



PAULY, ROGERS AND Co., P.C.
12700 SW 72nd Ave. ♦ Tigard, OR 97223
(503) 620-2632
www.paulyrogersandcpcpas.com

January 29, 2026

To the Board of Directors
Molalla River School District 35
Clackamas County, Oregon

We have audited the basic financial statements of the governmental activities, the business-type activities and each major fund, and the aggregate remaining fund information of Molalla River School District 35 (the District) for the year ended June 30, 2025. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards and *Government Auditing Standards and the Uniform Guidance* as well as certain information related to the planned scope and timing of our audit. Professional standards also require that we communicate to you the following information related to our audit.

Purpose of the Audit

Our audit was conducted using sampling, inquiries and analytical work to opine on the fair presentation of the basic financial statements and compliance with:

- generally accepted accounting principles and auditing standards
- the Oregon Municipal Audit Law and the related administrative rules
- federal, state and other agency rules and regulations related to expenditures of federal awards

Our Responsibility under U.S. Generally Accepted Auditing Standards and the Uniform Guidance

As stated in our engagement letter, our responsibility, as described by professional standards, is to express opinions about whether the basic financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Our audit of the basic financial statements does not relieve you or management of your responsibilities. Our engagement letter details our nonaudit services we provide; these services do not constitute an audit under Government Auditing Standards.

In planning and performing our audit, we considered the system of internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the basic financial statements and not to provide assurance on the system of internal control over financial reporting. We also considered the system of internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with the Uniform Guidance.

As part of obtaining reasonable assurance about whether the basic financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of the basic financial statement amounts. However, providing an opinion on compliance with those provisions is not an objective of our audit. Also in accordance with the Uniform Guidance, we examined, on a test basis, evidence about compliance with the types of compliance requirements described in the OMB's Compliance Supplement applicable to each of the major federal programs for the purpose of expressing an opinion on compliance with those requirements. While our audit provided a reasonable basis for our opinion, it does not provide a legal determination on compliance with those requirements.

Pauly, Rogers and Co., P.C.

Our responsibility for the supplementary information accompanying the basic financial statements, as described by professional standards, is to evaluate the presentation of the supplementary information in relation to the basic financial statements as a whole and to report on whether the supplementary information is fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Planned Scope and Timing of the Audit

An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the basic financial statements; therefore, our audit involved judgment about the number of transactions examined and the areas to be tested.

Our audit included obtaining an understanding of the District and its environment, including the system of internal control, sufficient to assess the risks of material misstatement of the basic financial statements and to design the nature, timing, and extent of further audit procedures. Material misstatements may result from (1) errors, (2) fraudulent financial reporting, (3) misappropriation of assets, or (4) violations of laws or governmental regulations that are attributable to the District or to acts by management or employees acting on behalf of the District. We also communicated any control related matters that are required to be communicated under professional standards.

Results of Audit

1. Audit opinion letter - an unmodified opinion on the basic financial statements has been issued. This means we have given a “clean” opinion with no reservations.
2. State minimum standards – We found no exceptions or issues requiring comment.
3. Federal Awards - We found no issues of non-compliance and no questioned costs. We have responsibility to review these programs and give our opinion on the schedule of expenditures of federal awards, and tests of the internal control system, compliance with laws and regulations, and general and specific requirements mandated by the various awards.
4. Management letter – No separate management letter was issued.

Significant Audit Matters

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used are described in Note 1 to the basic financial statements. No new accounting policies were adopted and the application of existing policies was not changed during fiscal 2024-25, except that GASB statement No. 101 *Compensated Absences* was implemented. We noted no transactions entered into during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the basic financial statements in the proper period.

Accounting estimates are an integral part of the basic financial statements prepared by management and are based on management’s knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the basic financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most significant estimates in the basic financial statements are the District’s portion of the statewide Net Pension Liability (or Asset), Other Post-Employment Benefits, estimate of Accounts Receivable, Capital Asset Depreciation, and the fair market value of investments, which are based on actuarial valuations, estimated collectability of receivables, useful lives of assets, and active market values or significant observable inputs. We have evaluated the methods, assumptions, and data used to develop these estimates in determining that they were reasonable in relation to the basic financial statements taken as a whole. Certain financial statement disclosures are particularly sensitive because of their significance to financial statement users. The basic financial statement disclosures are neutral, consistent, and clear.

Pauly, Rogers and Co., P.C.

Difficulties Encountered in Performing the Audit

We encountered no difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements or determined that their effects are immaterial. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, taken as a whole. There were immaterial uncorrected misstatements noted during the audit which were discussed with management. The uncorrected misstatements or the matters underlying them could potentially cause future period basic financial statements to be materially misstated, even if, in our judgment, such uncorrected misstatements are immaterial to the basic financial statements under audit.

Disagreements with Management

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the basic financial statements or the auditors' report. We are pleased to report that no such disagreements arose during the course of our audit.

Management Representations

We have requested certain representations from management that are included in the management representation letter.

Management Consultations with Other Independent Accountants

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the basic financial statements or a determination of the type of auditors' opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

Other Audit Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards with management each year prior to our retention as the auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Required Supplementary Information (RSI)

We applied certain limited procedures to the required supplementary information that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the required supplementary information and do not express an opinion or provide any assurance on it, except for the budgetary statements listed as required supplementary information.

Pauly, Rogers and Co., P.C.

Supplementary Information

We were engaged to report on the supplementary information, which accompany the basic financial statements but are not required supplementary information. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the basic financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the basic financial statements or to the basic financial statements themselves.

Other Information

We were not engaged to report on the other information, as listed in the table of contents, or the listing of Board members, located before the table of contents, which accompany the basic financial statements but are not required supplementary information. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements, and accordingly, we do not express an opinion or provide any assurance on it.

Other Matters – Future Accounting and Auditing Issues

In order to keep you aware of new auditing standards issued by the American Institute of Certified Public Accountants and accounting statements issued by the Governmental Accounting Standards Board (GASB), we have prepared the following summary of the more significant upcoming issues:

GASB 103 – Financial Reporting Model Improvements

The requirements of this Statement are effective for fiscal years beginning after June 15, 2025, and all reporting period thereafter. Earlier application is encouraged. The requirements for Management's Discussion and Analysis (MD&A) will improve the quality of the analysis of changes from the prior year, which will enhance the relevance of that information. They also will provide clarity regarding what information should be presented in MD&A. The requirements for the separate presentation of unusual or infrequent items will provide clarity regarding which items should be reported separately from other inflow and outflows of resources. The definitions of operating revenues and expenses and of nonoperating revenues and expenses will replace accounting policies that vary from government to government, thereby improving comparability. The addition of a subtotal for operating income (loss) and noncapital subsidies will improve the relevance of information provided in the proprietary fund statement of revenues, expenses, and changes in fund net position. The requirement for presentation of major component unit information will improve comparability. The requirement that budget comparison information be presented as required supplementary information (RSI) will improve comparability, and the inclusion of the specified variances and the explanation of significant variances will provide more useful information for making decisions and assessing accountability.

The objective of this Statement is to improve key components of the financial reporting model to enhance its effectiveness in providing information that is essential for decision making and assessing a government's accountability. This Statement also addresses certain application issues.

Management's Discussion and Analysis

This Statement continues the requirement that the basic financial statements be preceded by management's discussion and analysis (MD&A), which is presented as required supplementary information (RSI). MD&A provided an objective and easily readable analysis of the government's financial activities based on currently known facts, decisions, or conditions and presents comparisons between current and prior year. This Statement requires that the information presented in MD&A be limited to the related topics discussed in five sections: (1) Overview of the Financial Statements, (2) Financial Summary, (3) Detailed Analyses, (4) Significant Capital Asset and Long-Term Financing Activity, and (5) Currently Known Facts, Decisions, or Conditions. Furthermore, this Statement stresses that the detailed analyses should explain why balances and results of operations changed rather than simply presenting the amounts or percentages by which they changed. This Statement emphasizes that the analysis provided in MD&A should avoid unnecessary duplication by not repeating explanations that may be relevant to multiple sections and that "boilerplate" discussions should be avoided by presenting only the most relevant information, focused on the primary government. In addition, this Statement continues the requirement that information included in MD&A distinguish between that of the primary government and its discretely presented component units.

Unusual or Infrequent Items

This Statement describes unusual or infrequent items as transactions and other events that are either unusual in nature or infrequent in occurrence. Furthermore, governments are required to display the inflows and outflows related to each unusual or infrequent item separately as the last presented flow(s) of resources prior to the net change in resource flows in the government-wide, governmental fund, and proprietary fund statements of resource flows.

Presentation of the Proprietary Fund Statement of Revenues, Expenses, and Changes in Fund Net Position

This Statement requires that the proprietary fund statement of revenues, expenses, and changes in fund net position continue to distinguish between operating and nonoperating revenues and expenses. Operating revenues and expenses are defined as revenues and expenses other than nonoperating revenues and expenses. Nonoperating revenues and expenses are defined as (1) subsidies received and provided, (2) contributions to permanent and term endowments, (3) revenues and expenses related to financing, (4) resources from the disposal of capital assets and inventory, and (5) investment income and expenses.

In addition to the subtotals currently required in a proprietary fund statement of revenues, expenses, and changes in fund net position, this Statement requires that a subtotal for *operating income (loss) and noncapital subsidies* be presented before reporting other nonoperating revenues and expenses. Subsidies are defined as (1) resources received from another party or fund (a) for which the proprietary fund does not provide good and services to the other party or fund and (b) that directly or indirectly keep the proprietary fund's current or future fees and charges lower than they would be otherwise, (2) resources provided to another party of fund (a) for which the other party or fund does not provide goods and services to the proprietary fund and (b) that are recoverable through the proprietary funds current or future pricing policies, and (3) all other transfers.

Other Matters – Future Accounting and Auditing Issues

GASB 104 – Disclosure of Capital Assets

The requirements of this Statement are effective for fiscal years beginning after June 15, 2025, and all reporting periods thereafter. Earlier application is encouraged. The requirements of this Statement will improve financial reporting by providing users of financial statements with essential information about certain types of capital assets in order to make informed decisions and assess accountability. Additionally, the disclosure requirements will improve consistency and comparability between governments.

State and local governments are required to provide detailed information about capital assets in notes to financial statements. Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*, requires certain information regarding capital assets to be presented by major class. The objective of this Statement is to provide users of government financial statements with essential information about certain types of capital assets.

This Statement requires certain types of capital assets to be disclosed separately in the capital asset note disclosures requires by Statement 34. Lease assets recognized in accordance with Statement No. 87, *Leases*, and intangible right-to-use assets recognized in accordance with Statement No. 94, *Public-Private and Public-Public Partnerships and Availability Payment Agreements*, should be disclosed separately by major class of underlying asset in the capital asset note disclosures. Subscription assets recognized in accordance with Statement No. 96, *Subscription-Based Information Technology Arrangements*, also should be separately disclosed. In addition, this Statement requires intangible assets other than those three types to be disclosed separately by major class.

This Statement also requires additional disclosures for capital assets held for sale. A capital asset is a capital asset held for sale if (a) the government has decided to pursue the sale of capital asset and (b) it is probable that the sale will be finalized within one year of the financial statement date. Governments should consider relevant factors to evaluate the likelihood of the capital asset being sold within the established time frame. This Statement requires that capital assets held for sale be evaluated each reporting period. Governments should disclose (1) the ending balance of capital assets held for sale, with separate disclosure for historical cost and accumulated depreciation by major class of asset, and (2) the carrying amount of debt which the capital assets held for sale are pledged as collateral for each major class of asset.

Best Practices – Not Significant Deficiencies

1. Governing Body Monitoring

An integral part of internal controls is the monitoring of financial activities by those charged with the governance (the Board.) This can be accomplished by asking specifically designed questions to senior staff, by reviewing basic financial statements and projections and by comparing financial results to pre-established benchmarks. While the Board participates in the budget adoption process and receives staff prepared basic financial statements, these only partially fulfill the monitoring function. We recommend that the Board articulate their monitoring practices and record in the minutes when those activities occur.

2. Fidelity Insurance Coverage

In reviewing fidelity insurance (employee honesty) coverage we noticed that the District often carries cash and investment balances in excess of the insurance coverage amount. We recommend that the Board examine this exposure risk and make a determination as to the amount of insurance coverage they feel is prudent in regard to their oversight.

3. Service Organizations

The District has contracted with an Education Service District (ESD) as a service organization for accounting and information technology services. The ESD does not have a SSAE 18 (service provider) report or internal control report covering their operations, accounting processing and information technology controls. The possibility exists that errors or irregularities could exist and not be detected. While nothing came to our attention during our testing, we recommend the Board review the risks regarding this matter and consider getting assurance from the service provider that will reduce risks, including being named on their insurance policies.

4. IT Controls

During our review of IT Control Policies over the accounting system, we noted that the District does not have a policy regarding the use of special characters or numbers in passwords. We recommend that the District consider a policy to strengthen passwords used for the accounting systems and require password changes at least on a bi-annual basis to enhance internal control.

This information is intended solely for the information and use of the Board of Directors and management and is not intended to be and should not be used by anyone other than these specified parties.

ROY R. ROGERS, CPA
PAULY, ROGERS AND CO., P.C.