House Education Committee
Rep. Highland, chairman

HB-2393 – school district accounting

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Chairman and members of the House Education Committee:

My name is Mark Dick. I am a certified public accountant with Allen, Gibbs & Houlik, L.C. who has spent more than 45 years providing governmental entities with accounting, auditing and consulting services both in the state of Kansas and other states. Last fall, I was asked to testify and answer questions before the K-12 School Performance and Efficiency Commission. Today, I'm here to provide some explanation of the potential effect of House Bill 2393 – School District Accounting on school districts across the state and taxpayer dollars.

This bill's stated goal is to provide uniform financial data reporting among the state's school districts. This is a laudable and important goal that would increase transparency and comparability among districts – and we fully support that concept. However, while the end outcome is valuable, HB 2393's proposed path to get there adds an unnecessary government regulatory burden for school districts, and is likely to at least double the auditing and accounting cost to school districts to meet that mandate.

The legislature can reach the same important outcome – more consistent, transparent and comparable school district financial data – with less government regulation, fewer taxpayer dollars and more efficient use of school district and governmental resources.

Here's a broad overview of our recommended alternatives to the bill, followed by more detailed commentary on specific provisions and their effects.

Overview

At a high level, the bill will require school districts to take four actions:

- ONE: Change to an accounting and payroll system selected by the State.
- TWO: Prepare additional financial schedules as detailed in Section 2 of the bill.
- THREE: Although the wording isn't entirely clear, it appears that school districts will be either asked to:
    - Require the independent auditor to apply audit procedures to ensure the school district has complied with the requirement to prepare the financial data included in Section 2 of the bill
    - Or, audit the detailed financial data required by Section 2 of the bill.
- And FOUR: Move from the cash / budgetary basis of accounting used by nearly all school districts to what's called GAAP – generally accepted accounting principles – similar to that used by most commercial businesses.

Based on our years of experience in governmental and school district accounting and auditing, we are fully confident that these financial transparency goals can be achieved without HB 2393, reducing unnecessary government regulation and saving taxpayer dollars. Briefly, here's how:

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- **School districts already have uniform guidelines to report their financials that allow some level of comparability among districts.** If additional or new information is needed from the school districts, it can be requested by modifying or adding to an existing regulation instead of creating a new one.

  School districts are required by the Kansas Uniform Financial Accounting and Reporting Act (KSA 75-1123), to use the format and process specified by the Kansas Municipal Audit and Accounting Guide (KMAAG) to report their financials to the state board.

- **The most critical factor in comparability of financials is whether the districts use the same "chart of accounts" in reporting their financials – and this can be specified through the KMAAG already used by schools.** If different or additional information is needed, the KMAAG guidelines can be modified to require schools to provide that specific information needed. So, for example, if the information outlined in Section 2 of the bill is needed, that requirement can be added to KMAAG.

  The use of a new or different accounting system, as required in Section 1, and even the use of GAAP will have little if any impact on the comparability and uniformity of the districts' financials – nor will it be as cost-effective – as simply modifying the current KMAAG directives to gain the information needed.

In brief, the **most effective action the Kansas legislature could take to ensure more uniform, comparable and transparent financial information from the school districts in Kansas would be to modify the KMAAG as allowed by the Kansas Uniform Financial Accounting and Reporting Act,** to require that districts report any different or additional information legislators need.

It is neither cost-effective nor an efficient use of resources to place an entirely new regulatory framework on the school districts simply to elicit additional financial data which can be obtained easily through another method that is already in place.

Now that you have the high-level overview of our recommendations, we'll go into the step-by-step comments on HB 2393's sections.

Section 1 requires that the State Board choose a range of accounting and payroll software programs from which the school districts must select and adopt as their own financial software programs. It is important to understand that these are simply the computer software used to record transactions. As such, using the same software does not guarantee uniform input or output in the form of financial data.

- This directive confuses the TOOL with the desired OUTCOME. For example, if your goal is to get everyone to use correct grammar and spelling in their emails, they don't need to buy a new email system or all use the same one. You just need to tell them exactly what grammar and spelling rules you want them to use.

- If KMAAG specifies the way districts must report their financials, the districts themselves can configure their existing systems to provide the data needed. To require that all districts change to an entirely new accounting and payroll system adds needless complexity, dollars and human resources to reach a goal that can be accomplished within existing constraints.

Section 2 requires preparation of new financial reports and data and an annual compliance audit to be conducted to "determine whether the school district complies with the requirements of this section."

- The language in the bill does not specify whether the **audit would be conducted to check that the district filed the reports and information required** by Section 2, or whether the **auditor is performing testing to provide an opinion** on whether the information is presented fairly and accurately.

  In the first instance, having the auditor check to ensure the district filed the required reports could be accomplished in an efficient manner.

  However, if the intent is to have the auditor express an opinion on the detailed reports, the additional cost would be substantial.

  Additionally, the bill requires preparation of financial schedules at a very detailed level – for example, expenses and revenues associated with EACH extracurricular activity or club, including salaries of the district employees associated with each activity. This could result in, for example, schools or external auditors spending far more time and money on determining the costs, revenues and employee expenses associated with, say, the Spanish or chess club, than would ever be meaningful (or as accountants say, MATERIAL) to the district's financial statements.

  Spending big dollars to audit little dollars is a prime example of too much government regulation for little or no meaningful result.

- If the state board and legislature choose to seek additional external oversight to ensure school district compliance in providing the requested data, a compromise solution could be to require an external auditor to conduct what are called "agreed-upon procedures" to review the required data funneling into the financial statements. Such procedures could provide a measure of additional assurance to the governing body, but require less time and cost than a full-blown compliance audit.

Section 3 requires that all school districts use generally accepted accounting principles, called GAAP, to report their financials.

- To reach the goal of uniform, transparent and comparable financials from school districts, it's important to use the right tool for the job. Right now, the cash / budgetary basis that 97% of district use can provide the type of additional information legislators are seeking. Right now, not all of the information sought in HB 2393 has been required to be reported, but it can be integrated into the current basis districts are already using.

- If GAAP were adopted, each school district would have to prepare three different sets of financial statements – each requiring a separate audit from the independent auditor. GAAP requirements include entity-wide financial statements using the full accrual method of accounting. This type of financial statement was initially created to help users compare commercial enterprises as a basis for decisions such as on buying stock or giving a company a loan. It measures "net income," which is a foreign concept to government.

- Financial decisions in the government environment are based on analysis of cash flows. The straightforward concept of accounting for how many funds are received and spent has served Kansas governmental entities well. Adding GAAP concepts such as depreciation of school buses over their useful lives would provide little value to decision-makers in the day-to-day operations of the district, yet would require significant cost.

- Most school districts do not employ financial staff familiar with the complex details of governmental GAAP. The district's external auditors must be "independent" with respect to the financial statements on which they express an opinion. In other words, auditors cannot audit their own work. Consequently, they cannot prepare the GAAP financial statements on behalf of their client. As a result, **many school districts would need to engage a different accountant to prepare the financial statements which would then be audited by the independent auditor. The cost associated with the additional work would be substantial and could double current audit costs.**

  Mandating GAAP to improve the uniformity and consistency of districts' financial statements is using the wrong tool for the job. It's asking the school districts to buy a brand new sledgehammer to kill a fly, when an effective and proven flyswatter is already in the tool shed.

Summary

This bill's goals of providing uniform, comparable and transparent financial data from school districts across Kansas are laudable – but HB 2393 proposes more regulation and cost than necessary to achieve the same goal. School districts would incur substantial additional costs, reducing the funds available for the classroom. Such a shift might be justified if the benefits outweighed the costs. However, the perspective I've earned in 45 years of working with state and local governments and school districts tells me that the same outcomes can be achieved with less government regulation and more careful stewardship of taxpayer dollars.

I recommend the committee not pass this bill, but instead use the effective tools already in place through KMAAG. By modifying KMAAG to require the additional information the legislature seeks, you can reach the same outcome much more effectively and efficiently and serve as a guardian against additional regulatory red tape.

Respectfully,

ALLEN, GIBBS & HOULIK, L. C.

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