Fund increased by \$24.7 million due to the release of the certificate of participation reserves that flowed back to the District.
- The fund balance of the Capital Projects – Proposition MM Fund decreased by \$12.5 million due to significantly increased capital outlay expenditures resulting from increased modernization activity at the various schools and increased land acquisition and resident relocation activity.
- The fund balance of the Capital Projects – County School Facilities Fund increased by \$90.0 million due to the Proposition 1A grant funds received from the state for modernization and growth projects.
- The fund balances of the other governmental funds decreased by \$122.1 million. Of this change, the largest decrease, \$108.8 million, came from the defeasance of all remaining debt owed by the District's Public School Building Corporation.

***General Fund Budgetary Highlights***

Over the course of the year, the District revised its budget several times. The following were the major changes between original and amended budget:

- Revenues that were received during the year that were not included in the originally adopted budget – federal grants and special projects of \$39.0 million and state grants and special projects of \$47.0 million.
- Increase in expenditure budgets for certificated salaries of \$47.0 million. Classified salaries of \$26.0 million, employee benefits of \$18.0 million and services and other operating expense of \$72.0 million can be attributed to transfers made between major accounts such as books and supplies to salaries and benefits accounts. In addition, the District adopted in the budget \$39.0 million in federal grants and \$47.0 million in state grants and special projects funding during the year. These funds were appropriated in the salaries, benefits and service and other operating accounts. In 2002-2003, the District also received funds from the release of Certificates of Participation (COP) reserves that were appropriated in the service and other operating account to support the implementation of the District-wide application.
- Decrease in expenditure budget due to transfers made to realign the budget between major object categories – books and supplies of \$36.0 million.

Even with these adjustments, actual expenditures and other financing uses were \$161.7 million below final budget amounts. The most significant positive variances resulted from:

- Salaries and benefits were \$69.0 million below final budget amounts. This variance was primarily due to declining enrollment and the workforce reduction that occurred in the middle of the year.



**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
**Management's Discussion and Analysis (Unaudited)**  
**Year ended June 30, 2003**

- Books and supplies were \$60.0 million below final budget amounts and services and other operating expenses were \$27.8 million below final budget amounts. These variances can be attributed to the reductions that occurred in the middle of the year. Additionally, appropriations for these expenditures were not spent but were encumbered at the end of the year, resulting in an increase of \$42.0 million in encumbrances in the General Fund.

Actual resources available were \$99.8 million below the final budgeted amount. The most significant negative variances resulted from:

- ECIA/ESEA/IASA Title I grants (\$13.0 million), various other federal (\$14.0 million), state (\$49.0 million), and local (\$7.0 million) grants account for a total of \$83.0 million of this variance. This largely represents grant money that has been received but not spent by June 30, 2003, and therefore deferred. Budget reductions at the state level also accounted for the variances.
- Revenue Limit funding was \$11.0 million below appropriations primarily due to the District's continued declining enrollment.

**Capital Assets and Debt Administration**

***Capital Assets***

At the end of 2003, the District had invested \$927.8 million in a broad range of capital assets, including land, equipment, buildings, and vehicles (See Table A-4).

**Table A-4**  
**The District's Capital Assets**  
(In millions of dollars)

	<b>Governmental activities</b>		<b>Percentage change</b>
	<b>2003</b>	<b>2002</b>	
Land	\$ 111.9	56.0	99.8%
Land improvements	106.5	82.9	28.5%
Buildings	370.4	370.4	0.0%
Building improvements	177.1	133.3	32.9%
Personal property and equipment	136.3	134.6	1.3%
Construction in progress	366.6	193.3	89.7%
Totals at historical cost	1,268.8	970.5	30.7%
Total accumulated depreciation	(341.0)	(316.7)	7.7%
Net capital assets	\$ 927.8	653.8	41.9%

Net capital assets increased by \$274.0 million in 2002-2003. The primary components of this increase include: an increase of \$55.9 million for the purchase of land for six new schools; an increase of \$23.6 million in land improvements of which includes \$10.8 million for playground restorations, \$4.7 million for irrigation systems, \$2.5 million for fence installations, and \$3.1 million for slope repair; an increase in building improvements of \$43.8 million which includes \$31.4 million for the completion of various Proposition MM projects and \$12.4 million for classroom remodels; and an increase of \$173.3

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
 Management's Discussion and Analysis (Unaudited)  
 Year ended June 30, 2003

million in construction in progress for the continuation of Proposition MM projects for building new schools and remodeling existing schools. Completion of these projects will be occurring at various times through 2008.

The District's fiscal year 2004 capital budget projects spending another \$492.1 million for capital projects, principally for school construction and capital improvements. This spending will primarily be financed by the proceeds from the bonds issued this year. More detailed information about the District's capital assets is presented in note 1 to the financial statements.

**Long-Term Borrowings**

At year-end, the District had \$765.0 million in bonds and notes outstanding as shown in Table A-5. More detailed information about the District's debt is presented in the notes to the financial statements.

**Bond Ratings**

The District's bonds presently carry ratings as follows: Moody's Investor Services "Aa2" and Standard & Poors "AA."

**Table A-5**  
**The District's Long-Term Borrowings**  
 (In millions of dollars)

	<b>Governmental activities</b>		<b>Percentage change</b>
	<b>2003</b>	<b>2002</b>	
Bonds payable	\$ 765.0	490.0	56.1%
State school loans payable	—	0.1	(100.0)%
Certificates of participation payable	—	162.8	(100.0)%
Total bonds and notes payable	\$ <u>765.0</u>	<u>652.9</u>	17.2%

The increase in bonds payable is entirely due to the issuance of \$275.0 million of Series D bonds under Proposition MM. The certificates of participation were entirely defeased during the year.

**Short-Term Debt**

The District periodically issues short-term debt to facilitate its cash flow needs. On July 2, 2002, the District sold \$210,000,000 of tax-exempt Tax and Revenue Anticipation Notes at a rate of 3.00% maturing on July 28, 2003. The principal of the notes, together with the interest thereon, is payable from taxes, revenue, and other monies received by the District during fiscal year 2002-03. As of June 30, 2003, the District has transferred all required principal and interest on the notes to an irrevocable trust fund maintained by the San Diego County Treasury. The District does not reflect a liability for the notes at June 30, 2003, as the necessary amounts to repay the notes have been funded and, as such, are not expendable funds of the District. The tax-exempt notes were repaid in full on July 28, 2003.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
Management's Discussion and Analysis (Unaudited)  
Year ended June 30, 2003

**Economic Factors and Next Year's Budgets and Rates**

- Subsequent to the adoption of the District's 2003-2004 budget in June 2003, the state passed legislation to reduce revenue limit funding by 3%. This 3% deficit funding resulted in a net loss to the District of \$18.0 million. The state budget included funding of the Targeted Instructional Improvement Grant program that was deferred in the prior year for \$7.0 million.
- Assessed valuation used for the 2004 budget preparation assumed a \$5.7 billion increase, or 7.4% from 2003.
- The District's 2004 second period average daily attendance (excluding charter schools and adult education) is budgeted as 124,022, up less than 1%.

These indicators were taken into account when adopting the General Fund budget for 2004. Amounts available for appropriation in the General Fund budget are \$1,163.1 million, a decrease of 12.8% over the final 2003 budget of \$1,333.9 million. Property taxes are budgeted to increase due to an increase in assessed valuation.

Expenditures and other financing uses are budgeted to fall 10.5% to \$1,136.5 million. Some of the reasons for this decline are: a decrease of \$62.0 million in salaries and benefits due to early retirement incentive effective in 2003-2004, workforce reduction implemented in the middle of 2002-2003 that carried over to the following fiscal year, and declining enrollment; a decrease of \$27.0 million budgeted for District Wide Application expenditures in 2002-2003, that were not to occur in 2003-2004; a reduction of \$17.0 million in books and supplies allocations due to declining enrollment, budget reductions, and reduced special projects due to deferrals of funding by the State; and a decrease of \$10.0 million in capital outlay due to budget reductions and state deferral of funding for special projects.

The District has added one major new program to the 2004 budget. This is a local grant on behalf of New American Schools as fiscal agent on a grant from the Bill and Melinda Gates Foundation. The amount of this grant is \$1.7 million.

If these estimates are realized, the District's budgetary General Fund balance is expected to decrease by the close of 2004.

**Contacting the District's Financial Management**

This financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the District's Financial Operations Office.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Statement of Net Assets

June 30, 2003

	<u>Governmental activities</u>
Assets:	
Current assets:	
Cash	\$ 450,661,055
Investments	13,724,250
Accounts receivable:	
Federal and state government	70,423,186
Other	57,300,884
Prepaid expense	680,238
Inventory	2,168,664
Total current assets	<u>594,958,277</u>
Noncurrent assets:	
Capital assets:	
Land	111,921,411
Land improvements	106,484,342
Building and improvements	547,434,744
Equipment and vehicles	136,309,976
Construction in progress	366,597,991
Accumulated depreciation	<u>(340,983,523)</u>
Total noncurrent assets	<u>927,764,941</u>
Total assets	<u>1,522,723,218</u>

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Statement of Net Assets

June 30, 2003

	<u>Governmental activities</u>
<b>Liabilities:</b>	
<b>Current liabilities:</b>	
Accounts payable and other liabilities	\$ 70,091,667
Accrued interest payable	30,150,142
Deferred revenue	21,142,886
Current portion of state school loans payable	6,126
<b>Total current liabilities</b>	<u>121,390,821</u>
<b>Noncurrent liabilities:</b>	
<b>Due in less than one year:</b>	
Claims and judgments payable	14,718,846
Vacation benefits payable	11,336,892
Arbitrage liability payable	2,972,551
<b>Due in more than one year:</b>	
General obligation bonds payable	764,985,227
State school loans payable	17,887
Claims and judgments payable	35,382,640
Vacation benefits payable	2,322,015
Arbitrage liability payable	2,764,169
Deferred bond premium	22,480,287
<b>Total noncurrent liabilities</b>	<u>856,980,514</u>
<b>Total liabilities</b>	<u>978,371,335</u>
<b>Net assets:</b>	
Invested in capital assets, net of related debt	<u>441,775,192</u>
<b>Restricted net assets:</b>	
Restricted for debt service	14,338,831
Restricted for categorical programs	3,578,155
Restricted for economic uncertainties	17,583,936
	<u>35,500,922</u>
Unrestricted net assets	<u>67,075,769</u>
<b>Total net assets</b>	<u>\$ 544,351,883</u>

See accompanying notes to basic financial statements.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Statement of Activities

Year ended June 30, 2003

Functions/Programs	Expenses	Program revenues		Net (expense) revenue and changes in net assets
		Charges for services	Operating grants and contributions	
				Governmental activities
Governmental activities:				
1000 Instruction	\$ 707,344,275	819,652	282,692,682	(423,831,941)
2000 Instruction-related services	201,027,899	—	80,874,624	(120,153,275)
3000 Pupil services	162,460,618	10,443,453	63,574,254	(88,442,911)
4000 Ancillary services	963,837	—	392,671	(571,166)
5000 Community services	339,145	—	138,249	(200,896)
7000 General administration	41,831,213	—	16,744,604	(25,086,609)
8000 Plant services	112,598,076	—	175,544,316	62,946,240
9000 Other outgo	143,803,715	—	219,594,050	75,790,335
0000 Interest expense	63,552,025	—	—	(63,552,025)
Total governmental activities	\$ <u>1,433,920,803</u>	<u>11,263,105</u>	<u>839,555,450</u>	<u>(583,102,248)</u>
General revenues:				
Property taxes				430,189,658
Revenue limit – state aid				170,984,269
Federal aid				21,375,314
State aid – class size reduction				42,807,112
State aid – state lottery apportionment – nonrestricted				14,596,207
State aid – mandated cost programs				196,863
Other state aid				5,276,250
Other local aid				8,959,030
Investment earnings				9,685,777
Special item – loss on disposal of equipment				(684,870)
Total general revenues				<u>703,385,610</u>
Change in net assets				120,283,362
Net assets – beginning				<u>424,068,521</u>
Net assets – ending				\$ <u>544,351,883</u>

See accompanying notes to basic financial statements.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Balance Sheet – Governmental Funds

June 30, 2003

Assets	<u>General Fund</u>	<u>Capital Projects – Proposition MM</u>	<u>Capital Projects – County School Facilities</u>	<u>Other Governmental Funds</u>	<u>Totals</u>
Cash in county treasury	\$ 60,168,059	215,610,948	95,162,221	78,243,920	449,185,148
Cash on hand and in banks	1,077,814	—	—	348,093	1,425,907
Cash with fiscal agent	—	—	—	50,000	50,000
Short-term investments	—	—	—	13,724,250	13,724,250
Accounts receivable:					
Federal and state government	67,908,147	—	19,488,059	16,284,612	103,680,818
Other	21,505,234	1,164,854	428,492	944,672	24,043,252
Due from other funds	39,171,382	8,475	—	13,916,810	53,096,667
Prepaid expenses	680,238	—	—	—	680,238
Inventory	1,231,615	—	—	937,049	2,168,664
<b>Total assets</b>	<b>\$ 191,742,489</b>	<b>216,784,277</b>	<b>115,078,772</b>	<b>124,449,406</b>	<b>648,054,944</b>
<b>Liabilities and Fund Balances</b>					
<b>Liabilities:</b>					
Accounts payable	\$ 42,545,268	20,523,426	504,622	6,518,351	70,091,667
Accrued interest	—	—	—	13,925,905	13,925,905
Due to other funds	2,615,053	11,424,758	42,970	39,013,886	53,096,667
Deferred revenue	20,513,775	—	—	629,111	21,142,886
<b>Total liabilities</b>	<b>65,674,096</b>	<b>31,948,184</b>	<b>547,592</b>	<b>60,087,253</b>	<b>158,257,125</b>
<b>Fund balances:</b>					
Reserved	109,947,032	111,729,969	1,792,021	5,426,401	228,895,423
Unreserved	5,020,016	73,106,124	112,739,159	52,453,161	243,318,460
Designated for economic uncertainty	11,101,345	—	—	6,482,591	17,583,936
<b>Total fund balances</b>	<b>126,068,393</b>	<b>184,836,093</b>	<b>114,531,180</b>	<b>64,362,153</b>	<b>489,797,819</b>
<b>Total liabilities and fund balances</b>	<b>\$ 191,742,489</b>	<b>216,784,277</b>	<b>115,078,772</b>	<b>124,449,406</b>	<b>648,054,944</b>

See accompanying notes to basic financial statements.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

**Reconciliation of the Governmental Funds Balance Sheet to the  
Statement of Net Assets**

June 30, 2003

Total fund balances – governmental funds	\$ 489,797,819
Amounts reported for governmental activities in the statement of net assets are different because:	
Capital assets used in governmental activities are not financial resources and therefore, are not reported as assets in governmental funds	927,764,941
Bond premium not recorded at fund level	(22,480,287)
Long-term liabilities, including bonds payable, are not due and payable in the current period and therefore, are not reported as liabilities in the funds	—
Long-term liabilities at year-end consist of:	
Bonds payable/notes payable/COP	(765,009,240)
Accrued interest on the bonds	(16,224,237)
Arbitrage liability	(5,736,720)
Claims and judgments payable	(50,101,486)
Accrued vacation payable	(13,658,907)
Total net assets – governmental activities	<u>\$ 544,351,883</u>

See accompanying notes to basic financial statements.



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Statement of Revenues, Expenditures, and Changes in Fund Balances – Governmental Funds

Year ended June 30, 2003

	<u>General Fund</u>	<u>Capital Projects – Proposition MM</u>	<u>Capital Projects – County School Facilities</u>	<u>Other Governmental Funds</u>	<u>Totals</u>
<b>Revenues:</b>					
Revenue limits sources:					
State apportionment	\$ 198,165,039	—	—	30,860,566	229,025,605
Property taxes	430,193,560	—	—	—	430,193,560
Revenue from federal sources	121,252,604	—	—	35,315,785	156,568,389
Revenue from other state sources:					
Special purpose apportionment	186,938,034	—	101,506,057	1,543,332	289,987,423
Lottery apportionment	15,561,019	—	—	845,639	16,406,658
Other state revenue	103,724,847	—	—	7,997,853	111,722,700
Interest	9,786,966	7,136,660	1,083,284	26,444,255	44,451,165
Cafeteria sales	—	—	—	11,285,729	11,285,729
Other local revenue	33,205,664	375,452	—	113,030,693	146,611,809
<b>Total revenues</b>	<u>1,098,827,733</u>	<u>7,512,112</u>	<u>102,589,341</u>	<u>227,323,852</u>	<u>1,436,253,038</u>
<b>Expenditures:</b>					
Certificated salaries	549,185,428	117,004	—	27,770,026	577,072,458
Classified salaries	172,504,369	3,408,152	—	28,609,429	204,521,950
Employee benefits	156,410,490	1,152,894	—	15,138,061	172,701,445
Books and supplies	63,500,259	122,958	4,235,927	19,984,257	87,843,401
Service and other operating	125,995,181	13,594,787	5,660	16,549,806	156,145,434
Capital outlay	7,425,123	276,617,597	8,315,438	19,222,219	311,580,377
Other outgo	26,788,703	—	—	10,643,417	37,432,120
Debt service:					
Principal	—	—	—	132,510,000	132,510,000
Interest and fiscal charges	—	—	—	31,834,021	31,834,021
<b>Total expenditures</b>	<u>1,101,809,553</u>	<u>295,013,392</u>	<u>12,557,025</u>	<u>302,261,236</u>	<u>1,711,641,206</u>
Excess (deficiency) of revenues over expenditures	<u>(2,981,820)</u>	<u>(287,501,280)</u>	<u>90,032,316</u>	<u>(74,937,384)</u>	<u>(275,388,168)</u>
<b>Other financing sources (uses):</b>					
Bond proceeds	—	274,995,345	—	19,125,000	294,120,345
Payment to bond escrow agent	—	—	—	(38,613,541)	(38,613,541)
Transfers in	34,013,742	—	—	16,050,520	50,064,262
Transfers out	(6,294,811)	—	—	(43,769,451)	(50,064,262)
<b>Total other financing sources (uses)</b>	<u>27,718,931</u>	<u>274,995,345</u>	<u>—</u>	<u>(47,207,472)</u>	<u>255,506,804</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	24,737,111	(12,505,935)	90,032,316	(122,144,856)	(19,881,364)
Fund balances at beginning of year	101,331,282	197,342,028	24,498,864	186,507,009	509,679,183
Fund balances at end of year	\$ <u>126,068,393</u>	<u>184,836,093</u>	<u>114,531,180</u>	<u>64,362,153</u>	<u>489,797,819</u>

See accompanying notes to basic financial statements.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

**Reconciliation of the Statement of Revenues,  
Expenditures, and Changes in Fund Balances of Governmental Funds  
to the Statement of Activities**

Year ended June 30, 2003

Net change in fund balances – total governmental funds	\$ (19,881,364)
Amount reported for governmental activities in the statement of activities are different because:	
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capitalized assets (\$301,655,237) exceeded depreciation (\$26,964,922) in the current period	274,690,315
Bond proceeds provide current financial resources to governmental funds, but issuing debt increases long-term liabilities in the statement of net assets. Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the statement of net assets. This is the amount by which proceeds (\$274,995,345) exceeded repayments (\$132,510,000)	(142,485,345)
Bond premiums provide current financial resources to governmental funds, but increase long-term liabilities in the statement of net assets	(12,104,117)
Some expenses reported in the statement of activities do not require the use of current financial resources and therefore, are not reported as expenditures in governmental funds (includes accrued interest payable)	<u>20,063,873</u>
Change in net assets of governmental activities	<u>\$ 120,283,362</u>

See accompanying notes to basic financial statements.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Statement of Fiduciary Net Assets

June 30, 2003

	<u>Agency Funds</u>
<b>Assets:</b>	
Cash on hand and in bank	\$ 5,867,995
Investments	659,825
Accounts receivable	116,919
Deposits/prepaid items	27,531
Inventory	295,544
Total assets	<u>\$ 6,967,814</u>
<b>Liabilities:</b>	
Accounts payable	\$ 100,523
Due to student groups	6,867,291
Total liabilities	<u>\$ 6,967,814</u>

See accompanying notes to basic financial statements.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

General Fund

Statement of Revenues, Expenditures, and Changes in Fund Balance – Budget and Actual

Year ended June 30, 2003

	<u>Original budget</u>	<u>Final budget</u>	<u>Actual</u>	<u>Variance – positive (negative)</u>
Revenues:				
Revenue limit sources:				
State apportionment	\$ 211,239,404	211,239,404	198,165,039	(13,074,365)
Local property taxes	<u>428,577,648</u>	<u>428,577,648</u>	<u>430,193,560</u>	<u>1,615,912</u>
Total revenue limit	<u>639,817,052</u>	<u>639,817,052</u>	<u>628,358,599</u>	<u>(11,458,453)</u>
Revenue from federal sources	108,495,168	147,993,154	121,252,604	(26,740,550)
Revenue from other state sources:				
Special purpose apportionment	194,147,623	195,813,294	186,938,034	(8,875,260)
Lottery apportionment	16,265,636	16,265,636	15,561,019	(704,617)
Other state revenue	<u>96,997,208</u>	<u>143,986,326</u>	<u>103,724,847</u>	<u>(40,261,479)</u>
Total other state revenue	<u>307,410,467</u>	<u>356,065,256</u>	<u>306,223,900</u>	<u>(49,841,356)</u>
Revenue from other local sources:				
Interest	9,411,462	10,079,731	9,786,966	(292,765)
Other local revenue	<u>49,107,204</u>	<u>40,733,414</u>	<u>33,205,664</u>	<u>(7,527,750)</u>
Total other local revenue	<u>58,518,666</u>	<u>50,813,145</u>	<u>42,992,630</u>	<u>(7,820,515)</u>
Total revenues	<u>1,114,241,353</u>	<u>1,194,688,607</u>	<u>1,098,827,733</u>	<u>(95,860,874)</u>
Expenditures:				
Certificated salaries	538,572,406	585,117,475	549,185,428	35,932,047
Classified salaries	159,047,658	184,883,020	172,504,369	12,378,651
Employee benefits	159,155,206	177,055,609	156,410,490	20,645,119
Books and supplies	159,493,306	123,460,058	63,500,259	59,959,799
Service and other operating	81,485,873	153,814,013	125,995,181	27,818,832
Capital outlay	9,228,005	10,044,006	7,425,123	2,618,883
Other outgo	<u>37,215,726</u>	<u>26,422,114</u>	<u>26,788,703</u>	<u>(366,589)</u>
Total expenditures	<u>1,144,198,180</u>	<u>1,260,796,295</u>	<u>1,101,809,553</u>	<u>158,986,742</u>
Excess (deficiency) of revenues over expenditures	<u>(29,956,827)</u>	<u>(66,107,688)</u>	<u>(2,981,820)</u>	<u>63,125,868</u>
Other financing sources (uses):				
Transfers in	5,521,353	37,904,844	34,013,742	(3,891,102)
Transfers out	<u>(6,953,600)</u>	<u>(11,504,517)</u>	<u>(6,294,811)</u>	<u>5,209,706</u>
Other uses	<u>3,858,918</u>	<u>2,514,620</u>	<u>—</u>	<u>(2,514,620)</u>
Total other financing sources (uses)	<u>2,426,671</u>	<u>28,914,947</u>	<u>27,718,931</u>	<u>(1,196,016)</u>
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	<u>\$ (27,530,156)</u>	<u>(37,192,741)</u>	24,737,111	<u>61,929,852</u>
Fund balance – June 30, 2002			<u>101,331,282</u>	
Fund balance – June 30, 2003			\$ <u>126,068,393</u>	

See accompanying notes to basic financial statements.

# SAN DIEGO UNIFIED SCHOOL DISTRICT

## Notes to Basic Financial Statements

June 30, 2003

### (1) Summary of Significant Accounting Policies

The accounting policies of the San Diego Unified School District (the District) conform to accounting principles generally accepted in the United States of America as applicable to governmental units. The District also accounts for its financial transactions in accordance with policies and procedures of the Department of Education's California School Accounting Manual. The following is a summary of the more significant accounting policies.

#### (a) Reporting Entity

The District's basic financial statements include the operations of all organizations for which the Board of Education (the Board) exercises oversight responsibility. Oversight responsibility is demonstrated by financial interdependency, selection of governing authority, designation of management, ability to significantly influence operations, and accountability for fiscal matters.

The San Diego Unified School District Public School Building Corporation (the Corporation), formed in 1974 to finance properties leased by the District, has had a financial and operational relationship which meets the reporting entity definition criteria of the Governmental Accounting Standards Board (GASB) for inclusion of the Corporation as a blended component unit of the reporting entity. The Corporation ceased operations during fiscal year 2003, and transferred its net assets to the District or to its trustee to fund the retirement of its outstanding debt. Separate financial statements for the Corporation may be obtained at the District's administrative offices.

The Corporation is a nonprofit, public benefit corporation incorporated under the laws of the state of California and recorded by the Secretary of State on December 23, 1974. The Corporation was formed to provide financing assistance to the District for construction and acquisition of major capital facilities. The District currently occupies all completed Corporation facilities and, upon completion, intends to occupy all Corporation facilities under construction under lease purchase agreements. At the end of the lease terms and open dissolution of the Corporation, title to all Corporation property passed to the District for no additional consideration.

The Corporation's financial activity is presented in the accompanying basic financial statements as the Corporation Debt Service Fund and the Corporation Building Fund, which are combined with the District's Debt Service Funds and Capital Projects Funds, respectively. Certificates of Participation (COPs) issued by the Corporation are included in the debt of the District. Capital assets acquired or constructed by the Corporation are included in the capital assets of the District.

In fiscal year 2002, all charter schools were blended into the District's financials. In fiscal year 2003 it was determined that six charter schools which are incorporated under 501(c)(3) did not fall under the District's oversight and, so, were not blended into the District's financial information. This resulted in a restating of the 2003 beginning fund balance in the amount of \$55,812 which equals the 2002 ending fund balance for these six charter schools.

# SAN DIEGO UNIFIED SCHOOL DISTRICT

## Notes to Basic Financial Statements

June 30, 2003

**(b) Basis of Presentation – Government-Wide and Fund Financial Statements**

The statement of net assets and the statement of activities are government-wide financial statements. They report information on all of the District's nonfiduciary activities including its blended component unit with most of the interfund activities eliminated. Governmental activities include programs supported primarily by taxes, state funding, and other intergovernmental revenues.

The statement of activities demonstrates how other people or entities that participate in programs the District operates have shared in the payment of the direct costs. The program revenues include charges for services and operating grants and contributions. The charges for services include payments made by parties that purchase, use, or directly benefit from goods or services provided by a given function or segment of the District. The charges for services include fees charged by the Child Development Centers for childcare services and charges for reduced and full costs of student meals. The grants and contributions revenues include amounts paid by organizations outside the District to help meet the operational or capital requirements of a given function. If revenue is not labeled as a program revenue, it is a general revenue used to support all of the District's functions. Taxes are always general revenues.

The District reports all direct expenses by function in the statement of activities. Direct expenses are those clearly identifiable with a function. Indirect expenses of other functions are not allocated to those functions but are reported separately in the statement of activities. Depreciation expense is specifically identified by function and is included in the direct expense to each function. Interest on general long-term debt is considered an indirect expense and is reported separately on the statement of activities.

Interfund activities between governmental funds appear as due to/due from on the governmental Fund balance sheet. All interfund transactions between governmental funds are eliminated on the government-wide statements. Interfund activities between governmental funds and fiduciary funds remain as due to/due from on the government-wide statement of activities.

The fund financial statements provide reports on the financial condition and results of operations for governmental and fiduciary categories. The District does not have proprietary or business type activities. Since the resources in the fiduciary funds cannot be used for District operations, they are not included in the government-wide statements. Major individual governmental funds are reported as separate columns in the fund financial statements.

**(c) Basis of Accounting**

The modified-accrual basis of accounting is followed by the Governmental Funds. Under the modified-accrual basis of accounting, revenues are recorded when they become measurable and available to pay liabilities of the current period. Revenues not considered available are recorded as deferred revenue. Expenditures are recorded when the liability is incurred, except for interest on general long-term obligations which are recorded when due.

## SAN DIEGO UNIFIED SCHOOL DISTRICT

### Notes to Basic Financial Statements

June 30, 2003

In applying the susceptible-to-accrual concept to intergovernmental revenue, there are essentially two types of revenue. In one, monies must be expended on the specific purpose or project before any amounts will be paid to the District; therefore, revenue is recognized based upon the expenditures incurred. In the other, monies are virtually unrestricted and are usually revocable only for failure to comply with prescribed compliance requirements. These resources are reflected as revenue at the time of receipt or earlier if the susceptible-to-accrual criteria are met. Revenue that is accrued includes interest and state and federal grants.

The government-wide financial statements are accounted for on a flow of economic resources measurement focus and utilize the accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. With this measurement focus, all assets and all liabilities associated with the operation of these funds are included on the fund statement of net assets. The fund equity is segregated into the following three categories: 1) invested in capital assets net of related debt, 2) restricted net assets, and 3) unrestricted net assets. As a general rule, the effect of interfund activity has been eliminated from government-wide financial statements.

The Agency funds are unbudgeted funds that account for activities of student groups. These funds have no equity, and assets are equal to liabilities and do not include revenues and expenditures for general operations of the District.

#### **Governmental Funds**

Governmental funds are used to account for the District's expendable financial resources and the related liabilities. The measurement focus is based upon determination of changes in financial position. The following are the District's major governmental funds:

General Fund – The General Fund is the general operating fund of the District. It is used to account for all financial resources except those required to be accounted for in another fund. The General Fund includes certain funds, which the District reports separately on its Unaudited Actuals Financial Report (SACS Format). The General Fund includes the General Fund, Property Insurance Fund, Workers' Compensation Fund, Medical and Dental Fund, Liability Insurance Fund, State Instructional Materials Revolving Fund, and Stores Revolving Fund.

County School Facilities Capital Projects Fund – This fund is used to account for financial resources to be used for the acquisition or construction of major capital assets (other than those financed by Special Revenue Funds or the Proposition MM Building Fund).

Proposition MM Building Capital Projects Fund – This fund is used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by Special Revenue Funds or the Corporation).

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**Fiduciary Fund Type**

Agency Funds – Agency funds are used to account for the assets of others for which the District acts as an agent. The District maintains Agency funds for each school’s student body funds. These Agency funds are combined for financial statement purposes as the Associated Student Body Fund.

**(d) Capital Assets**

Capital assets, which include land, buildings, furniture, and equipment, are reported in the governmental column in the government-wide financial statements. Capital assets are generally defined by the District as assets with an initial, individual cost of more than \$5,000 and an estimated useful life in excess of two years and building improvements with an initial cost of more than \$100,000. Such assets are recorded at historical cost or estimated historical cost if purchased or constructed. Donated capital assets are recorded at estimated fair market value at the date of donation. Capital assets are recorded as capital outlay expenditures in the governmental funds.

The costs of normal maintenance and repairs that do not add to the value of the asset or materially extend assets lives are not capitalized. Major outlays for capital assets and improvements are capitalized as projects are constructed.

Buildings, furniture, and equipment of the District are depreciated using the straight-line method over the following estimated useful lives:

Assets	Years
Buildings	50
Portable buildings	25
Building improvements	50
Land improvements	20
Vehicles	6
Equipment	5 to 15

**(e) Cash, Cash Equivalents, and Investments**

The District’s cash and cash equivalents are considered to be cash on hand, demand deposits, and amounts held in the San Diego County Treasury. The District considers investments with maturities of three months or less at date of acquisition to be cash equivalents. Investments with maturities greater than three months at date of acquisition are considered long-term investments.

Investments are reported at fair value on the balance sheet, except that certain money market investments may be carried at amortized cost provided the investment has a remaining maturity of one year or less at the time of purchase. Additionally, all investment income, including changes in the fair value of investments, is reported as revenue in the operating statement.

**(f) Restricted Assets**

Restricted assets are those assets attributable to funds which have restrictions on spending imposed by outside agencies.



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(g) Inventory**

Inventory is valued at average cost, which approximates the first-in, first-out method. The cost of inventory is recorded as an expenditure at the time individual inventory items are consumed (consumption method). Reported governmental fund inventories are equally offset by a reservation of fund balance which indicates that these amounts are not "available for appropriation and expenditure," even though they are a component of assets.

**(h) Deferred Revenue**

Federal, state, and local grant revenues are recorded as revenues when earned. The District considers grant revenues earned when expenditures made under provisions of grants were incurred. Funds received and not earned are recorded as deferred revenue until earned. The District has received \$21,142,886 of federal, state, and local revenue for which expenditures have not been made by the end of the fiscal year; \$20,513,775 of this revenue has been deferred in the General Fund and will be recognized as revenue when allowable expenditures are incurred.

The District has \$629,111 of deferred revenue attributable to the Special Revenue Funds, including \$302,285 relating to the Property Management Fund representing lease revenue received in advance and \$326,826 relating to Charter Schools representing state and federal grant funds that have not been earned by incurring allowable expenditures.

**(i) Accumulated Vacation and Sick Leave Benefits**

Accumulated unpaid employee vacation benefits are recognized as liabilities of the District. All accumulated vacation is accrued in the government-wide financial statements. A liability for these amounts is only reported in the governmental funds if it has matured.

Accumulated sick leave benefits are not recognized as liabilities of the District. The District's policy is to record sick leave as an operating expenditure in the period taken. For classified employees employed prior to July 1, 1980, unused sick leave is added to the creditable service period for calculation of retirement benefits when the employee retires. For persons employed after July 1, 1980, each employee will receive 0.004 year of service credit for each day of unused sick leave if he or she retires after January 1, 1999.

**(j) Claims and Judgments**

For financial statement purposes, the District accrues claims and judgments payable in the government-wide financial statements. A liability for these amounts is only reported in the governmental funds if it has matured.

**(k) Long-Term Liabilities**

In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the statement of net assets. Bond premiums and discounts as well as issuance costs are deferred and amortized over the life of the bonds using the effective-interest method. Bonds payable are reported net of applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

## SAN DIEGO UNIFIED SCHOOL DISTRICT

### Notes to Basic Financial Statements

June 30, 2003

In the fund financial statements, governmental funds recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of the debt issued, premiums, or discounts is reported as other financing sources/uses.

**(l) Fund Balances and Net Assets**

In the fund financial statements, governmental funds report reservations of fund balances for amounts that are not available for appropriations or are legally restricted by outside parties for use for a specific purpose. Designations of fund balances represent tentative management plans that are subject to change.

**(m) Budgets and Budgetary Accounting**

The District follows these procedures in establishing the budgetary data reflected in the basic financial statements.

By state law, the District's Board must approve a budget for all funds no later than July 1. A public hearing must be conducted to receive comments prior to adoption. The District's Governing Board has satisfied these requirements.

The budget is revised by the District's Board of Education during the year to give consideration to unanticipated revenue and expenditures. It is this final revised budget that is presented in the basic financial statements.

Formal budgetary integration was employed as a management control device during the year for all budgeted funds.

The following were the major changes between the original and amended budget for the General Fund only:

- Revenues that were received during the year that were not included in the originally adopted budget – federal grants and special projects of \$39.0 million and state grants and special projects of \$49.0 million.
- The increase in expenditure budgets for certificated salaries of \$47.0 million, classified salaries of \$26.0 million, employee benefits of \$18.0 million were appropriated using the \$39.0 million in extra. Federal grants and \$47.0 million in extra state grants and special projects funding adopted during the year. The increase in Services and other operating expense of \$72.0 million can be attributed to \$27.0 million in transfers made between major accounts such as books and supplies to salaries and benefits accounts, \$21.0 million in grants and special projects received and appropriated during the year and \$23.0 million the District received from the release of COP reserves that were appropriated in the Service and other operating account to support the implementation of the district wide application.
- Decrease in expenditure budget due to transfers made to realign the budget between major object categories – books and supplies of \$36.0 million.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(n) District Revenues**

The District's major revenue sources are listed below:

- State apportionments, which consist of state revenue received, based on Average Daily Attendance (ADA).
- Special purpose apportionments, which consist of state revenue for specific uses, such as one-time apportionments based on the availability of state funding. The special purpose apportionment attributable to the County School Facilities fund represents monies received from the School Facility Program Fund, Office of Public School Construction.
- Local property taxes, which consist of secured property taxes payable from the County of San Diego to the District in two installments by December 15 and April 15. The majority of unsecured property taxes is payable by September 30. The County collects the taxes and remits 100% of the amount owed to the District. The County takes full responsibility for delinquent payments and is ultimately responsible for collection.

Revenues received from Operating Grants are allocated to function based on the percentage of expenses in each function. All functions have their proportionate share of revenue from general operating grants allocated to them. In addition, capital operating grants are allocated to plant services and other outgo functions based on their proportionate expenses.

**(o) Encumbrances**

Encumbrance accounting is utilized for budgetary control purposes. Encumbrances outstanding at year end are reported as part of the reserved fund balance since they do not constitute expenditures or liabilities. Encumbrances outstanding at year-end for unfulfilled obligations of the current year budget are re-appropriated in the succeeding year.

**(2) Deposits and Investments**

**(a) Bank Deposits**

A summary of deposits at June 30, 2003 is as follows:

	<b>Bank balance</b>	<b>Carrying amount</b>
Deposits:		
Cash in county treasury	\$ 449,185,148	449,185,148
Cash on hand and in bank	8,274,851	7,293,902
Cash with fiscal agent	50,000	50,000
	<b>\$ 457,509,999</b>	<b>456,529,050</b>

State statutes require that all deposits be insured or collateralized. Depositories holding public funds on deposit are required to maintain collateral in the form of a pool of securities with the agent of the depository having a market value of at least 10% to 50% in excess of the total amount of all public funds on deposit.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

The District's bank deposits at year-end included \$100,000 covered by federal depository insurance, and the remaining balance is covered by collateral held by the District's custodial banks as part of their local agency and public deposits with the collateral registered in the name of "Administrator of Local Agency Security."

In accordance with Education Code Section 41001, the District maintains substantially all of its cash in the San Diego County Treasury. The County pools these funds with those of other districts in the County and invests the cash. These pooled funds are carried at cost, which represents their contract value to the District. Interest earned is deposited quarterly into participating funds. Any investment losses are proportionately shared by all funds in the pool.

Monies invested in derivatives through the County investment pool are considered immaterial.

**(b) Investments**

The District categorizes investments according to the level of risk assumed by the District. Category one includes investments that are insured, registered, or held by the District's agent in the District's name. The summary below identifies the level of risk assumed by the District and the total carrying amount of the District's investments:

	<u>Category one</u>	<u>Uncategorized</u>	<u>Total investments</u>
Money market funds	\$ —	414,200	414,200
United States Treasury obligations	245,625	—	245,625
Other United States government obligations	—	3,171,656	3,171,656
Guaranteed investment contract	—	10,552,594	10,552,594
Total	<u>\$ 245,625</u>	<u>14,138,450</u>	<u>14,384,075</u>

The majority of the District's variable rate instruments are federal agency securities (AAA rated) with minimal credit risk. Although variable securities have market fluctuations that are greater than nonvariable instruments, all securities held in the portfolio should receive full par value at maturity.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(3) Receivables and Payables**

**(a) Receivables**

Receivables at June 30, 2003 were as follows:

	<u>Interest</u>	<u>Due from other government agencies</u>	<u>Local other</u>	<u>Total receivables</u>
Governmental Activities:				
General Fund	\$ 556,766	75,303,393	13,553,222	89,413,381
Prop MM	1,164,854	—	—	1,164,854
County School Facilities	428,492	19,488,059	—	19,916,551
Other governmental funds	468,466	16,284,612	476,206	17,229,284
Total governmental activities	<u>\$ 2,618,578</u>	<u>111,076,064</u>	<u>14,029,428</u>	<u>127,724,070</u>

**(b) Payables**

Payables at June 30, 2003 were as follows:

	<u>Vendors</u>	<u>Payroll and deductions</u>	<u>Other</u>	<u>Total payables</u>
Governmental Activities:				
General Fund	\$ 17,916,228	20,351,204	4,277,836	42,545,268
Prop MM	20,523,426	—	—	20,523,426
County School Facilities	504,622	—	—	504,622
Other governmental funds	3,022,380	—	3,495,971	6,518,351
Total governmental activities	<u>\$ 41,966,656</u>	<u>20,351,204</u>	<u>7,773,807</u>	<u>70,091,667</u>

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(4) Interfund Receivables, Payables, and Transfers**

Interfund receivables and payables balances at June 30, 2003 are as follows:

	<b>Due from</b>	<b>Due to</b>
General Fund:	\$ 39,171,382	\$ 2,615,053
Special Revenue Funds:		
Child Development	42,876	3,243,690
Adult Education	24	109,086
Deferred Maintenance	11,091,871	12,596,233
Pupil Transportation	218,109	—
Property Management	31,885	1,518,936
Cafeteria	—	6,009,864
Balboa Stadium	—	170
Charter Schools	4,072	8,271,175
Debt Service Funds:		
Pre-Field Tax Override	—	2,215
Prop XX Tax Override	—	2,090,473
Capital Projects Funds:		
Prop O/Preconstruction Costs	2,527,074	4,327,480
Capital Facilities III	899	844,564
Prop MM Building	8,475	11,424,758
County School Facilities	—	42,970
	\$ 53,096,667	\$ 53,096,667

***Interfund Transfers***

Interfund transfers consist of operating transfers from the fund receiving revenue to the fund through which the resources are to be expended.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

Interfund transfers for the 2002-2003 fiscal year were as follows:

Transfer from the Facilities Master Plan – Prop O to the General Fund to comply with Restricted Maintenance account requirements	\$ 842,891
Transfer from the General Fund to the Pupil Transportation Fund for replacement bus purchases	1,290,191
Transfer from the Property Management Fund to the General Fund for Hage’s Gateway Program	5,034
Transfer from the Property Management Fund to the General Fund for Wangenheim’s Gateways Program	10,518
Transfer from the Facilities Master Plan – Prop O to the General Fund to fund the District Wide Application (DWA) project	27,000,000
Transfer from the Facilities Master Plan – Prop O to the General Fund to comply with Prop 1A Restricted Maintenance Account requirements	3,312,839
Transfer from the Property Management Fund to the Facilities Master Plan – Prop O	450,000
Transfer from the Prop XX Tax Override Fund to the Facilities Master Plan – Prop O for Prop XX, Prop Y and Prop O defeasance completed in May 2003	2,077,074
Transfer from the Property Management Fund to the General Fund	1,212,206
Transfer from Energy Efficiency Program to Facilities Master Plan – Prop O for remaining balance in the 1996I Certificate Reserve Account	10,596
Transfer from the General Fund to Deferred Maintenance to reimburse General Fund for expenses paid on their behalf	4,550,917
Transfer from Public School Building Corporation to the General Fund representing excess reserve requirement refunds and release of reserves due to defeasance	1,630,254
Transfer from the General Fund to the Public School Building Corporation to meet to meet rebate reserve requirements	453,703
Transfer from the Public School Building Corporation – Capital Projects to the Public School Building Corporation – Debt Service to meet rebate reserve requirements	<u>7,218,039</u>
	<u>\$ 50,064,262</u>

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(5) Reserved Fund Balances**

Reservations of fund balance indicate the portions of fund balance not appropriate for expenditure or amounts legally segregated for a specific future use:

	General Fund	Capital Projects		Other Governmental Funds	Total
		Fund – Proposition MM	Fund – County School Facilities		
Revolving cash	\$ 66,250	—	—	50,500	116,750
Pre-field loan repayments	—	—	—	138,374	138,374
Debt service	—	—	—	274,552	274,552
Claims and judgments	14,718,846	—	—	—	14,718,846
Self-insurance fund balances	13,631,669	—	—	—	13,631,669
Encumbrances	38,053,703	111,729,969	1,792,021	4,025,926	155,601,619
State programs	41,564,711	—	—	—	41,564,711
Inventory and prepaid expenditures	1,911,853	—	—	937,049	2,848,902
	<u>\$ 109,947,032</u>	<u>111,729,969</u>	<u>1,792,021</u>	<u>5,426,401</u>	<u>228,895,423</u>

**(6) Capital Assets**

The following is a summary of changes in capital assets for the year ended June 30, 2003:

	Balance at June 30, 2002	Increases	Decreases	Balance at June 30, 2003
Site	\$ 56,046,882	55,874,529	—	111,921,411
Construction in progress	193,267,916	241,537,240	(68,207,165)	366,597,991
Total capital assets not being depreciated	<u>249,314,798</u>	<u>297,411,769</u>	<u>(68,207,165)</u>	<u>478,519,402</u>
Site improvements	82,908,303	23,576,039	—	106,484,342
Building and building improvements	503,675,517	44,631,127	(871,900)	547,434,744
Equipment	134,616,693	4,243,467	(2,550,184)	136,309,976
Total capital assets being depreciated	<u>721,200,513</u>	<u>72,450,633</u>	<u>(3,422,084)</u>	<u>790,229,062</u>
Less accumulated depreciation for:				
Site improvements	(42,940,613)	(4,734,816)	—	(47,675,429)
Buildings and building improvements	(171,064,690)	(11,373,395)	187,030	(182,251,055)
Equipment	(102,750,512)	(10,856,711)	2,550,184	(111,057,039)
	<u>(316,755,815)</u>	<u>(26,964,922)</u>	<u>2,737,214</u>	<u>(340,983,523)</u>
Total	<u>\$ 653,759,496</u>	<u>342,897,480</u>	<u>(68,892,035)</u>	<u>927,764,941</u>



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

For fiscal year 2002/2003, the District had capital outlay expenses of \$311,580,377. Of this amount, \$301,655,237 was capitalized. The remaining \$9,925,140 represented assets with costs below the established thresholds for capitalization which were expensed.

Commencing in fiscal year 1990-91, the Corporation began construction on various public school building projects. Construction was completed in fiscal year 2002-03. Interest costs incurred during the construction phase of the projects have been capitalized. Total interest costs incurred during the year ended June 30, 2003 by the Corporation were \$3,662,110, of which \$256,949 has been capitalized. Commencing in fiscal year 1999-2000, the District began construction on various Proposition MM school building projects. Construction is expected to continue through 2008-09.

Depreciation expense was charged to governmental functions as follows:

Instruction	\$	14,380,576
Instructional-related services		2,731,252
Pupil services		6,550,731
Ancillary services		560
General administration		754,311
Plant services		<u>2,547,492</u>
Total depreciation expense	\$	<u><u>26,964,922</u></u>

**(7) Long-Term Liabilities**

The following is a summary of changes in the District's long-term liabilities for the year ended June 30, 2003:

	<u>Balance at June 30, 2002</u>	<u>Additions</u>	<u>Reductions</u>	<u>Balance at June 30, 2003</u>	<u>Due in one year</u>
Claims and judgments	\$ 43,963,602	34,911,411	(28,773,527)	50,101,486	14,718,846
Accrued vacation	14,327,841	—	(668,934)	13,658,907	11,336,892
Arbitrage liability	6,379,426	—	(642,706)	5,736,720	2,972,551
Bonded debt	489,989,881	274,995,346	—	764,985,227	—
State school building loans	31,364	—	(7,351)	24,013	6,126
Certificates of participation	162,790,000	—	(162,790,000)	—	—
<b>Total</b>	<u>\$ 717,482,114</u>	<u>309,906,757</u>	<u>(192,882,518)</u>	<u>834,506,353</u>	<u>29,034,415</u>

**(8) General Obligation Bonds**

Under Proposition MM, which was approved by eligible voters on November 3, 1998, the District is authorized to issue general obligation bonds in an amount not to exceed \$1,510,000,000 for the purposes of repairing and improving deteriorating schools. These general obligation bonds are direct obligations and are secured by a pledge of the full faith and credit of the District. The revenue for the retirement of such bonds is provided by ad valorem taxes on property within the jurisdiction of the District.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

At June 30, 2003, the following bonds are outstanding:

<u>Series</u>	<u>Maturity date</u>	<u>Interest rates</u>	<u>Original principal amount</u>	<u>Principal balance outstanding</u>
Series 1999A	2023	5.00% – 12.00%	\$ 139,995,085	139,995,085
Series 2000B	2025	4.42% – 6.875%	149,999,084	149,999,084
Series 2001C	2026	4.00% – 5.00%	199,995,712	199,995,712
Series 2002D	2027	4.00% – 5.25%	274,995,346	274,995,346
Totals			<u>\$ 764,985,227</u>	<u>764,985,227</u>

No principal amounts are due within one year. Debt service requirements for the bonds are as follows:

	<u>Principal amount</u>	<u>Interest amount</u>	<u>Total payments</u>
Fiscal year ending June 30:	\$		
2004	—	27,851,809	27,851,809
2005	25,939,007	36,812,802	62,751,809
2006	21,551,197	36,840,612	58,391,809
2007	17,062,429	35,894,380	52,956,809
2008-2012	66,213,908	186,879,736	253,093,644
2013-2017	105,092,399	195,010,832	300,103,231
2018-2022	191,359,017	168,741,238	360,100,255
2023-2028	337,767,270	88,523,918	426,291,188
Totals	<u>\$ 764,985,227</u>	<u>776,555,327</u>	<u>1,541,540,554</u>

The 1999A bonds are not subject to early redemption. The 2000B current interest bonds maturing July 1, 2018 and July 1, 2019 and capital appreciation bonds are not subject to early redemption. The 2000B current interest bonds maturing on July 1, 2016 and July 1, 2017 and on or after July 1, 2020 are subject to redemption prior to maturity beginning in 2010 without premiums. The 2001C capital appreciation bonds are not subject to early redemption. The 2001C current interest bonds maturing on or after July 1, 2013 are subject to redemption prior to maturity beginning in 2011 at premiums ranging from 0% to 2%. The 2002D current interest bonds maturing on or after July 1, 2013 through and including July 1, 2016 and the term bond maturing July 1, 2027 shall be subject to redemption prior to their respective stated maturity dates beginning July 1, 2012 without premiums. The 2002D current interest bonds maturing July 1, 2017 through and including July 1, 2025 shall be subject to redemption prior to their respective stated maturity dates beginning July 1, 2012 at premiums ranging from 0% to 1.5%. The capital appreciation bonds and current interest bonds maturing on or before July 1, 2012 are not subject to redemption.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(9) State School Building Loans**

The following is a summary of the state school building loans activity of the District for the year ended June 30, 2003:

<u>Series</u>	<u>Interest rate</u>	<u>Outstanding at June 30, 2002</u>	<u>Principal payments 2002 - 2003</u>	<u>Outstanding at June 30, 2003</u>
1981 - 1982	4.8% - 5.3%	\$ 1,505	1,505	—
1983 - 1984	4.8%	11,027	3,518	7,509
1987 - 1988	4.8%	18,832	2,328	16,504
		<u>\$ 31,364</u>	<u>7,351</u>	<u>24,013</u>

The state school building loans are secured by all sites purchased and improved, all equipment purchased, and all buildings constructed, reconstructed, altered, or added-to, through the expenditure of such funds in accordance with Section 16019 of the Education Code. State school building loans are repayable with interest to the state over a 20-year period as determined by the State Controller in accordance with Section 16335 of the Education Code. Annual repayment amounts are determined by the State Controller in accordance with Section 16214 of the Education Code. Interest paid during fiscal year 2003 was \$1,509.

**(10) Certificates of Participation**

During the year ended June 30, 2003, Certificates of Participation (COP) amounting to \$132,510,000 were repaid or defeased. The District repaid COPs with a trustee in the amount of \$31,167,362, which is sufficient to repay, when due, the remaining COPs outstanding, amounting to \$30,280,000 at June 30, 2003.

**(11) Tax and Revenue Anticipation Notes**

On July 2, 2002, the District sold \$210,000,000 of tax-exempt Tax and Revenue Anticipation Notes at a rate of 3.00% maturing on July 28, 2003. The principal of the notes, together with the interest thereon, is payable from taxes, revenue, and other monies received by the District during fiscal year 2002-03.

As of June 30, 2003, the District has transferred all required principal and interest on the notes to an irrevocable trust fund maintained by the San Diego County Treasury. The District does not reflect a liability for the notes at June 30, 2003, as the necessary amounts to repay the notes have been funded and, as such, are not expendable funds of the District. The tax-exempt notes were repaid in full on July 28, 2003.

**(12) Risk Management**

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. In accordance with Section 39602 of the Education Code, the District has established self-insurance programs for workers' compensation, property insurance, and liability insurance. Funding for the programs is derived from employee salary rate charges, transfers at predetermined rates from other funds, and from interest earned on daily cash balances. Funds are used for the settlement of claims and for management provided by a contracted insurance

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

management firm. The District self-insures for the first \$500,000 per occurrence on workers' compensation claims; the first \$150,000 per occurrence of property claims; and the first \$150,000 per occurrence on liability claims. The District is covered up to \$10.0 million by an excess liability policy with commercial insurance corporations for any claims in excess of the above amounts. This level of coverage has been maintained for the past three fiscal years. Settled claims have not exceeded this commercial coverage in any of the past three fiscal years.

Claims expenditures and liabilities are reported when it is probable that a loss has occurred and the amount of that loss can be reasonably estimated. These losses include an actuarially determined estimate of claims that have been incurred but not reported. At June 30, 2003, claims outstanding including those incurred but not reported against the District are \$50,101,486. Changes in the balances of claims liability during fiscal years 2000-2001, 2001-2002, and 2002-2003 were as follows:

	<u>Beginning-of fiscal-year liability</u>	<u>Current-year claims and changes in estimates</u>	<u>Claim payments</u>	<u>Balance at fiscal year-end</u>
2000-2001	\$ 28,724,478	28,342,801	(23,042,584)	34,024,695
2001-2002	34,024,695	32,325,073	(22,386,166)	43,963,602
2002-2003	43,963,602	34,911,411	(28,773,527)	50,101,486

The District provides medical coverage through its membership in the Southern California Schools Voluntary Employee Benefits Association (VEBA). VEBA is a nonprofit labor-management employee benefits trust pool currently operating as a common risk management and insurance program for its members. The District pays an annual premium to VEBA for its medical coverage. The District's agreement with VEBA provides that VEBA will be self-sustaining through member premiums. VEBA reinsures with commercial medical insurance providers.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(13) Contractual Labor Commitments**

The District negotiates with five separate labor groups. These groups and the employees they represent are as follows:

<u>Labor group</u>	<u>District employees represented</u>
San Diego Education Association (SDEA)	Teachers and all other nonmanagement certificated employees of the District
California School Employees' Association (CSEA – OTBS)	Office-technical and business services employees
California School Employees' Association (CSEA – Paraeducators)	Paraeducators
California School Employees' Association (CSEA – OSS)	Transportation, building services, construction, maintenance, and food service employees
Peace Officers' Association	Security employees

The District has signed contracts with SDEA and CSEA-OTBS through June 30, 2006 and with the Paraeducators through June 30, 2004. The District has reached a tentative agreement with the CSEA-OSS Unit. The contract with the Peace Officers' Association expired on June 30, 2003. Negotiations with this employee group are ongoing.

**(14) Pension Plans**

Qualified employees are covered under multiple-employer defined benefit retirement plans maintained by agencies of the state of California. Certificated employees are members of the State Teachers' Retirement System, and classified employees are members of the California Public Employees' Retirement System.

**(a) California Public Employees' Retirement System**

**Plan Description**

The District contributes to the School Employer Pool under the California Public Employees' Retirement System (CalPERS), a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalPERS. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit provisions are established by state statutes, as legislatively amended, within the Public Employees' Retirement Law. CalPERS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS annual financial report may be obtained from the CalPERS Executive Office – 400 P Street – Sacramento, CA 95814.

**Funding Policy**

Active plan members are required to contribute 7.0% of their salary (7% of monthly salary over \$133.33 if the member participates in Social Security prior to January 1, 2002). The actuarial methods and assumptions used for determining the rate are those adopted by the CalPERS board of administration. The District contribution was made on behalf of the Peace Officers' Association, which requires a District contribution of 3.5% of the plan member's salary. The contribution

## SAN DIEGO UNIFIED SCHOOL DISTRICT

### Notes to Basic Financial Statements

June 30, 2003

requirements of the plan members are established by state statute. The District's contributions to CalPERS for the fiscal years ended June 30, 2003, 2002, and 2001 were \$6,254,990, \$555,015, and \$411,185, respectively, and equal 100% of the required contributions for each year.

#### **(b) State Teachers' Retirement System**

##### **Plan Description**

The District contributes to the State Teachers' Retirement System (STRS), a cost-sharing, multiple-employer, public employee retirement system defined benefit pension plan administered by STRS. The plan provides retirement, disability, and survivor benefits to beneficiaries. Benefit provisions are established by state statutes, as legislatively amended, within the State Teachers' Retirement Law. STRS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the STRS annual financial report may be obtained from the STRS – 7667 Folsom Boulevard – Sacramento, CA 95826.

##### **Funding Policy**

Active plan members are required to contribute 8% of their salary and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the STRS Teachers' Retirement Board. The required employer contribution rate for the fiscal year 2001-2002 was 8.25% of annual payroll. The contribution requirements of the plan members are established by state statute. The District's contributions to STRS for the fiscal years ended June 30, 2003, 2002, and 2001 were \$46,931,179 (including charter school contributions; \$46,671,711 excluding charter school contributions), \$43,165,923 (including charter school contributions; \$42,961,820 excluding charter school contributions), and \$42,346,058, respectively, and equal 100% of the required contributions for each year. The pension liability at adoption was determined in accordance with GASB Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers*. The pension liability was \$0 both before and after implementation.

#### **(15) Postretirement Health Care**

In addition to the pension benefits described in note 14, the District provides postretirement health care benefits to employees who retire from the District and meet certain age and service requirements. The provisions and obligations to contribute are established through collective bargaining agreements between the District and various unions.

Currently, 1068 retirees meet those eligibility requirements. The District's contributions are advance funded each year based on an amount arrived at through union negotiations. The amount to be deposited is calculated using a base amount, plus cost-of-living increases, less any advance deposits made in the prior year. The contributions are deposited into a fund designated to account for District monies used to reduce medical contributions paid by retirees participating in a District-sponsored group medical plan for medical insurance. Contributions of approximately \$1,090,642 were deposited in the General Fund in the current year for postretirement health care costs.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Basic Financial Statements

June 30, 2003

**(16) Commitments and Contingencies**

**(a) State and Federal Audits**

The District has received state and federal funds for specific purposes that are subject to review and audit by the grantor agencies. Such audits could generate expenditure disallowances under the terms of the grants. The District is presently undergoing an audit by the National Science Foundation (NSF) of the Urban System Initiative Grant program which is funded by the NSF. While the ultimate outcome of the audit is not known, the Inspector General of the NSF has issued a draft report which questions the allowability of approximately \$8.5 million of costs claimed and reimbursed by the NSF for the period from 1996 to 2002.

**(b) Construction**

Various construction contracts were in progress at June 30, 2003 with an estimated cost to complete of approximately \$111,937,000. The District expects all construction costs to be adequately covered from the proceeds of general obligation bonds.

**(c) Litigation**

The District is a named defendant in lawsuits arising in the ordinary course of business. In the opinion of management based in part on advice from legal counsel, the District has recorded a liability sufficient to cover probable losses on the various claims.

**(17) Subsequent Event**

On August 19, 2003 the District issued 2003 General Obligation bonds, Election 1998, Series E in the amount of \$349,993,599. The interest and yield rates range from 4.3% - 5.25% and 1.9% - 4.73%, respectively.

**SUPPLEMENTARY INFORMATION**



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Combining Balance Sheet – Other Governmental Funds

June 30, 2003

	Special Revenue							
	Child Development	Adult Education	Deferred Maintenance	Pupil Transportation Equipment	Property Management	Cafeteria Account	Balboa Stadium	Charter Schools
<b>Assets</b>								
Cash in county treasury	4,770,411	510,081	1,984,626	2,725,092	2,905,525	1,200,499	17,083	20,141,830
Cash on hand and in bank	500	—	—	—	—	347,593	—	—
Cash with fiscal agent	—	—	—	—	—	—	—	50,000
Short-term investments	614,298	368,132	300,000	—	—	11,269,985	—	2,515,039
Accounts receivable:	38,227	2,207	7,161	121,652	13,020	359,261	72	97,211
Federal and state government	42,876	24	11,091,871	218,109	31,885	—	—	4,072
Other	—	—	—	—	—	937,049	—	—
Due from other funds	—	—	—	—	—	—	—	—
Inventory	—	—	—	—	—	—	—	—
<b>Total assets</b>	<b>\$ 5,466,312</b>	<b>880,444</b>	<b>13,383,658</b>	<b>3,064,853</b>	<b>2,950,430</b>	<b>14,114,387</b>	<b>17,155</b>	<b>22,808,152</b>
<b>Liabilities and Fund Balances and Other Credits</b>								
Accounts payable and other liabilities	262,089	157,084	721,126	1,294,694	19,042	684,883	2,337	111,196
Accrued interest	—	—	—	—	—	—	—	—
Due to other funds	3,243,690	109,086	12,596,233	—	1,518,936	6,009,864	170	8,271,175
Deferred revenue	—	—	—	—	302,285	—	—	326,826
<b>Total liabilities</b>	<b>3,505,779</b>	<b>266,170</b>	<b>13,317,359</b>	<b>1,294,694</b>	<b>1,840,263</b>	<b>6,694,747</b>	<b>2,507</b>	<b>8,709,197</b>
Fund balances and other credits:								
Reserved	500	—	1,463,324	1,770,159	56,662	937,049	—	198,828
Unreserved	1,960,033	614,274	(1,397,025)	—	1,053,505	6,482,591	14,648	13,900,127
Designated for economic uncertainty	—	—	—	—	—	—	—	—
<b>Total fund balances</b>	<b>1,960,533</b>	<b>614,274</b>	<b>66,299</b>	<b>1,770,159</b>	<b>1,110,167</b>	<b>7,419,640</b>	<b>14,648</b>	<b>14,098,955</b>
<b>Total fund balances and other credits</b>	<b>\$ 5,466,312</b>	<b>880,444</b>	<b>13,383,658</b>	<b>3,064,853</b>	<b>2,950,430</b>	<b>14,114,387</b>	<b>17,155</b>	<b>22,808,152</b>

See accompanying independent auditors' report.

SAN DIEGO UNIFIED SCHOOL DISTRICT

Combining Balance Sheet – Other Governmental Funds

June 30, 2003

	State School Building	Capital Projects				Special Reserve	Building Corporation
		Prop O/ Preconstruction Costs	Capital Facilities Fund III	Energy Efficiency Fund	Redevelopment Agencies' Fund		
<b>Assets</b>							
Cash in county treasury	17,757	9,223,871	24,506,996	2,657,386	1,583,990	346,926	
Cash on hand and in bank	—	—	—	—	—	—	—
Cash with fiscal agent	—	—	—	—	—	—	—
Short-term investments	—	—	—	—	—	—	—
Accounts receivable:							
Federal and state government	—	1,217,158	—	—	—	—	—
Other	66	81,036	105,018	11,630	6,913	—	—
Due from other funds	—	2,527,074	899	—	—	—	—
Inventory	—	—	—	—	—	—	—
<b>Total assets</b>	<b>\$ 17,823</b>	<b>13,049,139</b>	<b>24,612,913</b>	<b>2,669,016</b>	<b>1,590,903</b>	<b>346,926</b>	
<b>Liabilities and Fund Balances and Other Credits</b>							
Accounts payable and other liabilities	—	199,532	18,254	—	—	2,338	—
Accrued interest	—	—	—	—	—	—	—
Due to other funds	—	4,327,480	844,564	—	—	—	—
Deferred revenue	—	—	—	—	—	—	—
<b>Total liabilities</b>	<b>—</b>	<b>4,527,012</b>	<b>862,818</b>	<b>—</b>	<b>—</b>	<b>2,338</b>	<b>—</b>
<b>Fund balances and other credits:</b>							
Fund balances:							
Reserved	—	506,222	80,731	—	—	—	—
Unreserved	17,823	8,015,905	23,669,364	2,669,016	1,590,903	344,588	—
Designated for economic uncertainty	—	—	—	—	—	—	—
<b>Total fund balances</b>	<b>17,823</b>	<b>8,522,127</b>	<b>23,750,095</b>	<b>2,669,016</b>	<b>1,590,903</b>	<b>344,588</b>	<b>—</b>
<b>Total fund balances and other credits</b>	<b>\$ 17,823</b>	<b>13,049,139</b>	<b>24,612,913</b>	<b>2,669,016</b>	<b>1,590,903</b>	<b>346,926</b>	<b>—</b>

See accompanying independent auditors' report.

SAN DIEGO UNIFIED SCHOOL DISTRICT

Combining Balance Sheet -- Other Governmental Funds

June 30, 2003

	Debt Service				Other Governmental Funds
	Pre-Field Tax Override	Bond Interest & Redemption	Corporation	Proposition XX Tax Override	
<b>Assets</b>					
Cash in county treasury	14,709	3,546,665	—	2,090,473	78,243,920
Cash on hand and in bank	—	—	—	—	348,093
Cash with fiscal agent	—	—	—	—	50,000
Short-term investments	—	10,552,594	—	3,171,656	13,724,250
Accounts receivable:					
Federal and state government	—	—	—	—	16,284,612
Other	—	101,198	—	—	944,672
Due from other funds	—	—	—	—	13,916,810
Inventory	—	—	—	—	937,049
<b>Total assets</b>	<b>14,709</b>	<b>14,200,457</b>	<b>—</b>	<b>5,262,129</b>	<b>124,449,406</b>
<b>Liabilities and Fund Balances and Other Credits</b>					
Accounts payable and other liabilities	—	—	—	3,045,776	6,518,351
Accrued interest	—	13,925,905	—	—	13,925,905
Due to other funds	2,215	—	—	2,090,473	39,013,886
Deferred revenue	—	—	—	—	629,111
<b>Total liabilities</b>	<b>2,215</b>	<b>13,925,905</b>	<b>—</b>	<b>5,136,249</b>	<b>60,087,253</b>
<b>Fund balances and other credits:</b>					
Fund balances:					
Reserved	12,494	274,552	—	125,880	5,426,401
Unreserved	—	—	—	—	52,453,161
Designated for economic uncertainty	—	—	—	—	6,482,591
<b>Total fund balances</b>	<b>12,494</b>	<b>274,552</b>	<b>—</b>	<b>125,880</b>	<b>64,362,153</b>
<b>Total fund balances and other credits</b>	<b>14,709</b>	<b>14,200,457</b>	<b>—</b>	<b>5,262,129</b>	<b>124,449,406</b>

See accompanying independent auditors' report.

SAN DIEGO UNIFIED SCHOOL DISTRICT

Combining Statement of Revenues, Expenditures, and Charges in Fund Balances - Other Governmental Funds

Year ended June 30, 2003

	Child Development	Adult Education	Deferred Maintenance	Special Revenue						Charter Schools		
				Pupil Transportation Equipment	Property Management	Cafeteria Account	Balboa Stadium					
<b>Revenues:</b>												
Revenue limit sources - state apportionment	\$ 16,712,107	1,505,815	—	—	—	—	—	—	—	—	—	12,418,929
Revenue from federal sources	698,207	—	—	—	—	—	—	—	—	—	—	3,201,403
Revenue from other state sources	319,816	1,436,249	300,000	—	—	—	—	—	—	—	—	5,410,123
Revenue from other local sources:												
Interest	160,903	18,597	105,208	57,955	47,010	—	—	—	—	—	—	436,064
Cafeteria sales	830,657	—	—	—	—	—	—	—	—	—	—	—
Other local revenue	991,560	18,597	10,128	1,329,583	4,320,233	—	—	—	—	—	—	22,651,428
Total other local revenue	18,721,690	2,960,661	115,336	1,387,538	4,367,243	—	—	—	—	—	—	23,087,492
Total revenues			415,336	1,387,538	4,367,243	—	—	—	—	—	—	44,117,947
<b>Expenditures:</b>												
Certificated salaries	7,254,285	732,879	—	—	—	—	—	—	—	—	—	19,320,456
Classified salaries	6,270,408	702,823	66	590	99,108	—	—	—	—	—	—	4,560,849
Employee benefits	4,058,037	309,686	7	1,049	35,191	—	—	—	—	—	—	5,391,531
Books and supplies	578,293	153,160	115	50,977	11,874	—	—	—	—	—	—	1,922,985
Service and other operating	594,537	1,839,985	498	4,400	782,456	—	—	—	—	—	—	8,552,286
Capital outlay	42,639	4,000	6,820,782	1,295,593	685,904	—	—	—	—	—	—	243,755
Other outgo	413,179	36,021	—	—	—	—	—	—	—	—	—	—
Debt service:												
Principal	—	—	—	—	—	—	—	—	—	—	—	—
Interest and fiscal charges	—	—	—	—	—	—	—	—	—	—	—	—
Total expenditures	19,211,378	3,778,554	6,821,468	1,352,609	1,657,783	—	—	—	—	—	—	39,991,862
Excess (deficiency) of revenues over expenditures	(489,688)	(817,893)	(6,406,132)	34,929	2,709,460	—	—	—	—	—	—	4,126,085
<b>Other financing sources (uses):</b>												
Proceeds from Cops	—	—	—	—	—	—	—	—	—	—	—	—
Payment to bond escrow agent	—	—	—	—	—	—	—	—	—	—	—	—
Transfers in	—	—	4,550,917	1,290,191	—	—	—	—	—	—	—	—
Transfers out	—	—	—	—	—	—	—	—	—	—	—	—
Other sources	200	—	—	—	(1,677,758)	—	—	—	—	—	—	—
Other uses	—	—	—	—	—	—	—	—	—	—	—	—
Total other financing sources (uses)	200	—	4,550,917	1,290,191	(1,677,758)	—	—	—	—	—	—	—
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	(489,488)	(817,893)	(1,855,215)	1,325,120	1,031,702	—	—	—	—	—	—	4,126,085
Fund balances - June 30, 2002	2,450,021	1,432,167	1,921,514	445,039	78,465	—	—	—	—	—	—	9,972,870
Fund balances - June 30, 2003	\$ 1,960,533	614,274	66,299	1,770,159	1,110,167	—	—	—	—	—	—	14,098,955

See accompanying independent auditors' report.

SAN DIEGO UNIFIED SCHOOL DISTRICT

Combining Statement of Revenues, Expenditures, and Charges in Fund Balances - Other Governmental Funds

Year ended June 30, 2003

	State School Building	Prop O/ Preconstruction Costs	Capital Projects				Special Reserve	Building Corporation
			Capital Facilities Fund III	Energy Efficiency Fund	Redevelopment Agencies' Fund			
Revenues:								
Revenue limit sources - state apportionment	\$ 223,715							
Revenue from federal sources		2,724,059						
Revenue from other state sources								
Revenue from other local sources:								
Interest	17,373							
Cafeteria sales		560,489	443,538	60,439	25,210		22,528,436	
Other local revenue		43,435,675	14,855,822	10,596	830,715			
Total other local revenue	17,373	43,996,164	15,299,360	71,035	855,925		22,528,436	
Total revenues	241,088	46,720,223	15,299,360	71,035	855,925		22,528,436	
Expenditures:								
Certificated salaries		419,156						
Classified salaries		440,577	31,713					
Employee benefits		194,901	11,862					
Books and supplies		22,907	818,161					
Service and other operating	41,970	1,025,169	16,991			2,231	21,500	
Capital outlay	1,024,167	3,516,032	4,128,349				1,135,878	
Other outgo		9,831,414						
Debt service:								
Principal								
Interest and fiscal charges								
Total expenditures	1,066,137	15,450,156	5,007,076			2,231	1,157,378	
Excess (deficiency) of revenues over expenditures	(825,049)	31,270,067	10,292,284	71,035	855,925	(2,231)	21,371,058	
Other financing sources (uses):								
Proceeds from Cops								
Payment to bond escrow agent								
Transfers in		2,537,670						
Transfers out		(31,155,730)		(10,595)			(89,776,749)	
Other sources								
Other uses								
Total other financing sources (uses)		(28,618,060)		(10,595)			(89,776,749)	
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	(825,049)	2,652,007	10,292,284	60,440	855,925	(2,231)	(68,405,691)	
Fund balances - June 30, 2002	842,872	5,870,120	13,457,811	2,608,576	734,978	346,819	68,405,691	
Fund balances - June 30, 2003	\$ 17,823	8,522,127	23,750,095	2,669,016	1,590,903	344,588		

See accompanying independent auditors' report.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Combining Statement of Revenues, Expenditures, and Charges in Fund Balances -- Other Governmental Funds

Year ended June 30, 2003

	Debt Service				Proposition XX Tax Override	Elimination Entries	Other Governmental Funds
	Pre-Field Tax Override	Bond Interest & Redemption	Corporation				
<b>Revenues:</b>							
Revenue limit sources -- state apportionment	\$						30,860,566
Revenue from federal sources							35,315,785
Revenue from other state sources				1,007,416			10,386,824
Revenue from other local sources:							
Interest		552,933					26,444,255
Cafeteria sales			1,327,989				11,285,729
Other local revenue			143,986,141	78,812,634	(198,123,600)		113,030,493
Total other local revenue			145,314,130	78,812,634	(198,123,600)		150,760,477
Total revenues			145,314,130	79,820,050	(198,123,600)		227,323,652
<b>Expenditures:</b>							
Certificated salaries							27,770,026
Classified salaries							28,609,429
Employee benefits							15,138,061
Books and supplies							19,984,257
Service and other operating							16,549,806
Capital outlay							19,222,219
Other outgo	8,860			92,292,958	(92,292,958)		102,936,375
Debt service:							
Principal							132,510,000
Interest and fiscal charges		27,424,394	132,510,000				31,834,021
Total expenditures	8,860	27,424,394	136,919,627	92,292,958	(92,292,958)		394,554,194
Excess (deficiency) of revenues over expenditures	(8,860)	(26,871,461)	8,394,503	(12,472,908)	(105,830,642)		(167,230,542)
<b>Other financing sources (uses):</b>							
Proceeds from Cops			19,125,000				19,125,000
Payment to bond escrow agent		12,104,117	(50,717,658)				(38,613,541)
Transfers in			42,056,292				16,050,520
Transfers out			(59,286,737)	(2,077,074)	(34,384,550)		(43,769,451)
Other sources					140,215,192		200
Other uses							
Total other financing sources (uses)		12,104,117	(48,823,103)	(2,077,074)	105,830,642		(47,207,272)
Excess (deficiency) of revenues and other financing sources over expenditures and other financing uses	(8,860)	(14,767,344)	(40,428,600)	(14,549,982)			(122,144,856)
Fund balances -- June 30, 2002	21,354	15,041,896	40,428,600	14,675,862			186,507,009
Fund balances -- June 30, 2003	12,494	274,552		125,880			64,362,153

See accompanying independent auditors' report.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Expenditures of Federal Awards

Year ended June 30, 2003

Federal Assistance	Federal Catalog Number	Grant Award Number	Program expenditures
U.S. Department of Education:			
Passed through California Department of Education:			
ESEA, Title I	84.010A	PCA 13797 RES 3010	\$ 46,790,182
ESEA, Title I – Charter Schools	84.010A	PCA 13797 RES 3010	812,446
ESEA, Title I – Delinquent	84.013	PCA 13798 RES 3025	9,760
Title I – Program Improvement	84.358	PCA 14106 RES 3171	991,986
IASA, Title I – Even Start Family Literacy	84.213	PCA 03700 RES 3105	651,033
ESEA, Title VI – Innovative Education Program Strategies	84.298	PCA 13340 RES 4110	1,108,900
ESEA, Title VI – Innovative Education Program Strategies – Charter Schools	84.298	PCA 13340 RES 4110	31,487
ESEA, Title VI – Class Size Reduction	84.340A	S340A990047	82,380
ESEA, Title VI – Class Size Reduction – Charter Schools	84.340A	S340A990047	24,643
Comprehensive School Reform Demonstration	84.010	99-3966-6833	303,258
Total ESEA			50,806,075
IDEA Part A:			
Workability Idea	84.027A	PCA 13705 RES 3405	535,330
Low Incidence Entitlement	84.027A	PCA 13459 RES 3360	36,930
Infant Discretionary Funds	84.027A	PCA 13612 RES 3330	80,317
Preschool Local Entitlement	84.027A	PCA 13682 RES 3320	881,745
Personnel Development	84.027A	PCA 13613 RES 3340	53,119
Special Learning Disability Program Intern	84.027A	PCA 03651 RES 3375	27,715
Subtotal 84.027A			1,615,156
Federal Preschool (IDEA, Part B)	84.173A	PCA 13430 RES 3315	978,720
Preschool Staff Development	84.173A	PCA 13431 RES 3345	5,784
Subtotal 84.173A			984,504
IDEA Part H:			
Early Intervention	84.181A	PCA 23761 RES 3385	297,052
Total Special Education			2,896,712
Title II – Part C – 231 – Secondary Schools Program			
Title II – Eisenhower	84.168	37-68338-IIC-231	1,602,456
Title II – Eisenhower – Charter Schools	84.168	PCA 03207 RES 4010	361,735
Title II – NCLB, Part A	84.367	PCA 03207 RES 4010	2,791
Title II – NCLB, Part A – Charter Schools	84.367	PCA 14341 RES 4035	8,824,327
Title II, Part D – Enhancing Rd – Formula	84.318	PCA 14341 RES 4035	96,192
Title III – NCLB Immigrant Education	84.365	PCA 14334 RES 4045	75,036
Title III – NCLB – Limited English	84.365	PCA 14346 RES 4201	62,673
Title IV – Safe and Drug Free Schools	84.186	PCA 10084 RES 4203	728,048
Title IV – Safe and Drug Free Schools – Charter Schools	84.186	PCA 03453 RES 3710	1,917,735
		PCA 03453 RES 3710	5,498

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Expenditures of Federal Awards

Year ended June 30, 2003

Federal Assistance	Federal Catalog Number	Grant Award Number	Program expenditures
NCLB – Title X – McKinney Homeless San Diego State University:	84.196	PCA 14332 RES 5630	\$ 50,549
GOALS 2000 Parent Involvement	84.287A	R287A990201	—
Natural Disaster Assistance	84.000		6,520
Indian Education Act	84.060		7,479
Total Passed through California Department of Education			67,443,826
<b>Direct Programs:</b>			
21st Century Community Learning Center	84.287A	R287A990201	17,700
21st Century Community Learning Center	84.287B	S287B011735	210,920
21st Century Community Learning Center	84.287A	S287A012684	1,505,744
21st Century CLC Secondary	84.287	37-2002-CCLC-005	3,454
School Renovation	84.352A	PCA 14318 RES 4141	2,490
Drug & Violence Prevention Coordination	84.184K	S184K000145	342,599
Drug & Violence Prevention Coordination	84.184K	S184K990237	545,811
Other Federal – Teaching American History	84.215X	S215X020182	6,153
East Project Grant – San Diego High	84.318X	PCA 13285	1,352,810
Indian Education Act	84.060A	S060A960074	74,293
FIE – Fund for Improvement of Education	84.215K	R215K010157	791,247
Transition to Teaching	84.35D	TT-1-0004	48,388
Charter School Federal Grant	84.282	CS68338A-1	18
NCLB Title V, Part B, Charter School Grants	84.282	CS68338A-1	549,653
Technology Hardware Grant	84.318X	PCA 13285	15,584
Peerworks 21st Century After School Learning	84.287A	S287A002027	179,736
Peerworks 21st Century After School Learning	84.287B	R287B990092	4,739
Emergency Immigration Act	84.162	98-3159-6833-00	(1)
Magnet Schools	84.165A	S165A010019	2,206,047
Smaller Learning Communities	84.215L	S215L000203	4,011
Reduce Alcohol Abuse	84.184A	S184A020086	53,944
Foreign – Elementary Schools	84.294A	T294A020133	40,519
Safe Schools Healthy Students	84.184L	S184L010009	2,087,568
Maintenance and Operation PL 103-382	84.041		19,304,724
PL 101-476 – Local Assistance	84.027A	01-3379-6833-01	16,187,909
Total Direct Programs			45,536,060
Total U.S. Department of Education			112,979,886



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Expenditures of Federal Awards

Year ended June 30, 2003

<u>Federal Assistance</u>	<u>Federal Catalog Number</u>	<u>Grant Award Number</u>	<u>Program expenditures</u>
National Science Foundation:			
Urban Systemic Initiative Grant	47.046	ESR-0115108	\$ 2,142,476
			<u>2,142,476</u>
U.S. Department of Labor:			
Passed through the San Diego Workforce Partnership:			
Neighborhood House – Summer Youth	17.25		228,976
JTPA/Summer Hire-A-Youth	17.25		302,728
Passed through City of San Diego:			
Urban/Rural Opportunity/SD High	17.249	U-7014-8-00-88-60	69,571
			<u>601,275</u>
U.S. Department of Health and Human Services:			
AIDS Prevention	93.938	U87/CCU908974-07	244,727
Child Development Block Grant	93.575		698,207
Medi-Cal Billing Option	93.778	PCA 10013 RES 5640	1,444,104
			<u>2,387,038</u>
U.S. Department of Agriculture – Forest Service:			
USDA Forest Service Grant – LLAMAS	10.67	CCS-5-97-02-007	44
Child Nutrition	10.555		28,692,116
			<u>28,692,160</u>
U.S. Department of Justice:			
Cops in Schools	16.71	1999SHWX0322	412,729
			<u>412,729</u>
Subtotal federal assistance			147,215,564
Federal Renovation Program – Charter Schools	84.352A	PCA 14313 RES 4140	12,595
Other Federal Assistance – R.O.T.C.	96.000		858,132
Other Federal Assistance – Advance Placement Examination Fees	96.000		114,202
Other Federal Assistance – DOD Special Ed Fund	96.000		1,034,221
Total federal assistance			\$ <u><u>149,234,714</u></u>

See accompanying independent auditors' report.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Instructional Time

Fiscal year ended June 30, 2003

The District presently meets the 1986-87 requirements for instructional minutes offered as outlined below:

<u>Grade level</u>	<u>1986-87 Minutes requirement</u>	<u>1982-83 Actual minutes offered</u>	<u>2002-2003 Actual minutes offered</u>	<u>Status</u>
Kindergarten	36,000	35,400	58,836	In Compliance
Grades 1-2	50,400	50,445	57,601	In Compliance
Grade 3	50,400	53,985	57,601	In Compliance
Grades 4-6	50,400	53,985	57,601	In Compliance
Grades 7-8	54,000	62,835	63,172	In Compliance
Grades 9-12	64,800	62,835	66,861	In Compliance

See accompanying independent auditors' report and notes to supplementary information.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Average Daily Attendance

Fiscal year ended June 30, 2003

The average daily attendance (ADA) by level of instruction for the 2002-2003 second period report and the 2002-2003 annual report are shown below:

	<u>2002-2003 Second period report</u>	<u>2002-2003 Annual report</u>
Elementary:		
Kindergarten	9,745.23	9,739.22
Regular day classes:		
Grades 1-3	31,754.45	31,652.14
Grades 4-8	46,511.31	46,287.58
Special education	3,216.84	3,229.50
Opportunity schools	2.88	2.54
Total elementary ADA	<u>91,230.71</u>	<u>90,910.98</u>
Secondary:		
Regular day classes	29,333.06	28,925.32
Special education classes	1,596.51	1,538.84
Compulsory continuation education	743.83	742.48
Total secondary ADA	<u>31,673.40</u>	<u>31,206.64</u>
Classes for adults:		
Concurrently enrolled in regular program	90.43	179.35
Not concurrently enrolled in regular program	302.07	407.40
Students 21 years or older and students 19 years or older not continuously enrolled since their 18th birthday, participating in full-time independent study	65.29	84.85
Total adult ADA	<u>457.79</u>	<u>671.60</u>
Home/Hospital	151.62	146.90
Community Day School	85.11	97.73
Extended year special education and nonpublic	774.61	705.31
Total District ADA	<u>124,373.24</u>	<u>123,739.16</u>
	<u>Hours of Attendance</u>	
Summer school:		
Elementary	2,927,648	3,806,384
Secondary	1,188,642	1,231,295
Total	<u>4,116,290</u>	<u>5,037,679</u>

See accompanying independent auditors' report and notes to supplementary information.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
 Schedule of Average Daily Attendance Charter Schools  
 Fiscal year ended June 30, 2003

The average daily attendance (ADA) by level of instruction for the 2002-2003 second period report and the 2002-2003 annual report are shown below:

	<b>2002-2003 Second period report</b>	<b>2002-2003 Annual report</b>
Elementary:		
Kindergarten	358.71	359.12
Regular day classes:		
Grades 1-3	887.78	880.41
Grades 4-8	3,929.94	3,863.20
Total elementary ADA	5,176.43	5,102.73
Secondary:		
Regular day classes	1,980.62	1,766.35
Total secondary ADA	1,980.62	1,766.35
Total District ADA	7,157.05	6,869.08

See accompanying independent auditors' report and notes to supplementary information.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Financial Trends and Analysis

Fiscal year ended June 30, 2003

<b>General Fund</b>	<b>Budget 2004 (unaudited)</b>	<b>2003</b>	<b>2002</b>	<b>2001(1)</b>
Revenue and other financing sources	\$ 1,065,013,054	1,132,841,475	1,089,371,332	1,028,810,468
Expenditures	1,129,220,084	1,101,809,553	1,059,994,319	1,018,200,483
Transfers out and other uses	7,286,385	6,294,811	9,286,690	8,017,031
<b>Total outgo</b>	<b>1,136,506,469</b>	<b>1,108,104,364</b>	<b>1,069,281,009</b>	<b>1,026,217,514</b>
<b>Change in fund balance</b>	<b>(71,493,415)</b>	<b>24,737,111</b>	<b>20,090,323</b>	<b>2,592,954</b>
Ending fund balance	\$ 54,574,978	126,068,393	101,331,282	68,267,055
Unreserved – undesignated fund balance	\$ 27,979,606	5,020,016	21,146,957	12,116,576
Unreserved fund balance as a percentage of total outgo	2.46%	0.45%	1.98%	1.18%
Total long-term debt	\$ 1,149,117,312	799,123,713	700,621,892	577,126,009
Average daily attendance at P-2 (excluding adult ADA)	124,022	123,915	125,529	125,464

The fiscal year 2002-2003 financial results indicate an increase of approximately \$25 million in ending fund balance. The increase can be attributed to the release of the certificate of participation reserves that flowed back to the District.

The District continues to set aside 1% of the General Fund budget (\$11 million) as a reserve for economic uncertainties.

The fiscal year 2003-2004 budget indicates an operating deficit without consideration of the beginning balance. Historical trends indicate that savings are generated from unexpended appropriations. In the 2003-2004 budget year, it is anticipated that savings of approximately \$21 million are expected to be generated in the salary and benefit accounts due to personnel turnover and vacancies, and committed but unexpended appropriations in the books and supplies, services, and capital outlay accounts. In addition, the District budgets as if all claims and judgments payable, including those which are long-term in nature, will be expended. This budget practice along with historical trends indicate that approximately \$8 million of appropriations will not be spent this year.

Considering these trends and budget practices identified by management, the District anticipates an ending balance decrease of approximately \$42 million for fiscal year 2003-2004. This would result in a budgeted ending fund balance of approximately \$84 million.

(1) Not restated for effect of GASB Interpretation No. 6

See accompanying independent auditors' report and notes to supplementary information.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
 Schedule of Average Daily Attendance Charter Schools

Fiscal year ended June 30, 2003

The average daily attendance (ADA) by level of instruction for the 2002-2003 second period report and the 2002-2003 annual report are shown below:

	<u>2002-2003 Second period report</u>	<u>2002-2003 Annual report</u>
Elementary:		
Kindergarten	358.71	359.12
Regular day classes:		
Grades 1-3	887.78	880.41
Grades 4-8	3,929.94	3,863.20
Total elementary ADA	<u>5,176.43</u>	<u>5,102.73</u>
Secondary:		
Regular day classes	<u>1,980.62</u>	<u>1,766.35</u>
Total secondary ADA	<u>1,980.62</u>	<u>1,766.35</u>
Total District ADA	<u><u>7,157.05</u></u>	<u><u>6,869.08</u></u>

See accompanying independent auditors' report and notes to supplementary information.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Financial Trends and Analysis

Fiscal year ended June 30, 2003

<b>General Fund</b>	<b>Budget 2004 (unaudited)</b>	<b>2003</b>	<b>2002</b>	<b>2001(1)</b>
Revenue and other financing sources	\$ 1,065,013,054	1,132,841,475	1,089,371,332	1,028,810,468
Expenditures	1,129,220,084	1,101,809,553	1,059,994,319	1,018,200,483
Transfers out and other uses	7,286,385	6,294,811	9,286,690	8,017,031
Total outgo	1,136,506,469	1,108,104,364	1,069,281,009	1,026,217,514
Change in fund balance	(71,493,415)	24,737,111	20,090,323	2,592,954
Ending fund balance	\$ 54,574,978	126,068,393	101,331,282	68,267,055
Unreserved – undesignated fund balance	\$ 27,979,606	5,020,016	21,146,957	12,116,576
Unreserved fund balance as a percentage of total outgo	2.46%	0.45%	1.98%	1.18%
Total long-term debt	\$ 1,149,117,312	799,123,713	700,621,892	577,126,009
Average daily attendance at P-2 (excluding adult ADA)	124,022	123,915	125,529	125,464

The fiscal year 2002-2003 financial results indicate an increase of approximately \$25 million in ending fund balance. The increase can be attributed to the release of the certificate of participation reserves that flowed back to the District.

The District continues to set aside 1% of the General Fund budget (\$11 million) as a reserve for economic uncertainties.

The fiscal year 2003-2004 budget indicates an operating deficit without consideration of the beginning balance. Historical trends indicate that savings are generated from unexpended appropriations. In the 2003-2004 budget year, it is anticipated that savings of approximately \$21 million are expected to be generated in the salary and benefit accounts due to personnel turnover and vacancies, and committed but unexpended appropriations in the books and supplies, services, and capital outlay accounts. In addition, the District budgets as if all claims and judgments payable, including those which are long-term in nature, will be expended. This budget practice along with historical trends indicate that approximately \$8 million of appropriations will not be spent this year.

Considering these trends and budget practices identified by management, the District anticipates an ending balance decrease of approximately \$42 million for fiscal year 2003-2004. This would result in a budgeted ending fund balance of approximately \$84 million.

(1) Not restated for effect of GASB Interpretation No. 6

See accompanying independent auditors' report and notes to supplementary information.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**  
 Reconciliation of Unaudited Actuals Financial Report (SACS Format)  
 to Audited Financial Statements  
 Fiscal year ended June 30, 2003

	<u>General Fund</u>	<u>Special Revenue Funds</u>	<u>Capital Projects Funds (1)</u>	<u>Debt Service Funds (2)</u>	<u>Total</u>
Fund balance as reported on Unaudited Actuals Financial report (SACS Format)	\$ 102,988,239	29,373,558	341,286,107	287,046	473,934,950
Add to fund balance to include the Corporation as a compont unit				125,880	125,880
Audit adjustment to record expense accrual	(848,556)	—	(5,024,282)	—	(5,872,838)
Audit adjustment for revenue accruals	(3,085,009)	—	—	—	(3,085,009)
Audit Adjustment to fund balance SACS compliance entry	—	(1,550,210)	—	—	(1,550,210)
Audit Adjustment to fund balance for self-insurance fund	6	—	—	—	6
Audit Adjustment for Charter Schools 501c3 Non-profit Corporation	—	(768,673)	—	—	(768,673)
Add to fund balance for self-insurance funds as reported on Unaudited Actuals Financial Report (SACS Format)	<u>27,013,713</u>	<u>—</u>	<u>—</u>	<u>—</u>	<u>27,013,713</u>
Fund balance per financial statements	<u>\$ 126,068,393</u>	<u>27,054,675</u>	<u>336,261,825</u>	<u>412,926</u>	<u>489,797,819</u>

- (1) Consists of Proposition O/Preconstruction Costs, Capital Facilities I, Capital Facilities III, Energy Efficiency Reserve, Redevelopment Agencies' Capital Facilities, Special Reserve Prop MM Building Fund, County School Facilities Fund, and Corporation Building Funds.
- (2) Consists of the Pre-Field Tax Override, Bond Interest and Redemption, Proposition XX Tax Override, and Corporation Debt Service Funds.

See accompanying independent auditors' report and notes to supplementary information.



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Supplementary Information

June 30, 2003

**(1) Purpose of Schedules**

**(a) *Combining Financial Statements***

**General**

The combining financial statements present the financial position of each of the individual funds of the San Diego Unified School District (the District) as of June 30, 2003, and the results of operations of such funds.

**Basis of Accounting**

The accompanying combining financial statements are presented on the modified-accrual basis of accounting which is described in note 1 to the District's general purpose financial statements.

**(b) *Schedule of Expenditures of Federal Awards***

**General**

OMB Circular A-133 requires a disclosure of the financial activities of all federally funded programs. This schedule was prepared to comply with OMB Circular A-133 and state requirements.

**Basis of Accounting**

The accompanying Schedule of Expenditures of Federal Awards is presented on the modified-accrual basis of accounting.

**(c) *Schedule of Instructional Time***

The District has received incentive funding for increasing instructional time as provided by the Incentives for Longer Instructional Day. This schedule presents information on the amount of instructional time offered by the District and whether the District complied with the provisions of Education Code Sections 46201 through 46206.

**(d) *Schedule of Average Daily Attendance***

Average daily attendance is a measurement of the number of pupils attending classes of the District. The purpose of attendance accounting from a fiscal standpoint is to provide the basis on which apportionments of state funds are made to school districts. This schedule provides information regarding the attendance of students at various grade levels and in different programs.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Notes to Supplementary Information

June 30, 2003

**(e) *Schedule of Financial Trends and Analysis***

This schedule provides General Fund balance trends over the past three fiscal years, along with current year budget information as obtained from the budget approved by the board of education in September 2002. The schedule complies with state requirements regarding the evaluation of the District's ability to continue as a going concern.

**(f) *Reconciliation of Annual Financial and Budget Report (Form J-200) to the Audited Financial Statements***

This schedule provides the information necessary to reconcile the fund balances of all funds as reported on Form J-200 to the audited general purpose financial statements.



KPMG LLP  
 Suite 1500  
 750 B Street  
 San Diego, CA 92101

### Independent Auditors' Report on State Compliance

The Honorable Board of Education  
 San Diego Unified School District:

We have audited the basic financial statements of the San Diego Unified School District (the District), as listed in the accompanying table of contents, as of and for the year ended June 30, 2003, and have issued our report thereon, dated April 15, 2004.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States and the standards for financial and compliance audits contained in (*Standards and Procedures for Audits of California K-12 Local Education Agencies*), issued by the Controller State of California, (*Audit Guide*). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

The District's management is responsible for the District's compliance with laws and regulations. In connection with the standards contained in the Audit Guide, we selected and tested transactions and records to determine the District's compliance with the state laws and regulations applicable to the following items noted in the following table.

Compliance section	Number of procedures in State Controller's Audit Guide	Procedures performed
Attendance accounting:		
Attendance reporting	4	Yes
Kindergarten enrollment	3	Yes
Independent study	13	Yes
Continuing education	11	Yes
Adult education	8	Yes
Regional occupational centers/programs	4	N/A
Staff development days	3	Yes



<u>Compliance section</u>	<u>Number of procedures in State Controller's Audit Guide</u>	<u>Procedures performed</u>
Incentives for longer instructional day:		
School districts	3	Yes
County offices of education	3	N/A
GANN limit calculation	2	Yes
Early retirement incentive program	5	N/A
Community day schools	8	Yes
Class size reduction program:		
Option one classes	11	Yes
Option two classes	10	Yes
Program to reduce class size in two courses in grade 9	8	Yes
State instructional materials fund:		
K-8	10	Yes
9-12	7	Yes
Schiff-Bustamante Standards – Basic Instructional Materials	9	Yes
Digital High School Education Technology Grant Program	5	Yes
California Public Schools Library Act of 1998	4	Yes
Computer Usage	2	Yes

Based on our audit, we found that, for the items tested, the District complied with the state laws and regulations referred to above, except as described in the schedule of findings and questioned costs section of this report. Further, based on our examination, for items not tested, nothing came to our attention to indicate that the District had not complied with the state laws and regulations, except as providing an opinion on compliance with state laws and regulations in the Audit Guide was not an objective of our audit, and accordingly, and we do not express such an opinion. The results of an audit discuss matters of noncompliance that are required to be reported under the Audit Guide which are described in the schedule of findings and questioned costs section of this report as findings 03-04 and 03-05.

This report is intended for the information and use of the board of education, management, the State Controller's Office, the Department of Education, and other agencies granting funds to the District, and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

April 15, 2004



KPMG LLP  
Suite 1500  
750 B Street  
San Diego, CA 92101

**Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards***

The Honorable Board of Education  
San Diego Unified School District:

We have audited the basic financial statements of the San Diego Unified School District (the District), as listed in the accompanying table of contents, as of and for the year ended June 30, 2003, and have issued our report thereon, dated April 15, 2004. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

**Compliance**

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed an instance of noncompliance that is required to be reported under *Government Auditing Standards* which is described in the accompanying schedule of findings and questioned costs as item 03-01.

**Internal Control over Financial Reporting**

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on internal control over financial reporting. However, we noted certain matters involving internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over financial reporting that, in our judgment, could adversely affect the District's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. The reportable condition is described in the accompanying schedule of findings and questioned costs as item 03-02.

A material weakness is a condition in which the design or operation of one or more of internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the basic financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over financial reporting would not necessarily disclose all matters in internal control



over financial reporting that might be reportable conditions and, accordingly, would not disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that the reportable condition described above is not a material weakness.

This report is intended for the information and use of the board of education, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

KPMG LLP

April 15, 2004



KPMG LLP  
Suite 1500  
750 B Street  
San Diego, CA 92101

**Report on Compliance with Requirements Applicable to Each Major  
Program and Internal Control over Compliance in Accordance  
with OMB Circular A-133**

The Honorable Board of Education  
San Diego Unified School District:

**Compliance**

We have audited the compliance of the San Diego Unified School District (the District), with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to each of its major federal programs for the year ended June 30, 2003. The District's major federal programs are identified in the summary of auditors' results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of the District's management. Our responsibility is to express an opinion on the District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures, as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the District's compliance with those requirements. As described in item 03-03 in the accompanying schedule of findings and questioned costs, the District did not comply with requirements regarding allowable costs that are applicable to its Title II-NCLB Part A-Charter Schools and Safe Schools Healthy Students programs. Compliance with such requirements is necessary, in our opinion, for the District to comply with requirements applicable to these programs.

In our opinion, because of the effects of the noncompliance described in the preceding paragraph, the District did not comply, in all material respects, with the requirements referred to above that are applicable to the Title II-NCLB Part A-Charter Schools and Safe Schools Healthy Students programs. Also, in our opinion, the District complied, in all material respects, with the requirements referred to above that are applicable to each of its other major federal programs for the year ended June 30, 2003.



### **Internal Control over Compliance**

The management of the District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving internal control over compliance and its operation that we consider to be reportable condition. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of internal control over compliance that, in our judgment, could adversely affect the District's ability to administer a major federal program in accordance with the applicable requirements of laws, regulations, contracts, and grants. The reportable condition is described in the accompanying schedule of findings and questioned costs as items 03-03.

A material weakness is a condition in which the design or operation of one or more internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of internal control over compliance would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider item 03-03 to be a material weakness.

This report is intended for the information and use of the board of education, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

**KPMG LLP**

April 15, 2004



**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Findings and Questioned Costs

June 30, 2003

**Section 1 – Summary of Auditors’ Results**

**Financial Statements**

The type of report issued on the financial statements. **Unqualified opinion**

Internal control over financial reporting:

Material weaknesses identified? **No**

Reportable conditions identified that are not considered

to be material weaknesses? **Yes**

Noncompliance material to the financial statements noted? **Yes**

**Federal Awards**

Internal control over major programs:

Material weakness identified? **Yes**

Reportable condition identified that is not considered to be a material weakness? **No**

The type of report issued on compliance for major programs: **Unqualified for all major programs except Title II-NCLB Part A-Charter Schools and Safe Schools Healthy Students which are qualified**

Any audit findings disclosed that are required to be reported in accordance with OMB Circular A-133, Section .510(a)? **Yes**

Identification of major programs:

<u>CFDA Numbers</u>	<u>Name of Federal Program or Cluster</u>
10.555	Child Nutrition Cluster
84.184	Safe Schools Healthy Students
84.367	Title II-NCLB Part A-Charter Schools

Dollar threshold used to distinguish between Type A and Type B programs: **\$3,000,000**

Auditee qualified as a low-risk auditee? **Yes**

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Findings and Questioned Costs

June 30, 2003

**State Awards**

Internal control over state awards:

Material weaknesses identified? **No**

Reportable conditions identified that are not considered to be material weaknesses? **No**

The type of report issued on compliance for state awards programs: **Unqualified**

**Section 2 – Financial Statement Findings**

**Summary of Current Year Findings Related to the Financial Statements Reported in Accordance with Government Auditing Standards**

***Finding 03-01: Board Review of Investment Information***

**Criteria:**

Government Code (GC) Sections 53600-53686

**Condition:**

During our test work, we noted the District is not presenting annually the written investment policy for Board adoption and is not presenting all required quarterly investment information and certification.

**Effect:**

Specific GC compliance requirements are not being fully met.

**Cause:**

The District, which maintains a significant portion of its total cash and investments with the County of San Diego, has relied solely on the County of San Diego's certification for those funds placed with the County.

**Recommendation:**

It is recommended that the District management establish policies and procedures for presenting annually the written investment policy for Board adoption and presenting all required quarterly investment information for certification by the board so as to be in compliance with GC compliance requirements.

**District's Response:**

The District's funds are invested in the County of San Diego Pooled Money Fund and in Guaranteed Interest Contracts (GICs). The District relies upon the County of San Diego's investment policy with regard to funds invested in the Pooled Money Fund. The Pooled Money Fund Investment Policy is reviewed and approved by the County of San Diego's Treasurer's Oversight Committee annually and is adopted by the board of supervisors in a public forum. The District's Chief Financial Officer is a

## SAN DIEGO UNIFIED SCHOOL DISTRICT

### Schedule of Findings and Questioned Costs

June 30, 2003

member of the Treasurer's Oversight Committee. The Pooled Money Fund is managed in accordance with prudent, money management principles and California State Law Sections 27000.1 – 27000.5, 27130 – 27137, and 53600 – 53686.

The District's investments in GIC's are in compliance with GC Section 53601 that limits investments in "commercial paper of prime quality of the highest ranking of the highest letter numerical rating as provided for by Moody's Investors Service Inc. or Standard and Poor's Corporation." The District's GIC investments are 'AAA' rated.

The District's investment policy will be presented to the Board of Education for adoption in a future board meeting and annually thereafter. Within 30 days after the end of each calendar quarter, a report on the District's investments will be provided to the Board of Education, as required under GC Section 53646.

#### ***Finding 03-02: Management Review of Financial Information***

##### **Criteria:**

Good internal control practices over financial reporting include management review of financial statements on a periodic basis.

##### **Condition:**

The District does not currently prepare and distribute monthly financial statements for use by management in monitoring the activities of the District. There is no formal review of the financial information of the District until the year-end reporting process, and that review is very limited.

Further, there do not seem to be adequate resources to complete the year-end reporting package and self-critique the data prior to fieldwork commencing, which results in ineffective controls over the financial reporting process. As a result, there were numerous entries made for the financial statements and numerous revisions made to financial statement schedules.

##### **Effect:**

By not reviewing the financial statements in a timely manner, the District increases the risk that misstatements, either due to error or irregularity, may not be identified and corrected in a timely manner. Our audit procedures resulted in a number of large dollar adjustments, indicating that the financial statements were not accurate and had not been reviewed in preparation for the current year audit.

Care in the preparation and review of financial reporting information is an important internal control. It is also essential that management and the governing body have comfort that these controls are functioning effectively in order to justify their reliance on the financial information provided to them for decision-making purposes.

##### **Cause:**

District procedures do not provide for top level review of financial information.

# SAN DIEGO UNIFIED SCHOOL DISTRICT

## Schedule of Findings and Questioned Costs

June 30, 2003

### **Recommendation:**

The District should established polices, procedures and internal controls over the financial reporting process. The design of the controls should include supervisory review of corrections to the general throughout the year and over the year end closing transactions. Further, there should be ledger internal controls designed and implemented to perform and verify a reconciliation of the general ledger to the month-end financial reports and year-end financial statements, footnotes and supplementary information.

### **District's Response:**

The automated financial reporting system in place for 2002-2003 did not allow for production of financial statements in a format meaningful for management review. While automated monthly financial statements are produced, the presentation is designed for private enterprise, not for public agency fund reporting. As a remedy, the financial reporting unit extracts financial information from the existing automated system and prepares separate financial reports which have been designed to present information to management in a useful format. This process is time-intensive, and while "management" financial statements are prepared monthly for the majority of District funds, the process is not consistently performed for all funds. However, management financial statements are prepared for all District funds at the end of the state required First Interim, Second Interim, and Final reporting periods. The District is implementing a new District-Wide Application (DWA) that will provide for greater financial reporting capability.

Due to a number of factors, i.e., the implementation of SACS, and resources redirected to development of DWA, existing resources available for financial reporting, both monthly and at year-end, have been taxed. These factors result in less time available for on-going review and analysis of financial transactions and activities. An increase in the number of post-preparation revisions to financial statements is an undesirable outcome.

Adjustments to financial statements often occur due to the accounting treatment afforded to financial activities rather than due to error or irregularity. When financial activities occur, the nature of which is new to the District, the accounting treatment afforded by the District may differ from the treatment later determined through the audit process to be the recommended method. Such adjustments are not unusual. A number of the post-preparation financial statement adjustments required were such adjustments and tended to be large dollar adjustments. These adjustments are more a reflection of differing accounting treatments being utilized rather than inaccuracies. Adjustments were also required due to the reduced review and analysis capability referenced above.

Implementation of the new financial reporting systems, will afford more time and better tools for reporting purposes. Management will be provided the information in a timely fashion and with greater review and analysis having taken place.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Findings and Questioned Costs

June 30, 2003

**Section 3 – Federal Award Findings and Questioned Costs**

**OMB Circular A-133 Audit Findings and Questioned Costs**

*Finding 03-03: Allowable Costs.*

**Federal Agency:** Department of Education

**Program Name:** Title II-NCLB Part A-Charter Schools/Safe Schools Healthy Students

**CFDA# and Program Expenditures:** 84.367(\$8,920,519)/84.184(\$3,029,922)

**Award Year:** FYE 6/30/03

**Criteria:**

OMB Circular A-87 Attachment B Section II. Paragraph h. Section 3. requires where employees are expected to work solely on a single federal award or cost objective, charges for their salaries and wages will be supported by periodic certifications that the employees worked solely on that program for the period covered by the certification. These certifications to be prepared at least semi-annually and are signed by the employee or supervisory official having first hand knowledge of the work performed by the employee.

**Condition:**

The District is not in compliance with OMB Circular A-87 for payroll costs charged to Title II-NCLB Part A-Charter Schools and Safe Schools Healthy Students because appropriate documentation supporting payroll costs, specified by OMB Circular A-87, is not maintained.

**Questioned costs:**

Not determinable

**Context:**

KPMG selected 30 employees who are funded from the two grants (crosscutting) for control and compliance testwork. Of the 30 employees tested, eight employees were subject to bi-annual certifications of which six certifications could be provided by the District.

**Cause:**

The District budget department request certifications from the employees funded by various federal programs. However, the budget department does not have an internal control system that monitors the compliance of the completion of the certifications as well as system that monitors when an employee changes funding sources which require new certifications.

**Effect:**

The District is not in compliance with certification requirements of OMB Circular A-87 for the Title II-NCLB Part A-Charter Schools and Safe Schools Healthy Students programs.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Findings and Questioned Costs

June 30, 2003

**Recommendation:**

Where employees work solely on a single federal program, charges for their salaries and wages should be supported by periodic certifications in accordance with OMB Circular A-87.

**District's Response:**

To strengthen existing controls and compliance, policy changes have been made and approved by the San Diego Unified School District Board of Trustees (Board Policy D-3500) to ensure that procedures for overall grant administration are in compliance with OMB Circular A-87, including time-accounting certifications. The District distributes a circular twice a year requesting semiannual time accounting certification for 100% funded and partially funded positions. Program directors are responsible for overseeing the collection of the time certification forms. They are to be retained within the District for a period of three years following the submission of the final project report. District Administrative Procedure No. 1320 is being revised to implement the proposed time and effort documentation requirements.

**Section 4 – State Compliance Awards Findings**

**Summary of Current Year Findings**

**Finding 03-04: State Compliance (Attendance Reporting)**

**Criteria:**

Because of the relationship between attendance and the state apportionments, the District must develop and maintain accurate and adequate attendance records to support the attendance reported to the State.

**Condition:**

For two student, the District's attendance records were missing, and as such, we were not able to verify the attendance reported to the State.

**Context:**

Attendance for one of the two school days tested for two of one-hundred students tested could not be verified due to missing teacher attendance rosters at the school sites.

**Effect:**

The attendance reported to the state and funding amounts were overstated.

**Cause:**

The District's school sites inadvertently misplaced the teacher attendance rosters and were unable to account for the attendance claimed on the J-18/19 P-2 report.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

Schedule of Findings and Questioned Costs

June 30, 2003

**Recommendation:**

We recommend that the District amend the P-2 and Annual attendance reports to reflect the above adjustments. We also recommend that the attendance clerks at all school sites make an effort to account for all teacher attendance rosters on a daily (period) basis to support attendance reported to the State.

**District's Response:**

Through Internal audits, the District will review records at sites to confirm whether correct record-keeping procedures are followed, and the attendance is reported accurately.

Additional staff training will be conducted to emphasize the record-keeping requirements. Procedures for the accounting of teachers' rosters and follow-up for missing reports will be consistently implemented at all sites.

The District will amend the P-2 attendance report to reflect the adjustments.

***Finding 03-05: State Compliance (Attendance Reporting)***

**Criteria:**

Because of the relationship between attendance and the state apportionments, the District must develop and maintain accurate and adequate attendance records to support the attendance reported to the State.

**Condition:**

During our test work to verify apportionment credit for independent study contract (CIS) we noted one student who received CIS credit was not marked as absent on the teacher attendance roster.

**Context:**

One-of-twenty students tested receiving apportionment credit for independent study contrast.

**Effect:**

The attendance reported to the state and funding amount was overstated.

**Cause:**

The student was given apportionment credit for both normal attendance and CIS because the student was not marked absent on the teacher attendance roster for that day.

**SAN DIEGO UNIFIED SCHOOL DISTRICT**

**Schedule of Findings and Questioned Costs**

June 30, 2003

**Recommendation:**

We recommend that the District amend the P-2 and Annual attendance reports to reflect the above adjustment. We also recommend that the attendance clerks at all school sites make an effort to account for all absences accurately in the accounting records.

**District's Response:**

This was a clerical error. Pupil Accounting will address this issue during training sessions and in internal site audits this year. The District's P-2 report will be amended.





KPMG LLP  
Suite 1500  
750 B Street  
San Diego, CA 92101

March 21, 2004

The Audit Committee of the Board of Education  
San Diego Unified School District  
San Diego, CA:

Ladies and Gentlemen:

We have audited the financial statements of the San Diego Unified School District (the District) as of and for the year ended June 30, 2003, and have issued our report thereon, dated April 15, 2004. In planning and performing our audit of the financial statements of the District, we considered internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. An audit does not include examining the effectiveness of internal control and does not provide assurance on internal control. We have not considered internal control since the date of our report.

During our audit, we noted certain matters involving internal control and other operational matters that are presented for your consideration. These comments and recommendations, all of which have been discussed with the appropriate members of management, are intended to improve internal control or result in other operating efficiencies and are summarized as follows:

### **Open Purchases Orders**

#### **Observation**

The District does not have documented policies and procedures for the monitoring of open purchase orders during the year and at the year-end. We were informed that the District has internal controls over the validity of recorded purchase order commitments; however, we were unable to verify this assertion because such controls are not documented.

#### **Recommendation**

We recommend that the District document the policies and the activities associated with the monitoring of open purchased orders.

#### **Management Concur with the Observation and Recommendation.**

Under the old legacy system, there were no written procedures to validate and document the actual procedure that existed. This procedure was performed monthly. At the end of each month, the Budget Department printed out a list of open encumbrances (Purchase Orders and Contracts). The report was provided to Accounts Payable for review. Each open item was researched to determine whether the open item was still valid. If an item is determined to be no longer valid, Accounts Payable submitted, to Budget, the list of encumbrances to be reversed. Budget prepared the journal entries to release the encumbrances. At year-end, the Accounts Payable technicians and the Budget Analysts reviewed the open items list as is done during a normal month-end, but the Budget Analysts took an additional step of calling the originator of the Purchase Order to determine its status.



The District will in fact be analyzing the capabilities of the new PeopleSoft Financial System to determine its ability to manage encumbrances. As part of this analysis, the District will incorporate the systemic controls within the PeopleSoft Financial System into written procedures. The written procedures will ensure appropriate internal controls over the validity of recorded purchase order commitments.

### **School Reduced Lunch Program**

#### **Observation**

The District does not have a procedure for a managerial review over the required sampling of applications for the reduced lunch program.

#### **Recommendation**

We suggest that the District develop policies and procedures for a managerial review over the required sampling of applications for the reduced lunch program and provide training in the implementation of those procedures.

#### **Management concurs with the Observation and suggests an alternative corrective action.**

Currently there are two managerial reviews that take place every year to validate the applications for the reduced lunch program. The first review is done by the principal at the school site. Each of the sites then forwards the applications to Food Services where the applications are reviewed again. Food Services Department reviews the applications during the August/September time frame.

And while the District believes the dual validation process performed by the site principals and Food Services is adequate, the auditors have noted that there is a legal requirement that an annual sampling of these applications be performed by management. The District will discuss this requirement with Internal Audit and ask for their assistance in performing this review and documentation of the review.

### **General Journal Entries**

#### **Observation**

Various individuals, approximately 20, have access to generate and post general journal entries. The process does not require a supervisory review or approval over the generation and posting of the general journal entries.

#### **Recommendation**

We recommend that levels of approval be designed to ensure that only qualified personnel have the ability to generate journal entries and that the ability to do so does not result in an employee performing incompatible functions. Further, we recommend that a review at a supervisory level be performed and documented in order to ensure the propriety of the transaction.

#### **Management concurs with the Observation and suggests an alternative corrective action.**

The Financial Data Base records all expense transactions for the District. Financial Accounting prepares journals for the General Ledger based on data from the Financial Data Base. On a monthly basis, the financial accountants must balance the General Ledger to the Financial Data Base, by fund, to ensure that the expenditure journals are recorded correctly.

Journal entries for revenue accruals are prepared by the financial accounting supervisor, which are then given to a financial accountant for input into the General Ledger. Revenue journals are prepared by financial accountants and reconciled monthly with the County Treasury to ensure that revenue journals are posted correctly.

The District will consult with the auditors to establish procedures for the appropriate review of journal entries for the fiscal year 2003/2004 and beyond.

### **Associated Student Body Investments**

#### **Observation**

KPMG noted that the District's Financial Services Department does not verify the account balances of the Associated Student Body (ASB) investments at year-end. Copies of bank statements and notifications are requested as of March 31.

#### **Recommendation**

In order to monitor and fairly present ASB assets at June 30, we recommend policies and procedures be developed that provide for verification of account balances and type of depositor investment held in the Associated Student Body accounts at year-end.

#### **Management concurs with the Observation and Recommendation.**

Financial Accounting will directly request from each site's financial institution(s) that they mail the June 30 statement directly to Financial Accounting.

### **Investment Earnings**

#### **Observation**

The District participates in the County of San Diego Investment Pool. The County forwards to the District monthly statements which include the earnings on the accounts. The statements are not reviewed by District staff to determine the reasonableness of the earnings posted to the District accounts.

#### **Recommendation**

We recommend that the District formulate policies and procedures for reviewing and recalculating the earnings received on monies held at the County Investment Pool on a monthly basis.

#### **Management concurs with the Observation and Recommendation.**

Financial Accounting will periodically review with the County its procedures on calculating interest. This review will ensure that the District is receiving the proper amount of revenue earned from the County.

### **Salary Overpayment Receivable**

#### **Observation**

A salary overpayment receivable is recorded for amounts due from overpayments to District employees. Some of the amounts are aged beyond a few years and some amounts are due from terminated employees. There is doubt as to whether the amounts will be collected; however, the District has not provided for an allowance for the potentially uncollectible amounts.

### **Recommendation**

KPMG recommends that policies and procedures be implemented to monitor receivables recorded as allowance for uncollectible balances of the Salary Overpayment Balances, and that an appropriate allowance for uncollectible balances be recorded.

### **Management concurs with the Observation and Recommendation.**

In order not to overstate the District's accounts receivable for salary overpayments, the District will record an allowance for accounts deemed to be uncollectible.

## **Dental Claims**

### **Observation**

The District is not monitoring the claims approved for payment by the third-party administrator. Claims are not verified by the District staff for legitimacy, accuracy, and that the amount paid out is reasonable. Furthermore, an analysis of the sufficiency of the reserve has not been conducted. Therefore, the District cannot verify either overpayment or that there are sufficient reserves. We also noted that the District does not receive a SAS 70 report from the third-party service provider. A SAS 70 report provides information regarding controls in place at the third-party administrator and the results of independent tests of such controls.

### **Recommendation**

KPMG recommends that policies and procedures be adopted and implemented regarding Dental Fund payments and reserves. We also recommend that the District request a SAS 70 report from its third-party administrator.

### **Management concurs with the Observation and Recommendation.**

The District has contacted our third-party administrators and the third-party administrators have agreed to provide a SAS 70 report in the future.

## **Payroll Processing**

### **Observation**

Controls over changes made by the Payroll Division include a system-generated Personnel Action Form (PAF) that reflects all changes to all employees. Through inquiry of the Payroll staff, it was explained that the PAFs are not reviewed and that there is no segregation of duties through system access controls between the Payroll Technicians who input new employees and change pay rates and with Payroll Technicians who process the payroll.

### **Recommendation**

KPMG recommends that individual payroll information be maintained solely by the Human Resources Department. Further, within the Human Resources Department, levels of system access should be designed to provide segregation of the input and deletion of employee's personal data from other payroll changes. Further, we recommend that the Personnel Action Forms be reviewed at a supervisory level during every payroll cycle. This review should be documented, either on each PAF or on a summary transmittal document.

**Management concurs with the Observation and Recommendation.**

Prior to the implementation of the new payroll system on January 1, 2004, there was little reliance placed on the computer system's ability to segregate duties through access control. Controls were maintained by properly segregating the duties of Payroll Technicians who perform input from those who processed timecards and timesheets. The old system generated a PAF for any change made by the Payroll Technician. A copy of this PAF was distributed to an independent group of technicians who were responsible for a daily review and for the processing of the timesheets. Neither group of Payroll Technicians had the ability to input time reported, leave reported, or pay line adjustments.

The new payroll system implemented on January 1, 2004 does segregate the Human Resources data maintenance from the Payroll processing functions. Payroll Technicians do not have access to add, change, or delete HR data with one caveat. Limited access has been provided to Payroll Supervisors for the purpose of resolving error messages that occasionally occur during payroll processing.

**Payroll Processing**

**Observation**

The District relies on a review and sign-off of batch headers of the periodic payroll reports by accounting technicians as a control over the proper classification of payroll. As part of our audit, we tested the sign-off control and found 4 instances out of a sample of 30 where the review was not documented.

**Recommendation**

KPMG recommends that all batch headers be reviewed and signed by a payroll technician other than the one who initially input the information.

**Management concurs with the Observation and Recommendation.**

With the implementation of the new payroll system on January 1, 2004, the process tested by the auditors above is now obsolete. Under the new process, the data input function is now segregated into two processes. The reporting of time and leave are now directly input by clerical personnel at the sites. This replaces the manual timesheets previously prepared at the site and then sent to and input by the Payroll Department. All adjustments and overrides are input by a Payroll Technician, replacing the batch headers and attachments that were previously submitted to the data entry clerks.

**Application Security Controls**

**Observation**

We noted weakness in the District's implementation of application security, as follows:

KeyMaster Payroll Data Entry System – Security groups have not been correctly configured within the KeyMaster system to prevent end-users from performing security administrator functions. There are currently seven end-users with security administrator privileges (HR Data Entry Personnel).

Aeries Attendance System – We selected five schools within the school district to verify that user access to modify attendance data within Aeries is restricted to authorized personnel. We noted that each school selected had incorrectly configured Aeries user access providing unauthorized individuals with access to modify student attendance data. Specifically, we noted that two schools had each granted user access to modify attendance data to twenty-four (24) user accounts. Access to modify attendance data appears to be excessive and should be further restricted to prevent unauthorized access. At three schools, we noted that unauthorized users have been assigned access to modify student attendance data within the Aeries system.

Central Database of Attendance Data (Batch Server) – We noted that user access to modify attendance data on the District's centralized Batch Server has been granted to fifty-two (52) user accounts (IT personnel). Access to modify attendance data appears to be excessive and should be further restricted to prevent unauthorized access.

Payroll Application – Seven unauthorized users have been assigned access to modify employee data within the Payroll application (Fiscal Control Technicians, Retired Payroll Staff, etc.).

A stronger security control environment will reduce the risk that information assets will be inappropriately protected from unauthorized disclosure and manipulation.

#### **Recommendation**

KPMG recommends that the application security control environment be strengthened as follows:

- Restrict user access only to personnel who require the access
- Implement a District-wide Aeries security configuration to ensure that user access within the Aeries system is appropriately restricted
- Process owners should perform a semi-annual review of user access by reviewing reports of specific transactions to which users have access.

#### **Management concurs with the Observation and Recommendation.**

KeyMaster Payroll Data Entry System – The KeyMaster system is no longer in use. No further action is necessary.

Aeries Attendance System – The District will reiterate our position on proper security and make recommendations to each of the sites as to the proper security configuration to ensure that the user access within the Aeries system is appropriately restricted.

Central Database of Attendance Data (Batch Server) – Access to the data via the batch server is not available directly. It is not possible to modify the data unless the user has knowledge of the upload process and the ability to create an ad hoc batch job to override the normal upload process. The District will review the access levels of the fifty-two (52) user accounts for appropriateness.

Payroll Application – This problem has been resolved with the District's implementation of the new Payroll system on January 1, 2004.

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**Management concurs with the Observation and Recommendation.**

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Payroll Application – This problem has been resolved with the District's implementation of the new Payroll system on January 1, 2004.

## **Disaster Recovery & Business Continuity Planning**

### **Observation**

A formal disaster recovery capability has not been developed to respond to emergencies affecting computer systems and to recover computer operations in the event of an unplanned processing disruption. Provisions for an off-site recovery of computer operations have not been formally considered or researched.

Business continuity plans have not been developed for the business units to continue operations after an unplanned processing disruption. The process of developing a Business Continuity Plan must include extensive involvement from business process owners to identify requirements and activities to be performed while systems are non-operational.

An example of the District's disaster scenario exposure would be the ability to re-establish Human Resources, Payroll, Budgeting, and Financial operations if the District's computer room were unavailable.

### **Recommendation**

KPMG recommends that management perform disaster recovery and business continuity planning. The first step in the planning effort is the development of a business impact analysis and risk assessment. This effort is especially critical for the District now since a new system environment is in the process of being implemented. It is much more efficient and cost-effective to build in disaster recovery while systems are being implemented instead of after they are implemented.

Once developed, KPMG recommends that the plans be tested and updated on an annual basis.

### **Management concurs with the Observation and Recommendation.**

Information Technology has developed plans and associated cost estimates to address disaster recovery and business continuity planning. Now that the District has implemented the District-wide Applications infrastructure and assuming the proper funding is available, this project can be completed at a reasonable cost.

## **Enterprise Security**

### **Observation**

KPMG noted several instances where the District's approach to enterprise security could be strengthened, as follows:

- The Information Technology security policy is not up to date and is not sufficient for the complexity and security requirements of the District's information technology environment.
- Active monitoring of the central network and firewall for security breaches and vulnerabilities is not performed.
- The Information Technology Department does not administer and track the use of modems by end-user departments that connect to network workstations.



**Recommendation**

KPMG recommends that the District continue efforts to develop its enterprise security approach. We understand that security responsibilities have been assigned to a designated group within the Information Technology Department. This group should have sponsorship at the senior management level. Senior management should foster the development of an entity-wide security program which should address areas such as the following:

- A comprehensive security policy with topics such as minimum security baseline standards, security monitoring requirements, and security incident handling requirements.
- Responsible resources (including staff and system tolls) to monitor security vulnerabilities.
- Modem acquisition, tracking, and security requirements

**Management concurs with the Observation and Recommendation.**

Information Technology has included the developing of "New Computer Security Policies" as a planned project to be completed in 2004.

A Network Intrusion Detection System (IDS) is now in place for the District's DWA environment. The District now needs to address the lack of resources to process the large amounts of data that have thus far prevented comprehensive District-wide active monitoring.

Information Technology is able to control modem access to the network workstations at the Central office but not at the sites. The Central office has a modem server, and IT controls user accounts and utilizes a digital phone switch which prevents users from installing personal modems. In addition, Information Technology controls VPN access to the District's internal applications.

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Our audit procedures are designed primarily to enable us to form an opinion on the financial statements, and therefore may not bring to light all weaknesses in policies or procedures that may exist. We aim, however, to use our knowledge of the District's organization gained during our work to make comments and suggestions that we hope will be useful to you.

We would be pleased to discuss these comments and recommendations with you at any time.

This report is intended solely for the information and use of the Board of Education, management, and others within the organization and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

**KPMG LLP**