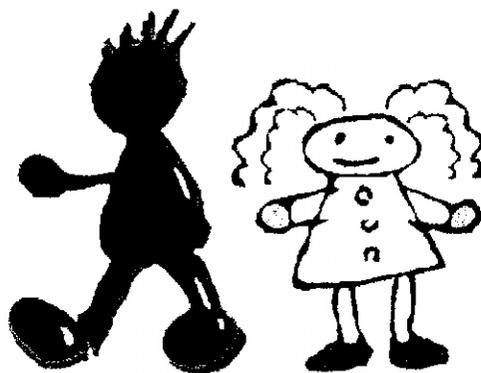


DISTRICT OF COLUMBIA PUBLIC SCHOOLS

children first



Comprehensive Annual Financial Report
Fiscal Year Ended September 30, 2001

District of Columbia Public Schools

Washington, D.C.

**Comprehensive Annual Financial Report
Fiscal Year Ended September 30, 2001**

Prepared by:

Office of the Chief Financial Officer

**Mathew Aloth
Acting Chief Financial Officer
825 North Capitol Street, NE, 7th Floor
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DISTRICT OF COLUMBIA PUBLIC SCHOOLS

Introductory Section

Comprehensive Annual Financial Report
Fiscal Year Ended September 30, 2001



**DISTRICT OF COLUMBIA
PUBLIC SCHOOLS**

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The Board of Education
Of The District of Columbia

January 22, 2002

Ladies and Gentlemen:

The Comprehensive Annual Financial Report (CAFR) of the District of Columbia Public Schools (DCPS) for the fiscal year ended September 30, 2001, is submitted herewith and includes the general purpose financial statements audited by KPMG LLP, independent certified public accountants. The Office of the Chief Financial Officer (OCFO) prepared the financial statements for the DCPS and is responsible for the accuracy, completeness and fair presentation of the data for independent audit, including all disclosures. The Board of Education and the management of the DCPS accept the representation of the OCFO that the data presented reflect the financial position and the result of operations of the DCPS. This data presents fairly, in all material respects, the aforementioned financial position of the DCPS, as measured by the financial activity of its various funds. Furthermore, all disclosures necessary for public understanding of the DCPS financial status have been incorporated in this report.

The CAFR is presented in three sections: introductory, financial, and statistical. The introductory section includes this transmittal letter, a list of current members of the Board of Education and selected Superintendent's executive officers, and the DCPS organizational chart. The financial section includes general-purpose financial statements and individual fund and account group financial statements and schedules. The statistical section includes selected financial and demographic information generally presented on a multi-year basis.

ECONOMIC CONDITION AND OUTLOOK

The DCPS concluded FY 2001 with a \$64.5 million deficit in locally appropriated funds. To an overwhelming extent, this deficit was caused by expenditures for court-ordered or statutorily mandated special education programs and related transportation programs that proved to be in excess of projected and budgeted amounts. At the same time, FY 2001 as well as prior years' over-estimates of Medicaid revenue resulted in an assumption of disallowed Medicaid costs by the local budget.

The OCFO has attributed these cost overruns to ineffective financial management, analysis, monitoring and reporting on the part of the Chief Financial Officer for the DCPS (DCPS CFO) who reports to the Chief Financial Officer of the District of Columbia. Neither the DCPS management nor the OCFO received financial information or forecasts that would have permitted timely remedy of FY 2001

spending pressures. As a result of OCFO management concerns, the DCPS CFO along with his senior deputies were replaced in July 2001. By late August, the new DCPS CFO had recognized and reported the extent of financial liability in excess of budgeted amounts. The new DCPS CFO and the DCPS management took immediate and drastic action to curtail spending and maximize revenue for the remainder of the fiscal year. However, too much of that period had elapsed to either augment the DCPS budget or limit spending to remaining availability.

With less than six weeks remaining in the fiscal year, management reduced planned spending by \$23.7 million and the District of Columbia Government reprogrammed \$12.1 million from other program areas. These steps, however, were not sufficient to offset all of the overspending earlier in the year resulting in total spending of \$64.5 million over locally appropriated funds for FY 2001. This overspending has been reported as required by Federal law to the appropriate officials.

Approximately \$39.9 million or 62% of the total overspending in FY 2001 resulted from prior year costs and unrealized revenues which were not known until FY 2001. Included in the \$39.9 million is \$17.4 million in Medicaid disallowances, recorded by the OCFO, per the Medical Assistance Administration's audit that identified this amount as potential overpayments received in fiscal years 1996 through 1998, another \$11.0 million in unrealized revenue from the FY 1999 Medicaid cost settlement report, \$4.8 million in accounts payable from fiscal years 1999 and 2000, \$2.9 million in accounts payable for special education tuition and attorney fees, \$2.2 million in retroactive pay for teachers, and \$1.2 in costs related to October 2001, arbitration award for Teamsters.

The prior years' disallowed Medicaid claims remain an open DCPS item. The Board of Education, the Superintendent of Schools and the OCFO are pursuing all means available for appeal and recovery of these disallowed costs.

The DCPS and the OCFO are also jointly addressing deficiencies with special education operations and related Medicaid estimating and billing to prevent future overspending. Action is also being taken by the Board of Education and the District of Columbia government to adjust the FY 2002 DCPS operating budget based on the FY 2001 experience. A combination of increased DCPS funding for special education-related programs and reductions elsewhere should result in a balanced budget for FY 2002.

THE REPORTING ENTITY AND SERVICES PROVIDED

The DCPS operates within the District of Columbia, a community of varied neighborhoods and home to approximately 572,000 residents. The District is the nation's capital and the seat of the federal government and its area covers 60 square miles of land and nine square miles of water.

Residents of the District were granted the right to elect the Board of Education of the District of Columbia (the Board) in a 1968 legislative reform. The Board consisted of 11 elected members who served staggered, four-year terms. A nonvoting member of the student body was elected to the Board annually. On November 15, 1996, an Emergency Transitional Board of Trustees (the Trustees) was appointed by the District of Columbia Financial Responsibility and Management Assistance Authority

(DCFRMAA). This Board of Trustees assumed immediate responsibility for the management and operation of the DCPS and served until January 2001.

In June 2000, voters of the District of Columbia passed a referendum to create a new school board structure. Under the new structure, the District residents elect five members and the Mayor appoints four members. The new Board of Trustees assumed responsibility for the governance of the DCPS in January 2001.

The DCPS number one priority is to meet the challenge of providing a comprehensive educational program in an atmosphere that is open to, concerned about, and responsive to the needs of students and the community.

As of September 30, 2001, the DCPS operated 103 elementary schools, 23 junior high schools, 16 senior high schools, and 7 special programs, including career and adult education and an arts center. The DCPS provides a range of educational services for preschool through adult-age students. The services include comprehensive educational programs and special learning opportunities for elementary, junior high, and senior high school enrollees. In addition, the Head Start program, the Visiting Instruction Corps, the Public/Private Partnership programs, and alternative academic/career-training/entrepreneurial programs are provided through the DCPS. The career enrichment program, under the auspices of the Public/Private partnership programs, offers opportunities to explore a broad range of career options for students in grades four through eight at selected elementary, middle, and junior high schools.

The Emergent Literacy Program, a segment of Early Childhood Education, provides early language development experiences to pre-kindergarten and kindergarten students. Special education programs are provided to students who have been identified as having physical handicaps, learning disabilities, mental and emotional problems, or behavioral patterns that require specialized instruction.

The DCPS is a fiscally dependent school system, and an agency of the Government of the District of Columbia (the District). A significant portion of the revenue of the DCPS is provided by District appropriations. Further, the DCPS funding is subject to the budgetary procedures followed by the District in its annual request to the United States Congress. As an agency of the District, the financial position and results of operations of the DCPS are included in the various funds and account groups of the general-purpose financial statements of the District.

The DCPS CAFR includes the instructional and operating activities and all related support functions of the 149 schools providing educational services as of September 30, 2001, as well as the activities of other instructional programs. The following are specifically excluded from the DCPS CAFR:

The DCPS does not have title to any land and school buildings; therefore, these are excluded from the DCPS' General Fixed Assets Account Group. The District owns these properties and includes them in its CAFR.

Employees of the DCPS are covered by various pensions and deferred compensation plans. The District and federal governments provide the employer's share of contributions to these plans. Further, the plans are operated and managed by the District and federal governments. Accordingly,

the financial activities of these plans are excluded from the DCPS CAFR. They are included in the District's CAFR.

- (3) The District has issued various long-term general obligation bonds and notes used, in part, to finance the operations of the DCPS. These long-term obligations are secured by the full faith and credit of the District government. The District has the ultimate responsibility for such debts and, as such, they are not reflected in the DCPS financial statements. Instead, they are reflected in the District's CAFR.
- (4) The DCPS does not have the authority to levy taxes on District residents; therefore, tax revenues are excluded from the DCPS financial statements.
- (5) The District of Columbia Public School Reform Act of 1995, as amended, established the chartering authority of the District of Columbia Board of Education to monitor the operations of each public charter school. Funding for these charter schools is provided in the Appropriation Act of Congress under the Public Education System, separate from that of the DCPS. Accordingly, the financial activities of the charter schools are excluded from the DCPS CAFR.

INTERNAL ACCOUNTING CONTROLS

The accounting system of the DCPS depends on a foundation of internal control structure to ensure that financial information generated is both accurate and reliable. The internal control structure is designed to provide reasonable, but not absolute, assurance regarding the safeguarding of assets against loss from unauthorized use or disposition and the reliability of financial records for preparing financial statements and maintaining accountability for assets. The concept of reasonable assurance recognizes that the cost of the control should not exceed the benefits to be derived, and the evaluation of costs and benefits requires estimates and judgment by management. The financial accounting and budgetary systems are automated and include edits necessary to ensure that all system-generated transactions agree with predetermined totals before entering into the accounting system.

All internal control evaluations occur within the above framework. The relationship of internal control to basic management responsibilities emphasizes the interaction of the accounting system with other management control systems.

ACCOUNTING SYSTEM AND BUDGETARY CONTROL

The DCPS accounting system is organized and operates on a fund basis. A fund is an independent fiscal and accounting entity with a self-balancing set of accounts that is used for recording assets, liabilities, fund equity, revenues, and expenditures. The types of funds used are determined by generally accepted accounting principles (GAAP) practiced in the United States of America. The number of funds established is determined by financial administration.

This report has been prepared in accordance with GAAP for governmental entities. The report includes all funds and account groups of the DCPS. The funds and account groups included in the CAFR are:

- (1) General Fund
- (2) Capital Projects Fund
- (3) Fiduciary Funds – Central Investment (Trust) and Student Activity (Agency)
- (4) General Fixed Assets Account Group
- (5) General Long-Term Debt Account Group

Financial transactions related to school breakfast and lunch programs are reported in the General Fund. This operation depends heavily on federal and District subsidies to supplement and support the overall breakfast and lunch programs. The District's System of Accounting and Reporting (SOAR), under which the DCPS operates, has the capability to separately identify revenue and expenditures for food services operations and other programs using federal grants. Approximately 74 percent of the student population receives free or reduced-price meals; therefore, the food services program has not been presented as a proprietary fund.

The DCPS financial statements have been prepared on the modified accrual basis of accounting in accordance with GAAP for governmental units. The notes to the financial statements include additional information on the DCPS accounting policies.

The DCPS annual budget is included in the District's overall budget request to Congress. In a period other than a control period, as defined in Section 305(4) of the District of Columbia FRMAA Act of 1995, approved April 17, 1995, the DCPS budget is subject to approval by both the Council of the District of Columbia and the federal government, prior to actual congressional appropriation of funds for each fiscal year. During a control period, there are modifications to the budget process as described in Note 1 to the general-purpose financial statements. The DCFRMAA formally went out of existence as of September 30, 2001 because the District met the requirements for its termination.

All accounting transactions, including revenue recognition, payroll, and vendor payments, are processed through SOAR.

The DCPS appropriated General Fund budget is enacted on a basis consistent with GAAP. Total expenditures of the DCPS may not legally exceed its budget appropriations at the fund level; however, the DCPS reserves the right to allocate its budget by organization code, program code, and object code as a management control device.

As a part of the normal financial reporting process, all actual activities are compared to budget. In addition, projected expenditures, and unexpended balances are reported monthly to school administrators and members of the Board. These monthly reports compare each line item account balance to the annual

budget with accumulations by organization code, program code and fund levels. However, these monthly reports were not produced nor provided to DCPS management during FY 01.

FINANCIAL HIGHLIGHTS

General Fund

Revenues of the General Fund totaled \$797,552,000, an increase of 1.1% over the preceding year. The amount of revenues from various sources and the changes from the previous fiscal year are as follows (all amounts are in thousands):

<u>Source of Revenue</u>	<u>Fiscal Year 2001</u>		<u>Increase (Decrease) From Fiscal Year 2000</u>	
	<u>Amount</u>	<u>% Of Total</u>	<u>Amount</u>	<u>% Increase (Decrease)</u>
District of Columbia appropriations	\$ 674,648	84.6%	\$ 72,859	12.1%
Restricted federal grants	77,263	9.7%	(79,562)	-50.7%
Unrestricted federal grants	5,235	0.7%	(83)	-1.6%
Charges to other District agencies	33,029	4.1%	16,151	95.7%
Restricted private grants	2,465	0.3%	(1,118)	-31.2%
Miscellaneous	4,912	0.6%	186	3.9%
Total	\$ 797,552	100.0%	\$ 8,433	1.1%

Expenditures for the general fund totaled \$862,675,000, an increase of 9.6% over fiscal year 2000. Variances in levels of general fund expenditures by major functions of the DCPS compared to the preceding year are shown in the following table (all amounts in thousands):

<u>Function</u>	<u>Fiscal Year 2001</u>		<u>Increase (Decrease) From Fiscal Year 2000</u>	
	<u>Amount</u>	<u>% Of Total</u>	<u>Amount</u>	<u>% Increase (Decrease)</u>
Administration	\$ 21,972	2.5%	\$ (10,078)	-31.4%
Instruction	417,190	48.5%	76,559	22.5%
Instructional Support	27,000	3.1%	(36,630)	-57.5%
Special Populations	199,688	23.1%	30,257	17.8%
Pupil personal services	4,277	0.5%	(1,801)	-29.6%
Other operational costs	37,887	4.4%	13,544	55.6%
Building operations and maintenance	79,373	9.2%	1,034	1.3%
Transportation	52,491	6.1%	6,854	15.0%
Food services	22,797	2.6%	(4,126)	-15.3%
Total	\$ 862,675	100.0%	\$ 75,613	9.6%

Expenditures for instruction and instructional support represent 51.5 percent of total expenditures. These two functions reflect a 9.8% increase over FY2000 expenditures.

Administrative costs decreased by 31.4% because equipment and software compliance issues were fully executed in FY2000 and because of the reclassification of Management Information Services to Other Operational Costs.

The 22.5% increase in Instruction expenditures was primarily due to teachers' pay increases.

Special Population expenditures increased 17.8% due to an increase in Special Education students and tuition payments and an audit settlement for prior year Medicaid payments.

Pupil Personal Services decreased by 29.6% due to a 50% budget reduction in Teaching and Learning services.

Other Operational Costs increased by 55.6% due to an organizational change which resulted in the reclassification of Management Information Systems from Administration to Other Operational Cost and an increase in services connected with the preparation of a new software system.

Building Operations and Maintenance increased by 1.3% due to an increase in salaries and overtime associated with the increase in capital projects.

The 15.0% increase in Transportation expenditures was due to a liability of \$7.9 million created by the teamsters pay negotiation settlement.

The 15.3% decrease in Food Services was due to an adjustment in fiscal year 2001 that moved the State agency function from the DCPS to the District.

Variances in levels of general fund expenditures by DCPS object classes compared to the preceding year are shown in the following table (all amounts in thousands):

Object Class	Fiscal Year 2001		Increase (Decrease) From Fiscal Year 2000	
	Amount	% Of Total	Amount	% Increase (Decrease)
Salaries, wages and benefits	\$ 561,032	65.1%	\$ 55,731	9.3%
Supplies and materials	31,912	3.7%	(687)	-0.1%
Energy, communications and rentals	31,207	3.6%	2,982	0.5%
Other services and charges	93,537	10.8%	(9,324)	-1.5%
Subsidies and transfers	123,972	14.4%	36,461	6.1%
Equipment, rentals and textbooks	21,015	2.4%	(9,550)	-1.6%
Total	\$ 862,675	100.0%	\$ 75,613	9.6%

Salaries and benefits increased by 9.3% as a result of pay increases of 3% to teachers and 6% to non-union employees. Other related costs included \$15 million in administrative premium; \$16.9 million in teamsters pay negotiation, and grievances and retroactive payments to other employees.

Subsidies and transfers increased due to special education tuition payments.

The DCPS budget is labor-intensive, with 65.1% of general fund expenditures designated for personnel services.

Capital Projects Fund

The DCPS is charged with the creation and maintenance of a safe, nurturing and stimulating educational environment in which all children can develop their academic, creative and intellectual potential. The upgrading of the DCPS facilities is a continuous process.

The Capital Projects Fund accounts for expenditures for roof and boiler replacements, emergency generators, asbestos abatement, underground storage tanks, safety systems, and other building improvements. Purchases of vehicles and equipment by the capital projects fund are capitalized as additions to the General Fixed Assets Account Group.

In fiscal year 2001, the capital project fund received \$175,605,000 in total revenue comprising \$168,896,000 in appropriated funds, \$1,096,000 in Federal grants and \$5,613,000 from the sale of surplus property.

Fiduciary Fund – Student Activity Funds

This fund accounts for all revenue raised in the name of a school or for school organizations, monies collected from students, and all revenue collected at school sponsored activities. Agency funds are custodial in nature (assets are offset by a liability) and do not involve measurement of results of operations. There are 149 schools administering these funds, each of which has its own bank account, and each of which is subject to central office internal audit controls and a staggered annual external audit. As of September 30, 2001, assets of these funds totaled approximately \$2,383,153.

Fiduciary Fund –Central Investment Expendable Trust Fund

Idle funds are invested primarily in money market funds, certificates of deposit, and U.S. government securities. As of September 30, 2001, the market value of the invested funds was approximately \$1,164,000. In addition, \$786,000 was due from other funds.

General Fixed Assets Account Group

The facilities and other general fixed assets of the DCPS are used to carry out the main educational functions of the school system and are not financial resources available for expenditures. As of September 30, 2001, the general fixed assets of the DCPS amounted to approximately \$18,127,000. This amount represents the actual or estimated historical cost of the assets, net of accumulated depreciation. Historical cost is considerably less than the present replacement value. Additions may include vehicles and equipment purchased by the capital projects fund and the general fund.

General Long-Term Debt Account Group

This fund is used to account for the long-term portion of employees' unused vested annual leave entitlements, employee compensation agreements and amounts owed under long-term leases of school buses. In practice, the current-year costs of annual leave taken and early retirement benefit payments are financed through the General Fund's annual budget. At September 30, 2001, the total long-term liability of the DCPS was approximately \$11,344,000.

CASH MANAGEMENT

The DCPS has no significant cash and investments of its own. The District's Office of Finance and Treasury has the responsibility for the cash management and investment functions for all District agencies, including the DCPS. The DCPS, however, manages four imprest bank accounts, 154 checking accounts for direct purchases of supplies by local schools, bank accounts maintained by local schools for the deposit of student activity funds, and a central investment pool to consolidate resources of private donations for scholarships and educational programs.

As of September 30, 2001, the DCPS controlled cash and investments (all short-term) totaled \$4,345,000. All checking accounts (imprest, direct purchases, student activity and emergency payroll assistance) are all interest-bearing accounts. Investments are maintained in mutual funds, U.S. Treasury notes, notes issued by federal agencies, secured certificates of deposit, and in the District of Columbia Teachers' Credit Union. Total interest income for fiscal year 2001 amounted to \$45,266.

RISK MANAGEMENT

Consistent with the policies of the District of Columbia government, the DCPS retains the risk of loss arising out of the ownership of property or from some other cause, except health care and life insurance benefits for employees. Significant losses, when determinable, are reported. In addition, these losses are paid by the District through a separate appropriation. No significant losses occurred during fiscal year 2001.

OTHER INFORMATION

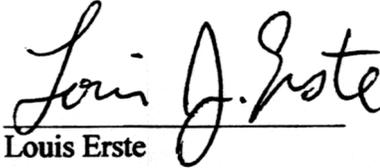
Independent Audit

Although not required by statute, the DCPS has had its financial statements audited annually over the past 20 years by independent certified public accountants. The DCPS auditors for fiscal year 2001 are KPMG LLP. The auditors' unqualified opinion on the financial statements is included in this report. In addition, as a recipient of federal financial assistance, the DCPS is subject to the audit requirements of the Single Audit Act Amendments of 1996 and OMB Circular A-133.

Respectfully submitted,



Natwar M. Gandhi
Chief Financial Officer
The District of Columbia



Louis Erste
Chief Operating Officer
The District of Columbia Public Schools



Dr. Paul Vance
Superintendent
The District of Columbia Public Schools

**Members of the Board of Education and Executive Officers
September 30, 2001**

Board Members

Ms. Peggy Cooper Cafritz	President	
Ms. Julie Mikuta	District 1 Member	Wards 1 & 2
Mr. Dwight E. Singleton	District 2 Member	Wards 3 & 4
Mr. Tommy Wells	District 3 Member	Wards 5 & 6
Mr. William Lockridge	District 4 Member	Wards 7 & 8
Ms. Laura Gardner	Appointed Member	
Mr. Charles Lawrence	Appointed Member	
Mr. Roger Wilkins	Appointed Member	
Vacant	Appointed Member	
Mr. Don Folden	Student Representative	
Mr. German Vigil	Student Representative	

Executive Officers

Dr. Paul Vance	Superintendent of Schools Chief State School Officer
Dr. Steven G. Seleznow	Chief of Staff
Mr. Louis J. Erste	Chief Operating Officer
Ms. Janie S. McCullough	Executive Officer
Ms. Patricia Watkins Lattimore	Director of Human Resources
Mr. Mathew Aloth	Acting Chief Financial Officer
Dr. Linda Wharton Boyd	Chief of Communications
Ms. Veleter M.B. Mazyek	General Counsel