

INDEPENDENT SCHOOL DISTRICT NO. 22
Detroit Lakes, Minnesota

COMMUNICATIONS LETTER

Year Ended June 30, 2014

INDEPENDENT SCHOOL DISTRICT NO. 22

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**REPORT ON MATTERS IDENTIFIED AS A RESULT OF
THE AUDIT OF THE FINANCIAL STATEMENTS**

To the School Board and Management
Independent School District No. 22
Detroit Lakes, Minnesota

In planning and performing our audit of the financial statements of Independent School District No. 22, Detroit Lakes, Minnesota, as of and for the year ended June 30, 2014, in accordance with auditing standards generally accepted in the United States of America, we considered the District's internal control over financial reporting (internal control) as a basis for designing our auditing procedures that are appropriate in the circumstances for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

Our consideration of internal control was for the limited purpose described in the preceding paragraph and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies and, therefore, material weaknesses or significant deficiencies may exist that were not identified.

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 a combination of deficiencies in internal control, such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented or detected and corrected, on a timely basis. We did not identify any deficiencies in internal control that we consider to be material weaknesses.

A significant deficiency is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance. The significant deficiency identified is stated within this letter.

The accompanying memorandum also includes financial analysis provided as a basis for discussion. The matters discussed herein were considered by us during our audit and they do not modify the opinion expressed in our Independent Auditor's Report dated October 28, 2014, on such statements.



This communication is intended solely for the information and use of management, the School Board and others within the District and state oversight agencies is not intended to be and should not be used by anyone other than these specified parties.

Kern, DeWenter, Viere, Ltd.

KERN, DEWENTER, VIERE, LTD.

St. Cloud, Minnesota

October 28, 2014

INDEPENDENT SCHOOL DISTRICT NO. 22

SIGNIFICANT DEFICIENCY June 30, 2014

LACK OF SEGREGATION OF ACCOUNTING DUTIES

The District has a lack of segregation of accounting duties due to a limited number of office employees. The lack of adequate segregation of accounting duties could adversely affect the District's ability to initiate, record, process and report financial data consistent with the assertions of management in the financial statements.

Management is aware of this condition and has taken certain steps to compensate for the lack of segregation but due to the number staff needed to properly segregate all of the accounting duties, the cost of obtaining desirable segregation of accounting duties can often exceed benefits which could be derived. Due to this reason, management has determined a complete segregation of accounting duties is impractical to correct. However, management and the School Board must remain aware of this situation and should continually monitor the accounting system, including changes that occur.

This lack of segregation of accounting duties can be demonstrated in the following areas, which is not intended to be an all-inclusive list:

- The Fiscal Affairs Coordinator has access to enter invoices into the system, processes checks and has access to the digital signatures.
- The Fiscal Affairs Coordinator is able to receipt money, code receipts, enter receipts into the accounting system, prepare bank deposits, bring deposits to the bank and reconcile accounts receivable.
- The Fiscal Affairs Coordinator prepares and posts all journal entries.
- The Fiscal Affairs Coordinator prepares federal funding draw requests, submits the request and receipts the funds.
- Building secretaries responsible for collecting money also prepare deposits. There is also no independent review of receipt backup documentation by someone other than the building secretaries to ensure all money collected was deposited.
- The Payroll Coordinator is able to enter new employees and all related information.

We recommend management and the School Board remain aware of this situation and continually monitor the accounting system including changes that occur. We further recommend that management review process to determine if any systems could be automated or done in an electronic fashion to eliminate redundancies in processes.

INDEPENDENT SCHOOL DISTRICT NO. 22

REQUIRED COMMUNICATION June 30, 2014

We have audited the financial statements of Independent School District No. 22, Detroit Lakes, Minnesota for the year ended June 30, 2014, and have issued our report dated October 28, 2014. Professional standards require that we provide you with the following information related to our audit.

OUR RESPONSIBILITY UNDER AUDITING STANDARDS GENERALLY ACCEPTED IN THE UNITED STATES OF AMERICA, GOVERNMENT AUDITING STANDARDS AND OMB CIRCULAR A-133

As stated in our engagement letter, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing an opinion on the financial statements and not to provide assurance on the internal control over financial reporting. We also considered 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 U.S. Office of Management and Budget (OMB) *Circular A-133*.

As part of obtaining reasonable assurance about whether the District's 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 financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit. Also in accordance with OMB *Circular A-133*, we examined, on a test basis, evidence about the District's compliance with the types of compliance requirements described in the OMB *Circular A-133* Compliance Supplement applicable to each of its major federal programs for the purpose of expressing an opinion on the District's compliance with those requirements. While our audit provided a reasonable basis for our opinion, it did not provide a legal determination on the District's compliance with those requirements.

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

INDEPENDENT SCHOOL DISTRICT NO. 22

REQUIRED COMMUNICATION

June 30, 2014

PLANNED SCOPE AND TIMING OF THE AUDIT

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

Our audit included obtaining an understanding of the District and its environment, including internal control, sufficient to assess the risks of material misstatement of the 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.

QUALITATIVE ASPECTS OF ACCOUNTING PRACTICES

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 to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year ended June 30, 2014. 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 proper period.

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 were:

Depreciation – The District is currently depreciating its capital assets over their estimated useful lives, as determined by management, using the straight-line method.

Expenditure Allocation – Certain expenditures are allocated to functions based on an estimate of the benefit to that particular function. Examples include salaries, benefits, insurance and supplies.

General Education and Special Education Aid – General Education Aid is an estimate until average daily membership (ADM) values are final. Since this is normally not done until after the reporting deadline, this Aid is an estimate. Special Education Aid is also dependent upon ADM value; however, in addition to those, this Aid is dependent on the availability of funds and complex formulas that are finalized after reporting deadlines.

Net Other Post Employment Benefits (OPEB) Obligation – This obligation is based on an actuarial study using estimates of future obligations of the District for post employment benefits.

The financial statement disclosures are neutral, consistent and clear.

DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT

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

INDEPENDENT SCHOOL DISTRICT NO. 22

REQUIRED COMMUNICATION

June 30, 2014

CORRECTED AND UNCORRECTED MISSTATEMENTS

Professional standards require us to accumulate all misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. We identified the following uncorrected misstatement of the financial statements. Management has determined its effect is immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

- Property tax receivable is understated
- State Aids are understated

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 financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

MANAGEMENT REPRESENTATIONS

We 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 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.

INDEPENDENT SCHOOL DISTRICT NO. 22

REQUIRED COMMUNICATION

June 30, 2014

OTHER MATTERS

With respect to the supplementary information accompanying the financial statements, 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 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 financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

INDEPENDENT SCHOOL DISTRICT NO. 22

FINANCIAL ANALYSIS June 30, 2014

The following pages provide graphic representation of select data pertaining to the financial position and operations of the District for the past seven years. Our analysis of each graph is presented to provide a basis for discussion of past performance and how implementing certain changes may enhance future performance. We suggest you view each graph and document if our analysis is consistent with yours. A subsequent discussion of this information should be useful for planning purposes.

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

AVERAGE DAILY MEMBERSHIP AND PUPIL UNITS

The largest single funding source for Minnesota school districts is basic General Education Aid. Each year, the State 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 ADM. Over the years, various modifications have been made to this calculation, including changes in weighting and special consideration for declining enrollment districts.

Year	General Education Aid Formula Allowance	
	Amount	Percent Increase
2004	\$ 4,601	0.0%
2005	4,601	0.0%
2006	4,782	4.0%
2007	4,974	4.0%
2008	5,074	2.0%
2009	5,124	1.0%
2010	5,124	0.0%
2011	5,124	0.0%
2012	5,174	1.0%
2013	5,224	1.0%
2014	5,302	1.5%
2015*	5,831	1.9%

* General Education Aid - Of the \$ 529 increase over 2014, \$ 105 is for inflation at 1.9%; the remaining \$ 424 is a shifting of revenue to adjust for pupil weight changes, pension adjustments changes and other restructuring.

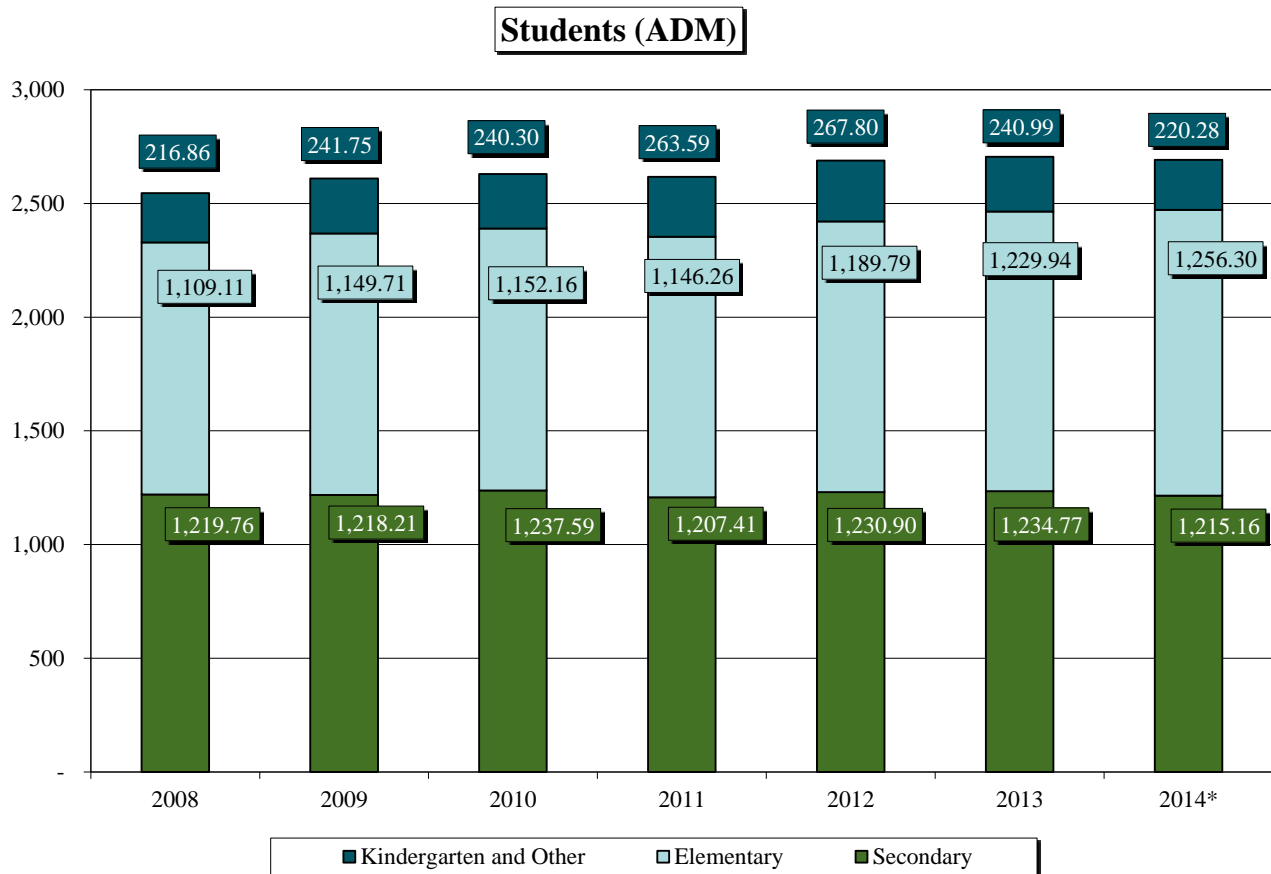
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FINANCIAL ANALYSIS June 30, 2014

AVERAGE DAILY MEMBERSHIP AND PUPIL UNITS

The following information summarizes resident ADM of the District over the past seven years ended June 30:

ADM	2008	2009	2010	2011	2012	2013	2014*
Other	76.97	86.48	81.86	95.83	106.62	91.18	85.87
Kindergarten	139.89	155.27	158.44	167.76	161.18	149.81	134.41
Elementary	1,109.11	1,149.71	1,152.16	1,146.26	1,189.79	1,229.94	1,256.30
Secondary	1,219.76	1,218.21	1,237.59	1,207.41	1,230.90	1,234.77	1,215.16
Total Resident ADM	2,545.73	2,609.67	2,630.05	2,617.26	2,688.49	2,705.70	2,691.74



* The resident ADM for 2014 are estimated.

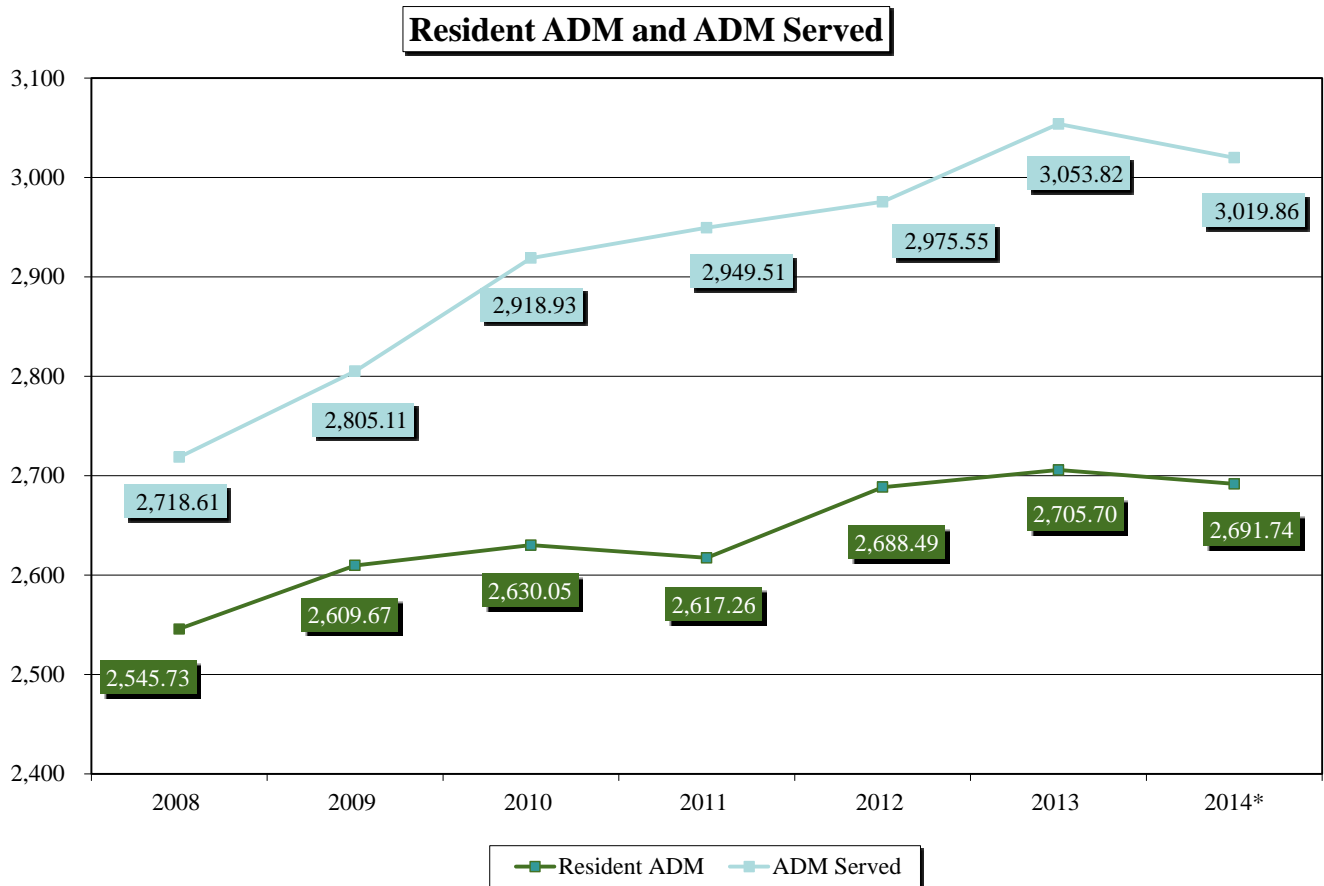
As the above chart indicates, total resident ADM has fluctuated over the last seven years, increasing from 2008 to 2010, then decreasing in 2011, increasing in 2012 and 2013 and decreasing in 2014. ADM decreased by 13.96 pupil units from 2013 to 2014. As the chart above indicates, this decrease came mostly in the kindergarten and other and secondary levels. Over the past seven years shown, the District has experienced an increase of 146.01 resident students, or 5.7%.

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**FINANCIAL ANALYSIS
June 30, 2014**

AVERAGE DAILY MEMBERSHIP AND STUDENTS SERVED

The next graph illustrates the comparison between resident ADM versus the ADM served over the last seven years.



* The resident ADM for 2014 are estimated.

As the graph above shows, total ADM served declined from 2013 to 2014, which is the first decrease in the seven years presented. The decline is due to decreases in resident students and fewer students open enrolling from other school districts. The ADM amounts are weighted based on the number of students in each grade level and are used to calculate the majority of the District education aids. The following table displays that weighting.

Pupil Units Weighting					
	Pre-Kindergarten and Handicapped		Kindergarten	Elementary	Secondary
2008-2014	1.250/1.000	0.612	1.115/1.060	1.300	

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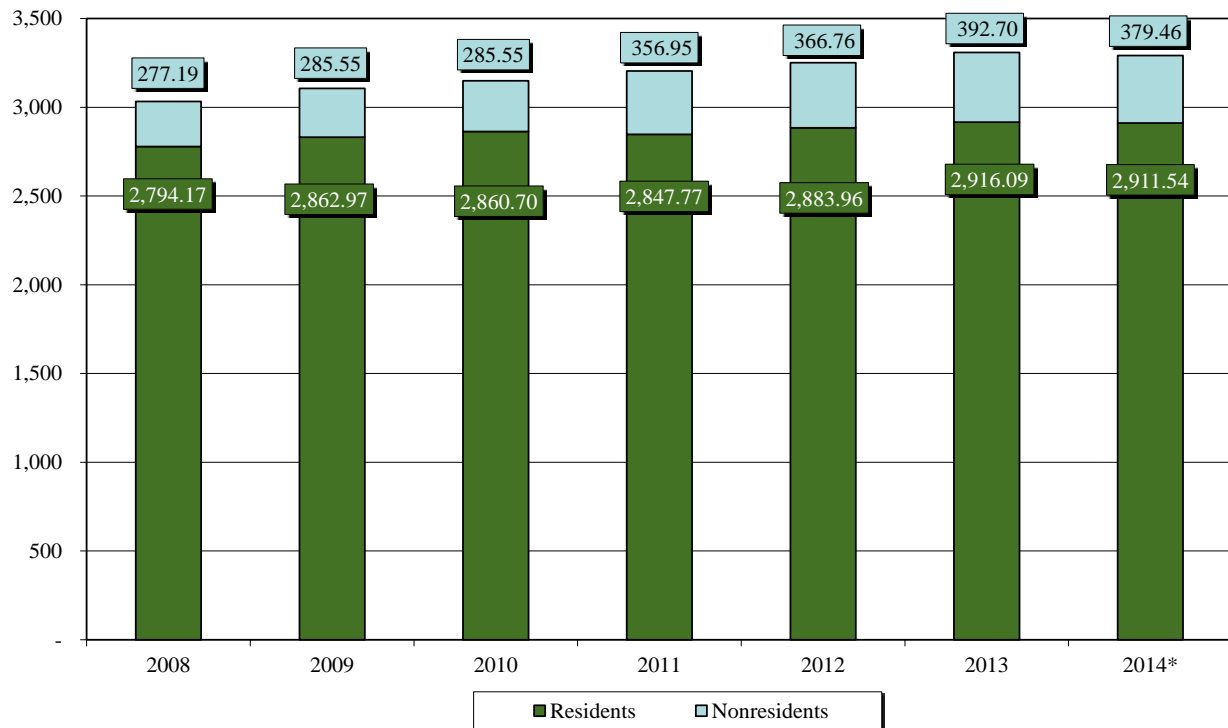
FINANCIAL ANALYSIS June 30, 2014

AVERAGE DAILY MEMBERSHIP AND PUPIL UNITS

After the weighting is applied to resident ADM, the open enrollment adjustment is also considered. The following table and graph illustrates total weighted/adjusted average daily membership (WADM) served for fiscal years 2008 through 2014.

WADM	2008	2009	2010	2011	2012	2013	2014*
Residents	2,962.51	3,024.04	3,051.29	3,025.97	3,111.89	3,137.30	3,124.96
Resident WADM Going Elsewhere	(168.34)	(161.07)	(190.59)	(178.20)	(227.93)	(221.21)	(213.42)
Nonresident WADM Coming In	277.19	285.55	346.19	356.95	366.76	392.70	379.46
Total WADM Served	3,071.36	3,148.52	3,206.89	3,204.72	3,250.72	3,308.79	3,291.00

Students Served



* The resident WADM served for 2014 are estimated.

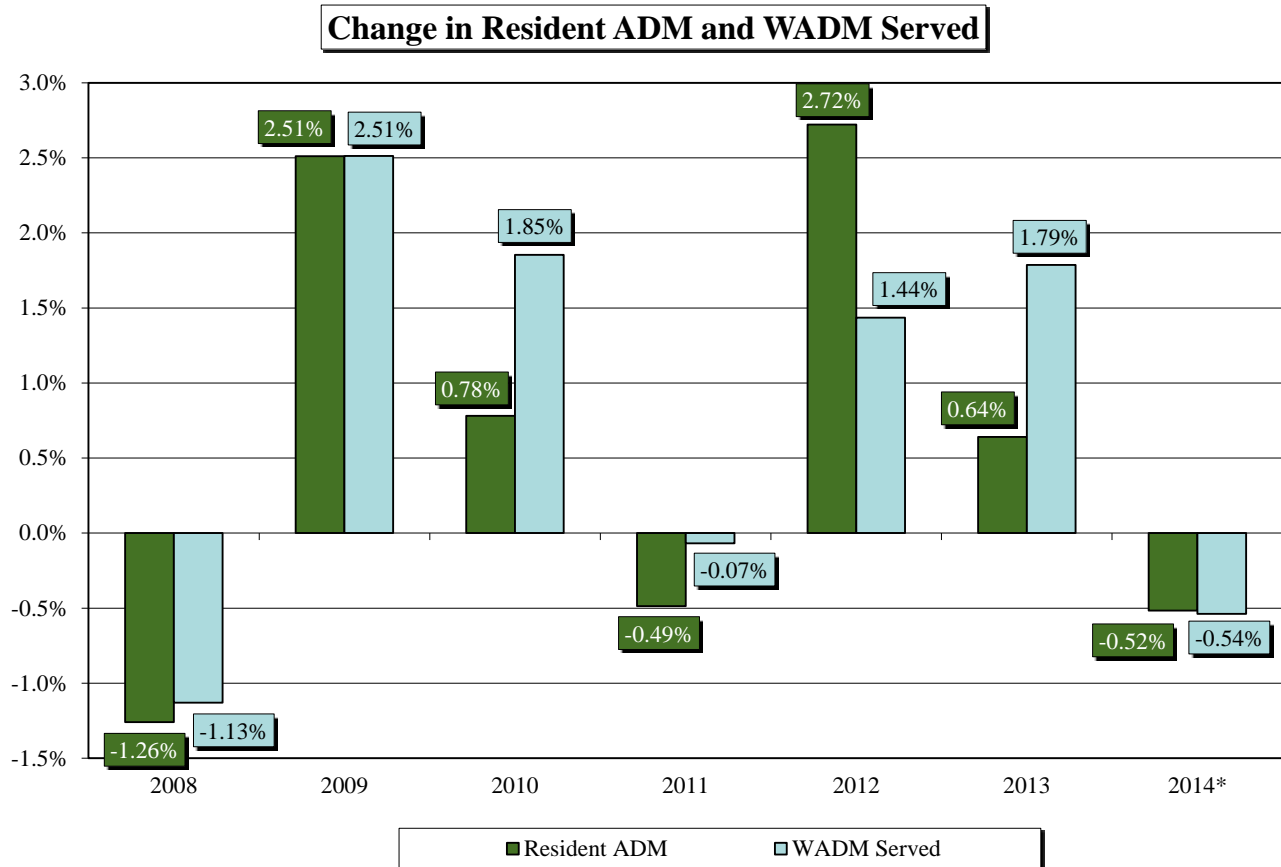
Comparing 2013 and 2014, total WADM served decreased by 17.79, or 0.5%. Resident students decreased by 0.4%, while the net gain from open enrollment decreased 3.2% as a result of fewer students from other districts enrolling with the District, coupled with a decrease in resident students going to other school districts. The District continues to benefit from open enrollment. Net gains in open enrollment totaled 166.04 in 2014, a decrease from 171.49 in 2013. This amount also includes students attending the Detroit Lakes Area Learning Center.

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FINANCIAL ANALYSIS June 30, 2014

AVERAGE DAILY MEMBERSHIP AND PUPIL UNITS

The following graph illustrates the percent change in resident ADM and WADM served over the past seven years.



* The resident WADM served for 2014 are estimated.

During 2014, ADM and WADM decreased slightly. Open enrollment has helped offset the overall relatively consistent resident enrollment numbers. The net gain from open enrollment has increased from 108.85 in 2008 to 166.04 in 2014. Student enrollment in the District is projected to continue to increase through 2017.

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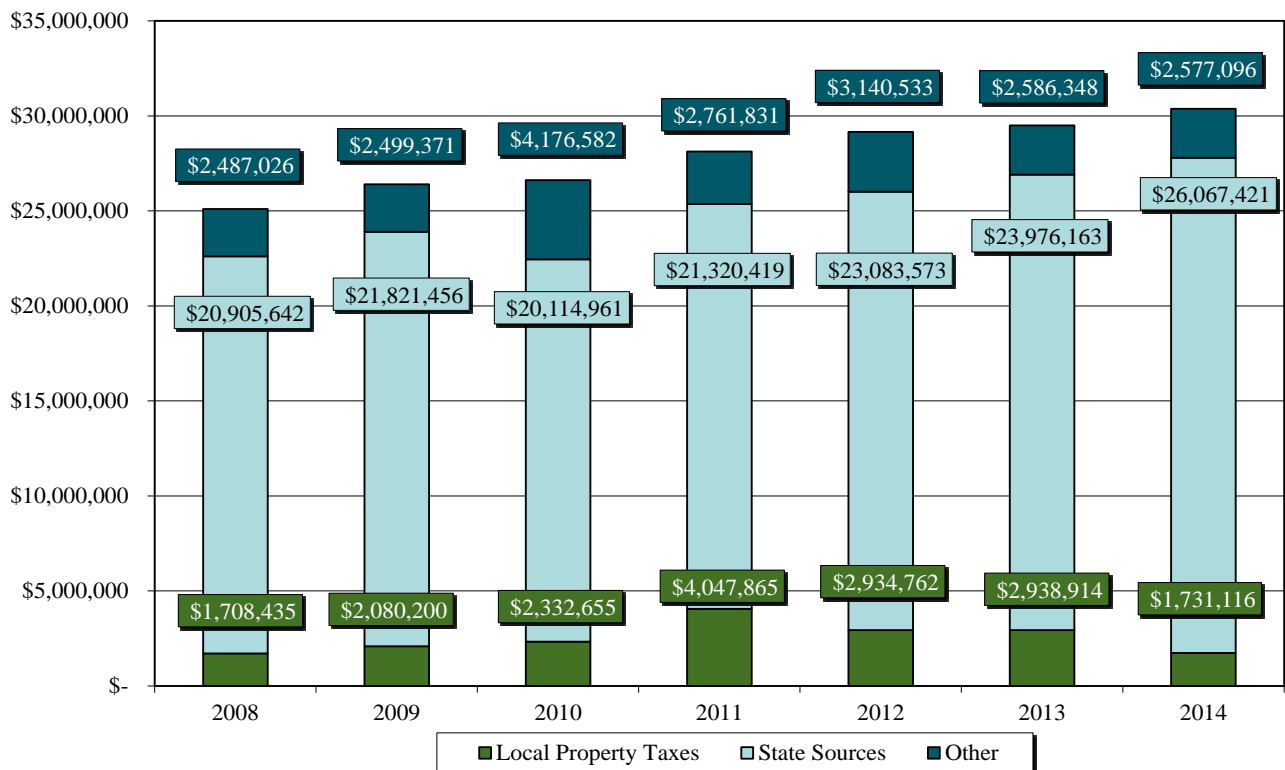
FINANCIAL ANALYSIS June 30, 2014

GENERAL FUND SOURCES OF REVENUE

General Fund sources of revenue are summarized as follows:

	2008	2009	2010	2011	2012	2013	2014
Local Property Tax Levies	\$ 1,708,435	\$ 2,080,200	\$ 2,332,655	\$ 4,047,865	\$ 2,934,762	\$ 2,938,914	\$ 1,731,116
State Revenue	20,905,642	21,821,456	20,114,961	21,320,419	23,083,573	23,976,163	26,067,421
Other Revenue	2,487,026	2,499,371	4,176,582	2,761,831	3,140,533	2,586,348	2,577,096
Total	\$ 25,101,103	\$ 26,401,027	\$ 26,624,198	\$ 28,130,115	\$ 29,158,868	\$ 29,501,425	\$ 30,375,633

General Fund Sources of Revenue



State sources represent 85.8% of the General Fund's total revenue, with local tax payers contributing 5.7% of the funding and federal and other sources making up the remaining 8.5%. Local property tax revenue decreased in 2012 compared to 2011 by \$ 1,113,103 due to a tax shift of approximately \$ 1,223,000 from state aids to property tax revenue in 2011. The tax shift was brought back in 2011 by the State Legislature as a way for the state to balance their budget. As a result of the tax shift, 48.6% of the 2012 tax levy was recognized as revenue in 2011, with state aid decreasing as the offset. The tax shift remained at the same level until 2014 when it was paid back. This resulted in an increase in state aids and a decrease in property tax revenues in 2014. In addition to the tax shift, state aids also increased due to an increase in the formula allowance, higher compensatory funding and higher special education aid.

Included in other revenues are local, county and federal revenues. Other revenues remained very consistent from the prior year, decreasing only \$ 9,252.

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FINANCIAL ANALYSIS

June 30, 2014

REVENUES PER STUDENT (ADM) SERVED

The table below shows a comparison of total revenue per ADM received by the District, districts with ADM between 2,200-4,499 and by all Minnesota school districts.

General Fund	Detroit Lakes				
	2010	2011	2012	2013	2014 (est.)
Property Taxes	\$ 771	\$ 1,339	\$ 947	\$ 928	\$ 573
Other Local Sources	286	412	386	441	394
State Aid	6,924	7,243	7,774	7,851	8,632
Federal Aid	1,184	562	713	440	460
Total General Fund Revenue	\$ 9,165	\$ 9,556	\$ 9,820	\$ 9,660	\$ 10,059

General Fund	Districts with 2,200-4,499 ADM**				
	2010	2011	2012	2013	2014
Property Taxes	\$ 1,210	\$ 1,740	\$ 1,252	\$ 1,218	N/A
Other Local Sources	471	456	499	486	N/A
State Aid	7,020	7,213	7,831	8,010	N/A
Federal Aid	1,131	635	467	369	N/A
Total General Fund Revenue	\$ 9,832	\$ 10,044	\$ 10,049	\$ 10,083	N/A

General Fund	State-Wide**				
	2010	2011	2012	2013	2014
Property Taxes	\$ 1,412	\$ 2,132	\$ 1,550	\$ 1,608	N/A
Other Local Sources	431	429	444	442	N/A
State Aid	7,217	7,341	8,033	8,234	N/A
Federal Aid	1,241	729	590	494	N/A
Total General Fund Revenue	\$ 10,301	\$ 10,631	\$ 10,617	\$ 10,778	N/A

** Source of districts with 2,200-4,499 ADM and state-wide data: *School District Profiles* report published by the Minnesota Department of Education (MDE)

The mix of local and state revenues vary from year-to-year primarily based on funding formulas and the state's financial condition. As a result, the District saw an increase in tax revenue in 2011 as a result of the tax shift by the state. In 2012 and 2013 revenue sources were more consistent with historical trends. In 2014, the District saw a decrease in property taxes and increase in state aids due to the tax shift being paid back by the state. The mix of revenue components from district to district varies due to factors such as the strengths of property values, mix of property types, operating and bond referendums, enrollment trends, density of population, types of programs offered and countless other criteria.

From 2013 to 2014, the District's revenue per ADM served increased an estimated \$ 399 per unit. This increase in the current year reflects an increase in revenue while ADMs served decreased. Property taxes decreased with the tax shift payback. This was offset with the state aid revenue increasing due to increased compensatory and special education aids and the tax shift. Other local sources decreased due to less miscellaneous local grants. Federal aid increased with additional Title I funding.

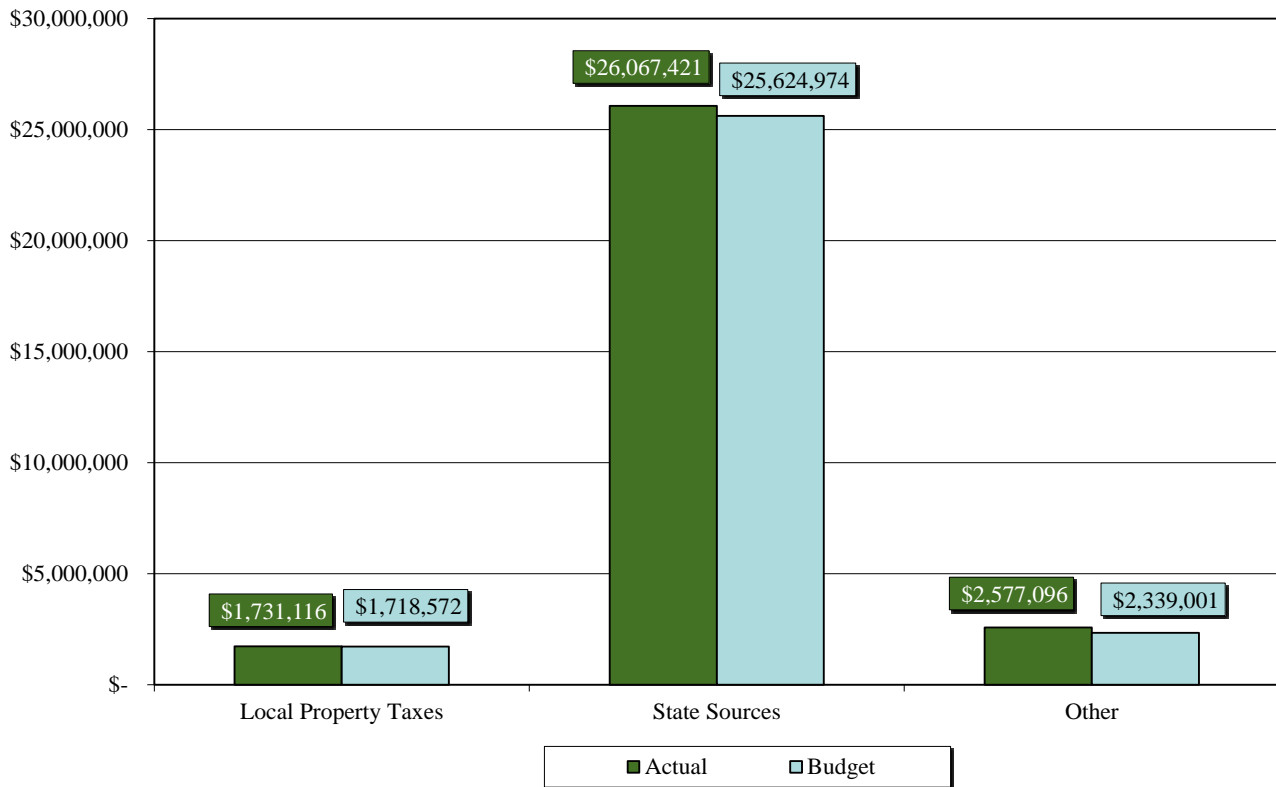
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FINANCIAL ANALYSIS June 30, 2014

GENERAL FUND BUDGET AND ACTUAL

The following graph outlines the budget and actual of the General Fund revenue. Overall, actual revenue was \$ 693,086 over budget. State sources were over budget \$ 442,447 due to the District budgeting for fewer students than they had and conservatively budgeting for special education funding. Other sources of revenue were over budget \$ 238,095 due to budgeting conservatively for medical assistance billings which can vary greatly from year to year.

2014 General Fund Revenues Budget and Actual



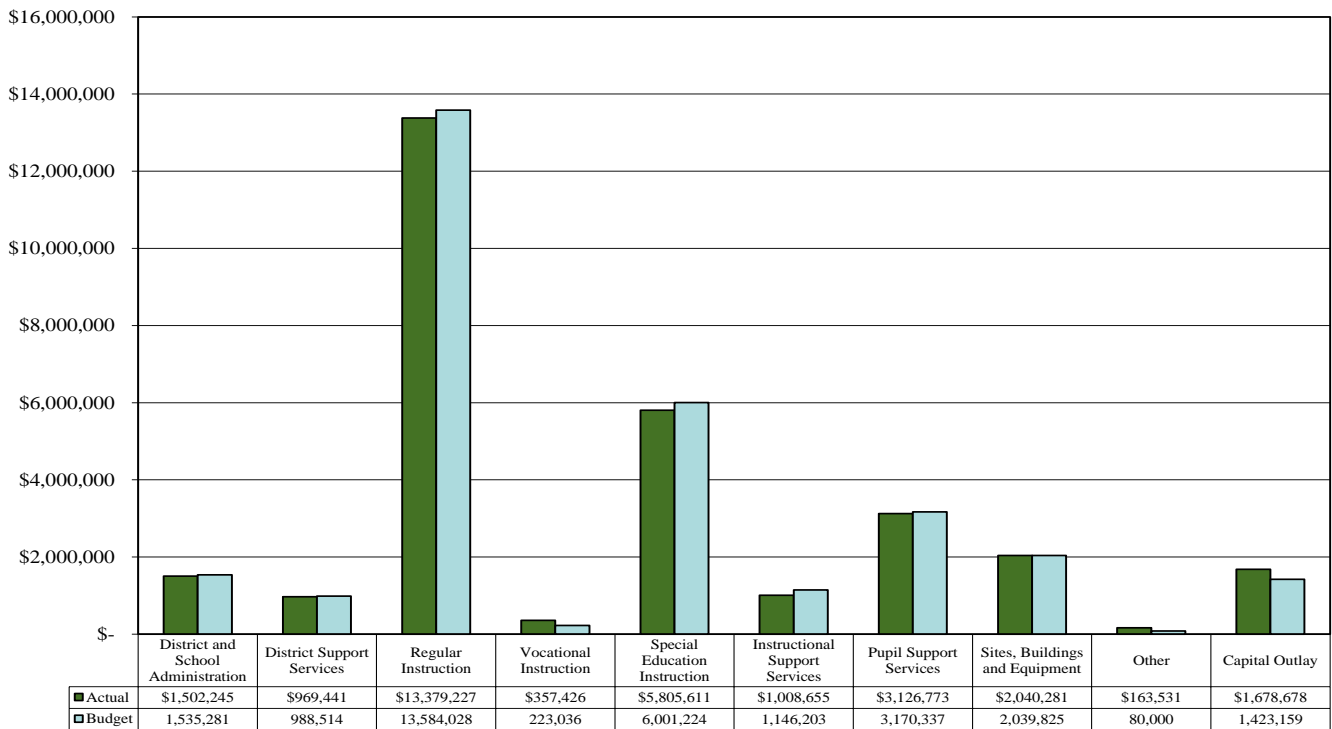
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FINANCIAL ANALYSIS June 30, 2014

GENERAL FUND BUDGET AND ACTUAL

The following graph outlines the budget and actual of the General Fund's expenditures. Overall, actual expenditures were \$ 159,739 under budget. Regular instruction was under budget \$ 204,801 due to budgeting for different programming that did not occur and moving teachers out of the regular program where they were budgeted to the vocational program. Special education instruction was under budget \$ 195,613 as a result of budgeting for a speech pathologist that was not hired and needing fewer paraprofessionals than were budgeted for. Capital outlay was over budget \$ 255,519 with the issuance of a capital lease during the year that was not budgeted for since it is offset with lease proceeds.

2014 General Fund Expenditures Budget and Actual



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FINANCIAL ANALYSIS

June 30, 2014

EXPENDITURES PER STUDENT

Expenditures per student (ADM) for all General Fund programs, including transportation and operating capital are summarized as follows:

Detroit Lakes Schools	2008*	2009*	2010*	2011*	2012*	2013*	2014 (est.)
General Fund	\$ 8,893	\$ 9,501	\$ 9,156	\$ 9,358	\$ 9,503	\$ 9,353	\$ 9,945
State Average	2008	2009	2010	2011	2012	2013	2014
General Fund - ADM Size**	\$ 9,324	\$ 10,395	\$ 9,754	\$ 9,776	\$ 9,849	\$ 9,927	N/A
General Fund - State-Wide Average***	9,797	10,630	10,228	10,207	10,297	10,634	N/A

* Denotes amount taken from the MDE's publication *School District Profiles*

** State average expenditures per ADM served for the 2,200-4,449 ADM group as listed in the MDE publication *School District Profiles*

*** State-wide average expenditures per ADM served as listed in the MDE publication *School District Profiles*

In 2014, General Fund expenditures increased 5.2% from the prior year, while ADM served decreased 1.1% causing expenditures per student to increase 6.3%.

GENERAL FUND OPERATIONS

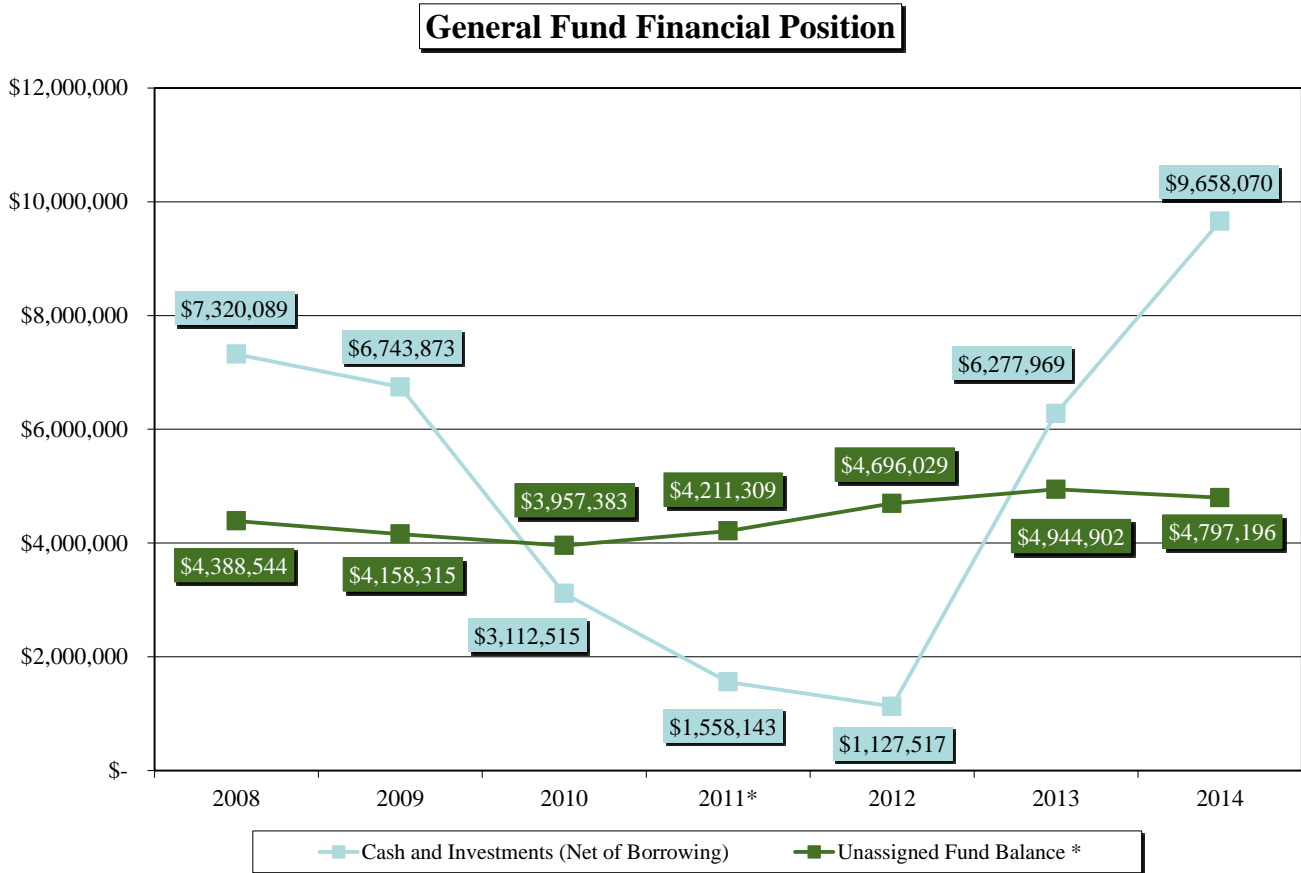
The following table presents seven years of comparative operating results for the District's General Fund.

For the Year Ended June 30,	2008	2009	2010	2011	2012	2013	2014
Revenue	\$ 25,101,103	\$ 26,401,027	\$ 26,624,198	\$ 28,130,115	\$ 29,158,868	\$ 29,501,425	\$ 30,375,633
Expenditures	24,177,667	26,651,160	26,599,768	27,550,575	28,215,865	28,561,064	30,031,868
Excess of Revenue Over (Under) Expenditures	923,436	(250,133)	24,430	579,540	943,003	940,361	343,765
Other Financing Sources	8,428	-	502	-	400	-	318,250
Fund Balance, July 1	6,647,111	7,578,975	7,328,842	7,353,774	7,933,314	8,876,717	9,817,078
Fund Balance, June 30	7,578,975	7,328,842	7,353,774	7,933,314	8,876,717	9,817,078	10,479,093
Less Restricted Fund Balances	3,190,431	3,170,527	1,218,466	1,339,391	1,696,432	1,919,073	2,654,901
Unrestricted Fund Balance, June 30	\$ 4,388,544	\$ 4,158,315	\$ 6,135,308	\$ 6,593,923	\$ 7,180,285	\$ 7,898,005	\$ 7,824,192

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FINANCIAL ANALYSIS June 30, 2014

GENERAL FUND OPERATIONS AND FINANCIAL POSITION



* In 2011, the District implemented GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, which changed the classification of fund balance components. Amounts previously classified as unreserved are now reported as nonspendable, committed or unassigned. This chart has been updated to reflect only the unassigned balances of the General Fund.

The District's unassigned General Fund balance as a percentage of total expenditures decreased from 17.3% in 2013 to 16.0% to 2014. Although the District is in adequate financial condition, it should continue to monitor its unassigned General Fund balance.

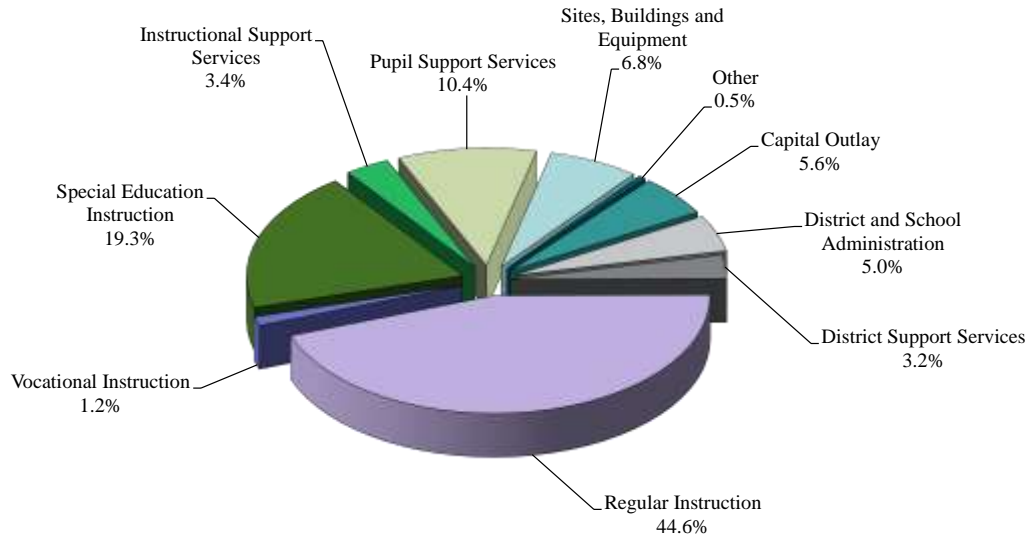
Over the course of the seven year-ends presented, the General Fund cash balance increased \$ 2,337,981 and unassigned fund balance increased \$ 408,652. In 2010, the MDE increased its withholding percentage to 27% due to state budget constraints. As a result, the District only received approximately 73% of its state aid entitlement prior to June 30. This funding holdback caused cash to decrease from 2009 to 2010 by \$ 3,631,358. The holdback increased to 30% in 2011 and 35.7% in 2012 which resulted in decreases in the cash balance of \$ 1,554,372 and \$ 430,626, respectively. By the end of 2013, the holdback percentage decreased to 14.6%, causing the cash increase of \$ 5,150,452. During 2014, the state decreased the holdback percentage to 10% and paid back the tax shift resulting in an increase in cash in the amount of \$ 3,380,101.

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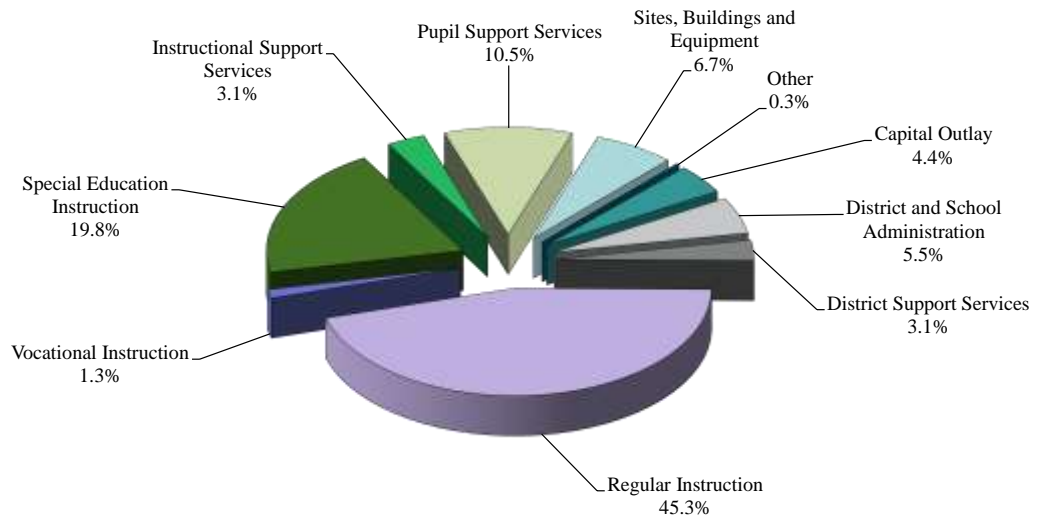
FINANCIAL ANALYSIS June 30, 2014

GENERAL FUND OPERATIONS

2014 District Expenditures



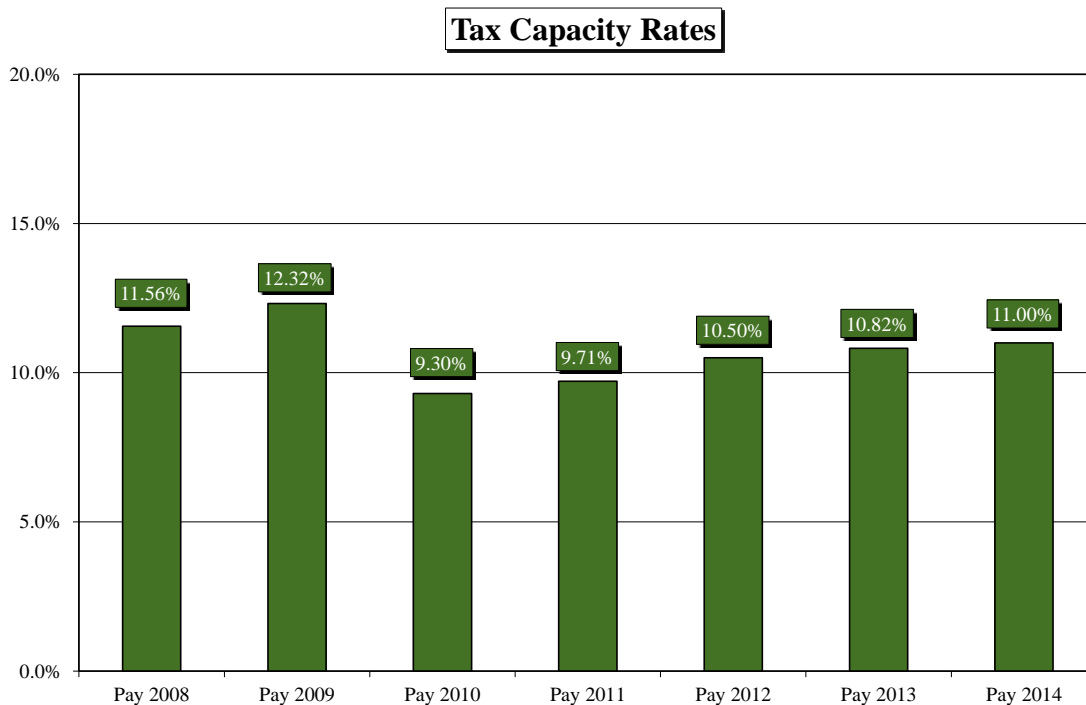
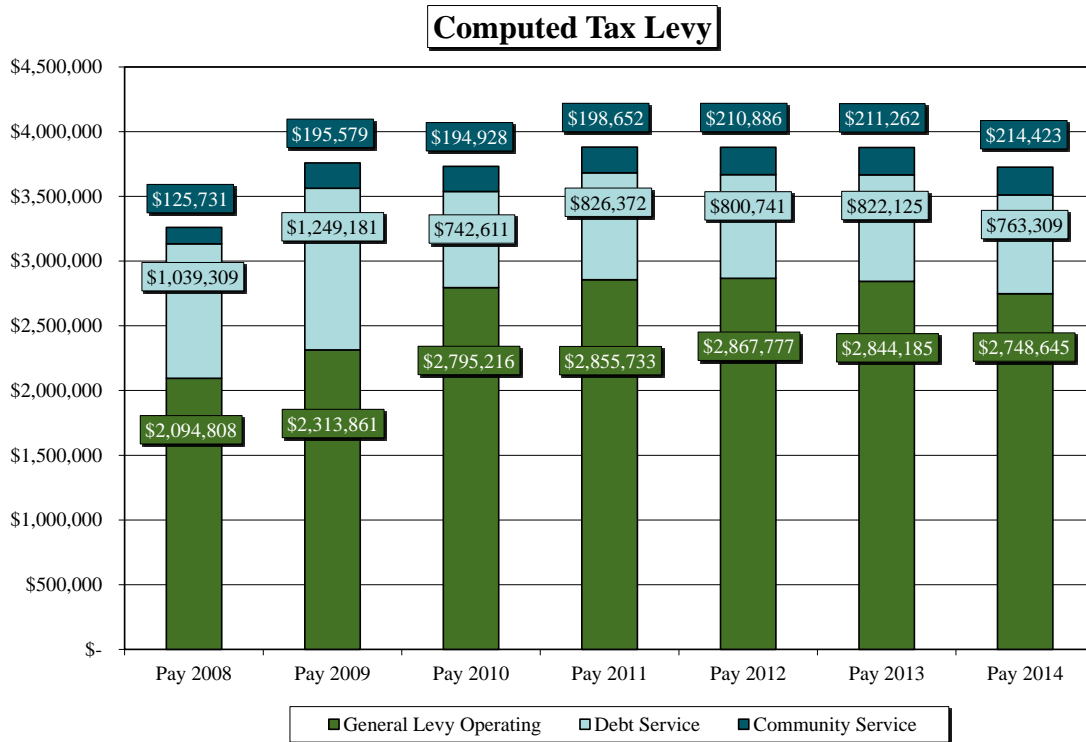
2013 District Expenditures



INDEPENDENT SCHOOL DISTRICT NO. 22

FINANCIAL ANALYSIS June 30, 2014

TAX LEVY



INDEPENDENT SCHOOL DISTRICT NO. 22

**FINANCIAL ANALYSIS
June 30, 2014**

FOOD SERVICE FUND

The following table presents seven years of comparative operating results for the District's Food Service Fund:

For the Year Ended June 30,	2008	2009	2010	2011	2012	2013	2014
Revenue	\$ 1,032,941	\$ 1,143,763	\$ 1,219,673	\$ 1,269,820	\$ 1,352,430	\$ 1,452,468	\$ 1,428,651
Expenditures	1,017,106	1,089,003	1,107,183	1,181,958	1,248,625	1,357,815	1,392,401
Excess of Revenue Over							
Expenditures	15,835	54,760	112,490	87,862	103,805	94,653	36,250
Other Financing Sources	757	-	-	600	-	900	-
Fund Balance, July 1	291,740	308,332	363,092	475,582	564,044	667,849	763,402
Fund Balance, June 30	\$ 308,332	\$ 363,092	\$ 475,582	\$ 564,044	\$ 667,849	\$ 763,402	\$ 799,652

The Food Service Fund fully supported its operations in each of the last seven years. This activity increased the Food Service Fund balance to \$ 799,652 at the end of the year. The MDE recommends districts' net cash resources not exceed three months of expenditures, based on a nine month operating year. Based on this calculation, the maximum net cash resources at June 30, 2014 would be \$ 464,134. The net cash resources of the District at June 30, 2014 were \$ 767,989.

COMMUNITY SERVICE FUND

The following table presents seven years of comparative operating results for the District's Community Service Fund:

For the Year Ended June 30,	2008	2009	2010	2011	2012	2013	2014
Revenue	\$ 726,474	\$ 694,469	\$ 690,154	\$ 692,681	\$ 685,758	\$ 700,850	\$ 776,434
Expenditures	725,457	683,553	684,685	701,725	663,686	700,749	748,004
Excess of Revenue Over							
(Under) Expenditures	1,017	10,916	5,469	(9,044)	22,072	101	28,430
Fund Balance, July 1	110,022	111,039	121,955	127,424	118,380	140,452	140,553
Fund Balance, June 30	\$ 111,039	\$ 121,955	\$ 127,424	\$ 118,380	\$ 140,452	\$ 140,553	\$ 168,983

In 2014, Community Service Fund revenues exceeded expenditures by \$ 28,430, resulting in the fund balance increasing to \$ 168,983. Revenues and expenditures fluctuate year to year depending on the number of classes and programs offered. Additionally, the District received new funding for the Pathways II programming in 2014.

INDEPENDENT SCHOOL DISTRICT NO. 22

LEGISLATIVE SUMMARY

June 30, 2014

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

STATE AID APPROPRIATIONS

Total appropriations from the state general fund for E-12 education for the 2014-2015 biennium are \$ 15.6 billion including \$ 7.6 billion for 2014 and \$ 8.0 billion for 2015. This includes the addition of funding for all-day kindergarten, beginning in 2015.

The formula allowance for 2014 General Education Aid was increased \$ 78 (1.5%) to \$ 5,302. For 2015 and later, the formula allowance is set at \$ 5,831, which is an increase of 1.9% over 2014 after adjusting for the change in pupil unit weights and the elimination of the aid subtraction for pension rate changes. Beginning in 2015, basic revenue is calculated using adjusted pupil units with the new pupil weights rather than adjusted marginal cost pupil units.

As of the November 2013 forecast for the state, education appropriations have been restored to the 90%/10% payment schedule, and the tax shift was fully paid back on June 20, 2014.

In 2015, the extended time revenue allowance increases from \$ 4,601 to \$ 5,017 to adjust for the change in pupil weights. Also in 2015, the gifted and talented revenue increases from \$ 12 to \$ 13 to adjust for the change in pupil weights.

For 2015 and later, alternative teacher compensation revenue (Q Comp) will be changed from a component of general education revenue to a separate categorical revenue. The funding amount will not change. Declining enrollment revenue, pension adjustment revenue and location equity revenue will be added as new components of general education revenue.

For 2015 only, teacher development and evaluation revenue is available for districts not enrolled in Q Comp for teachers employed on October 1 of the prior school year. A teacher is defined to include all staff required to be licensed including administrators.

Marginal cost calculations will be eliminated from the definition of pupil units. Beginning in 2015, a new component of general education revenue, "declining enrollment revenue," will be established to replace funding previously provided to districts with declining enrollment through marginal cost pupil units. The declining enrollment revenue is set to equal the decline in adjusted pupil units between the prior year and the current year times 28% of the formula allowance.

The compensatory revenue formula for 2015 and later is adjusted to neutralize the impact of the change in pupil unit weights by deducting \$ 839 from the formula allowance for compensatory revenue calculations instead of \$ 415. Districts will be allowed to use up to 5% of its compensatory revenue for programs designed to prepare children for entry into school including early education programs, parent-training programs, school readiness programs, early kindergarten programs for four-year olds and voluntary home visits and other outreach. This is in addition to the 5% that districts currently have flexibility with. The remaining 90% of compensatory revenue must be spent at the site where the revenue is generated.

INDEPENDENT SCHOOL DISTRICT NO. 22

LEGISLATIVE SUMMARY

June 30, 2014

STATE AID APPROPRIATIONS

For 2015 and later, \$ 530 will be deducted from the formula allowance used in calculating elementary and secondary sparsity revenue to neutralize the impact of pupil unit weighting changes. The transportation sparsity formula was also adjusted to account for the removal of marginal cost pupil unit accounting and the new pupil weights.

Beginning in 2015, the operating capital allowances are adjusted to compensate for the elimination of marginal cost pupil units and the new pupil unit weights. The basic rate increases from \$ 73 to \$ 79; the sliding scale rate based on building age increases from \$ 100 to \$ 109; and the learning year rate increases from \$ 30 to \$ 31. Beginning in 2015, the equalizing factor for operating capital will increase from \$ 10,194 to \$ 14,500 to adjust for the change in pupil unit weights and reduce the property tax share of operating capital revenue to offset the new general education levy. The allowable uses of operating capital revenue are also clarified by including computer hardware, software, annual licensing fees and cross referencing the definition of textbooks in the nonpublic pupil aid statute.

Beginning in 2015, a new component of general education revenue for districts with below average reduction for changes in employer pension contributions is established. The revenue per pupil unit is set to equal the difference between the district's 2014 pension adjustment per pupil unit and the state average year 2014 aid reduction per pupil unit.

Beginning in 2015, location equity revenue is established as a new component of general education revenue. For a district with any of its area in the seven-county metropolitan area, the revenue equals \$ 424 times the adjusted pupil units (APU) for that school year. For all other school districts with more than 2,000 pupils in average daily membership, for the year ending in the year before the levy is certified (2012 for 2015 revenue), the revenue equals \$ 212 times the APU for the school year. Location equity is an equalized levy spread on referendum market value (RMV); the equalizing factor is \$ 510,000. If a district levies less than the maximum amount, the aid is reduced proportionately. A district may opt out of the revenue by adopting a board resolution prior to September 1 of the year prior to the year for which the decision to opt out becomes effective (September 1, 2013 for FY 2015 revenue). For participating districts, the location equity allowance is subtracted from the referendum allowance.

Beginning in 2015, school districts are allowed to use general education revenue generated for all-day kindergarten to meet the needs of three and four year olds in the district. This does not apply to a district with a fee-based all-day kindergarten.

Beginning in 2015, the statewide revenue limit for career and technical education (CTE) revenue expires and revenue is computed using the new formula enacted in 2012 that bases funding on 35% of approved program expenditures.

English learner revenue has been extended from five to six years for 2015. Students with less than six years of ADM in Minnesota whose test results indicate proficiency in English will continue to be eligible for aid if the classroom teacher determines that the student is not proficient.

INDEPENDENT SCHOOL DISTRICT NO. 22

LEGISLATIVE SUMMARY June 30, 2014

PUPIL ACCOUNTING REFORM

Beginning in 2015, pupil accounting reform will occur and pupil unit weights will change as follows:

Prekindergarten and Disabled	From 1.25	To 1.0
Part-time Kindergarten	From .612	To .55
All-Day Kindergarten	From .612	To 1.0
Grades 1-3	From 1.115	To 1.0
Grades 4-6	From 1.06	To 1.0
Grades 7-12	From 1.3	To 1.2

To qualify for all-day kindergarten weight, a pupil must be enrolled in a free all-day every day kindergarten program that is available to all kindergarten students at the pupil's school and must include at least 850 hours of instruction.

GENERAL EDUCATION LEVY REFORM

Beginning in 2015, a district is allowed to convert up to \$ 300 per APU of voter-approved referendum revenue to board-approved referendum revenue by board vote. For a district with less than \$ 300 per APU of referendum revenue after the location equity revenue subtraction, the school board is allowed to authorize new referendum revenue up to the difference between \$ 300 per APU and the district's net referendum allowance after the location equity revenue subtraction.

A new uniform general education levy called the "Student Achievement Levy" has been established for 2015 in the amount of \$ 20 million. All districts may levy up to the general education rate. If a district levies less than the permitted rate, its general education aid is reduced proportionally.

MISCELLANEOUS LEVIES

The maximum rate for the building lease levy is changed from \$ 150 to \$ 162 per pupil unit for districts and from \$ 43 to \$ 46 for intermediate district members to adjust for the pupil unit weighting changes.

The safe school levy for taxes payable in 2014 and later was increased from \$ 30 to \$ 36 per pupil unit. \$ 4 of the increase is new revenue while the other \$ 2 is to adjust for pupil unit weighting changes. The uses of the levy are also expanded to include facility security enhancements, efforts to improve the school climate and costs associate with mental health services.

EARLY CHILDHOOD AND COMMUNITY EDUCATION

An early learning scholarship program was established. For a family to receive a scholarship, it must have a child age 3 or 4 on September 1 of the current year and have income equal to or less than 185% of the federal poverty level. Scholarships may be awarded up to \$ 5,000 per child per year for 2015 and the cap is lifted for 2016.

The growth factor for adult basic education increased from 1.02 to 1.025 for 2015 and later. School readiness aid entitlement is increased by \$ 2 million per year, ongoing. The early childhood family education allowance will be set at 2.3% of the general education formula allowance starting in 2015.

INDEPENDENT SCHOOL DISTRICT NO. 22

LEGISLATIVE SUMMARY

June 30, 2014

EDUCATION EXCELLENCE

Districts may now use the 2% of basic revenue set aside for staff development for teacher evaluation.

SPECIAL EDUCATION

A new special education formula is enacted beginning in 2016. To provide for a transition to the new formula, the current special education regular formula with the addition of the cross subsidy reduction aid remains in place for 2015.

Beginning in 2016, special education aid equals the sum of the new formula aid plus the new formula excess cost aid.

State total special education aid is increased by \$ 39 million for 2016 and by \$ 41 million for 2017.

Beginning in 2015, tuition billing is changed so that the resident district is responsible for 90% of unfunded costs (vs. 100% currently) and the serving district/charter school is responsible for 10% of unfunded costs for open-enrolled students. Intermediate districts, cooperatives and charter schools where at least 70% of students are eligible for special education are exempt from this provision and continue to be able to recover 100% of unfunded special education costs from the resident district. This also does not apply to students placed by the resident district (e.g. at an intermediate district) or served at a charter school with very high special education concentration.

Beginning in 2016, special education aid will be paid directly to cooperatives and intermediate districts, rather than having those aids flow through the resident district. Tuition bills will be reduced to offset the aid paid to the cooperative and intermediaries.

ACCOUNTING

The authority for districts to make unlimited fund transfers that do not increase state aid or levy obligations is extended to 2015. Districts will follow the same procedures outlined for 2014. Transfers are not allowed from the food service or community service funds. The school board must adopt a resolution stating the transfer will not diminish instructional opportunities for students and the district must apply to the Commissioner to make the transfer. The application must include the amount to be transferred and the funds/accounts involved. The application must also be signed by the superintendent and approved by the school board. A transfer cannot be made from the reserved account for staff development revenue as the 2% set aside requirement has been reinstated for those years.

SCHOOL NUTRITION

The rate for each school lunch served increased from 12.5 to 52.5 cents for 2015 for reduced priced students. Districts must now make lunches free for these students.

INDEPENDENT SCHOOL DISTRICT NO. 22

EMERGING ISSUES

June 30, 2014

Executive Summary

The following is an executive summary of financial and business related updates to assist you in staying current on emerging issues in accounting and finance. This summary will give you a preview of the new standards that have been recently issued and what is on the horizon for the near future. The most recent and significant updates include:

- **Internal Control Integrated Framework** – COSO has issued an updated integrated framework for internal control. The update is expected to make the integrated internal control framework easier to use and apply. In addition, the update takes into account globalization of businesses today and its interdependence on technology. This update has been issued and will supersede the original framework at the end of 2014.
- **Accounting Standard Update – Accounting for Pensions** – GASB has issued new statements relating to accounting and disclosures for pension. The new statements require governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability. In addition, the statement includes new requirements for required supplementary information and more extensive footnote disclosures.

The following are extensive summaries of each of the current updates. As your continued business partner, we are committed to keeping you informed of new and emerging issues. We are happy to discuss these issues with you further and their applicability to your district.

COSO PROJECT – INTERNAL CONTROL INTEGRATED FRAMEWORK

In 1992, the Committee on Sponsoring Organizations of the Treadway Commission (COSO) developed an internal control framework that has been adopted and used by entities worldwide. In 2013, COSO finalized and released an updated integrated internal control framework. The update is expected to make the integrated framework easier to use and apply. In addition, the update takes into account, the business environment of today and the reliance on and interdependence of technology within business systems.

The internal control update is not changing the core definition of internal control, the three categories of objectives or the five components of internal control.

COSO defines internal control as a process, affected by an entity's board of directors, management and other personnel. This process is designed to provide reasonable assurance regarding the achievement of the three objectives, as follows: effectiveness and efficiency of operations; reliability of financial reporting; and compliance with applicable laws and regulations.

1. Internal control is a process. It is a means to an end, not an end in itself.
2. Internal control is not merely documented by policy manuals and forms. Rather, it is put in by people at every level of an organization.
3. Internal control can provide only reasonable assurance, not absolute assurance, to an entity's management and board.
4. Internal control is geared to the achievement of objectives in one or more separate but overlapping categories.

INDEPENDENT SCHOOL DISTRICT NO. 22

EMERGING ISSUES

June 30, 2014

COSO PROJECT – INTERNAL CONTROL INTEGRATED FRAMEWORK (CONTINUED)

The five components of internal control, which are unchanged, are as follows:

1. Control Environment - integrity, ethics, management style, etc.
2. Risk Assessment - identification and analysis of relevant risks
3. Control Activities - policies, procedures and activities, including segregation of duties
4. Information and Communication - ensure information effectively flows up, down and across the organization, both internally and externally
5. Monitoring Activities - assessment of the systems performance over time

The updated framework has changed to address the changes in business and operating environments, such as globalization of markets and operations, greater complexities in businesses, reliance on evolving technologies and expectations relating to preventing and detecting fraud. In addition, principles of effective internal controls have been added to each of the components of internal control as follows:

Control Environment:

1. Demonstrates a commitment to integrity and ethical values.
2. The board of directors is independent from management and exercises oversight responsibility of the performance of internal controls.
3. Management establishes structure, reporting lines, authority and responsibility.
4. Demonstrates a commitment to attract, develop and retain competent individuals.
5. Enforces accountability for individual's internal control responsibilities.

Risk Assessment:

1. Specifies suitable objectives with sufficient clarity.
2. Identifies and analyzes risk as a basis for how risks should be managed.
3. Assesses the potential for fraud risk.
4. Identifies and analyzes significant changes that could impact the system of internal controls.

Control Activities:

1. Selects and develops control activities that contribute to the mitigation of risks.
2. Selects and develops general controls over technology.
3. Deploys control activities through policies that establish what is expected and procedures that put policies into place.

Information and Communication:

1. Uses relevant information to support the functioning of other components of internal control.
2. Communicates information internally, including objectives and responsibilities necessary to support the internal controls.
3. Communicates with external parties regarding matters affecting internal control.

Monitoring Activities:

1. Conducts ongoing and/or separate evaluations to ascertain whether the components of internal control are present and functioning.
2. Evaluates and communicates deficiencies to those parties responsible for corrective actions.

The updated framework also has additional examples relevant to operation, compliance and reporting objectives added.

INDEPENDENT SCHOOL DISTRICT NO. 22

EMERGING ISSUES

June 30, 2014

COSO PROJECT – INTERNAL CONTROL INTEGRATED FRAMEWORK (CONTINUED)

While COSO integrated internal control framework is very extensive, this is only a short summary of some of the changes of the updated framework. The updated framework will supersede the original framework at the end of 2014; however, users of the framework are encouraged to transition to the updated framework as soon as possible.

ACCOUNTING STANDARD UPDATE – ACCOUNTING FOR PENSIONS

GASB Statement No. 68 replaces the requirements of Statement No. 27, *Accounting for Pensions by State and Local Governmental Employers* and Statement No. 50, *Pension Disclosures*, as they relate to governments that provide pensions through pension plans administered as trusts or similar arrangements that meet certain criteria. Statement No. 68 requires governments providing defined benefit pensions to recognize their long-term obligation for pension benefits as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. GASB Statement No. 71 – *Pension Transition for Contributions Made Subsequent to the Measurement Date* – is an amendment of GASB No. 68.

- GASB 68 will require presentation of the local government’s proportionate share of the pension plan’s Net Pension Liability to be reported on the government-wide statement of net position and the proprietary fund statements of net position – based on last year’s employer contributions
- The Net Pension Liability is measured as the total pension liability less the amount of the pension plan’s fiduciary net position – PERA and TRA currently estimating this around \$6-7 billion each
- Governmental Funds will present pension expenditures equal to the total of 1) amounts paid by employer to the pension plan and 2) the change between the beginning and ending balances of amounts normally expected to be liquidated with expendable available financial resources (i.e. No Change)
- PERA and TRA have been proactive in steps toward implementation and the outlook for reporting to members appears good, based on current plans – the hope is that most of the implementation will be a “plug-in” of PERA and TRA generated data
- PERA and TRA both have a June 30 fiscal year-end – this is the measurement date you will utilize for your presentation in your June 30 financial statements twelve months subsequent to that date
- Other Deferred Inflows/Outflows will include: differences between expected and actual economic experience and investment earnings, changes in assumptions and changes in employer proportion and difference between contributions and proportionate share of pension expense
- Required Supplementary Information will be two separate schedules – Schedule of Changes in Net Pension Liability and Related Ratios & Schedule of Contributions – 10-year presentation for each with notes
- GASB 71 clarifies that in the year of implementation you must determine the deferred outflows associated with pension contributions made subsequent to the measurement date – even if it is not practical to determine the other deferred inflows and outflows

INDEPENDENT SCHOOL DISTRICT NO. 22

EMERGING ISSUES

June 30, 2014

ACCOUNTING STANDARD UPDATE – ACCOUNTING FOR PENSIONS (CONTINUED)

PERA and TRA Plan:

- Perform annual actuarial valuations to determine funded status and liabilities
- Require plan actuary to calculate collective amount of items requiring deferred treatment
- Engage external auditor or audit actuarial census data and schedule of employer's proportionate share
- Communicate results to the school districts
- Provide RSI and suggested footnotes

Local Impacts:

- Your district's proportionate share of the plan's net pension liability will be recognized as a liability on your district's government-wide statements
- Expenditures will continue to be tracked in the fund statements for your statutory contributions, but a reconciling item will be needed to adjust these contributions with your government-wide expenses which will be represented by the change in the net pension liability
- As a result, your financial statements/financial position will be immediately impacted by funding shortfalls at the pension plan
- Additional RSI presenting 10 years of information regarding net pension liability, required & actual contributions and related ratios
- Adds more extensive note disclosures, including sensitivity analysis of investment return assumption
- Requires employer to track annual balances of deferred outflows of resources and inflows of resources.
- Must describe signification assumptions and other inputs used to measure total pension liability.