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January 23, 2020

Terry Dade, Superintendent  
Rochester City School District  
131 West Broad St.  
Rochester, NY 14614

Report Number: B20-2-1

Dear Superintendent Dade and Members of the Board of Education:

Following the Rochester City School District's (District) September 19, 2019 disclosure that preliminary results of its annual external audit revealed that an unplanned deficit had occurred during the 2018-19 fiscal year, numerous interested stakeholders called upon this office to provide an independent review of the District's finances. Given the severity of the situation, Comptroller DiNapoli immediately deployed staff to begin a review. Our Office developed a two-part approach. The first effort is the recent review of the adopted budgets for the 2018-19 and 2019-20 fiscal years. Thereafter we will review and report on the District's financial procedures used to develop its budgets, including improvement recommendations.

### **Summary**

Due to several inaccurate estimates, the District is on track to incur a 2019-20 budgetary deficit of approximately \$31.6 million, even accounting for the numerous cost-savings and avoidance measures, including personnel layoffs, recently implemented by the Superintendent and Board of Education (Board). In addition, the District has no available unrestricted fund balance to mitigate this budgetary deficit. The District reported a deficit unrestricted general fund balance of \$8.9 million at June 30, 2019. Therefore, if current District operating trends continue, we project the District will have a fiscal year-end deficit of approximately \$40.5 million. Further, absent additional severe budget cuts,<sup>1</sup> short-term borrowings or outside intervention, the District will not have sufficient resources to meet its financial obligations by the end of the fiscal year ending June 30, 2020.

While we commend the Superintendent and Board for the actions they have taken to modify the 2019-20 budget, many of them were one-time budgetary savings and do not alleviate the structural deficits that may exist in future budgets. Consequently, without additional recurring revenues, the Superintendent and Board will need to implement additional budget and/or staffing cuts in the District's 2020-21 budget.

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<sup>1</sup> The current projected year-end deficit represents 34.8 percent of the remaining fiscal year's general fund budget net of personnel services.

Our review addressed the following questions:

- Were significant revenue and expenditure projections in the adopted 2018-19 budget reasonable?
- Were significant revenue and expenditure projections in the adopted 2019-20 budget reasonable?
- Were the revised significant revenue and expenditure 2019-20 budget projections and the proposed mid-year reductions and efficiencies presented by the Superintendent on November 12, 2019 reasonable?

To accomplish our objectives in this review, we requested the 2018-19 and 2019-20 budgets, salary schedules, debt payment schedules and other pertinent information. We identified and examined significant estimated revenues and expenditures for reasonableness with emphasis on significant and/or unrealistic increases or decreases. We analyzed, verified and/or corroborated trend data and estimates, where appropriate. We identified any significant new or unusually high revenue or expenditure estimates, made appropriate inquiries and reviewed supporting documentation to determine the nature of the items and to assess whether the estimate was realistic and reasonable. We also evaluated the amount of fund balance appropriated in the 2018-19 and 2019-20 budgets to be used as a financing source and determined if the amount of fund balance was available and sufficient for that purpose. Additionally, we have reviewed the District's revised 2019-20 budget projections as well as the reasonableness of realizing projected cost reductions and efficiencies identified. Both the Chief Financial Officer (CFO) and Budget Director who were responsible for developing the budgets under review resigned prior the commencement of our review. Additionally, the current Superintendent began his employment with the District on July 1, 2019.

The scope of our review does not constitute an audit under generally accepted government auditing standards (GAGAS). We do not offer comments or make specific recommendations on public policy decisions, such as the type and level of services under consideration to be provided.

### **2018-19 Adopted Budget**

We found the adopted 2018-19 general fund budget revenues of \$778.6 million were reasonably estimated. However, several significant expenditure estimates were not reasonable. The District's audited financial statements for the period ending June 30, 2019 state that expenditures exceeded revenue by \$42.4 million. The adopted budget included \$20 million of appropriated fund balance to balance the budget. However, the Board amended this amount downward at mid-year to \$15 million, resulting in an unplanned deficit of \$27.4 million.

We analyzed the District's year-end financials and found that the predominate cause of the 2018-19 budget deficit was severe underbudgeting of several appropriations<sup>2</sup>, all of which should have been better estimated by the District's Central Office. The top six areas where appropriations were underestimated totaled \$41.1 million and are highlighted in Figure 1.

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<sup>2</sup> New York State Education Law Section 2576[7] prohibits the Board from incurring a liability or expenditure for which there is not an available appropriation.

<b>Figure 1: Underestimated Appropriations in the 2018-19 Budget</b>				
<b>General Fund Account</b>	<b>2018-19 Appropriations</b>	<b>2018-19 Expenditures</b>	<b>Underestimated Appropriations</b>	<b>Percentage Underestimated</b>
Health & Dental Insurance	\$69,710,529	\$85,634,917	(\$15,924,388)	-19%
Substitutes	\$10,002,500	\$17,807,658	(\$7,805,158)	-44%
Charter School Tuition	\$79,563,000	\$86,057,100	(\$6,494,100)	-8%
Retirement	\$33,399,403	\$38,001,333	(\$4,601,930)	-12%
Contract Transportation	\$65,020,235	\$68,340,496	(\$3,320,261)	-5%
BOCES	\$22,905,088	\$25,868,662	(\$2,963,574)	-11%

**2019-20 Adopted Budget**

Due to the severity of the concerns, we immediately began a review of the District’s 2019-20 budget to determine whether District officials had a reasonable financial plan for the current fiscal year. To his credit, the Superintendent also instructed his team to begin an immediate review of the current budget (see 2019-20 Mid-Year Budget Modifications).

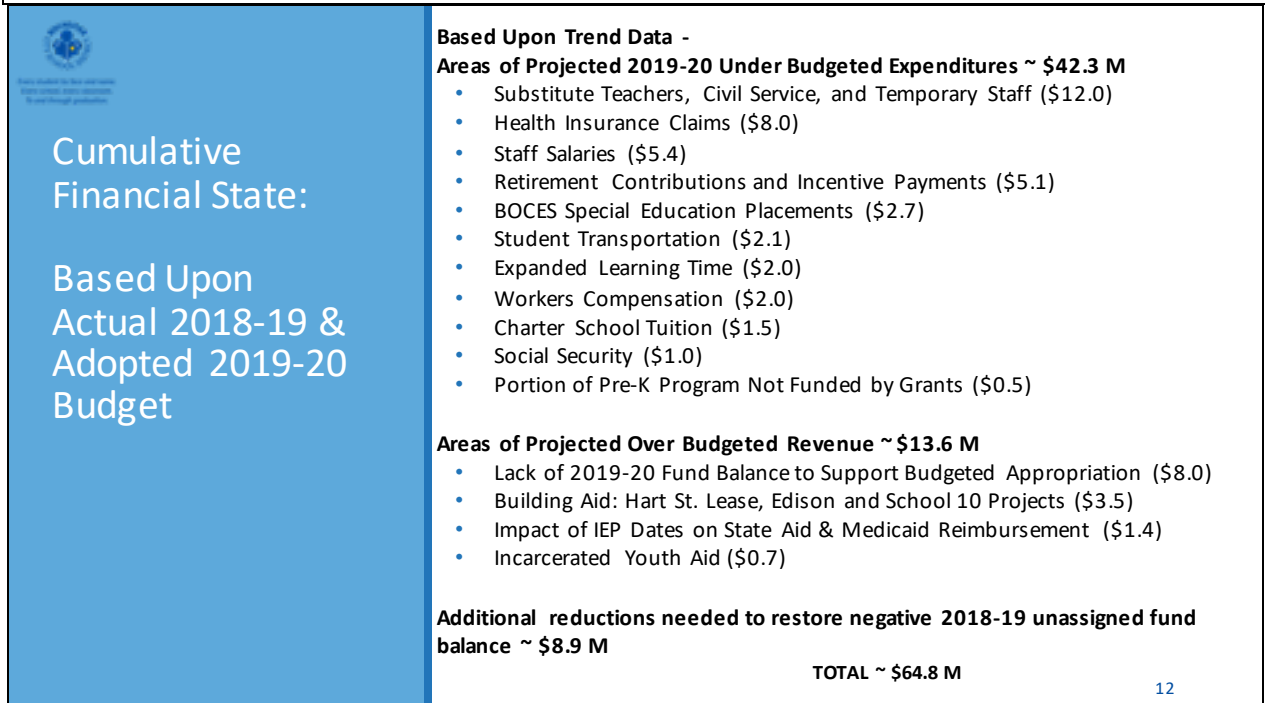
We again found a number of appropriation accounts had been severely underestimated by approximately \$45.3 million, with the same top six appropriations categories as the previous year (see Figure 1). On the revenue side, the Board appropriated \$8 million of fund balance that did not exist and therefore was unavailable to fund appropriations in the budget. Additionally, we project that some revenue sources were overestimated by \$8.5 million, the largest differences being building aid \$3.3 million and transportation aid \$3.3 million. We project in total that the adopted 2019-20 budget would have incurred an approximately \$61.8 million deficit had the Superintendent and Board not taken action during the fiscal year. Because the District had an \$8.9 million negative unassigned general fund balance at June 30, 2019, without the District’s actions, it would have finished the 2019-20 fiscal year with a cumulative deficit of approximately \$70.7 million.

**2019-20 Mid-Year Budget Modifications**

As previously noted, upon discovering the extent of the 2018-19 deficit, the Superintendent instructed his staff to complete a review of the 2019-20 budget. On November 12, 2019 the Superintendent made a presentation to the Board, which contained an explanation of the *Cumulative Financial State: Based Upon Actual 2018-19 & Adopted 2019-20 Budget*.<sup>3</sup> The Superintendent’s presentation included a slide (see Figure 2) which summarized areas of underbudgeted expenditures, overbudgeted revenue and the reductions needed to restore negative unassigned fund balance. The Superintendent projected the District’s total shortfall at \$64.8 million.

<sup>3</sup> <https://www.rcsdk12.org/cms/lib/NY01001156/Centricity/Domain/92/Budget11-12-19.pdf>

**Figure 2: Cumulative Financial State: Based Upon Actual 2018-19 & Adopted 2019-20 Budget**



Our estimates differ from the Superintendent's by \$5.9 million. There are two areas that account for the majority of the difference, charter school tuition and transportation aid. We believe the District underestimated its charter school tuition because it used 300 fewer students than the number enrolled and the 2018-19 charter school tuition rate (\$13,684 per-student) instead of the increased 2019-20 rate (\$13,995 per-student) when projecting its 2019-20 expenditures. Additionally, we believe that based upon the State aid information we received from the New York State Education Department as of November 2019, the District overestimated transportation aid by \$3.3 million.

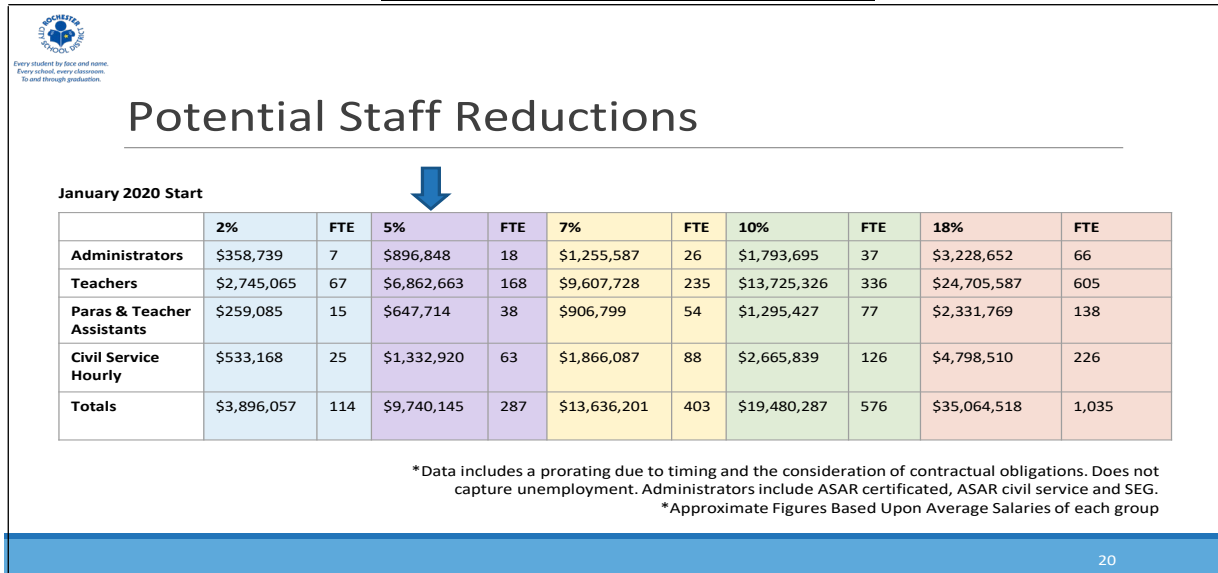
The Superintendent also presented the Board with a number of proposed reductions and efficiencies which his team estimated would total approximately \$28 million. We reviewed these proposed measures and arrived at a more conservative amount of \$21.6 million in potential savings. The \$6.4 million difference being attributed primarily to collective bargained benefits which seem unlikely to materialize,<sup>4</sup> extended day learning which is accounted for in the grants fund instead of the general fund and a more conservative estimate of the substitute teacher cost efficiencies based upon the limited amount of data available since its implementation. In addition, we note the majority of the proposed reductions and efficiencies to close the current year's gap are one-shot items and will not address the District's structural budget deficit in future years.<sup>5</sup> Future structural deficits are likely to increase due to contractual salary increases, rising health care costs, charter school tuition and other contractual and operating increases.

<sup>4</sup> <http://rochesterteachers.org/adams-update-1-1-20-rumor-control/>; <http://rochesterteachers.org/adams-update-1-8-20/>

<sup>5</sup> [https://go.boarddocs.com/ny/rochny/Board.nsf/files/B8FK8J507BC8/\\$file/Investing%20in%20Student%20and%20School%20Success2.pdf](https://go.boarddocs.com/ny/rochny/Board.nsf/files/B8FK8J507BC8/$file/Investing%20in%20Student%20and%20School%20Success2.pdf)

To further close the current year’s budget gap, the Superintendent presented a number of potential staff reduction scenarios (see Figure 3). After much discussion the Board agreed to allow the Superintendent to proceed with a 5 percent reduction in staff, the projected total of these reductions was approximately \$9.7 million (prorated for the remainder of the fiscal year). However, they did note that this figure did not factor in unemployment (the District is self-insured for unemployment insurance). Using the agreed upon 5 percent reduction in staff, we project the total of the reductions to be approximately \$8.6 million inclusive of unemployment insurance payments.

**Figure 3: Potential Staff Reductions**



In conclusion, based upon the Superintendent’s November 12, 2019 presentation, the District calculated it needed \$64.8 million in budget modifications. District officials presented their estimates of \$28 million in reductions and efficiencies implemented as well as \$9.7 million in staff reductions, leaving a deficit balance by their estimates of approximately \$27.1 million.

These estimates differ from our projection of \$70.7 million in total 2019-20 budget modification needs. We project the actions taken by the Superintendent and Board will result in \$21.6 million in reductions and efficiencies and \$8.6 million in staff reductions, meaning absent any further modifications, the District is on course to finish the 2019-20 school year with a cumulative \$40.5 million deficit.

If you have any questions on the scope of our work, please feel free to contact Edward V. Grant, Jr., Chief Examiner of the Rochester Regional Office, at (585) 454-2460.

Sincerely,

Elliott Auerbach  
Deputy Comptroller

cc: Van Henri White, President, Board of Education  
Cynthia Elliott, Vice President, Board of Education  
Ricardo Adams, Commissioner, Board of Education  
Beatriz LeBron, Commissioner, Board of Education  
Amy Maloy, Commissioner, Board of Education  
Willa Powell, Commissioner, Board of Education  
Natalie Sheppard, Commissioner, Board of Education  
Marisol Ramos-Lopez, Clerk of the Board  
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Edward V. Grant, Jr., Chief Examiner, Rochester Regional Office