



## STATE OF COLORADO

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### MEMORANDUM

Date: September 12, 2003

To: Members of the Legislative Audit Committee

From: Joanne Hill, CPA  
State Auditor

Re: Boulder Valley School District and the Interest-Free School Loan Program, Fiscal Year 2003 - Report No.1587

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#### Overview

In July 2003, the State Treasurer's Office requested that pursuant to Section 22-54-110(4) C.R.S, we conduct an audit of the Boulder Valley School District's (BVSD) participation in the Interest-Free Loan Program for Fiscal Year 2003. The request was prompted by concerns that the District had used borrowed funds to earn interest rather than to alleviate cash flow problems.

In order to determine if BVSD had appropriately used the State's interest-free loans, we reviewed both the District's requests for loans and repayment of loans. We traced amounts reported on BVSD's worksheets to the District's accounting records, financial statements, bank statements, and investment statements. Finally, we tested the calculation of the repayments to ensure that BVSD correctly calculated its cash deficits and resources available for repayment and repaid in compliance with statutes.

We found that BVSD's documentation supported the need for loans and that the loans were repaid within the statutorily required deadlines. We also found that the worksheets related to the loans submitted by BVSD to the Treasurer's Office contained errors. While these errors did not materially affect BVSD's overall need for borrowing, they do indicate that both BVSD and the Treasurer's Office need to improve oversight of basic financial information. A description of our testwork and conclusions follows.

#### Background

School districts receive their revenue from local and state sources. The local share (about 39 percent in Fiscal Year 2004) comes from property taxes and vehicle registration taxes. The state share (about 61 percent in Fiscal Year 2004), commonly known as equalization payments, is funded primarily from individual and corporate income taxes and sales and use taxes. The cash flows to the districts from the state share are fairly steady from month to month, while cash flows to the districts from the local share, which consists primarily of property taxes, occur during the months of March, May, and June.

The Interest-Free School Loan Program began in 1993 when the General Assembly mandated that the fiscal year for all school districts be converted from a calendar year to a year ending June 30, which is the State's fiscal year. During the transitional year, which occurred between January and June 1992, the State required school districts to first utilize property tax receipts to fund expenditures. The State deferred making equalization payments if a district's property tax receipts were sufficient to cover expenditures. In addition, the State required those districts to use property tax balances, referred to as "property tax carryforwards," to partially offset those districts' equalization payments in the following fiscal year. The Interest-Free School Loan Program was intended to alleviate some of the cash flow problems that the districts experienced as a result of these funding changes. Pursuant to Section 22-54-110, C.R.S., school districts may apply to the Treasurer's Office for interest-free loans to alleviate General Fund cash flow shortfalls. Once the district has demonstrated, to the satisfaction of the State Treasurer, that a General Fund cash deficit will exist for any month of the budget year, an interest-free loan will be made available.

School districts receive the majority of their property tax revenue toward the end of the June 30 fiscal year, but since expenditures are relatively stable throughout the year, districts sometimes experience cash flow problems for several months before the bulk of property taxes are received beginning in March. Cash flow problems are greatest for school districts that rely more heavily property tax revenue than on equalization payments. Boulder Valley School District, for example, received approximately 75 percent of its revenues from property taxes during Fiscal Year 2003.

### **Boulder's Fiscal Year 2003 Loans**

We reviewed BVSD's loans and related repayments under the Interest-Free School Loan Program during Fiscal Year 2003. In total, BVSD borrowed and repaid about \$60.4 million during the months of October 2002 through June 2003. The loan requests were as follows:

<b>Boulder Valley School District Interest-Free Loan Requests Fiscal Year 2003</b>	
<b>Date</b>	<b>Amount</b>
October 10	\$16,017,764
November 8	16,422,505
December 10	2,500,000
December 20	15,677,095
February 28	2,703,242
March 10	7,041,614
<b>Total Loans</b>	<b>\$60,362,220</b>
<b>Source:</b> Office of the State Auditor analysis of Treasurer's Office records.	

We tested the documentation supporting the loans. While we identified errors in the worksheets submitted by BVSD in support of the loans to the Treasurer's Office, we concluded that Boulder was able to support its requests for interest-free borrowing. In fact, had its worksheets been completed accurately, Boulder could have requested about \$2 million in additional loans.

We then looked at the repayment of the loans. Section 22-54-110 (2)(a), C.R.S., provides that:

For the months of March, April, and May of each budget year, any district receiving a loan under the provisions of this section **shall begin to repay** such loan if the district's available resources, **as of the last day of the month**, increased by the next month's revenues exceed the next month's expenditures plus a cash reserve. The excess resources must be remitted to the state treasurer by the close of the business on the **fifteenth day**, or the first business day following the fifteenth day, of the following month. All loans shall be repaid by June 25 of the state fiscal year in which the loan was made or on an alternative date as determined by the state treasurer . . .  
*(Emphasis added.)*

For example, for the month of March, if property taxes came in by March 10, a district would calculate its projected financial condition for the month of April on March 31. If its projections showed adequate resources, the district would be required to repay the State Treasurer by April 15. Boulder made three repayments (April 7, June 6, and June 25); each was based on calculated cash flow, and each was remitted timely. The entire \$60.4 million was repaid by the final deadline of June 25. During the days that the loans were outstanding, we estimate that BVSD may have earned about \$49,000 in interest for the days from when the property taxes were remitted to when the loans were repaid. Obviously, the closer a district repays its loan in relation to the deadline, the more opportunity the district has to earn interest. The original intent of the Interest-Free Loan Program was to help the districts with cash flow problems resulting from the mandated change in fiscal year-end to June 30 and the delay in state equalization payments. As noted earlier, when the change occurred the State deferred making equalization payments if the district's property tax receipts were sufficient to cover expenditures.

We also reviewed the loan repayment dates in Fiscal Year 2003 for the five school districts with the largest loans. These districts borrowed 82 percent of interest-free school loan dollars in that year. We found that districts varied significantly on the timing of loan repayments, although all five repaid their loans by final the statutory deadline for the fiscal year of June 25. As illustrated by the table in Appendix A, some school districts made loan payments within several days or weeks after receiving property tax receipts (e.g., Cherry Creek received property tax on February 10 and made a payment on February 25; Douglas County received property tax on March 10 and made a payment on March 10). In other cases, districts did not make payments until the month following the receipt of property taxes.

While all of the districts were within the statutory deadlines for repayment of their loans, the districts may have earned interest on the loans after property taxes were in and before required loan payment

dates. The State Treasurer, concerned about the increase in loan requests (\$259 million in 2002 vs. \$341 million in 2003) and about potential interest lost to the State, worked with the General Assembly during the 2003 Legislative Session on the passage of House Bill 03-1274. This bill enacted substantial modifications to the Interest-Free School Loan Program effective Fiscal Year 2004. The bill authorized the State Treasurer to issue tax and revenue anticipation notes (TRANS) on behalf of school districts participating in the program. The proceeds from the TRANS are used to make the interest-free loans to school districts, using the property tax revenues of each respective district as the collateral for the TRANS. Beginning in Fiscal Year 2004, State Treasurer policies require that school districts deposit property taxes with the State within one business day of receipt.

This change essentially means that school districts with interest-free loans cannot invest property tax receipts and earn interest prior to repayment of loans as may have occurred under the previous statute. The recent modification to the program means that some school districts may choose different means of financing their cash flow needs than the Interest-Free School Loan Program. For example, BVSD has indicated that it will not participate in the Interest-Free School Loan Program for Fiscal Year 2004, but instead has issued its own TRANS. While these TRANS will not be interest-free, BVSD believes that it will have more flexibility in managing its cash flows than under the State's program.

### **Errors in Worksheets**

While we concluded that overall BVSD met statutory requirements, our audit identified a number of errors in the worksheets submitted by BVSD to the Treasurer's Office in relation to the loan program. The State Treasurer requires that monthly worksheets be submitted for each month in which a school district participates in the Interest-Free School Loan Program. Districts must demonstrate their cash flow need by preparing a "Request and Repayment Worksheet" and a "Cash Reconciliation Worksheet."

We noted numerous problems with BVSD's worksheets. While these errors did not result in overborrowing by the District or additional interest cost to the State, they do indicate a lack of review by both the District and the Treasurer's Office. Specifically, we found:

**Request and Repayment Worksheets.** The request and repayment worksheet estimates the need for the loan and the ability to repay. The worksheet documents the district's beginning cash balance for the month, its estimated receipts and other available funds, capital and insurance reserves, estimated disbursements, an 8 percent reserve factor (for repayment only), and an estimated monthly cash ending balance. We found the following errors in BVSD's request and repayment worksheets:

- **Estimated Revenues and Expenditures.** BVSD used the previous instead of the current month's estimated revenues and expenditures. For example, the District used September estimates for its October loan request when it should have used October estimates. If its financial need had been estimated with the correct information, the District could have started borrowing in August rather than in October.

- **Cash Flows vs. Cash Balances.** BVSD used monthly cash *flows* of other available funds and of capital and insurance reserves rather than monthly cash *balances*. In some cases, this meant that BVSD reported negative cash flows, although a positive cash balance existed. As a result, BVSD understated its cash available from other funds for several months.
- **TABOR Cash Balance Inclusion.** BVSD incorrectly included the cash balance restricted for the TABOR emergency reserve in its available funds at the beginning of Fiscal Year 2003. By including the TABOR reserves, BVSD understated the amount of loans for which it was eligible during Fiscal Year 2003.

**Cash Reconciliation Worksheet.** The cash reconciliation worksheet is a “look back” form that documents what actually occurred. The purpose of this worksheet is to show how accurate a district’s estimates are on its request and repayment worksheets. The cash reconciliation worksheet documents for the prior month the actual beginning cash balance, plus actual receipts and less actual expenditures for the month, and the actual ending cash balance. We found BVSD used the beginning cash balance from the month prior to the correct month on its cash reconciliation worksheets. For example, in performing the cash reconciliation for November 2002, BVSD used the October 1, 2002, cash balance when it should have used the November 1, 2002, cash balance.

Taken altogether, had the District followed the Treasurer’s Office instructions correctly, BVSD could have borrowed a total of \$62.1 million or about \$2 million more than the \$60.4 million actually requested. The estimated interest cost to the State was about \$81,000 less than if BVSD had properly followed the instructions and applied for the full amount for which it was eligible.

## Conclusions

As noted earlier, our review indicated that BVSD’s information supported the need for loans, and we found that the district repaid the loans within the statutory deadlines. Our audit also indicates that improvements are needed by both BVSD and the Treasurer’s Office with respect to ensuring that information submitted under the Interest-Free Loan Program is accurate and complete. The Treasurer’s Office has the responsibility to approve all loans to school districts participating in the program and establish mechanisms to ensure that school districts are consistently and accurately reporting cash deficits. The errors we noted during our review of the worksheets for BVSD were not identified by the District prior to submission, and they were not detected by the Treasurer’s Office before the loans were approved and issued to BVSD. Boulder Valley School District should improve its oversight and review of basic loan information to ensure its accuracy and completeness. The Treasurer’s Office should have controls in place to ensure information submitted in support of loans by the districts is adequate and reasonable before releasing funds. Specifically, we found that the Treasurer’s Office had adequate supporting documentation to identify several of the errors on the BVSD worksheets noted during our review.

We have discussed the issues identified with the Boulder Valley School District and the Treasurer's Office. Boulder Valley School District stated that the errors occurred due to misinterpretation of the regulations. If the District applies for loans in the future, it will strengthen review procedures and ensure that the information submitted is correct.

With respect to the Treasurer's Office, under the new provisions for the Interest-Free School Loan Program established in HB 03-1274 the State Treasurer has the authority, among other things, to enter into contracts with financial advisors and other parties in connection with the issuance of the tax anticipation notes. The Treasurer's Office is responsible for determining the amount of TRANS that should be issued on behalf of a district and defining the districts' responsibilities under the program. The Treasurer's Office reports that it has established procedures for both the financial advisor and Treasury staff to review spreadsheets submitted by the districts in support of loan requests.

Report No. 1587

**APPENDIX A**

<b>Interest-Free School Loan Program Repayment Dates for Five Largest Borrowers Fiscal Year 2003</b>					
<b>School District</b>	<b>Date Property Taxes Received <sup>1</sup></b>	<b>Date Loan Repaid</b>	<b>Loan Due Date</b>	<b>Days Late (Early)</b>	<b>Days Between Tax Receipt and Loan Repayment</b>
Boulder Valley	March 11	April 7	April 15	(8)	27
	May 12	June 6	June 15	(9)	25
	June 20	June 25	June 25	0	5
Cherry Creek	February 10	February 25	April 15	(49)	15
	March 10	March 28	April 15	(18)	18
	May 12	May 27	June 15	(19)	15
	June 20	June 24	June 25	(1)	4
Denver	March 10	April 3	April 15	(12)	24
	April 10	May 5	May 15	(10)	25
	May 12	June 4	June 15	(11)	23
	June 20	June 25	June 25	0	5
Douglas County	February 10	February 26	April 15	(48)	16
	March 10	March 10	April 15	(36)	0
St. Vrain Valley	March 10	April 16	April 15	1	37
	May 12	May 15	June 15	(31)	3
	June 20	June 25 <sup>2</sup>	June 25	0	5
<p><b>Source:</b> Office of the State Auditor analysis of Treasurer’s Office and Boulder Valley School District information.  <sup>1</sup> Although we did not review the accounting records of any school district other than BVSD, we estimated the dates property taxes were received to be on the 10<sup>th</sup> business day of each month, with the final payment received on June 20<sup>th</sup>. In Boulder Valley School District’s case, we used actual receipt dates.  <sup>2</sup> St. Vrain School District did not make a full cash repayment on June 25, but instead negotiated a building sale/leaseback with the Treasurer’s Office.</p>					