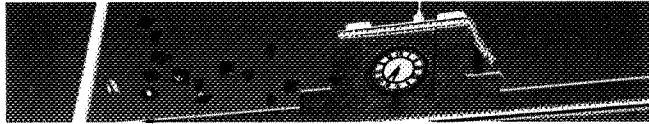


Sag Harbor Union Free School District



**FINANCIAL STATEMENTS AND
SUPPLEMENTARY SCHEDULES WITH
INDEPENDENT AUDITOR'S REPORT**

June 30, 2010

SAG HARBOR UNION FREE SCHOOL DISTRICT
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INDEPENDENT AUDITOR'S REPORT

To the Board of Education
Sag Harbor Union Free School District
Sag Harbor, New York

We have audited the accompanying financial statements of the governmental activities, each major fund and the fiduciary funds of the Sag Harbor Union Free School District (District), as of and for the year ended June 30, 2010, 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 the 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 consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 fiduciary funds of the Sag Harbor Union Free School District, as of June 30, 2010, and the respective changes in financial position thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 22, 2010, on our consideration of the Sag Harbor Union Free School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

The management's discussion and analysis, budgetary comparison information and the schedule of funding progress – other postemployment benefits on pages 3 through 12 and 40 through 42, respectively, are not required parts of the basic financial statements but are 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 opinions on the financial statements that collectively comprise the Sag Harbor Union Free School District's basic financial statements. The other supplementary information on pages 43 through 46 is not a required part of the basic financial statements but is supplementary information required by the New York State Education Department. The other supplementary information 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.

Cullen & Danowski, LLP

October 22, 2010

**SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT’S DISCUSSION AND ANALYSIS**

The Sag Harbor Union Free School District’s (District) discussion and analysis of the financial performance provides an overall review of the District’s financial activities for the fiscal year ended June 30, 2010. The intent of this discussion and analysis is to look at the District’s financial performance as a whole. This should be read in conjunction with the financial statements, which immediately follow this section.

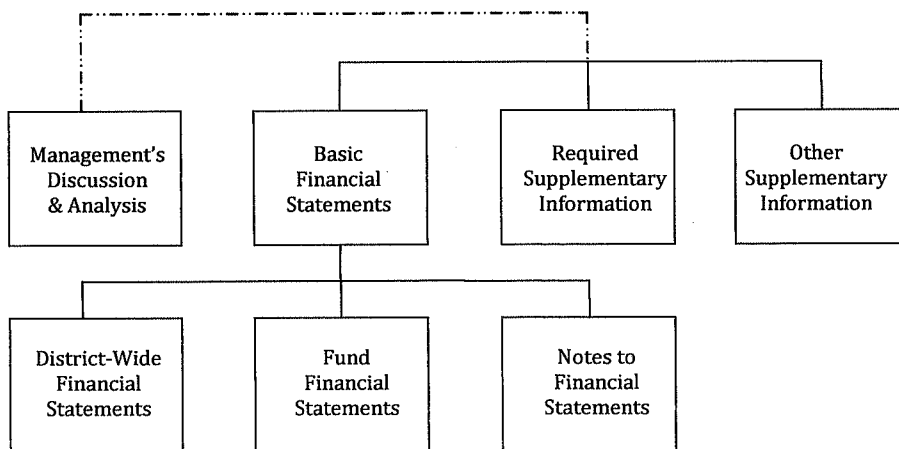
1. FINANCIAL HIGHLIGHTS

Key financial highlights for fiscal year 2010 are as follows:

- The District’s total net assets, as reflected in the district-wide financial statements, decreased by \$2,139,042. This was due to an excess of expenses over revenues based on the accrual basis of accounting.
- The District’s expenses for the year, as reflected in the district-wide financial statements, totaled \$31,935,041. Of this amount, \$1,381,871 was offset by program charges for services and operating grants. General revenues of \$28,414,128 amount to 95% of total revenues, and were not adequate to cover the balance of program expenses.
- The District received \$752,388 in operating grants to support instructional programs. Of this amount, \$288,359 was a federal grant under the American Recovery and Reinvestment Act (ARRA), which was awarded to supplement the loss of state aid.
- The general fund’s total fund balance, as reflected in the fund financial statements, decreased by \$307,337. This was due to an excess of expenditures over revenues based on the modified accrual basis of accounting.
- On the balance sheet, the general fund’s unreserved – undesignated fund balance at year end was \$308,015. This represents an increase of \$242,197 over the prior year.

2. OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of four parts – Management’s Discussion and Analysis (MD&A), the basic financial statements, required supplementary information, and other supplementary information. The basic financial statements consist of district-wide financial statements, fund financial statements, and notes to the financial statements. A graphic display of the relationship of these statements follows:



SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

A. District-Wide Financial Statements

The district-wide financial statements present the governmental activities of the District and are organized to provide an understanding of the fiscal performance of the District as a whole in a manner similar to a private sector business. There are two district-wide financial statements - the Statement of Net Assets and the Statement of Activities. These statements provide both an aggregate and long-term view of the District's finances.

These statements utilize the accrual basis of accounting. This basis of accounting recognizes the financial effects of events when they occur, without regard to the timing of cash flows related to the events.

The Statement of Net Assets

The Statement of Net Assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The Statement of Activities

The Statement of Activities presents information showing the change in net assets during the fiscal year. All changes in net assets are recorded at the time the underlying financial event occurs. Therefore, revenues and expenses are reported in the statement for some items that will result in cash flow in future fiscal periods.

B. Fund Financial Statements

The fund financial statements provide more detailed information about the District's funds, not the District as a whole. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District also uses fund accounting to ensure compliance with finance-related legal requirements. The funds of the District are reported in the governmental funds and the fiduciary funds.

These statements utilize the modified accrual basis of accounting. This basis of accounting recognizes revenues in the period that they become measurable and available. It recognizes expenditures in the period that they become measurable, funded through available resources and payable within a current period.

Governmental Funds

Governmental funds are used to account for essentially the same functions reported as governmental activities in the district-wide financial statements. However, the governmental fund financial statements focus on shorter term inflows and outflows of spendable resources, as well as, on balances of spendable resources available at the end of the fiscal year for spending in future years. Consequently, the governmental fund statements provide a detailed short-term view of the District's operations and the services it provides.

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Because the focus of governmental funds is narrower than that of district-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the district-wide financial statements. By doing so, you may better understand the long-term impact of the District's near-term financing decisions. Both the governmental fund Balance Sheet and the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balance provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The District maintains five individual governmental funds: general fund, special aid fund, school lunch fund, debt service fund and capital projects fund; each of which is considered to be a major fund and is presented separately in the fund financial statements.

Fiduciary Funds

Fiduciary funds are used to account for assets held by the District in its capacity as agent or trustee. All of the District's fiduciary activities are reported in a separate Statement of Fiduciary Net Assets. The fiduciary activities have been excluded from the District's district-wide financial statements because the District cannot use these assets to finance its operations.

3. FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

A. Net Assets

A summary of the District's Statement of Net Assets for June 30, 2010 and 2009 is as follows:

| | <u>2010</u> | <u>2009</u> | <u>Increase (Decrease)</u> | <u>Percentage Change</u> |
|--|--------------------|---------------------|--------------------------------|------------------------------|
| Current and Other Assets | \$ 3,666,008 | \$ 3,458,734 | \$ 207,274 | 5.99 % |
| Capital Assets, Net | 17,758,899 | 17,834,206 | (75,307) | (0.42)% |
| Total Assets | <u>21,424,907</u> | <u>21,292,940</u> | <u>131,967</u> | 0.62 % |
| Current and Other Liabilities | 2,830,082 | 2,446,420 | 383,662 | 15.68 % |
| Long-Term Liabilities | 13,019,060 | 13,910,014 | (890,954) | (6.41)% |
| Net Other Postemployment Benefits Obligation | <u>5,418,529</u> | <u>2,640,228</u> | <u>2,778,301</u> | 105.23 % |
| Total Liabilities | <u>21,267,671</u> | <u>18,996,662</u> | <u>2,271,009</u> | 11.95 % |
| Net Assets | | | | |
| Invested in Capital Assets, Net of Related Debt | 5,325,177 | 4,433,169 | 892,008 | 20.12 % |
| Restricted | 82,280 | 136,147 | (53,867) | (39.57)% |
| Unrestricted (Deficit) | <u>(5,250,221)</u> | <u>(2,273,038)</u> | <u>(2,977,183)</u> | 130.98 % |
| Total Net Assets | <u>\$ 157,236</u> | <u>\$ 2,296,278</u> | <u>\$ (2,139,042)</u> | (93.15)% |

Current and other assets increased by \$207,274, as compared to the prior year. The increase is primarily due to an increase in due from other governments of approximately \$990,000 in excess of a decrease in cash of approximately \$830,000.

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

The capital assets, net decreased by \$75,307 as compared to the prior year. This net change is due to capital asset additions less depreciation expense. The accompanying Notes to Financial Statements, Note 7 "Capital Assets" provides additional information.

Current and other liabilities increased by \$383,662 as compared to the prior year. This increase was primarily in connection with the District's accrued liabilities due to estimated compensation payable.

Long-term liabilities decreased by \$890,954 as compared to the prior year. This decrease is primarily the result of the repayment of the current maturity of the bond indebtedness of \$1,115,000, partially offset by a new bond issue of \$155,968.

Net other postemployment benefits obligation increased by \$2,778,301, as the current year OPEB cost exceeded contributions in accordance with GASB Statement No. 45. The accompanying Notes to Financial Statements, Note 12 "Postemployment Benefits" provides additional information.

The net assets invested in capital assets, net of related debt, relates to the investment in capital assets at cost such as land; construction in progress; buildings and improvements; and, furniture and equipment, net of depreciation and related debt. This number increased over the prior year by \$892,008 as follows:

| | Increase (Decrease) |
|--|------------------------|
| Capital assets additions | \$ 572,719 |
| Additions financed by debt | (155,132) |
| Additions financed by appropriations | 417,587 |
| Principal debt reduction of construction bonds | 1,115,000 |
| Depreciation expense | (648,026) |
| Amortization of deferred charges on refunding and bond premium | 7,447 |
| | \$ 892,008 |

The restricted net assets in the amount of \$82,280, relates to the District's debt service reserve. This number decreased from the prior year by \$53,867 due to a transfer to the general fund of \$54,629 in excess of interest earnings of \$762.

The unrestricted net assets (deficit) in the amount of \$(5,250,221) relates to the balance of the District's net assets. This number includes the District's reserves and fund balances less unfunded liabilities such as compensated absences and net other postemployment benefits obligation. This number increased over the prior year by \$2,977,183.

The District's total net assets decreased by \$2,139,042 or 93.15%; \$157,236 at June 30, 2010, compared to \$2,296,278 at June 30, 2009.

B. Changes in Net Assets

The results of this year's operations as a whole are reported in the Statement of Activities in a programmatic format in the accompanying financial statements. In the accompanying financial statements STAR (school tax relief) revenue is included in the other tax items line. However, in this MD&A, STAR revenue has been combined with property taxes. A summary of this statement for the years ended June 30, 2010 and 2009 is as follows:

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

| | <u>2010</u> | <u>2009</u> | <u>Increase (Decrease)</u> | <u>Percentage Change</u> |
|----------------------------|-----------------------|-----------------------|--------------------------------|------------------------------|
| Revenues | | | | |
| Program Revenues | | | | |
| Charges for Services | \$ 600,821 | \$ 518,713 | \$ 82,108 | 15.83 % |
| Operating Grants | 781,050 | 349,212 | 431,838 | 123.66 % |
| General Revenues | | | | |
| Property Taxes and STAR | 26,347,982 | 25,074,580 | 1,273,402 | 5.08 % |
| State Sources | 1,762,527 | 1,747,165 | 15,362 | 0.88 % |
| Other | 303,619 | 219,268 | 84,351 | 38.47 % |
| Total Revenues | <u>29,795,999</u> | <u>27,908,938</u> | <u>1,887,061</u> | 6.76 % |
| Expenses | | | | |
| General Support | 3,851,162 | 3,927,640 | (76,478) | (1.95)% |
| Instruction | 25,780,231 | 24,927,374 | 852,857 | 3.42 % |
| Pupil Transportation | 1,289,586 | 1,576,101 | (286,515) | (18.18)% |
| Community Service | 99,041 | 120,400 | (21,359) | (17.74)% |
| Debt Service - Interest | 639,637 | 852,895 | (213,258) | (25.00)% |
| Food Service Program | 275,384 | 215,631 | 59,753 | 27.71 % |
| Total Expenses | <u>31,935,041</u> | <u>31,620,041</u> | <u>315,000</u> | 1.00 % |
| Total Change in Net Assets | <u>\$ (2,139,042)</u> | <u>\$ (3,711,103)</u> | <u>\$ 1,572,061</u> | (42.36)% |

The District's net assets decreased by \$2,139,042 and \$3,711,103 for the years ended June 30, 2010 and 2009, respectively.

The District's revenues increased by a net of \$1,887,061 or 6.76%. The major factors that contributed to the change were:

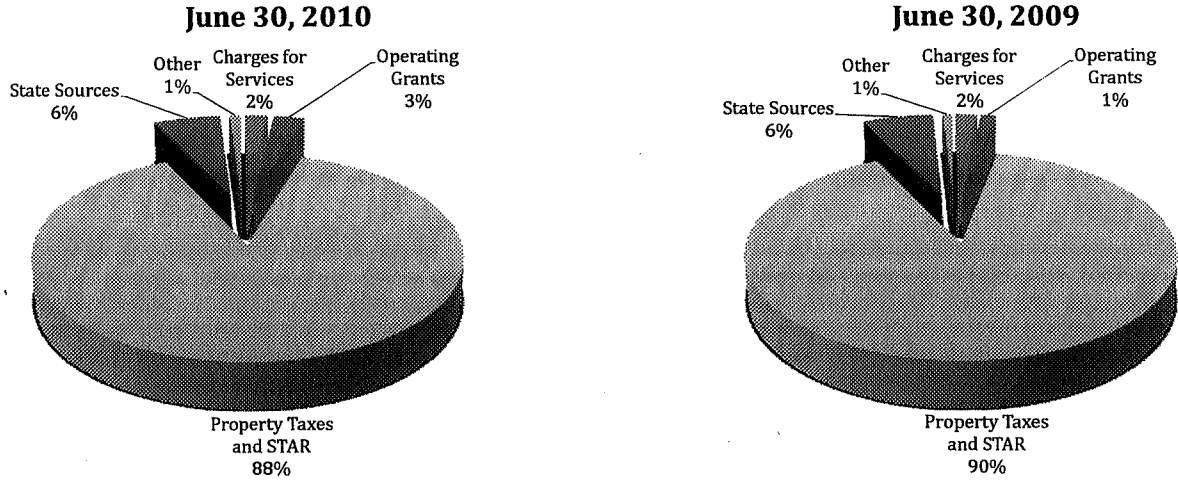
- Operating grants increased as a result of a federal grant which offset general state aid reductions.
- State EXCEL aid of \$298,548 was received as funding for certain capital projects.
- Property taxes and STAR increased by \$1,273,402 or 5.08%.

The District's expenses for the year increased by a net of \$315,000 or 1.0%. The major contributing factors to this increase was the increase in costs required for instructional purposes, offset in part by, the decrease in debt service-interest which was related to lower short-term borrowing rates and a decrease in pupil transportation costs due to contract transportation savings and the purchase of District buses.

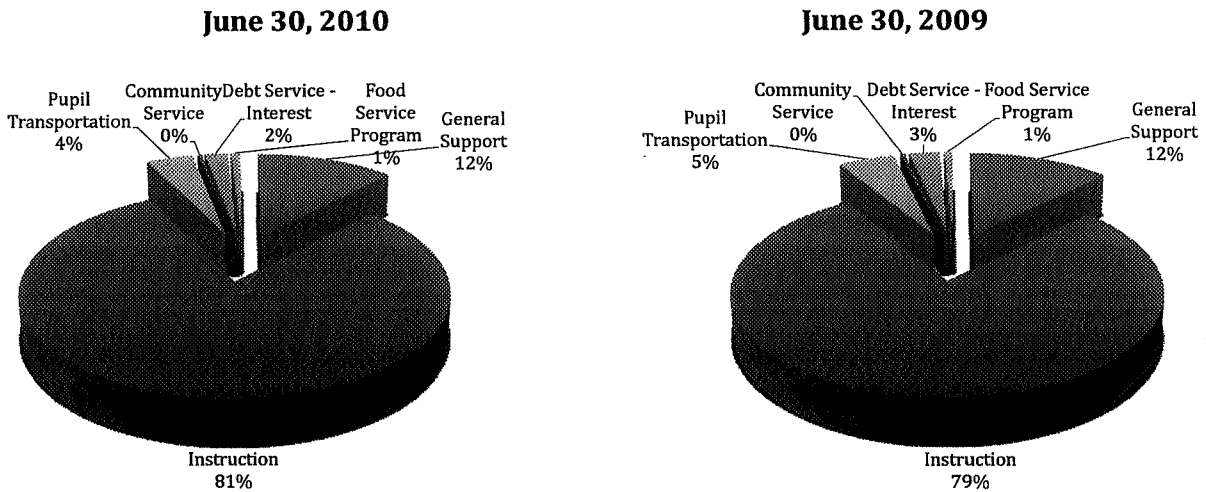
As indicated on the pie charts that follow, property taxes and STAR is the largest component of revenues recognized (i.e., 88% and 90% for the years 2010 and 2009, respectively). Instructional expenses is the largest category of expenses incurred (i.e., 81% and 79% for the years ended 2010 and 2009, respectively).

**SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

A graphic display of the distribution of revenues for the two years follows:



A graphic display of the distribution of expenses for the two years follows:



4. FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

At June 30, 2010, the District's governmental funds reported a combined fund balance of \$693,865, which is a decrease of \$246,347 from the prior year. This decrease is due to an excess of expenditures over revenues. A summary of the change in fund balance by fund is as follows:

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

| | <u>2010</u> | <u>2009</u> | <u>Changes</u> |
|--|-------------------|-------------------|---------------------|
| General Fund | | | |
| Reserve for: | | | |
| Encumbrances | \$ 7,978 | \$ 7,846 | \$ 132 |
| Employee benefit accrued liability | 118,711 | 189,953 | (71,242) |
| Advances | 117,697 | 91,121 | 26,576 |
| Unreserved - Designated for subsequent year's expenditures | | 505,000 | (505,000) |
| Unreserved - Undesignated | <u>308,015</u> | <u>65,818</u> | <u>242,197</u> |
| | <u>552,401</u> | <u>859,738</u> | <u>(307,337)</u> |
| School Lunch Fund | | | |
| Reserve for inventory | 2,326 | 1,294 | 1,032 |
| Unreserved - Undesignated (Deficit) | <u>(117,697)</u> | <u>(91,121)</u> | <u>(26,576)</u> |
| | <u>(115,371)</u> | <u>(89,827)</u> | <u>(25,544)</u> |
| Debt Service Fund | | | |
| Reserve for debt | <u>82,280</u> | <u>136,147</u> | <u>(53,867)</u> |
| Capital Projects Fund | | | |
| Reserve for encumbrances | 147,302 | | 147,302 |
| Unreserved - Undesignated | <u>27,253</u> | <u>34,154</u> | <u>(6,901)</u> |
| | <u>174,555</u> | <u>34,154</u> | <u>140,401</u> |
| Total Fund Balance | <u>\$ 693,865</u> | <u>\$ 940,212</u> | <u>\$ (246,347)</u> |

A. General Fund

The net change in the general fund - fund balance is a decrease of \$307,337. This resulted from expenditures in excess of revenues. Actual revenues fell short of budgeted revenues. As a result, the District did not designate any fund balance to reduce taxes for the 2011 budget.

B. School Lunch Fund

The net change in the school lunch fund - fund balance is a decrease of \$25,544, which was the net loss of the school lunch fund.

An amount equal to the deficit of \$117,697 has been reserved within the general fund since the repayment of the advance is not expected to be made within the current period.

C. Debt Service Fund

The net change in the debt service fund - fund balance is a decrease of \$53,867. This resulted from a transfer of \$54,629 to the general fund in excess of interest earnings of \$762.

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

D. Capital Projects Fund

The net change in the capital projects fund - fund balance is an increase of \$140,401. This resulted from capital outlay of \$420,712, a transfer of \$19,265 to the general fund for unexpended balances, offset by a transfer of \$125,862 from the general fund for the heating and air conditioning project, a new bond issuance of \$155,968 for the purchase of new buses and the recognition of \$298,548 in EXCEL aid.

5. GENERAL FUND BUDGETARY HIGHLIGHTS

A. 2010-11 Budget

The District's general fund adopted budget for the year ended June 30, 2010 was \$29,640,657. This amount was increased by encumbrances carried forward from the prior year in the amount of \$7,846, for a total final budget of \$29,648,503.

The budget was funded through a combination of revenues and designated fund balance. The majority of this funding source was \$26,346,644 in estimated property taxes and STAR aid, and state aid in the amount of \$1,720,385.

B. Change in General Fund's Unreserved - Undesignated Fund Balance (Budget to Actual)

The general fund's unreserved - undesignated fund balance is the component of total fund balance that is the residual of prior years' excess revenues over expenditures, net of transfers to reserves and designations to fund the subsequent year's budget. It is this balance that is commonly referred to as the "fund balance". The change in this balance demonstrated through a comparison of the actual revenues and expenditures for the year compared to budget follows:

| | |
|---|------------|
| Opening, Unreserved - Undesignated Fund Balance | \$ 65,818 |
| Revenues Under Budget | (303,906) |
| Expenditures and Encumbrances Under Budget | 501,437 |
| Net Change in Reserves | 44,666 |
| Closing, Unreserved - Undesignated Fund Balance | \$ 308,015 |

Opening, Unreserved - Undesignated Fund Balance

The \$65,818 shown in the table is the portion of the District's June 30, 2009 fund balance that was retained as undesignated. The undesignated fund balance was approximately 0.22% of the District's 2009-10 voter-approved budget, which is under the statutory maximum of 4%, according to New York State Real Property Tax Law.

Revenues Under Budget

The 2009-10 final budget for revenues was \$29,135,657. Actual revenues received for the year were \$28,831,751. Actual revenues were less than budgeted revenues by \$303,906. Revenues under budget contributes directly to the change to the undesignated portion of the general fund-fund balance from June 30, 2009 to June 30, 2010.

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Expenditures and Encumbrances Under Budget

The 2009-10 final budget for expenditures, including prior year open encumbrances was \$29,648,503. Actual expenditures as of June 30, 2010 were \$29,139,088 and outstanding encumbrances were \$7,978. Combined, the expenditures plus encumbrances for 2009-10 was \$29,147,066. The final budget was under expended by \$501,437. Budget categories which contributed significantly to this were as follows: central services – savings on facility expenditures and pupil transportation – expenditures were less due to contract savings and the purchase of new buses. Expenditures and encumbrances under budget contributes directly to the change to the undesignated portion of the general fund-fund balance from June 30, 2009 to June 30, 2010.

Net Change in Reserves

Monies transferred from budget lines within the general fund operating budget into and out of reserves such as the employee benefit accrued liability reserve do not affect the combined reserved, designated and undesignated fund balance unless, and until these monies are actually expended. The transfers do, however, reduce the District's discretion regarding the use of these transferred monies, and thus, reduce the undesignated portion of the fund balance by the amount of the transfers.

The \$44,666 shown in the above table is made up of a transfer from the employee benefit accrued liability reserve of \$71,683 in excess of interest earnings of \$442 and an increase in the reserve for advances of \$26,575 to equal the amount of the school lunch fund deficit.

Closing, Unreserved - Undesignated Fund Balance

Based upon the summary changes shown in the above table, the District will begin the 2010-11 fiscal year with an undesignated fund balance of \$308,015. This is an increase of \$242,197 over the undesignated balance from the prior year as of June 30, 2009. This undesignated portion is 0.98% of the subsequent year's approved operating budget, which is under the 4% maximum undesignated fund balance permitted by New York State Real Property Tax Law §1318.

6. CAPITAL ASSETS AND DEBT ADMINISTRATION

A. Capital Assets

At June 30, 2010, the District had invested in a broad range of capital assets, as indicated in the table below. The net decrease in capital assets is the result of capital additions of \$572,719 that were less than the depreciation expense of \$648,026 recorded for the year ended June 30, 2010. A summary of the District's capital assets, net of depreciation at June 30, 2010 and 2009 is as follows:

| | 2010 | 2009 | Increase (Decrease) |
|----------------------------|----------------------|----------------------|------------------------|
| Land | \$ 309,243 | \$ 309,243 | \$ - |
| Construction in progress | 278,951 | 40,850 | 238,101 |
| Buildings and improvements | 16,324,934 | 16,702,441 | (377,507) |
| Furniture and equipment | 845,771 | 781,672 | 64,099 |
| Capital assets, net | <u>\$ 17,758,899</u> | <u>\$ 17,834,206</u> | <u>\$ (75,307)</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

B. Debt Administration

At June 30, 2010, the District had total bonds payable of \$11,945,968. The bonds were issued for school bus purchases, school building improvements or to advance refund bonds that were issued for school building improvements. The decrease in outstanding debt represents principal payments of \$1,115,000 offset by the issuance of new bonds during the ended June 30, 2010, in the amount of \$155,968. A summary of the outstanding debt at June 30, 2010 and 2009 is as follows:

| Issue Date | Interest Rate | 2010 | 2009 | Increase (Decrease) |
|---------------|------------------|----------------------|----------------------|------------------------|
| 1997 | 4.875-5.125% | \$ | \$ 250,000 | \$ (250,000) |
| 2002 | 4.20-4.80% | 3,060,000 | 3,245,000 | (185,000) |
| 2006 | 3.75 - 5.00% | 8,730,000 | 9,410,000 | (680,000) |
| 2009 | 3.10 - 3.375% | 155,968 | | 155,968 |
| | | <u>\$ 11,945,968</u> | <u>\$ 12,905,000</u> | <u>\$ (959,032)</u> |

The District's latest underlying, long-term credit rating from Moody's Investors Service, Inc. is A1. The District's total outstanding indebtedness currently does not exceed its debt limit, which is 10% of the full valuation of the taxable real property within the District.

7. ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The general fund budget, the only fund with a legally adopted budget, as approved by the voters on May 18, 2010, for the year ending June 30, 2011, is \$31,500,811. This is an increase of \$1,860,154 or 6.28% over the previous year's budget. The increase is attributable to projected increases in salaries, benefits and special education costs.

The District budgeted non-property tax revenues at \$1,944,546. This amount is less than the 2009-10 budgeted amount and has been calculated more closely in relation to actual revenues for the current year.

8. CONTACTING THE DISTRICT

This financial report is designed to provide the reader with a general overview of the District's finances and to demonstrate the District's accountability for the funds it receives. Requests for additional information can be directed to:

Ms. Janet Verneuille
Director of Business Operations
Sag Harbor Union Free School District
200 Jermain Avenue
Sag Harbor, NY 11963

SAG HARBOR UNION FREE SCHOOL DISTRICT
Statement of Net Assets
June 30, 2010

| | |
|---|---------------------------------|
| ASSETS | |
| Cash | \$ 1,896,501 |
| Receivables | |
| Accounts receivable | 48,819 |
| Due from other governments | 1,501,297 |
| Deferred expenditures | 91,676 |
| Inventories | 2,326 |
| Other assets | 125,389 |
| Capital assets not being depreciated | 588,194 |
| Capital assets being depreciated, net of accumulated depreciation | <u>17,170,705</u> |
| Total Assets | <u><u>\$ 21,424,907</u></u> |
| LIABILITIES | |
| Payables | |
| Accounts payable | \$ 575,368 |
| Accrued liabilities | 975,352 |
| Due to other funds | 75,513 |
| Due to other governments | 87,520 |
| Due to teachers' retirement system | 978,228 |
| Due to employees' retirement system | 72,171 |
| Deferred credits | |
| Deferred revenues | 65,930 |
| Long-term liabilities | |
| Due and payable within one year | |
| Bonds payable, net | 995,256 |
| Compensated absences payable | 50,000 |
| Due and payable after one year | |
| Bonds payable, net | 11,439,302 |
| Compensated absences payable | 225,177 |
| Workers' compensation liabilities | 309,325 |
| Net other postemployment benefits obligation | <u>5,418,529</u> |
| Total Liabilities | <u>21,267,671</u> |
| NET ASSETS | |
| Investment in capital assets, net of related debt | 5,325,177 |
| Restricted for debt service | 82,280 |
| Unrestricted (Deficit) | <u>(5,250,221)</u> |
| Total Net Assets | <u>157,236</u> |
| Total Liabilities and Net Assets | <u><u>\$ 21,424,907</u></u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Statement of Activities
For The Year Ended June 30, 2010

| | | Program Revenues | | Net (Expense) Revenue and Changes in Net Assets |
|---|----------------------|-------------------------|---------------------|--|
| | Expenses | Charges for Services | Operating Grants | |
| PROGRAMS/FUNCTIONS | | | | |
| General support | \$ 3,851,162 | \$ | \$ | \$ (3,851,162) |
| Instruction | 25,780,231 | 375,743 | 752,388 | (24,652,100) |
| Pupil transportation | 1,289,586 | | | (1,289,586) |
| Community service | 99,041 | | | (99,041) |
| Debt service - interest | 639,637 | | | (639,637) |
| Food service program | 275,384 | 225,078 | 28,662 | (21,644) |
| | <u>\$ 31,935,041</u> | <u>\$ 600,821</u> | <u>\$ 781,050</u> | <u>(30,553,170)</u> |
| GENERAL REVENUES | | | | |
| Real property taxes | | | | 25,750,731 |
| Other tax items | | | | 715,708 |
| Use of money and property | | | | 24,934 |
| Sale of property and compensation for loss | | | | 5,393 |
| Miscellaneous | | | | 149,623 |
| State sources | | | | 1,762,527 |
| Medicaid reimbursement | | | | 5,212 |
| | | | | <u>28,414,128</u> |
| Total General Revenues | | | | <u>28,414,128</u> |
| Change in Net Assets | | | | (2,139,042) |
| Total Net Assets - Beginning of year | | | | <u>2,296,278</u> |
| Total Net Assets - End of year | | | | <u>\$ 157,236</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Balance Sheet - Governmental Funds
June 30, 2010

| | General | Special Aid | School Lunch | Debt Service | Capital Projects | Total Governmental Funds |
|-------------------------------------|---------------------|-------------------|------------------|------------------|---------------------|--------------------------------|
| ASSETS | | | | | | |
| Cash | \$ 1,672,228 | \$ 71,262 | \$ 64,688 | \$ 61,892 | \$ 26,431 | \$ 1,896,501 |
| Receivables | | | | | | |
| Accounts receivable | 41,743 | | 7,076 | | | 48,819 |
| Due from other funds | 672,891 | 2,500 | | 20,388 | | 695,779 |
| Due from other governments | 786,301 | 414,457 | 1,991 | | 298,548 | 1,501,297 |
| Inventories | | | 2,326 | | | 2,326 |
| Total Assets | <u>\$ 3,173,163</u> | <u>\$ 488,219</u> | <u>\$ 76,081</u> | <u>\$ 82,280</u> | <u>\$ 324,979</u> | <u>\$ 4,144,722</u> |
| LIABILITIES | | | | | | |
| Payables | | | | | | |
| Accounts payable | \$ 506,263 | \$ 49,138 | \$ 1,086 | | \$ 18,881 | \$ 575,368 |
| Accrued liabilities | 879,292 | | | | | 879,292 |
| Due to other funds | 76,401 | 375,942 | 187,406 | | 131,543 | 771,292 |
| Due to other governments | 87,351 | | 169 | | | 87,520 |
| Due to teachers' retirement system | 978,228 | | | | | 978,228 |
| Due to employees' retirement system | 72,171 | | | | | 72,171 |
| Deferred credits | | | | | | |
| Deferred revenues | 21,056 | 63,139 | 2,791 | | | 86,986 |
| Total Liabilities | <u>2,620,762</u> | <u>488,219</u> | <u>191,452</u> | <u>-</u> | <u>150,424</u> | <u>3,450,857</u> |
| FUND BALANCES | | | | | | |
| Reserved for encumbrances | 7,978 | | | | 147,302 | 155,280 |
| Reserved for: | | | | | | |
| Employee benefit accrued liability | 118,711 | | | | | 118,711 |
| Advances | 117,697 | | | | | 117,697 |
| Inventory | | | 2,326 | | | 2,326 |
| Debt service | | | | 82,280 | | 82,280 |
| Unreserved - Undesignated (Deficit) | <u>308,015</u> | | <u>(117,697)</u> | | <u>27,253</u> | <u>217,571</u> |
| Total Fund Balances (Deficit) | <u>552,401</u> | <u>-</u> | <u>(115,371)</u> | <u>82,280</u> | <u>174,555</u> | <u>693,865</u> |
| Total Liabilities and Fund Balances | <u>\$ 3,173,163</u> | <u>\$ 488,219</u> | <u>\$ 76,081</u> | <u>\$ 82,280</u> | <u>\$ 324,979</u> | <u>\$ 4,144,722</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Assets
June 30, 2010

| | | |
|--|--------------------|----------------|
| Total Governmental Fund Balances | \$ | 693,865 |
| Amounts reported for governmental activities in the Statement of Net Assets are different because: | | |
| Some of the District's revenues will be collected after the year end, but are not available soon enough to pay for the current period's expenditures and, therefore, are deferred in the governmental funds. | | 21,056 |
| Cash held by third-party administrator is treated as a long-term asset and included in net assets. | | 125,389 |
| The cost of building and acquiring capital assets (land, buildings, equipment) financed from the governmental funds are reported as expenditures in the year they are incurred, and the assets do not appear on the Balance Sheet. However, the Statement of Net Assets includes those capital assets among the assets of the District as a whole, and their original costs are expensed annually over their useful lives. | | |
| Original cost of capital assets | \$ 26,017,446 | |
| Accumulated depreciation | <u>(8,258,547)</u> | 17,758,899 |
| Total cost of refinancing bond issues is recorded as a deferred expenditure in the Statement of Net Assets and amortized over the remaining terms of the bond issue. | | |
| Total deferred expenditure | 126,618 | |
| Accumulated amortization | <u>(34,942)</u> | 91,676 |
| Long-term liabilities, including bonds payable, are not due and payable in the current period and, therefore, are not reported as liabilities in the governmental funds. Long-term liabilities at year end consist of: | | |
| Accrued interest on bonds payable | (96,060) | |
| Bonds payable, net | (12,434,558) | |
| Compensated absences payable | (275,177) | |
| Workers' compensation liabilities | (309,325) | |
| Net other postemployment benefits obligation | <u>(5,418,529)</u> | (18,533,649) |
| Total Net Assets | \$ | <u>157,236</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Statement of Revenues, Expenditures
and Changes in Fund Balances - Governmental Funds
For The Year Ended June 30, 2010

| | General | Special Aid | School Lunch | Debt Service | Capital Projects | Total Governmental Funds |
|--|--------------------|----------------|---------------------|------------------|---------------------|--------------------------------|
| REVENUES | | | | | | |
| Real property taxes | \$ 25,750,731 | \$ | \$ | \$ | \$ | \$ 25,750,731 |
| Other tax items | 715,708 | | | | | 715,708 |
| Charges for services | 375,743 | | | | | 375,743 |
| Use of money and property | 24,166 | | 6 | 762 | | 24,934 |
| Sale of property and compensation for loss | 5,393 | | | | | 5,393 |
| Miscellaneous | 128,567 | 67,539 | | | | 196,106 |
| State sources | 1,463,979 | 26,810 | 1,590 | | 298,548 | 1,790,927 |
| Medicaid reimbursement | 5,212 | | | | | 5,212 |
| Federal sources | 288,359 | 369,680 | 23,681 | | | 681,720 |
| Surplus food | | | 3,391 | | | 3,391 |
| Sales - school lunch | | | 225,078 | | | 225,078 |
| Total Revenues | 28,757,858 | 464,029 | 253,746 | 762 | 298,548 | 29,774,943 |
| EXPENDITURES | | | | | | |
| General support | 2,952,873 | | | | | 2,952,873 |
| Instruction | 17,729,998 | 390,693 | | | | 18,120,691 |
| Pupil transportation | 1,242,806 | | | | | 1,242,806 |
| Community service | 21,502 | 77,539 | | | | 99,041 |
| Employee benefits | 5,296,896 | | | | | 5,296,896 |
| Debt service | | | | | | |
| Principal | | | | 1,115,000 | | 1,115,000 |
| Interest | 67,456 | | | 582,493 | | 649,949 |
| Cost of sales | | | 279,290 | | | 279,290 |
| Capital outlay | | | | | 420,712 | 420,712 |
| Total Expenditures | 27,311,531 | 468,232 | 279,290 | 1,697,493 | 420,712 | 30,177,258 |
| Excess (Deficiency) of Revenues Over Expenditures | 1,446,327 | (4,203) | (25,544) | (1,696,731) | (122,164) | (402,315) |
| OTHER FINANCING SOURCES AND USES | | | | | | |
| Operating transfers in | 73,893 | 4,203 | | 1,697,493 | 125,862 | 1,901,451 |
| Operating transfers (out) | (1,827,557) | | | (54,629) | (19,265) | (1,901,451) |
| Proceeds from debt | | | | | 155,968 | 155,968 |
| Total Other Financing Sources and (Uses) | (1,753,664) | 4,203 | - | 1,642,864 | 262,565 | 155,968 |
| Net Changes in Fund Balances | (307,337) | - | (25,544) | (53,867) | 140,401 | (246,347) |
| Fund Balances (Deficit) - Beginning of year | 859,738 | | (89,827) | 136,147 | 34,154 | 940,212 |
| Fund Balances (Deficit) - End of year | <u>\$ 552,401</u> | <u>\$ -</u> | <u>\$ (115,371)</u> | <u>\$ 82,280</u> | <u>\$ 174,555</u> | <u>\$ 693,865</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Reconciliation of the Governmental Funds Statement of Revenues, Expenditures and
Changes in Fund Balances to the Statement of Activities
For The Year Ended June 30, 2010

| | | |
|---|----|-------------|
| Net Changes in Fund Balances | \$ | (246,347) |
| Amounts reported for governmental activities in the Statement of Activities are different because: | | |
| <u>Long-Term Revenue and Expense Differences</u> | | |
| In the Statement of Activities, certain operating revenues are measured by the amounts earned during the year. In the governmental funds, however, revenue for these items are measured by the amount of financial resources provided (essentially, the amounts actually received). | | |
| Change in deferred revenue | \$ | 21,056 |
| Disbursements to third-party administrator expended in the governmental funds are treated as long-term assets and increase net assets. | | 55,904 |
| Certain expenditures in the governmental funds requiring the use of current financial resources (amounts paid) may exceed the amounts incurred during the year, resulting in a reduction of the long-term liability and an increase in net assets. | | 26,416 |
| Decrease in compensated absences liability | | 26,416 |
| In the Statement of Activities, certain operating expenses do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds. | | |
| Increase in workers' compensation liability | | (101,941) |
| Increase in net other postemployment benefits obligation | | (2,778,301) |
| | | (2,776,866) |
| <u>Capital Related Differences</u> | | |
| Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, for governmental activities those costs are capitalized and shown in the Statement of Net Assets and allocated over their useful lives as annual depreciation expenses in the Statement of Activities. This is the amount by which depreciation exceeded capital outlays in the period. | | |
| Capital outlays | | 572,719 |
| Depreciation expense | | (648,026) |
| | | (75,307) |
| <u>Long-Term Debt Transaction Differences</u> | | |
| Proceeds from the issuance of bonds is an other funding source in the governmental funds, but it increases long-term liabilities in the Statement of Net Assets and does not affect the Statement of Activities. | | (155,968) |
| Transactions regarding the defeasance of debt are recorded as an expenditure / revenue in the governmental funds when debt is issued, whereas these amounts are deferred and amortized in the Statement of Activities. | | |
| Amortization of deferred bond issuance costs | | (9,866) |
| Amortization of deferred charges on refunding | | 7,447 |
| Repayment of bond principal is an expenditure in the governmental funds, but it reduces long-term liabilities in the Statement of Net Assets and does not affect the Statement of Activities. | | 1,115,000 |
| Interest on long-term debt in the Statement of Activities differs from the amount reported in the governmental funds because interest is recorded as an expenditure in the funds when it is due, and thus requires the use of current financial resources. In the Statement of Activities, however, interest expense is recognized as the interest accrues, regardless of when it is due. This is the amount by which accrued interest decreased from June 30, 2009 to June 30, 2010. | | 2,865 |
| | | 959,478 |
| Change in Net Assets of Governmental Activities | \$ | (2,139,042) |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Statement of Fiduciary Net Assets -
Fiduciary Funds
June 30, 2010

| | Agency | Private Purpose Trust |
|----------------------------------|------------|-----------------------------|
| ASSETS | | |
| Cash | \$ 136,264 | \$ 144,016 |
| Accounts receivable | 2,061 | |
| Due from other funds | 75,513 | |
| Total Assets | \$ 213,838 | \$ 144,016 |
| LIABILITIES | | |
| Extraclassroom activity balances | \$ 64,027 | \$ |
| Other liabilities | 149,811 | |
| Total Liabilities | \$ 213,838 | - |
| NET ASSETS | | |
| Reserved for scholarships | | 144,016 |
| Total Liabilities and Net Assets | | \$ 144,016 |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Statement of Changes in Fiduciary Net Assets -
Fiduciary Funds
For The Year Ended June 30, 2010

| | Private Purpose Trust |
|--------------------------------|-----------------------------|
| ADDITIONS | |
| Contributions | \$ 37,075 |
| Investment earnings | |
| Interest | 285 |
| Total Additions | 37,360 |
| DEDUCTIONS | |
| Scholarships and awards | 9,698 |
| Change in Net Assets | 27,662 |
| Net Assets - Beginning of year | 116,354 |
| Net Assets - End of Year | \$ 144,016 |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Sag Harbor Union Free School District (District) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) for governmental units. The Governmental Accounting Standards Board (GASB) is the standard-setting body for establishing governmental accounting and financial reporting principles. Significant accounting principles and policies used by the District are as follows:

A. Reporting Entity

The District is governed by the laws of New York State. The District is an independent entity governed by an elected Board of Education consisting of seven members. The President of the Board serves as the chief fiscal officer and the Superintendent is the chief executive officer. The Board is responsible for, and controls all activities related to public school education within the District. Board members have authority to make decisions, power to appoint management, and primary accountability for all fiscal matters.

The financial reporting entity is based on criteria set forth by GASB Statement No. 14, *The Financial Reporting Entity* and No. 39, *Determining Whether Certain Organizations are Component Units*. The financial reporting entity consists of the primary government, organizations for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The accompanying financial statements present the activities of the District. The District is not a component unit of another reporting entity. The decision to include a potential component unit in the District's reporting entity is based on several criteria including legal standing, fiscal dependency, and financial accountability. Based on the application of these criteria, there are no other entities which would be included in the District's reporting entity as a component unit. However, the following is included in the District's financial statements.

Extraclassroom Activity Funds

The extraclassroom activity funds of the District represent funds of the students of the District. The Board of Education exercises general oversight of these funds. The extraclassroom activity funds are independent of the District with respect to its financial transactions and the designation of student management. The District reports these assets held by it as agent for the extraclassroom organizations in the Statement of Fiduciary Net Assets - Fiduciary Fund. Separate audited financial statements of the extraclassroom activity funds can be found at the District's Business Office.

B. Joint Venture

The District is a component district in the Board of Cooperative Educational Services of Eastern Suffolk (BOCES). A BOCES is a voluntary, cooperative association of school districts in a geographic area that share planning, services, and programs which provide educational and support activities. BOCES are organized under Section §1950 of the Education Law. A BOCES Board is considered a corporate body. Members of a BOCES Board are nominated and elected by their component member boards in accordance with provisions of Section §1950 of the Education Law. All BOCES property is held by the BOCES Board as a corporation under Section §1950(6). In addition, BOCES Boards also are considered municipal corporations to permit them to contract with other municipalities on a cooperative basis under Section §119-n(a) of the General Municipal Law. A BOCES budget is comprised of separate budgets for

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

administrative, program, and capital costs. Each component district's share of administrative and capital cost is determined by resident public school district enrollment as defined in Education Law, Section §1950(4)(b)(7). There is no authority or process by which a school district can terminate its status as a BOCES component. In addition, component school districts pay tuition or a service fee for programs in which its students participate.

C. Basis of Presentation

District-Wide Financial Statements

The Statement of Net Assets and the Statement of Activities present information about the overall governmental financial activities of the District, except for fiduciary activities. Eliminations have been made to minimize the double counting of interfund transactions. Governmental activities generally are financed through taxes, state aid, intergovernmental revenues, and other exchange and nonexchange transactions. Operating grants include operating-specific and discretionary (either operating or capital) grants.

The Statement of Net Assets presents the financial position of the District at fiscal year end. The Statement of Activities presents a comparison between program expenses and revenues for each function of the District's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Indirect expenses, principally employee benefits, are allocated to functional areas in proportion to the payroll expended for those areas. Program revenues include (a) charges paid by the recipients of goods or services offered by the programs and (b) grants, contributions, and other revenues that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including real property taxes and state aid, are presented as general revenues.

Fund Financial Statements

The fund financial statements provide information about the District's funds, including fiduciary funds. Separate statements for each fund category, governmental and fiduciary, are presented. The emphasis of fund financial statements is on major governmental funds as defined by GASB, each displayed in a separate column. The District's financial statements reflect the following major fund categories:

Governmental Funds:

General Fund - is the general operating fund and is used to account for all financial transactions except those required to be accounted for in another fund.

Special Aid Fund - is used to account for the proceeds of specific revenue sources such as federal and state grants that are legally restricted to expenditures for specified purposes. These legal restrictions may be imposed by either governments that provide the funds or outside parties.

School Lunch Fund - is used to account for the activities of the school lunch operations.

Debt Service Fund - accounts for the accumulation of resources and the payment of principal and interest on long-term general obligation debt of governmental activities.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Capital Projects Fund – is used to account for the financial resources used for acquisition, construction, or major repair of capital facilities.

Fiduciary Funds – are used to account for activities in which the District acts as trustee or agent for resources that belong to others. These activities are not included in the district-wide financial statements, because their resources do not belong to the District, and are not available to be used. There are two classes of fiduciary funds:

Agency Funds - These funds are strictly custodial in nature and do not involve the measurement of results of operations. Assets are held by the District as agent for various student groups or extraclassroom activity funds and for payroll or employee withholding.

Private Purpose Trust Funds - These funds are used to account for trust arrangements in which principal and income benefits annual third party awards and scholarships for students. Established criteria govern the use of the funds and members of the District or representatives of the donors may serve on committees to determine who benefits.

D. Basis of Accounting and Measurement Focus

The district-wide and fiduciary fund financial statements are reported on the accrual basis of accounting using the economic resources measurement focus. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash transaction takes place. Nonexchange transactions, in which the District gives or receives value without directly receiving or giving equal value in exchange, include real property taxes, grants and donations. On an accrual basis, revenue from real property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied and the related expenditures are incurred.

The fund statements are reported on the modified accrual basis of accounting using the current financial resources measurement focus. Revenues are recognized when measurable and available. The District considers all revenues reported in the governmental funds to be available if the revenues are collected within 180 days after the end of the fiscal year, except for real property taxes, which are considered to be available if they are collected within 60 days after the end of the fiscal year. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, compensated absences, and other postemployment benefits, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

E. Real Property Taxes

Calendar

Real property taxes are levied annually by the Board no later than November 1st and become a lien on December 1st. Taxes are collected by the towns of Southampton and East Hampton and remitted to the District from December to June.

Enforcement

Uncollected real property taxes are subsequently enforced by Suffolk County in June.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

F. Restricted Resources

When an expense is incurred for purposes for which both restricted and unrestricted net assets are available, the District's policy concerning which to apply first varies with the intended use, and with associated legal requirements, many of which are described elsewhere in these Notes to Financial Statements.

G. Interfund Transactions

The operations of the District include transactions between funds. These transactions may be temporary in nature, such as with interfund borrowings. The District typically loans resources between funds for the purpose of providing cash flow. These interfund receivables and payables are expected to be repaid within one year. Permanent transfers of funds include transfers to provide financing or other services. This includes the transfer of unrestricted general fund revenues to finance various programs that the District must account for in other funds in accordance with budgetary authorizations.

In the district-wide statements, the amounts reported on the Statement of Net Assets for interfund receivables and payables represent amounts due between different fund types (governmental activities and fiduciary funds). Eliminations have been made for all interfund receivables and payables between the funds, with the exception of those due from or to the fiduciary funds.

The governmental funds report all interfund transactions as originally recorded. Interfund receivables and payables are netted on the accompanying governmental funds balance sheet when it is the District's practice to settle these amounts at a net balance based upon the right of legal offset.

A detailed disclosure by individual fund for interfund receivables, payables, transfers in and transfers out activity is provided subsequently in these Notes to Financial Statements.

H. Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimates. Estimates and assumptions are made in a variety of areas, including compensated absences, other postemployment benefits, potential contingent liabilities and useful lives of long-lived assets.

I. Cash and Cash Equivalents

Cash and cash equivalents consist of cash on hand, bank deposits and investments with a maturity date of three months or less from date of acquisition.

J. Receivables

Receivables are shown net of allowance for uncollectibles, if any. However, no allowance for uncollectibles has been provided since it is believed that such allowance would not be material.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

K. Inventories and Prepaid Items

Inventories of food in the school lunch fund are recorded at cost on a first-in, first-out basis or in the case of surplus food donated by the U.S. Department of Agriculture, at the Government's assigned value, which approximates market. These inventories are accounted for on the consumption method. A reserve for inventory has been recognized to indicate that this does not constitute available spendable resources.

Purchases of inventoriable items in other funds are recorded as expenditures at the time of purchase, and are considered immaterial in amount.

Prepaid items represent payments made by the District for which benefits extend beyond year-end. These payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the district-wide and fund financial statements. These items are reported as assets on the Statement of Net Assets or Balance Sheet using the consumption method. A current asset for the prepaid amounts is recorded at the time of purchase and an expense/expenditure is reported in the year the goods or services are consumed.

L. Capital Assets

Capital assets are reflected in the district-wide financial statements. Capital assets are reported at actual cost, when the information is available, or estimated historical cost based on professional third-party information. Donated assets are reported at estimated fair market value at the date of donation.

All capital assets, except land and construction in progress, are depreciated on a straight line basis over their estimated useful lives. Capitalization thresholds, the dollar value above which asset acquisitions are added to the capital asset accounts, and estimated useful lives of capital assets as reported in the district-wide statements are as follows:

| | <u>Capitalization Threshold</u> | <u>Estimated Useful Life</u> |
|----------------------------|-------------------------------------|----------------------------------|
| Buildings and improvements | \$ 5,000 | 30 years |
| Site improvements | 5,000 | 20 years |
| Furniture and equipment | 2,500 | 5 years |

M. Deferred Revenues

Deferred revenues in the governmental funds arise when potential revenues do not meet both the measurable and available criteria for recognition in the current period. Deferred revenues also arise when resources are received by the District before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both recognition criteria are met, or when the District has legal claim to the resources, the liability for deferred revenues is removed and revenues are recognized.

N. Vested Employee Benefits – Compensated Absences

Compensated absences consist of unpaid accumulated sick leave.

Sick leave eligibility and accumulation is specified in collective bargaining agreements and in individual employment contracts. Upon retirement, resignation or death, employees may contractually receive a payment based on unused accumulated sick leave. Based on the terms of employment contracts, this payment can be made in the form of a non-elective contribution to the employee's 403(b) account.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Consistent with GASB Statement No. 16, *Accounting for Compensated Absences*, the liability has been calculated using the vesting method and an accrual for that liability is included in the district-wide financial statements. The compensated absences liability is calculated based on the pay rates in effect at year end.

In the fund financial statements only the amount of matured liabilities is accrued within the general fund based upon expendable and available financial resources.

O. Other Benefits

Eligible District employees participate in the New York State Teachers' Retirement System or the New York State Employees' Retirement System.

In addition to providing pension benefits, the District provides postemployment health insurance coverage and survivor benefits for retired employees and their survivors. Collective bargaining agreements determine if District employees are eligible for these benefits if they reach normal retirement age while working for the District. Health care benefits are provided through plans whose premiums are based on the benefits paid during the year. The cost of providing post-retirement benefits is shared between the District and the retired employee. The District accounts for these postemployment benefits in accordance with GASB Statement No. 45 (GASB 45) *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The District recognizes the cost of providing health insurance by recording its share of insurance premiums as an expenditure in the general fund, in the year paid. In the District-wide statements, postemployment costs are measured and disclosed using the accrual basis of accounting.

P. Short-Term Debt

The District may issue revenue anticipation notes (RAN) and tax anticipation notes (TAN), in anticipation of the receipt of revenues. These notes are recorded as a liability of the fund that will actually receive the proceeds from the issuance of the notes. The RANs and TANs represent a liability that will be extinguished by the use of expendable, available resources of the fund.

The District may issue bond anticipation notes (BAN), in anticipation of proceeds from the subsequent sale of bonds. These notes are recorded as current liabilities of the funds that will actually receive the proceeds from the issuance of bonds. State law requires that BANs issued for capital purposes be converted to long-term financing within five years after the original issue date.

Q. Accrued Liabilities and Long-Term Obligations

Payables, accrued liabilities and long-term obligations are reported in the district-wide financial statements. In the governmental funds, payables and accrued liabilities are paid in a timely manner and in full from current financial resources. Claims and judgments, and compensated absences that will be paid from governmental funds, are reported as a liability in the fund financial statements only to the extent that they are due for payment in the current year. Bonds and other long-term obligations that will be paid from governmental funds are recognized as a liability in the fund financial statements when due.

Long-term obligations represent the District's future obligations or future economic outflows. The liabilities are reported as due and payable within one year or due and payable after one year in the Statement of Net Assets.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

R. Equity Classifications

District-Wide Statements

In the district-wide statements there are three classes of net assets:

Invested in capital assets, net of related debt – consists of net capital assets (cost less accumulated depreciation) reduced by outstanding balances of related debt obligations from the acquisition, construction or improvement of those assets.

Restricted net assets – reports net assets when constraints placed on the assets are either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments, or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets – reports all other net assets that do not meet the definition of the above two classifications and are deemed to be available for general use by the District.

Fund Statements

Unreserved fund balance may consist of two classifications. First, a designation of unreserved fund balance indicates the planned use of these resources in the subsequent year's budget. Second, the undesignated portion reports remaining fund balance that has not been designated or reserved. NYS Real Property Tax Law §1318, as amended with an effective date of July 1, 2007, restricts the unreserved, undesignated fund balance of the general fund to an amount not greater than 4% of the subsequent year's budget.

Fund balance reserves are created to satisfy legal restrictions, plan for future expenditures or relate to resources not available for general use or appropriation. These reserve funds are established through Board action or voter approval and a separate identity must be maintained for each reserve. Earnings on the invested resources become part of the respective reserve funds; however, separate bank accounts are not necessary for each reserve fund. Fund balance reserves currently in use by the District include the following:

Reserve for Encumbrances

Reserve for encumbrances represents the amount of outstanding encumbrances at the end of the fiscal year. The reserve is accounted for in the general and capital projects funds.

Employee Benefit Accrued Liability Reserve

Reserve for employee benefit accrued liability (GML §6-p) is used to reserve funds for the payment of accrued employee benefit due an employee upon termination of the employee's service. This reserve may be established by a majority vote of the Board, and is funded by budgetary appropriations and such other reserves and funds that may be legally appropriated. The reserve is accounted for in the general fund.

Reserve for Advances

Reserve for advances is used to reserve for loans to other funds that are not expected to be repaid within a current period. The reserve is accounted for in the general fund.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Reserve for Inventory

Reserve for inventory is used to restrict that portion of fund balance, which is not available for appropriation. The reserve is accounted for in the school lunch fund.

Reserve for Debt Service

Mandatory reserve for debt Service (GML §6-1) is used to establish a reserve for the purpose of retiring the outstanding obligations upon the sale of District property or capital improvement that was financed by obligations that remain outstanding at the time of sale. The funding of the reserve is from the proceeds of the sale of District property or capital improvement. Unexpended balances of proceeds of borrowings for capital projects; interest and earnings from investing proceeds of obligations, and premium and accrued interest are recorded in the Reserve for Debt and held until appropriated for debt payments. The reserve is accounted for in the debt service fund.

Reserve for Scholarships

Reserve for scholarships is used to account for monies donated for scholarship purposes, net of earnings and awards. The reserve is accounted for in the private purpose trust fund.

2. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN THE GOVERNMENTAL FUND STATEMENTS AND THE DISTRICT-WIDE STATEMENTS

Due to the differences in the measurement focus and basis of accounting used in the governmental fund statements and the district-wide statements, certain financial transactions are treated differently. The basic financial statements contain a full reconciliation of these items. The differences result primarily from the economic resource measurement focus of the Statement of Activities, compared with the current financial resource measurement focus of the governmental funds.

A. Total Fund Balances of Governmental Funds vs. Net Assets of Governmental Activities

Total fund balances of the District's governmental funds differ from "net assets" of governmental activities reported in the Statement of Net Assets. This difference primarily results from the additional long-term economic focus of the Statement of Net Assets versus the solely current financial resources focus of the governmental fund Balance Sheet.

B. Statement of Revenues, Expenditures and Changes in Fund Balance vs. Statement of Activities

Differences between the Statement of Revenues, Expenditures and Changes in Fund Balance and the Statement of Activities fall into one of three broad categories.

Long-Term Revenue and Expense Differences

Long-term revenue differences arise because governmental funds report revenues only when they are considered "available", whereas the Statement of Activities reports revenues when earned. Differences in long-term expenses arise because governmental funds report on a modified accrual basis, whereas the accrual basis of accounting is used on the Statement of Activities.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Capital Related Differences

Capital related differences include the difference between proceeds from the sale of capital assets reported on fund statements and the gain or loss on the sale of assets as reported on the Statement of Activities, and the difference between recording an expenditure for the purchase of capital items in the fund statements and depreciation expense on those items as recorded in the Statement of Activities.

Long-Term Debt Transaction Differences

Long-term debt transaction differences occur because the issuance of long-term debt provides current financial resources to governmental funds, but is recorded as a liability in the Statement of Net Assets. In addition, both interest and principal are recorded as expenditures in the fund statements when due and payable, whereas interest expense is recorded in the Statement of Activities as it accrues, and principal payments are recorded as a reduction of liabilities in the Statement of Net Assets.

3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgets

The District administration prepares a proposed budget for approval by the Board of Education for the general fund, the only fund with a legally adopted budget.

The voters of the District approved the proposed appropriation budget for the general fund.

Appropriations are adopted at the program line item level.

Appropriations established by the adoption of the budget constitute a limitation on expenditures (and encumbrances) that may be incurred. Appropriations lapse at the end of the fiscal year unless expended or encumbered. Encumbrances will lapse if not expended in the subsequent year. Appropriations authorized for the current year are increased by the planned use of specific reserves, and budget amendments approved by the Board of Education as a result of selected new revenue sources not included in the original budget (when permitted by law). These supplemental appropriations may occur subject to legal restrictions, if the Board approves them because of a need that exists which was not determined at the time the budget was adopted. No supplemental appropriations occurred during the year.

Budgets are adopted annually on a basis consistent with GAAP. Appropriations authorized for the year are increased by the amount of encumbrances carried forward from the prior year.

Budgets are established and used for individual capital project funds expenditures as approved by a special referendum of the District's voters. The maximum project amount authorized is based primarily upon the cost of the project, plus any requirements for external borrowings, not annual appropriations. These budgets do not lapse and are carried over to subsequent fiscal years until the completion of the projects.

B. Encumbrances

Encumbrance accounting is used for budget control and monitoring purposes and is reported as a part of the governmental funds. Under this method, purchase orders, contracts and other commitments for the expenditure of monies are recorded to reserve applicable appropriations. Outstanding encumbrances as of year end are presented as reservations of fund balance and do not represent expenditures or liabilities. These commitments will be honored in the subsequent period. Related expenditures are recognized at that time, as the liability is incurred or the commitment is paid.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

C. School Lunch Fund Deficit

The school lunch fund had a deficit fund balance of \$115,371. The District is exploring ways to operate the food service program profitably.

4. DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS

The District's investment policies are governed by state statutes and District policy. Resources must be deposited in Federal Deposit Insurance Corporation (FDIC) insured commercial banks or trust companies located within the state. Permissible investments include obligations of the U.S. Treasury and U.S. Agencies, repurchase agreements and obligations of New York State or its localities. Collateral is required for demand and time deposits and certificates of deposit not covered by FDIC insurance. Obligations that may be pledged as collateral are obligations of the United State and its Agencies and obligations of New York State and its municipalities. Investments are stated at fair value.

Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. GASB directs that deposits be disclosed as exposed to custodial credit risk if they are not covered by depository insurance and the deposits are either:

- A. Uncollateralized,
- B. Collateralized by securities held by the pledging financial institution, or
- C. Collateralized by securities held by the pledging financial institution's trust department or agent but not in the District's name.

None of the District's aggregate bank balances, not covered by depository insurance, were exposed to custodial credit risk as described above at year end.

Investment pool:

The District participates in a multi-municipal cooperative investment pool agreement pursuant to New York State General Municipal Law Article 5-G, §119-O, whereby it holds a portion of the investments in cooperation with other participants. The investments are highly liquid and are considered to be cash equivalents.

Total investments of the cooperative as of year-end are \$672,607,829, which consisted of \$327,630,555 in repurchase agreements, \$244,977,274 in U.S. Treasury Securities, and \$100,000,000 in collateralized bank deposits with various interest rate and due dates.

The following amounts are included as cash:

| Fund | Carrying Amount |
|-----------------------|--------------------|
| General Fund | \$ 825,307 |
| Debt Service Fund | 61,892 |
| Capital Projects Fund | 26,429 |
| Trust and Agency Fund | 130,753 |
| | \$ 1,044,381 |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

The above amounts represent the cost of the investment pool shares, and are considered to approximate market value. The investment pool is categorically exempt from the New York State collateral requirements. Additional information concerning the cooperative is presented in the annual report of New York Class – Board of Cooperative Educational Services of Putnam/Northern Westchester, 200 Boces Drive, Yorktown Heights, New York 10596-4399.

5. PARTICIPATION IN BOCES

During the year ended June 30, 2010, the District was billed \$628,968 for BOCES administrative and program costs. The District's share of BOCES aid amounted to \$100,678. Financial statements for the BOCES are available from the BOCES administrative offices at 201 Sunrise Highway, Patchogue, New York 11772.

6. DUE FROM OTHER GOVERNMENTS

Due from other governments at June 30, 2010 consisted of:

| | |
|--|---------------------|
| General Fund | |
| New York State Aid | \$ 144,928 |
| BOCES aid | 100,678 |
| Medicaid reimbursement | 1,325 |
| Other districts - charges for services | 197,512 |
| MTA payroll tax reimbursement | 53,499 |
| New York State - ARRA - education stabilization | <u>288,359</u> |
| | 786,301 |
| Special Aid Fund | |
| Federal and state grants | 414,457 |
| School Lunch Fund | |
| Federal and state food service program reimbursements | 1,991 |
| Capital Projects Fund | |
| New York State - EXCEL aid | <u>298,548</u> |
| | <u>\$ 1,501,297</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

7. CAPITAL ASSETS

Capital asset balances and activity for the year ended June 30, 2010 were as follows:

| | Balance June 30, 2009 | Additions | Reductions | Balance June 30, 2010 |
|---|--------------------------|--------------------|--------------------|--------------------------|
| Governmental activities | | | | |
| Capital assets not being depreciated | | | | |
| Land | \$ 309,243 | \$ | \$ | \$ 309,243 |
| Construction in progress | 40,850 | 265,580 | (27,479) | 278,951 |
| Total capital assets not being depreciated | <u>350,093</u> | <u>265,580</u> | <u>(27,479)</u> | <u>588,194</u> |
| Capital assets being depreciated | | | | |
| Buildings and improvements | 23,090,829 | 67,465 | | 23,158,294 |
| Furniture and equipment | 2,186,410 | 267,153 | (182,605) | 2,270,958 |
| Total capital assets being depreciated | <u>25,277,239</u> | <u>334,618</u> | <u>(182,605)</u> | <u>25,429,252</u> |
| Less accumulated depreciation for: | | | | |
| Buildings and improvements | 6,388,388 | 444,972 | | 6,833,360 |
| Furniture and equipment | 1,404,738 | 203,054 | (182,605) | 1,425,187 |
| Total accumulated depreciation | <u>7,793,126</u> | <u>648,026</u> | <u>(182,605)</u> | <u>8,258,547</u> |
| Total capital assets being depreciated, net | <u>17,484,113</u> | <u>(313,408)</u> | | <u>17,170,705</u> |
| Capital assets, net | <u>\$ 17,834,206</u> | <u>\$ (47,828)</u> | <u>\$ (27,479)</u> | <u>\$ 17,758,899</u> |

Depreciation expense was charged to governmental functions as follows:

| | |
|----------------------------|-------------------|
| General support | \$ 224,520 |
| Instruction | 419,112 |
| Food service program | 4,394 |
| Total depreciation expense | <u>\$ 648,026</u> |

8. INTERFUND TRANSACTIONS

Interfund balances and activities at June 30, 2010, are as follows:

| | Interfund | | | |
|-----------------------|-------------------|-------------------|---------------------|---------------------|
| | Receivable | Payable | Transfers In | Transfers Out |
| General Fund | \$ 672,891 | \$ 76,401 | \$ 73,893 | \$ 1,827,557 |
| Special Aid Fund | 2,500 | 375,942 | 4,203 | |
| School Lunch Fund | | 187,406 | | |
| Debt Service Fund | 20,388 | | 1,697,493 | 54,629 |
| Capital Projects Fund | | 131,543 | 125,862 | 19,265 |
| Fiduciary Fund | 75,513 | | | |
| Total | <u>\$ 771,292</u> | <u>\$ 771,292</u> | <u>\$ 1,901,451</u> | <u>\$ 1,901,451</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

The District typically transfers from the general fund to the special aid fund, the debt service fund and the capital projects fund in accordance with the general fund budget. The District transferred from the debt service fund to the general fund for the payment of debt, and from the capital projects fund to the general fund for unexpended funds on completed capital projects.

9. SHORT-TERM DEBT

Transactions in short-term debt for the year are summarized below:

| | <u>Maturity</u> | <u>Interest Rate</u> | <u>Balance June 30, 2009</u> | <u>Issued</u> | <u>Redeemed</u> | <u>Balance June 30, 2010</u> |
|-----|-----------------|----------------------|----------------------------------|---------------|-----------------|----------------------------------|
| TAN | 6/30/2010 | 1.50% | \$ - | \$ 9,700,000 | \$ (9,700,000) | \$ - |

Interest on short term debt for the year was \$67,456.

10. LONG-TERM LIABILITIES

Long-term liability balances and activity for the year were summarized below:

| | <u>Balance June 30, 2009</u> | <u>Additions</u> | <u>Reductions</u> | <u>Balance June 30, 2010</u> | <u>Amounts Due Within One Year</u> |
|---------------------------------|----------------------------------|-------------------|-----------------------|----------------------------------|--|
| Long-term debt: | | | | | |
| Bonds payable | \$ 12,905,000 | \$ 155,968 | \$ (1,115,000) | \$ 11,945,968 | \$ 940,968 |
| Deferred amount on refunding | 496,037 | | (7,447) | 488,590 | 54,288 |
| | <u>13,401,037</u> | <u>155,968</u> | <u>(1,122,447)</u> | <u>12,434,558</u> | <u>995,256</u> |
| Other long-term liabilities: | | | | | |
| Compensated absences | 301,593 | | (26,416) | 275,177 | 50,000 |
| Workers' compensation | 207,384 | 138,402 | (36,461) | 309,325 | |
| | <u>\$ 13,910,014</u> | <u>\$ 294,370</u> | <u>\$ (1,185,324)</u> | <u>\$ 13,019,060</u> | <u>\$ 1,045,256</u> |

The general fund has typically been used to liquidate other long-term liabilities.

Bonds payable are comprised of the following:

| <u>Description</u> | <u>Issue Date</u> | <u>Final Maturity</u> | <u>Interest Rate</u> | <u>Outstanding at June 30, 2010</u> |
|-------------------------------|-----------------------|---------------------------|--------------------------|---|
| Construction bond | 2002 | 2022 | 4.20-4.80% | \$ 3,060,000 |
| Construction bond - refunding | 2006 | 2020 | 3.75 - 5.00% | 8,730,000 |
| Serial bond - buses | 2009 | 2015 | 3.10 - 3.375% | 155,968 |
| | | | | <u>\$ 11,945,968</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

The following is a summary of debt service requirements:

| <u>Fiscal Year Ending June 30,</u> | <u>Principal</u> | <u>Interest</u> | <u>Total</u> |
|------------------------------------|----------------------|---------------------|----------------------|
| 2011 | \$ 940,968 | \$ 538,661 | \$ 1,479,629 |
| 2012 | 975,000 | 498,783 | 1,473,783 |
| 2013 | 1,015,000 | 455,148 | 1,470,148 |
| 2014 | 1,060,000 | 405,749 | 1,465,749 |
| 2015 | 1,110,000 | 354,036 | 1,464,036 |
| 2016 - 2020 | 6,210,000 | 919,063 | 7,129,063 |
| 2021 - 2022 | 635,000 | 45,925 | 680,925 |
| Total | <u>\$ 11,945,968</u> | <u>\$ 3,217,365</u> | <u>\$ 15,163,333</u> |

In December 2006, the District defeased certain general obligations by placing the proceeds of new bonds in an irrevocable trust to provide for all future debt service payments on the old bonds. Accordingly, the trust account assets and the liability for the defeased bonds are not included in the District's financial statements. The outstanding principal balance of the defeased bonds was callable and was satisfied on October 15, 2009.

The District is amortizing deferred charges on the advanced refunding and a refunding bond premium. The amortization is netted against the bonds payable and is calculated on a straight-line basis over the respective bond term, as applicable. The future net amortization is as follows:

| <u>Fiscal Year Ending June 30,</u> | <u>Net Revenue (Expense)</u> |
|------------------------------------|----------------------------------|
| 2011 | \$ 54,288 |
| 2012 | 54,288 |
| 2013 | 54,288 |
| 2014 | 54,288 |
| 2015 | 54,288 |
| 2016 - 2019 | 217,150 |
| | <u>\$ 488,590</u> |

Interest on long-term debt for the year was composed of:

| | |
|---|-------------------|
| Interest paid | \$ 582,493 |
| Less interest accrued in the prior year | (98,925) |
| Plus interest accrued in the current year | 96,060 |
| Plus amortization of deferred charges on advanced refunding, net of premium | (7,447) |
| Total interest expense on long-term debt | <u>\$ 572,181</u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

11. PENSION PLANS

A. General Information

The District participates in the New York State Teachers' Retirement System (NYSTRS) and the New York State and Local Employees' Retirement System (NYSERS). These are cost-sharing multiple employer, public employee retirement systems. The Systems offer a wide range of plans and benefits which are related to years of service and final average salary, vesting of retirement benefits, death, and disability.

B. Provisions and Administration

Teachers' Retirement System

The NYSTRS is administered by the New York State Teachers' Retirement Board. The System provides benefits to plan members and beneficiaries as authorized by the Education Law and the Retirement and Social Security Law of the state of New York. The NYSTRS issues a publicly available financial report that contains financial statements and required supplementary information for the System. The report may be obtained by writing to the New York State Teachers' Retirement System, 10 Corporate Woods Drive, Albany, NY 12211-2395.

Employees' Retirement System

The NYSERS provides retirement benefits as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security Law. The System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York State and Local Employees' Retirement System, Gov. Alfred E. Smith State Office Building, Albany, NY 12244.

C. Funding Policies

The Systems are noncontributory for the employee except for those who either joined the Systems after July 27, 1976 with less than ten years of credited service, who contribute 3% of their salary, or joined the Systems on or after January 1, 2010 who contribute 3% of their salary to NYSERS or 3.5% of their salary to NYSTRS throughout active membership. For the NYSERS, the Comptroller shall certify annually the rates expressed as proportions of members' payroll annually, which shall be used in computing the contributions required to be made by employers to the pension accumulation fund. Pursuant to Article 11 of the Education Law, rates are established annually for NYSTRS by the New York State Teachers' Retirement Board.

The District is required to contribute at an actuarially determined rate. The District contributions made to the Systems were equal to 100% of the contributions required for each year. The required contributions for the current year and two preceding years were:

| Year | NYSTRS | NYSERS |
|------|------------|------------|
| 2010 | \$ 872,630 | \$ 172,678 |
| 2009 | 1,055,286 | 147,987 |
| 2008 | 1,098,110 | 155,508 |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

12. POSTEMPLOYMENT BENEFITS

A. Plan Description

The District provides medical, Medicare part B reimbursement, and dental and vision coverage (the healthcare plan) to retired employees in accordance with employment contracts. The plan is a single-employer defined benefit healthcare plan primarily administered through the New York State Health Insurance Program – Empire Plan.

B. Funding Policy

The District assumes its share of the cost of the premiums, which ranges from 85 – 100%, as determined by the employment contract of the District’s retiree and recognizes the cost of the healthcare plan annually as expenditures in the general fund of the fund financial statements as payments are made. For the year ended June 30, 2010, the District recognized a general fund expenditure of \$533,199 for insurance premiums for 54 currently enrolled retirees. Currently, there is no provision in the law to permit the District to fund other postemployment benefits by any means other than the “pay as you go” method.

C. Annual OPEB Cost and Net OPEB Obligation

The District’s annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years. The following table shows the components of the District’s annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District’s net OPEB obligation.

| | |
|---|----------------------------|
| Annual required contribution (ARC) | \$ 3,300,300 |
| Interest on net OPEB obligation | 105,600 |
| Adjustment to ARC | <u>(94,400)</u> |
| Annual OPEB cost (expense) | 3,311,500 |
| Contributions made | <u>(533,199)</u> |
| | |
| Increase in net OPEB obligation | 2,778,301 |
| Net OPEB obligation - beginning of year | <u>2,640,228</u> |
| | |
| Net OPEB obligation - end of year | <u><u>\$ 5,418,529</u></u> |

The District’s annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the years ended June 30, 2010 and 2009 are as follows:

| Fiscal Year Ended | Annual OPEB Cost | Percentage of Annual OPEB Cost Contributed | Net OPEB Obligation |
|----------------------|---------------------|--|------------------------|
| June 30, 2010 | \$ 3,311,500 | 16% | \$ 5,418,529 |
| June 30, 2009 | 2,989,500 | 12% | 2,640,228 |

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

D. Funded Status and Funding Progress

As of January 1, 2010, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability for benefits was \$33,966,800 and the actuarial value of assets was \$-0-, resulting in an unfunded actuarial accrued liability (UAAL) of \$33,966,800. The covered payroll (annual payroll of active employees covered by the plan) was \$16,876,252, and the ratio of the UAAL to the covered payroll was 201.3%.

Actuarial valuations of an ongoing plan involved estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The required schedule of funding progress following the notes to the financial statements presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

E. Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive plan (the plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the January 1, 2010, actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% discount rate and an annual healthcare cost trend rate of 7.3% initially, reduced by decrements to an ultimate rate of 6% after 9 years. The UAAL is being amortized to increase over time as projected payrolls increase. The remaining amortization period at June 30, 2010, was 28 years.

13. RISK MANAGEMENT

A. General Information

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; injuries to employees; errors and omissions; and natural disasters. These risks are covered by a combination of self-insurance reserves and commercial insurance purchased from independent third parties. Settled claims from these risks have not exceeded available reserves and commercial insurance coverage for the past three years.

B. Public Entity Risk Pool

The District participates in a risk pool, the East End Workers' Compensation Consortium (EEWCC), to insure workers' compensation claims. This public entity risk pool was created under Article 5 of Workers' Compensation Law, to evaluate, process, administer, and pay workers' compensation claims. The District retains the risk of loss.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

The District pays an annual assessment to the pool for its workers' compensation claims coverage and related expenses. The EEWCC has obtained an excess compensation insurance policy to buffer the effect that a single large claim may have on the District's loss experience. The EEWCC established a non-discounted liability for both reported and unreported insured events, which includes estimates of both future payments or losses and related claim adjustment expenses. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. However, because actual claim costs depend on complex factors, the process used in computing claims liabilities does not necessarily result in an exact amount. Such claims are based on the ultimate cost of claims (including future claim adjustment expenses) that have been reported but not settled, and claims that have been incurred but not reported.

The District's liability for incurred but unpaid claims and incurred but not reported claims at June 30, 2010, as processed by the EEWCC, is \$309,325. Claims activity is summarized as follows:

| | 2009 | 2010 |
|---|------------|------------|
| Claims at beginning of year | \$ 191,392 | \$ 207,384 |
| Incurred claims and claim adjustment expenses | 106,392 | 138,402 |
| Claim payments and expenses | (90,400) | (36,461) |
| Claim liabilities at end of year | \$ 207,384 | \$ 309,325 |

The EEWCC is holding \$125,389 of cash on account for the District to satisfy these liabilities at June 30, 2010 which is reflected in other assets.

The EEWCC has issued financial statements for the year ended June 30, 2010. Copies of these statements can be obtained from the District's administrative office.

14. COMMITMENTS AND CONTINGENCIES

A. Grants

The District has received grants, which are subject to audit by agencies of the state and federal governments. Such audits may result in disallowances and a request for a return of funds. Based on prior audits, the District's administration believes disallowances, if any, will be immaterial.

B. Litigation

The District is involved in lawsuits arising from the normal conduct of its affairs. Some of these lawsuits seek damages which may be in excess of the District's insurance coverage. However, it is not possible to determine the District's potential exposure, if any, at this time.

SAG HARBOR UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

C. Operating Leases

The District leases various equipment under non-cancelable operating leases. Rental expense for the year was \$65,525. The minimum remaining operating lease payments are as follows:

| <u>Fiscal Year Ending June 30,</u> | <u>Amount</u> |
|------------------------------------|-------------------|
| 2011 | \$ 64,786 |
| 2012 | 40,830 |
| 2013 | 4,437 |
| 2014 | <u>1,827</u> |
| | <u>\$ 111,880</u> |

15. SUBSEQUENT EVENTS

On July 1, 2010, the District issued tax anticipation notes in the amount of \$12,500,000, which are due June 30, 2011, and bear interest at a rate of 1.50%. The proceeds of the note amounted to \$12,552,581, which included a premium of \$52,581.

On July 1, 2010, the District issued a bond anticipation note for the purchase of various vehicles in the amount of \$227,039, which is due on July 1, 2011, and bears interest at a rate of 1.45%.

SAG HARBOR UNION FREE SCHOOL DISTRICT
Schedule of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund
For The Year Ended June 30, 2010

| | Original Budget | Final Budget | Actual | Final Budget Variance with Actual |
|---|--------------------|-------------------|-------------------|---|
| REVENUES | | | | |
| Local Sources | | | | |
| Real property taxes | \$ 25,737,321 | \$ 25,737,321 | \$ 25,750,731 | \$ 13,410 |
| Other tax items | 609,323 | 609,323 | 715,708 | 106,385 |
| Charges for services | 285,000 | 285,000 | 375,743 | 90,743 |
| Use of money and property | 260,000 | 260,000 | 24,166 | (235,834) |
| Sale of property and compensation for loss | | | 5,393 | 5,393 |
| Miscellaneous | 136,185 | 136,185 | 128,567 | (7,618) |
| Total Local Sources | 27,027,829 | 27,027,829 | 27,000,308 | (27,521) |
| State Sources | 1,720,385 | 1,507,762 | 1,463,979 | (43,783) |
| Medicaid Reimbursement | | | 5,212 | 5,212 |
| Federal Sources | | 212,623 | 288,359 | 75,736 |
| Total Revenues | 28,748,214 | 28,748,214 | 28,757,858 | 9,644 |
| OTHER SOURCES | | | | |
| Operating transfers in | 387,443 | 387,443 | 73,893 | (313,550) |
| Total Revenues and Other Sources | 29,135,657 | 29,135,657 | 28,831,751 | \$ (303,906) |

Note to Required Supplementary Information

Budget Basis of Accounting

Budgets are adopted on the modified accrual basis of accounting consistent with accounting principles generally accepted in the United States of America.

See Paragraph on Supplementary Information Included in Auditor's Report

SAG HARBOR UNION FREE SCHOOL DISTRICT
Schedule of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund (Continued)
For The Year Ended June 30, 2010

| | Original Budget | Final Budget | Actual | Year End Encumbrances | Final Budget Variance with Actual & Encumbrances |
|--|--------------------|-------------------|-------------------|--------------------------|---|
| EXPENDITURES | | | | | |
| General Support | | | | | |
| Board of education | \$ 37,001 | \$ 29,456 | \$ 28,457 | \$ | \$ 999 |
| Central administration | 259,965 | 275,145 | 274,072 | | 1,073 |
| Finance | 395,947 | 421,324 | 419,636 | | 1,688 |
| Staff | 186,450 | 160,323 | 160,139 | | 184 |
| Central services | 2,099,787 | 1,807,013 | 1,783,988 | 7,978 | 15,047 |
| Special items | 250,746 | 288,170 | 286,581 | | 1,589 |
| Total General Support | 3,229,896 | 2,981,431 | 2,952,873 | 7,978 | 20,580 |
| Instruction | | | | | |
| Instruction, administration & improvement | 1,159,021 | 1,281,788 | 1,276,438 | | 5,350 |
| Teaching - regular school Programs for children with handicapping conditions | 9,369,435 | 9,592,247 | 9,497,178 | | 95,069 |
| Occupational education | 3,777,802 | 3,642,159 | 3,607,362 | | 34,797 |
| Teaching - special school | 353,518 | 376,241 | 373,855 | | 2,386 |
| Instructional media | 119,000 | 148,064 | 146,020 | | 2,044 |
| Pupil services | 978,147 | 835,854 | 821,476 | | 14,378 |
| | 2,114,643 | 2,024,677 | 2,007,669 | | 17,008 |
| Total Instruction | 17,871,566 | 17,901,030 | 17,729,998 | - | 171,032 |
| Pupil Transportation | 1,563,819 | 1,353,905 | 1,242,806 | | 111,099 |
| Community Services | 25,250 | 25,502 | 21,502 | | 4,000 |
| Employee Benefits | 5,130,484 | 5,488,843 | 5,296,896 | | 191,947 |
| Debt Service | | | | | |
| Interest | 130,000 | 69,545 | 67,456 | | 2,089 |
| Total Debt Service | 130,000 | 69,545 | 67,456 | - | 2,089 |
| Total Expenditures | 27,951,015 | 27,820,256 | 27,311,531 | 7,978 | 500,747 |
| OTHER USES | | | | | |
| Operating transfers out | 1,697,488 | 1,828,247 | 1,827,557 | | 690 |
| Total Expenditures and Other Uses | 29,648,503 | 29,648,503 | 29,139,088 | \$ 7,978 | \$ 501,437 |
| Net Change in Fund Balances | (512,846) | (512,846) | (307,337) | | |
| Fund Balances - Beginning of Year | 512,846 | 512,846 | 859,738 | | |
| Fund Balances - End of Year | \$ - | \$ - | \$ 552,401 | | |

Note to Required Supplementary Information

Budget Basis of Accounting

Budgets are adopted on the modified accrual basis of accounting consistent with accounting principles generally accepted in the United States of America.

SAG HARBOR UNION FREE SCHOOL DISTRICT
Schedule of Funding Progress - Other Postemployment Benefits
For The Year Ended June 30, 2010

| Valuation Date | Actuarial Value of Assets | Accrued Liability | Unfunded Actuarial Accrual Liability (UAAL) | Funded Ratio | Covered Payroll | UAAL as a Percentage of Covered Payroll |
|-------------------|---------------------------------|----------------------|---|-----------------|--------------------|--|
| January 1, 2010 | \$ - | \$ 33,966,800 | \$ 33,966,800 | 0% | \$ 16,876,252 | 201.3% |
| January 1, 2008 | - | 27,146,800 | 27,146,800 | 0% | 12,062,246 | 225.1% |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Schedules of Change from Adopted Budget to Final Budget
And Use of Unreserved Fund Balance - General Fund
For The Year Ended June 30, 2010

CHANGE FROM ADOPTED BUDGET TO FINAL BUDGET

| | |
|---------------------------|-----------------------------|
| Adopted Budget | \$ 29,640,657 |
| Additions: | |
| Prior year's encumbrances | <u>7,846</u> |
| Original Budget | 29,648,503 |
| Budget revision | <u>-</u> |
| Final Budget | <u><u>\$ 29,648,503</u></u> |

| | |
|--|-----------------------------|
| Next year's budget is a voter-approved budget of | <u><u>\$ 31,500,811</u></u> |
|--|-----------------------------|

USE OF UNRESERVED FUND BALANCE

| | |
|--|-------------------------|
| Unreserved Fund Balance - As of the beginning of the year | \$ 570,818 |
| Less: | |
| Designated fund balance used for the levy of taxes - Adopted budget | <u>505,000</u> |
| Undesignated Fund Balance - As of the beginning of the year | <u><u>\$ 65,818</u></u> |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Schedule of Certain Revenues and Expenditures
Compared to ST-3 Data
For The Year Ended June 30, 2010

| | <u>Code</u> | <u>ST-3 Amount</u> | <u>Audited Amount</u> |
|--------------------------|-------------|--------------------|---------------------------|
| REVENUES | | | |
| Real Property Taxes | A -1001 | \$ 25,750,731 | \$ 25,750,731 |
| Non-Property Taxes | AT-1199 | - | - |
| State Aid | AT-3999 | 1,463,979 | 1,463,979 |
| Federal Aid | AT-4999 | 293,571 | 293,571 |
| Total Revenues | AT-5999 | 28,831,751 | 28,831,751 |
| EXPENDITURES | | | |
| General Support | AT-1999 | 2,952,873 | 2,952,873 |
| Pupil Transportation | AT-5599 | 1,242,806 | 1,242,806 |
| Debt Service - Principal | AT-9798.6 | - | - |
| Debt Service - Interest | AT-9798.7 | 67,456 | 67,456 |
| Total Expenditures | AT-9999 | 29,139,088 | 29,139,088 |

SAG HARBOR UNION FREE SCHOOL DISTRICT
Investment in Capital Assets, Net of Related Debt
For The Year Ended June 30, 2010

| | |
|---|----------------------------|
| Capital assets, net | <u>\$ 17,758,899</u> |
| Deduct: | |
| Short-term portion of bonds payable | (995,256) |
| Long-term portion of bonds payable | (11,439,302) |
| Less: | |
| Unspent bond proceeds | <u>836</u> |
| | <u>(12,433,722)</u> |
| Investment in capital assets, net of related debt | <u><u>\$ 5,325,177</u></u> |

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

To the Board of Education
Sag Harbor Union Free School District
Sag Harbor, New York

We have audited the financial statements of the governmental activities, each major fund and the fiduciary funds of the Sag Harbor Union Free School District (District), as of and for the year ended June 30, 2010, which collectively comprise the District's basic financial statements and have issued our report thereon dated October 22, 2010. 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.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Sag Harbor Union Free School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Sag Harbor Union Free School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Sag Harbor Union Free School District's internal control over financial reporting.

A deficiency in internal control exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency or combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Sag Harbor Union Free School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, 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 no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

We noted certain matters that we have reported to the Board of Education, Audit Committee and management of the Sag Harbor Union Free School District in a separate letter dated October 22, 2010.

This report is intended solely for the use and information of the Board of Education, Audit Committee, management, others you deem appropriate within the District, and any governmental authorities you need to share this information with and is not intended to be and should not be used by anyone other than these specified parties.

Cullen & Danowski, LLP
October 22, 2010

