

Management Report

for

Independent School District No. 831  
Forest Lake, Minnesota  
June 30, 2010



PRINCIPALS

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To the School Board of  
Independent School District No. 831  
Forest Lake, Minnesota

We have prepared this management report in conjunction with our audit of Independent School District No. 831, Forest Lake, Minnesota's (the District) financial statements for the year ended June 30, 2010. The purpose of this report is to communicate information relevant to the financing of public education in Minnesota and to provide comments resulting from our audit process. We have organized this report into the following sections:

- Audit Summary
- Funding Public Education in Minnesota
- Financial Trends of Your District
- Accounting and Auditing Updates
- Legislative Summary

We would be pleased to further discuss any of the information contained in this report or any other concerns that you would like us to address. We would also like to express our thanks for the courtesy and assistance extended to us during the course of our audit.

This report is intended solely for the information and use of those charged with governance of the District, the School Board, management, and those who have responsibility for oversight of the financial reporting process and is not intended to be, and should not be, used by anyone other than these specified parties.

*Malloy, Montague, Karnowski, Radosevich, & Co., P.A.*

November 17, 2010

## **AUDIT SUMMARY**

We hereby provide you with the following summary of our audit work, key conclusions, and other information that we consider important or that is required to be communicated to the School Board, administration, or those charged with governance of the District.

### **OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA, *GOVERNMENT AUDITING STANDARDS*, AND THE U.S. OFFICE OF MANAGEMENT AND BUDGET CIRCULAR A-133**

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the District as of and for the year ended June 30, 2010. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and the U.S. Office of Management and Budget Circular A-133, as well as certain information related to the planned scope and timing of our audit. We have communicated such information to you verbally and in our audit engagement letter. Professional standards also require that we communicate to you the following information related to our audit.

### **PLANNED SCOPE AND TIMING OF THE AUDIT**

We performed the audit according to the planned scope and timing previously discussed and coordinated in order to obtain sufficient audit evidence and complete an effective audit.

### **AUDIT OPINION AND FINDINGS**

Based on our audit of the District's financial statements for the year ended June 30, 2010:

- We have issued an unqualified opinion on the District's annual financial statements.
- We noted no matters involving the District's internal control over financial reporting that we consider to be significant deficiencies or material weaknesses.
- The results of our testing disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.
- We noted that the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the basic financial statements.
- The results of our tests noted one instance of noncompliance relating to the reporting of American Recovery and Reinvestment Act (ARRA) funds for each major federal program, which is further detailed in the Schedule of Findings and Questioned Costs.
- We noted one matter involving the internal control over compliance and its operation that we consider to be a material weakness in our testing of major federal programs. This matter relates to the reporting of ARRA funds for each major federal program and is further detailed in the Schedule of Findings and Questioned Costs.
- We have reported one finding based on our testing of the District's compliance with Minnesota laws and regulations relating to the timely payment of vendor obligations which is further detailed in the Schedule of Findings and Questioned Costs.

### **EXTRACURRICULAR STUDENT ACTIVITY ACCOUNTS**

In accordance with Minnesota Statutes, the District's School Board has elected not to exercise control over the transactions of the extracurricular student activity accounts maintained at various district sites. Consequently, the cash receipts and disbursements of the District's extracurricular student activity accounts are reported in a separate set of financial statements, rather than being reported within the District's General Fund. We have issued an opinion on these separate financial statements, stating that they fairly present the recorded cash transactions of these accounts for the year ended June 30, 2010.

We also issued a report on compliance with the Minnesota Department of Education's (MDE) *Manual for Activity Fund Accounting*, in which we reported the results of that testing as detailed in the Schedule of Findings and Corrective Action.

### **SIGNIFICANT ACCOUNTING POLICIES**

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the District are described in Note 1 of the notes to basic financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year.

We noted no transactions entered into by the District during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

### **ACCOUNTING ESTIMATES AND MANAGEMENT JUDGMENTS**

Accounting estimates are an integral part of the 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 financial statements and because of the possibility that future events affecting them may differ significantly from those expected.

The most sensitive estimates affecting the financial statements of the District include the following:

General education revenue and certain other revenues are computed by applying an allowance per student to the number of students served by the District. Student attendance is accumulated in a state-wide database—MARSS. Because of the complexity of student accounting and because of certain enrollment options, student information is input by other school districts and the MARSS data for fiscal year 2010 is not finalized until well into fiscal year 2011. General education revenue and certain other revenues are computed using preliminary information on the number of students served in the resident district and also utilizing some estimates, particularly in the area of enrollment options.

Special education state aid includes an adjustment related to tuition billings to and from other school districts for special education services which are computed using formulas derived by the MDE. Because of the timing of the calculations, this adjustment for fiscal 2010 is not finalized until after the District has closed its financial records for the fiscal period. The impact of this adjustment on the receivable and revenue recorded for state special education aid is calculated using preliminary information available to the District.

The District has recorded a liability for severance benefits payable for which it is probable employees will be compensated. The "vesting method" used by the District to calculate this liability is based on assumptions involving the probability of employees becoming eligible to receive the benefits (vesting), the potential use of accumulated sick leave prior to termination, and the age at which such employees are likely to retire.

The District has recorded activity for other post-employment benefits (OPEB). These obligations are calculated using actuarial methodologies described in Governmental Accounting Standards Board (GASB) Statement No. 45. These actuarial calculations include significant assumptions, including projected changes, healthcare insurance costs, investment returns, retirement ages, and employee turnover.

The depreciation of capital assets involves estimates pertaining to useful lives.

Management expects any differences between estimates and actual amounts of these estimates to be insignificant. We evaluated the key factors and assumptions used by management in the areas discussed above in determining that they are reasonable in relation to the financial statements taken as a whole.

#### **CORRECTED AND UNCORRECTED MISSTATEMENTS**

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Where applicable, management has corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management, when applicable, were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

#### **DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT**

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

#### **DISAGREEMENTS WITH MANAGEMENT**

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

#### **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 District's financial statements or a determination of the type of auditor's 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 retention as the District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

#### **MANAGEMENT REPRESENTATIONS**

We have requested certain representations from management that are included in the management representation letter dated November 10, 2010.

## FUNDING PUBLIC EDUCATION IN MINNESOTA

Due to its complexity, it would be impossible to fully explain the funding of public education in Minnesota within this report. The last section of this report, which contains a summary of legislative changes affecting school districts, gives an indication of how complicated the funding system is. The following section provides some state-wide funding and financial trend information.

### BASIC GENERAL EDUCATION REVENUE

The largest single funding source for Minnesota school districts is basic general education aid. Each year, the Legislature sets a basic formula allowance. Total basic general education revenue is calculated by multiplying the formula allowance by the number of pupil units for which a district is entitled to aid. Pupil units are calculated using a legislatively determined weighting system applied to average daily membership (ADM). Over the years, various modifications have been made to this calculation, including changes in weighting and special consideration for declining enrollment districts.

The table below presents a summary of the formula allowance for the past decade and as approved for the next fiscal year. We have adjusted the percentage change from year to year for non-comparable changes such as referendum reduction and aids that were previously separately funded and subsequently “rolled-in” or “rolled-out” to general education revenue.

Fiscal Year Ended June 30,	Formula Allowance	
	Amount	Percent Increase
2001	\$ 3,964	4.2 % (1)
2002	\$ 4,068	2.6 %
2003	\$ 4,601	2.6 % (1)
2004	\$ 4,601	– %
2005	\$ 4,601	– %
2006	\$ 4,783	4.0 %
2007	\$ 4,974	4.0 %
2008	\$ 5,074	2.0 %
2009	\$ 5,124	1.0 %
2010	\$ 5,124	– %
2011	\$ 5,124	– %

(1) Percentage adjusted to eliminate changes caused by referendum reduction and rolled-in (out) aids which does not affect total district revenue.

As noted in the table above, current legislation has frozen the basic formula allowance at the fiscal 2009 level for both fiscal 2010 and 2011. In general, the moderate increases in the formula allowance have forced districts to continually cut expenditure budgets or increase referendum revenue in order to maintain programs.

The table above does not reflect temporary funding changes such as the \$51 per pupil unit one-time additional general education aid school districts and charter schools received in 2008–2009, or the technology and operating capital aid received by school districts and charter schools in 2007–2008 (\$40 per pupil unit) and 2008–2009 (\$55 per pupil unit).

The table also does not reflect the one-time reduction to general education aid, totaling \$500 million, in fiscal 2010 that was offset dollar-for-dollar by federal fiscal stabilization funds.

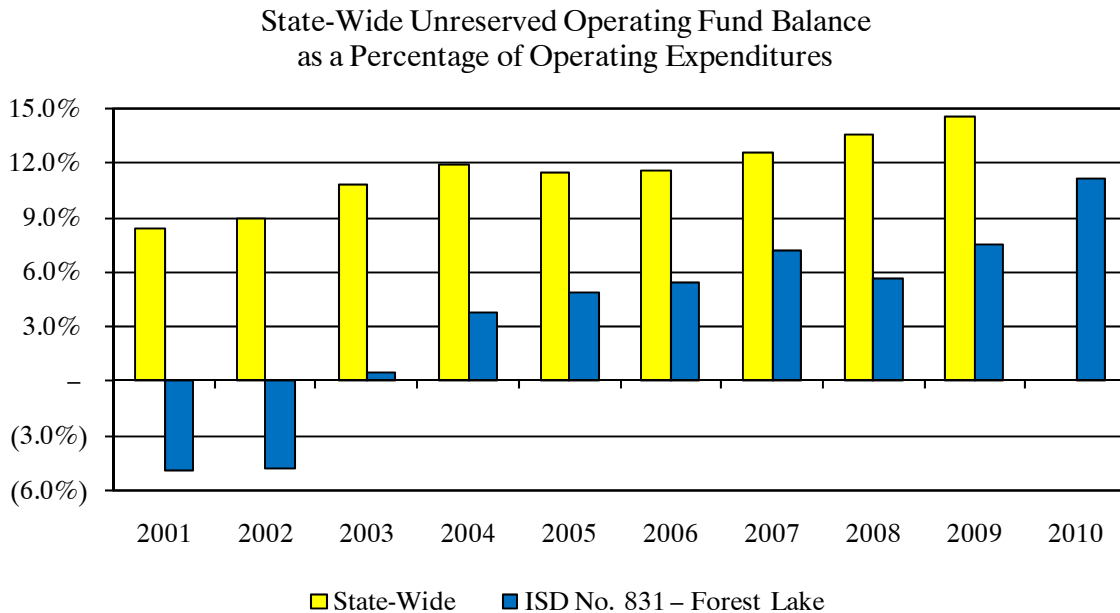
## STATE GENERAL FUND BUDGET OUTLOOK

The state of Minnesota has experienced a series of major budget shortfalls and a steadily deteriorating financial condition in recent years. Local governments and other entities dependant on the state for funding have, in turn, had to deal with the resulting state aid cuts, holdbacks, and unallotments. For the fiscal year 2010–2011 biennium, the adopted state budget was balanced using several large accounting “shifts,” one-time federal stabilization funds, and aid reductions. The accounting shifts, further explained in the Legislative Summary section of this report, include delaying state aid payments to school districts and charter schools, and accelerating the recognition of districts’ tax levy revenue with an offsetting reduction in state aid. Both of these types of shifts typically do not reduce district or charter school revenues but significantly reduce their cash flow, forcing an increasing number to use short-term borrowing for daily cash-flow needs. The state intends to pay these shifts back when it has the financial ability.

Current state budget projections for the fiscal year 2012–2013 biennium predict further significant shortfalls that will likely need to be addressed. Realistically, the state has already used up most of the accounting shifts available for this purpose, and additional federal assistance cannot be counted on. The upcoming election, which will result in a new Governor and potentially a number of new legislators, will have a substantial impact on how the state will address its budget predicament and the future direction of education funding. And, of course, the economy, while showing some signs of recovery, is unlikely to turn around quickly enough to solve the state’s budget issues in the short-term. All of this adds up to a period of continued financial uncertainty for Minnesota school districts and charter schools.

## STATE-WIDE SCHOOL DISTRICT FINANCIAL HEALTH

One of the most common and comparable statistics used to evaluate school district financial health is the unreserved operating fund balance as a percentage of operating expenditures.



Note: State-wide information is not available for fiscal 2010.

The calculation above reflects only the unreserved fund balance of the General Fund, and the corresponding expenditures, which is the same method which the state now uses for the calculation of statutory operating debt (SOD).

Even with limited funding increases, school districts have maintained a relatively stable unreserved fund balance on a state-wide basis in recent years. This stability may be the result of districts adapting to funding restrictions, effective cost containment measures, in some cases community support in the way of operating referendums, and other factors.

As of June 30, 2009, this ratio was 7.5 percent for the District, as compared to a state-wide average of 14.5 percent. The District's unreserved operating fund balance as a percentage of operating expenditures was 11.1 percent at the end of the current year.

The table below shows a comparison of total revenue per ADM received by Minnesota school districts and your district. Revenues for all governmental funds are included, except for the Capital Projects – Building Construction Fund; proceeds from sales of real property and equipment; insurance recoveries; and sales of bonds, loans, and interfund transfers.

<b>Revenue per Student (ADM) Served</b>								
	State-Wide		Seven-County Metro Area		ISD No. 831 – Forest Lake			
	2008	2009	2008	2009	2008	2009	2010	
General Fund								
Property taxes	\$ 1,160	\$ 1,318	\$ 1,527	\$ 1,833	\$ 1,415	\$ 1,560	\$ 1,537	
Other local sources	487	456	417	381	274	213	246	
State	7,833	7,943	8,029	7,920	7,228	7,305	6,417	
Federal	456	467	492	489	374	335	1,087	
Total General Fund	<u>9,936</u>	<u>10,184</u>	<u>10,465</u>	<u>10,623</u>	<u>9,291</u>	<u>9,413</u>	<u>9,287</u>	
Special revenue funds								
Food Service	433	449	434	453	526	537	548	
Community Service	474	490	570	613	575	599	582	
Debt Service Fund	993	994	1,114	1,131	706	619	568	
Total revenue	<u>\$ 11,836</u>	<u>\$ 12,117</u>	<u>\$ 12,583</u>	<u>\$ 12,820</u>	<u>\$ 11,098</u>	<u>\$ 11,168</u>	<u>\$ 10,985</u>	
ADM served and tuition paid					<u>7,113</u>	<u>6,998</u>	<u>6,785</u>	
Source of state-wide and seven-county metro area data: School District Profiles Report published by the MDE								

The mix of local and state revenues vary from year to year primarily based on funding formulas and the state's financial condition. The mix of revenue components from district to district varies due to factors such as the strength of property values, mix of property types, operating and bond referendums, enrollment trends, density of population, types of programs offered, and countless other criteria.

Total revenue per ADM served decreased by \$183, or 1.6 percent, to \$10,985, as presented in the table above. The decrease is due to the one-time funding districts received in prior years which is discussed elsewhere in this report. Also, the District did not participate in the alternative teacher compensation program in fiscal 2010, which reduced both revenues and related expenditures.

The table reflects the one-time reduction to general education aid (state sources of the General Fund) in fiscal 2010 that was offset dollar-for-dollar by federal fiscal stabilization funds.



The table below reflects comparative data available from the MDE for all expenditures, excluding the Capital Projects – Building Construction Fund:

<b>Expenditures per Student (ADM) Served</b>							
	State-Wide		Seven-County Metro Area		ISD No. 831 – Forest Lake		
	2008	2009	2008	2009	2008	2009	2010
General Fund							
Administration	\$ 412	\$ 463	\$ 405	\$ 440	\$ 417	\$ 516	\$ 448
District support services	399	424	412	436	315	279	249
Elementary and secondary							
regular instruction	4,528	5,090	4,730	5,411	4,058	4,539	4,280
Vocational education instruction	142	149	141	152	153	153	140
Special education instruction	1,703	1,794	1,904	2,002	1,357	1,381	1,398
Instructional support services	461	493	536	598	765	840	339
Pupil support services	835	868	914	968	1,092	1,208	1,090
Sites and buildings and other	811	840	778	824	907	1,144	1,063
Total General Fund expenditures (excluding capital)	9,291	10,121	9,820	10,831	9,064	10,060	9,007
General Fund capital expenditures	505	519	494	443	362	193	222
Special revenue funds							
Food Service	437	451	432	453	600	547	574
Community Service	470	505	564	634	544	594	583
Debt Service Fund	1,064	1,196	1,151	1,334	832	585	635
Total expenditures	<u>\$ 11,767</u>	<u>\$ 12,792</u>	<u>\$ 12,461</u>	<u>\$ 13,695</u>	<u>\$ 11,402</u>	<u>\$ 11,979</u>	<u>\$ 11,021</u>
ADM served and tuition paid					<u>7,113</u>	<u>6,998</u>	<u>6,785</u>
Source of state-wide and seven-county metro area data: School District Profiles Report published by the MDE							

Expenditure patterns also vary from district to district for various reasons. Factors affecting the comparison include the growth cycle or maturity of the District, average employee experience, availability of funding, population density, and even methods of allocating costs.

The differences from program to program reflect the District’s particular character, such as its community service programs, as well as the fluctuations from year to year for such things as capital expenditures.

Total expenditures per ADM served decreased by \$958, or 8.0 percent, to \$11,021, as presented in the table above. As the table reflects, the District experienced a decrease in nearly every General Fund expenditure program presented above. The considerable decrease in per ADM expenditures was largely due to the issuance of approximately \$6.5 million of OPEB bonds in the prior year that were placed into an irrevocable trust for OPEB benefit obligations of the District. Accounting standards required the receipt of these bond proceeds to be reported as an “other financing source,” while the payment to the Trust Fund be reflected as an expenditure in the fund statements. Expenditures for costs of the alternative compensation program were also down as discussed on the previous page.

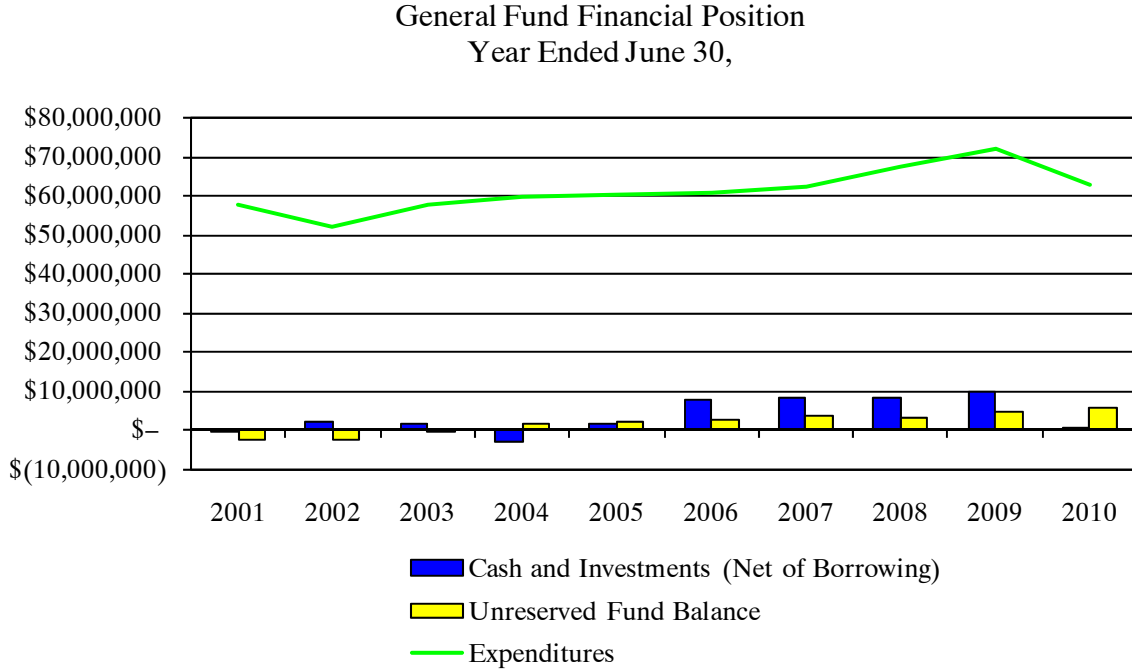
## SUMMARY

The funding for and financial position of Minnesota school districts has fluctuated significantly over the past several years due to a number of factors, including those discussed above. This situation has created a challenge for school boards, administrators, and management of these districts in providing the best education with the limited resources available in a climate of unknown future funding levels.

## FINANCIAL TRENDS OF YOUR DISTRICT

### GENERAL FUND FINANCIAL POSITION

The following graph displays the District's General Fund trends of financial position and changes in the volume of financial activity. Unreserved fund balance and cash balance are typically used as indicators of financial health or equity, while annual expenditures are often used to measure the size of the operation.



The District ended fiscal year 2010 with a General Fund cash balance (net of borrowing) of \$961,916 and an unreserved fund balance of \$5,818,084.

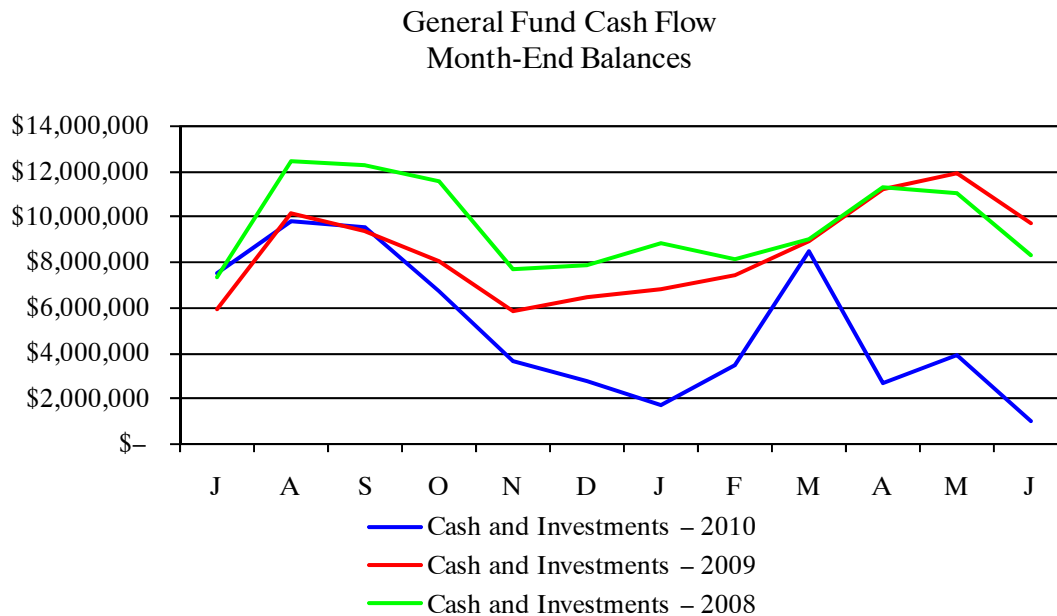
The following table presents the components of the General Fund balance for the past five years:

	June 30,				
	2006	2007	2008	2009	2010
Reserved fund balances	\$3,158,103	\$2,645,478	\$2,123,001	\$ 981,890	\$ 150,927
Unreserved fund balances	2,842,336	3,674,218	3,234,676	4,596,302	5,818,084
<b>Total fund balances</b>	<b>\$6,000,439</b>	<b>\$6,319,696</b>	<b>\$5,357,677</b>	<b>\$5,578,192</b>	<b>\$5,969,011</b>
Unreserved fund balances as a percentage of total expenditures	4.7%	5.9%	4.8%	6.4%	9.3%

The table above reflects the total General Fund unreserved fund balance and percentages, which are different from those used in the previous discussion of state-wide fund balances, based on a different formula. The resources represented by this fund balance are critical to a district's ability to maintain adequate cash flow throughout the year, to retain its programs, and to cushion against the impact of unexpected costs or funding shortfalls.

## GENERAL FUND CASH FLOW

The level of cash and investments varies considerably during the year due to the timing of various revenues and expenditures. The following graph summarizes the level of cash and investments over the past three years:

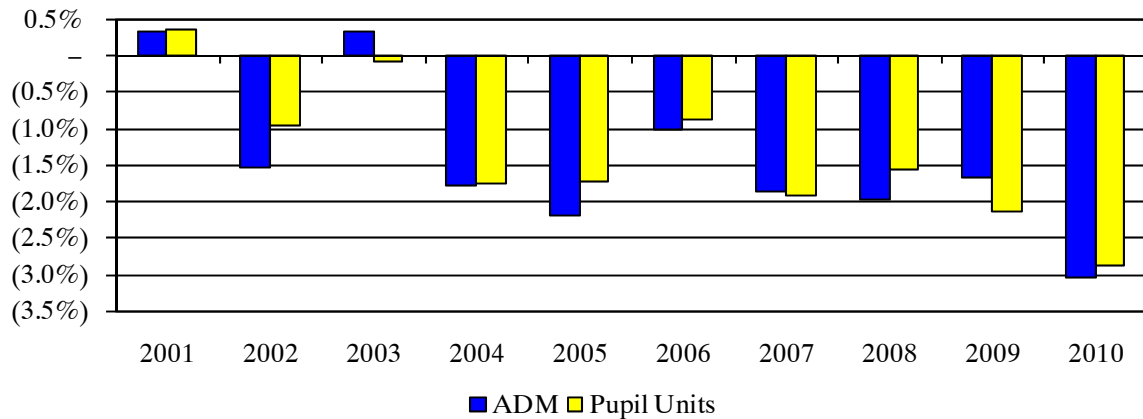


The graph above shows the peaks and valleys of the General Fund cash and investments balance (net of borrowing) on a monthly basis. The swing between its high and low month-end cash balances is about \$8.8 million.

Changes in funding structure and state aid payment schedules significantly affect the cash flow of Minnesota school districts. As further described in the Legislative Summary section of this report, state aids normally paid on a 90–10 schedule were changed to a 73–27 schedule for fiscal year 2009–2010 and will be 70–30 for fiscal year 2010–2011. Beginning in fiscal year 2010–2011, a further delay in aid payments will occur with a change in the recognition of property tax revenue.

**AVERAGE DAILY MEMBERSHIP AND PUPIL UNITS**

Change in ADM and Pupil Units



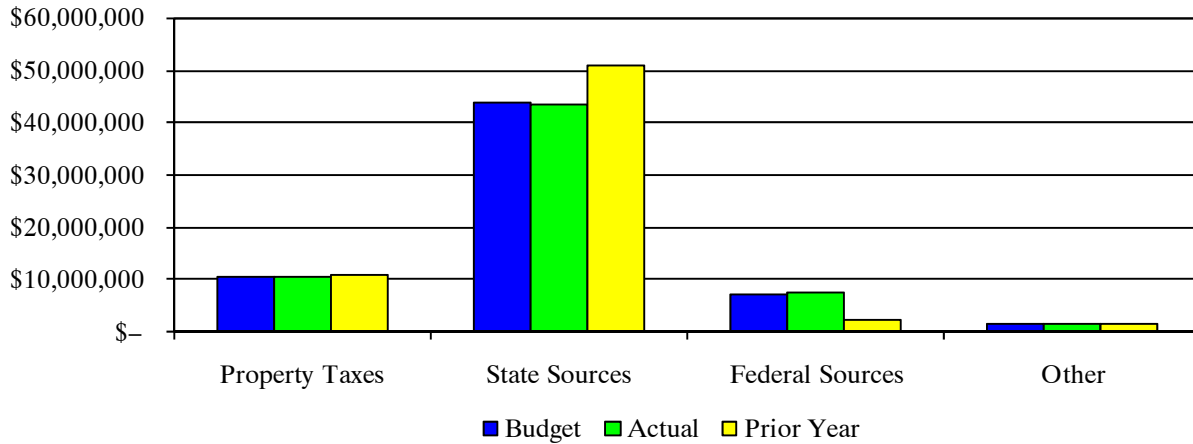
ADM is a measure of students attending class, which is then converted to pupil units (the base for determining revenue) using a statutory formula. Not only is the original budget based on ADM estimates, the final audited financial statements are based on updated, but still estimated, ADM since the counts are not finalized until around January of the following year. When viewing revenue budget variances, one needs to consider these ADM changes, the impact of the prior year final adjustments which affect this year’s revenue, and also the final adjustments caused by open enrollment gains and losses.

The ADM served by the District for 2010 is estimated to be 6,785, a decrease of about 213 ADM, or about 3 percent, from the prior year. The ADM served and resulting pupil units for the past 10 years, corresponding to the graph above, are presented as supplemental information within the District’s financial report.

## GENERAL FUND REVENUE AND EXPENDITURES

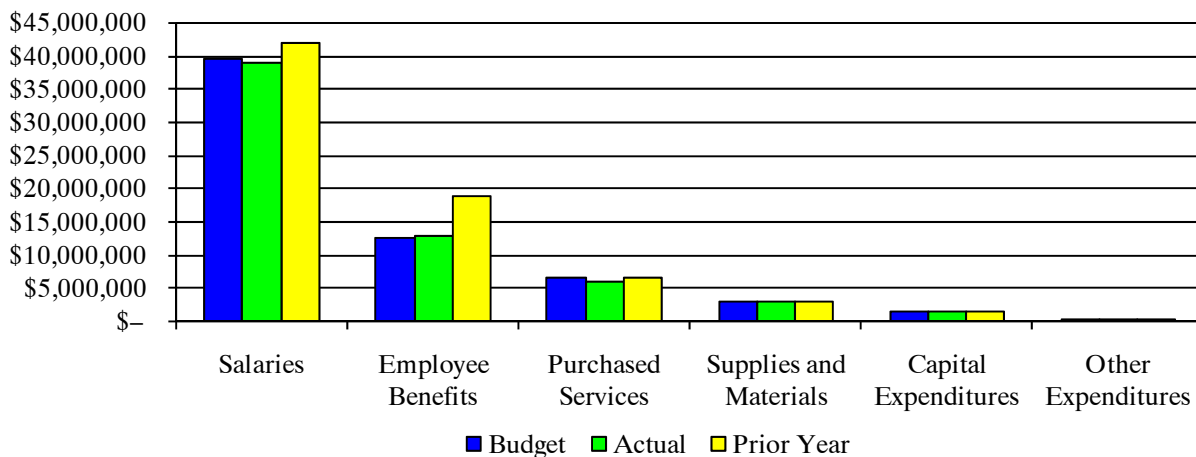
The following graphs summarize the District's General Fund revenues and expenditures for 2010:

### General Fund Revenue



For 2010, revenues of \$63,013,537 were over budget by \$355,717, or 0.6 percent, and were \$2,856,624 less than the prior year. The decrease from the prior year was due to the decline in enrollment as reflected on the previous graph, the elimination of the one-time funding districts received in prior years, and for alternative compensation revenue received in the prior year, as previously discussed. The revenue variance was spread across all sources. Favorable variances in federal and other local sources were partially offset by variances in investment earnings and state sources that were below anticipated levels.

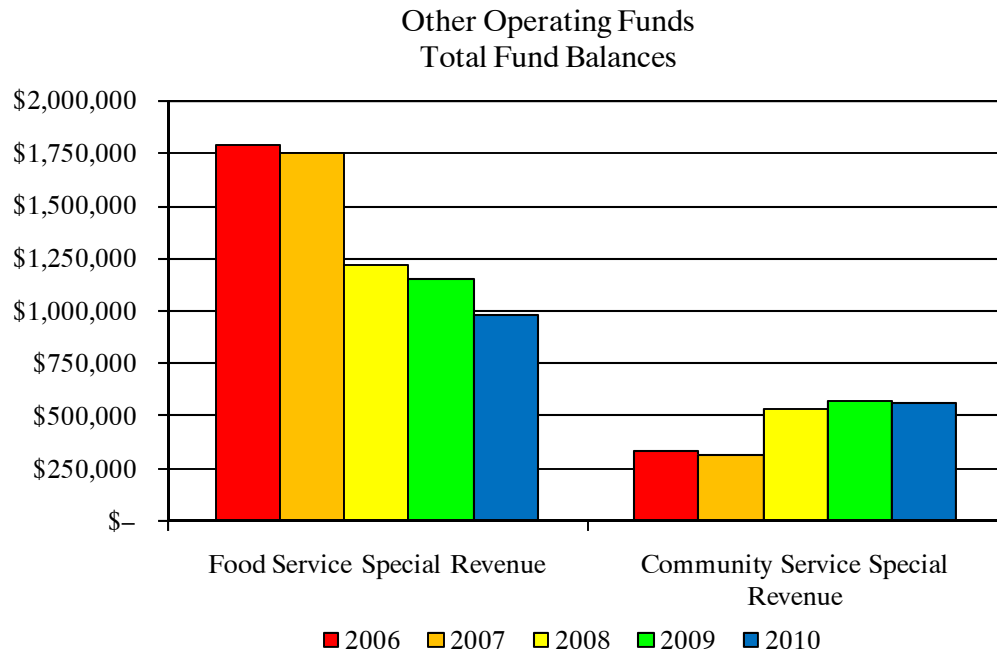
### General Fund Expenditures



In 2010, expenditures of \$62,622,718 were \$535,102, or 0.9 percent, under budget and were \$9,118,737 less than the prior year. The decrease from the prior year was primarily due to OPEB contributions made to the irrevocable OPEB trust as discussed earlier. Prior year OPEB contributions were reported as employee benefit expenditures in accordance with Uniform Financial Accounting and Reporting Standards. Salary costs were down from the prior with the District no longer participating in the alternative compensation program. As presented in the graph above, expenditures were less than projected in nearly every category and spread across several programs.

## OTHER FUNDS OF THE DISTRICT

The following graph shows what is referred to as the other operating funds. The remaining non-operating funds are only included in narrative form below, since their level of fund balance can fluctuate significantly due to such things as issuing and spending the proceeds of refunding or building bonds and, therefore, the trend of fund balance levels are not necessarily a key indicator of financial health. It does not mean that these funds cannot experience financial trouble or that their fund balances are unimportant.



### Food Service Special Revenue Fund

The District's Food Service Special Revenue Fund experienced a decrease in fund balance of \$172,265 in 2010, compared to a budgeted increase of \$46,861. Revenues were \$74,655 under budget. Regular meals sales were down from the prior year offset with an increase in federal sources. Expenditures were over budget \$144,471 with the largest variance occurring in personnel expenditures. The Food Service Special Revenue Fund had a year-end fund balance of \$981,987, representing 25.2 percent of annual expenditures totaling \$3,893,521.

This operation has maintained a healthy fund balance for several years and has also been able to assist in funding a portion of several capital improvements to food service facilities in recent years. The District should review upcoming capital needs of the child nutrition operation and incorporate that information in establishing an optimal level of fund balance that is also within state and federal fund balance limits.

### Community Service Special Revenue Fund

The District's Community Service Special Revenue Fund experienced a fund balance decrease of \$7,927 in 2010, compared to a budgeted decrease of \$110,552. Revenues were \$111,037 over budget, as property taxes and tuition were higher than expected. Expenditures also surpassed projected levels, ending \$8,412 over budget. The Community Service Special Revenue Fund had a year-end fund balance of \$559,886, representing 14.2 percent of annual expenditures totaling \$3,956,491.

The Community Service Special Revenue Fund, like the Food Service Special Revenue Fund, needs to be self-sustaining. In addition to cost controls, financial analysis of the costs of providing programs, including overhead, is important. Fees and tuition charges should be sufficient to cover these costs as well as potential funding shortfalls from state, federal, or property tax sources.

## Debt Service Fund

The funding of debt service is controlled in accordance with each outstanding debt issue's financing plan. It is important to remember that resources of the Debt Service Fund are dedicated to payment of outstanding debt obligations of the District.

## Post-Employment Benefits Trust Fund

The Post-Employment Benefits Trust Fund is considered a fiduciary fund, where assets are held in trust to finance OPEB payable to former employees of the District.

## GOVERNMENT-WIDE FINANCIAL STATEMENTS

The District's financial statements include fund-based information that focuses on budgetary compliance, and the sufficiency of the District's current assets to finance its current liabilities. The GASB Statement No. 34 reporting model also requires the inclusion of two government-wide financial statements designed to present a clear picture of the District as a single, unified entity. These government-wide statements provide information on the total cost of delivering educational services, including capital assets and long-term liabilities.

Theoretically, net assets represent the resources the District has leftover to use for providing services after its debts are settled. However, those resources are not always in expendable form, or there may be restrictions on how some of those resources can be used. Therefore, the statement divides the net assets into three components: net assets invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets. The following table presents a summarized conversion of the District's governmental fund balances (as discussed earlier) to net assets and the separate components for the last three years:

	June 30,		
	2008	2009	2010
Net assets – governmental activities			
Total fund balances – governmental funds	\$ 8,246,024	\$ 9,052,433	\$ 8,806,673
Negative net OPEB obligation	–	5,443,682	5,040,521
Total capital assets, net of depreciation	54,539,109	52,663,362	50,860,841
Total long-term debt	(43,351,035)	(43,834,330)	(40,707,970)
Other adjustments	(3,058,747)	(2,790,197)	(2,412,765)
Total net assets – governmental activities	<u>\$ 16,375,351</u>	<u>\$ 20,534,950</u>	<u>\$ 21,587,300</u>
Net assets			
Invested in capital assets, net of related debt	\$ 17,827,581	\$ 18,575,722	\$ 19,466,942
Restricted	3,234,695	3,800,266	2,382,628
Unrestricted	<u>(4,686,925)</u>	<u>(1,841,038)</u>	<u>(262,270)</u>
Total net assets	<u>\$ 16,375,351</u>	<u>\$ 20,534,950</u>	<u>\$ 21,587,300</u>

Some of the District's fund balances translate into restricted net assets by virtue of external restrictions (statutory reserves) or by the nature of the fund they are in (e.g. unreserved Food Service Special Revenue Fund balance can only be spent for food service program costs). The unrestricted net assets category consists mainly of the General Fund unreserved fund balances, offset against non-capital long-term obligations such as vacation or severance payable. Consequently, many Minnesota school districts have accumulated deficits in this component of net assets.

Total net assets increased by \$1,052,350 during fiscal 2010. This is partially due to the relationship between the rate of depreciation on capital assets and the repayment rate of related debt, as well as the general operating results of the District as a whole.

## **ACCOUNTING AND AUDITING UPDATES**

### **GASB STATEMENT NO. 54 – FUND BALANCE REPORTING AND GOVERNMENTAL FUND TYPE DEFINITIONS**

The objective of this statement is to enhance the usefulness of fund balance information by providing clearer fund balance classifications that can be more consistently applied and by clarifying the existing governmental fund type definitions. This statement establishes fund balance classifications (nonspendable, restricted, committed, assigned, and unassigned) that comprise a hierarchy based primarily on the extent to which a government is bound to observe constraints imposed upon the use of the resources reported in governmental funds. The definitions of the General Fund, special revenue, capital projects, debt service, and permanent fund types are clarified by the provisions in this statement. Elimination of the reserved component of fund balance in favor of a restricted classification will enhance the consistency between information reported in the government-wide statements and information in the governmental fund financial statements and avoid confusion about the relationship between reserved fund balance and restricted net assets. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2010.

### **GASB STATEMENT NO. 59 – FINANCIAL INSTRUMENTS OMNIBUS**

The objective of this statement is to update and improve existing standards regarding financial reporting and disclosure requirements of certain financial instruments and external investment pools for which significant issues have been identified in practice. The requirements of this statement will improve financial reporting by providing more complete information, by improving consistency of measurements, and by providing clarifications of existing standards. Applying the reporting provisions of Statement No. 31 for interest-earning investment contracts to unallocated insurance contracts improves consistency of investment measurements that are reported by pension and OPEB plans. Emphasizing the applicability of SEC requirements to 2a7-like external investment pools provides practitioners with improved guidance. Limiting interest rate risk disclosures for investments in mutual funds, external investment pools, and other pooled investments to debt investment pools provides better guidance regarding the applicability of interest rate risk disclosures. Finally, addressing the applicability of Statement No. 53 to certain financial instruments refines which financial instruments are within the scope of that statement. The requirements of this statement are effective for financial statements for periods beginning after June 15, 2010.



## LEGISLATIVE SUMMARY

The following is a brief summary of recent legislative changes and issues affecting the funding of Minnesota school districts. More detailed and extensive summaries are available from the MDE.

**Basic General Education Revenue** – The basic general education formula allowance for fiscal year (FY) 2010 and FY 2011 is \$5,124, reflecting no increase from the FY 2009 level.

**FY 2010 One-Time General Education Aid Reduction Offset by Federal Fiscal Stabilization Funds** – Reduced the FY 2010 general education aid entitlement by \$500 million. The reduction is allocated among school districts and charter schools. This one-time reduction is offset on a dollar-for-dollar basis by federal fiscal stabilization funds.

**Temporary Suspension of Reserved Revenue for Staff Development** – Temporarily suspends the staff development reserve for FY 2010 and FY 2011. The staff development reserve is equal to 2 percent of the district's basic general education revenue.

**Federal Recovery Act** – The American Recovery and Reinvestment Act (ARRA) of 2009 provided additional federal funds to districts in the form of stabilization funds and additional grants. The ARRA mandates that there be an unprecedented level of oversight and transparency around the spending of these funds, including added audit and internal control requirements. In addition to increased accountability, districts have new reporting requirements for ARRA funds.

**Alternative Teacher Compensation Revenue (Q Comp)** – Clarification of change made reducing the basic Q Comp aid from 73.1 percent to 65 percent effective for FY 2010 and later. This results in a decrease in the basic aid, with a corresponding increase in the equalized levy revenue.

**Operating Capital Reserve Account Transfers** – Allowed districts to transfer up to \$51 per adjusted marginal cost pupil unit (AMCPU) from the operating capital reserved fund balance to its unreserved General Fund balance for FY 2010.

**Repeal of the Endowment Fund Reduction** – Beginning in FY 2010, districts no longer receive a reduction in their general education aid by the amount of endowment payments received. This increased revenue by about \$28 per resident ADM for FY 2010 (based on ADM for FY 2009).

**State Aid Payment Deferral** – All state aids normally paid on a 90–10 schedule is changed to a 73–27 schedule for FY 2010 and 70–30 for FY 2011. The 90–10 schedule is reinstated for FY 2012.

**Final Payment for Districts in SOD** – Districts in SOD as of June 30th of the previous year can receive an early final payment on June 20th to bring total general education aid up to 90 percent, but not exceeding the SOD amount.

**Additional State Aid Payment Delays** – Before the state needs to enter into short-term borrowing, it has the option to make additional payment delays to districts with General Fund balances of \$700 or more per resident pupil unit.

**Property Tax Revenue Recognition Change (Tax Shift)** – Beginning in FY 2011, 48.6 percent of property taxes levied for the next school year will be recognized as revenue in the current year, and state aids will be reduced by that same amount. This will be repaid (decreased) when the state attains certain specific financial goals, and the aid payment schedule is restored to 90–10.

**Safe Schools Levy** – Districts are required to set aside \$3 per AMCPU for specific costs and annual certifications on spending are required beginning in FY 2010.

**Safe Schools Levy – Maintenance of Effort (MOE)** – Beginning in FY 2010, districts are required to maintain effort at FY 2009 levels for licensed school support staff, including guidance counselors, nurses, social workers, and others from all funding sources other than the safe schools levy. This also modifies existing law requiring MOE to be calculated in terms of total spending. This provision adds a second option allowing districts to meet the MOE requirement in terms of number of full-time equivalent staff instead.

**Telecommunications/Internet Access Equity Aid** – Clarifies that intermediate school districts are eligible to receive telecommunications/internet access equity aid. Appropriates \$3.75 million for equity in telecommunications access aid for FY 2010 and for FY 2011 (versus \$8.7 million in FY 2009).

**Other Post-Employment Benefit (OPEB) Bonding and Levies** – New legislation approved in 2009 impacted existing legislation regarding OPEB in the following ways:

- Clarifies that districts may only levy for costs of employees who retired between July 1, 1992 and July 1, 1998, if the district has a sunset clause in their current bargaining agreement.
- Creates a new levy for districts to fund annual costs associated with OPEB expenses conditional on certain requirements, including a sunset clause in effect. Limits the total amount of this new levy to not more than \$9.242 million for taxes payable in 2010, \$29.863 million for taxes payable in 2011, and an amount equal to the previous year's levy plus \$14 million for taxes payable in 2012 and later.
- Required voter approval for any bonds to pay OPEB issued after October 1, 2009.

**Accounting for Separation and Retirement Benefits** – Clarifies accounting requirements for reserved and designated for separation and retirement benefits with the following:

- Designated for separation and retirement benefit account includes compensated absences, termination benefits, pension benefits, and OPEB not accounted for elsewhere.
- Designated account will no longer be limited to 50 percent of the amount necessary to meet obligations for the portion of severance pay that constitutes compensation for accumulated sick leave.
- MDE eliminated the reserve for severance account beginning with FY 2010 reporting.

**PERA and TRA Rates** – Contribution rates for employers and employees of the PERA Coordinated Plan increase by 0.25 percent effective January 1, 2011. Contribution rates for employers and employees for both the TRA Basic and Coordinated Plans increase by 0.5 percent each year through FY 2015. There is no additional aid to help fund these increases.

**Minnesota Department of Education Budget** – The MDE budget has been reduced by 3.8 percent for FY 2010 and 5.4 percent for FY 2011.