Management Report

for

Intermediate School District No. 917
Rosemount, Minnesota
June 30, 2014

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To the School Board and Management of
Intermediate School District No. 917
Rosemount, Minnesota

We have prepared this management report in conjunction with our audit of Intermediate School District No. 917's (the District) financial statements for the year ended June 30, 2014. 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
- Legislative Summary
- Accounting and Auditing Updates

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.

The purpose of this report is solely to provide those charged with governance of the District, management, and those who have responsibility for oversight of the financial reporting process comments resulting from our audit process and information relevant to school district financing in Minnesota. Accordingly, this report is not suitable for any other purpose.

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

Minneapolis, Minnesota
October 30, 2014

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AUDIT SUMMARY

The following is a 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 AND *GOVERNMENT AUDITING STANDARDS*

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, 2014, and the related notes to the financial statements. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America and *Government Auditing Standards,* 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, 2014:

- We have issued an unmodified opinion on the District's annual financial statements.
- We reported no deficiencies in the District's internal control over financial reporting that we considered to be material weaknesses.
- The results of our testing disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.
- We reported no findings based on our testing of the District's compliance with Minnesota laws and regulations.

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 cash balances and cash receipts and disbursements of these accounts as of and for the year ended June 30, 2014 on the cash basis of accounting. Our opinion was qualified for a limitation related to the completeness of cash receipts reported.

We reported one deficiency involving internal controls over financial reporting for the District's extracurricular student activities that we consider to be a material weakness. The District reports student activities on a cash basis, and has not established procedures to assure that all cash collections are recorded in the accounting records. Procedures such as the use and reconciliation of pre-numbered receipts and inventory controls over items sold for fundraisers would help strengthen the controls in this area.

We also issued a report on compliance with the Minnesota Department of Education's (MDE) *Manual for Activity Fund Accounting* (MAFA), in which we reported one finding.

1. We noted 8 of 10 cash receipts we tested accounted for by the District as student activities lacked documentation to allow us to determine if it was deposited in a timely manner.

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 fiscal 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 financial statements in the proper period.

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. During our audit, we noted uncorrected misstatements totaling approximately $50,000, overstating the balances within salaries payable and compensated absences payable. This misstatement detected as a result of audit procedures and not corrected by management was considered immaterial, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

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 were:

> 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 the current fiscal year is not finalized until after the District has closed its financial records. 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 in the Statement of Net Position 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). This obligation is calculated using actuarial methodologies described in Governmental Accounting Standards Board (GASB) Statement No. 45. This actuarial calculation includes 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.

The District's self-insured activities require recording a liability for claims incurred but not yet reported, which are based on estimates.

We evaluated the key factors and assumptions used by management to develop the estimates discussed above in determining that they are reasonable in relation to the financial statements taken as a whole.

The financial statement disclosures are neutral, consistent, and clear.

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 REPRESENTATIONS

We have requested certain representations from management that are included in the management representation letter dated October 30, 2014.

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.

OTHER MATTERS

We applied certain limited procedures to Management's Discussion and Analysis and the Schedule of Funding Progress for the Other Post-Employment Benefits Plan, which are required supplementary information (RSI) that supplements the basic financial statements. Our procedures consisted of inquiries of management regarding the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We did not audit the RSI and do not express an opinion or provide any assurance on the RSI.

We were engaged to report on the supplemental information and Uniform Financial Accounting and Reporting Standards (UFARS) Compliance Table accompanying the financial statements, which are not RSI. With respect to this supplementary information, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the 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.

We were not engaged to report on the introductory section and other information, which accompany the financial statements but are not RSI. We did not audit or perform other procedures on this other information and we do not express an opinion or provide any assurance on it.

Due to its complexity, it would be impossible to fully explain the funding of public education in Minnesota within this report. A summary of legislative changes affecting school districts and charter schools included later in this report gives an indication of how complicated the funding system is. This 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 2015 fiscal year. The amount of the formula allowance and the percentage change from year to year excludes non-comparable changes such as temporary funding increases, the “roll-in” of aids that were previously funded separately, potential reductions due to levying less than the maximum student achievement levy rate, and the one-time replacement of a portion of general education aid with federal fiscal stabilization funds in fiscal 2010.

	Formula Allowance	
Fiscal Year Ended June 30,	Amount	Percent Increase
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	– %
2012	$ 5,174	1.0 %
2013	$ 5,224	1.0 %
2014	$ 5,302	1.5 %
2015	$ 5,831	2.0 % *

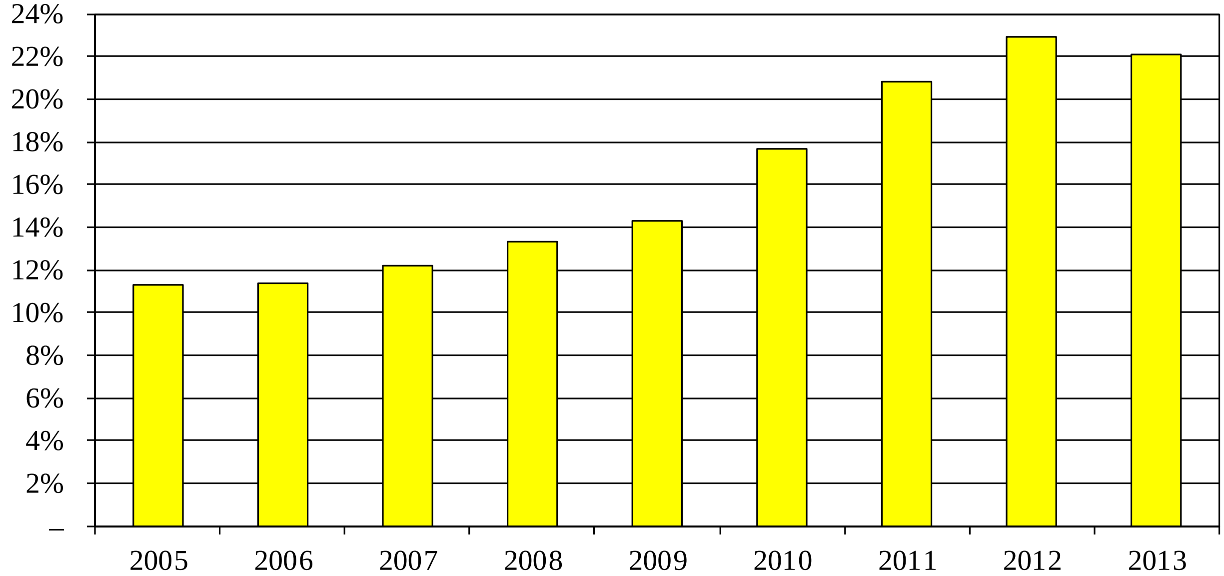
* The $529 increase in 2015 is offset by changes to pupil weightings and the general education aid formula that reduced the increase to the equivalent of $105, or 2.0 percent, state-wide.

In recent years, modest increases in the formula allowance have forced many districts to continually cut expenditure budgets or seek increased referendum revenue in order to maintain programs.

STATE-WIDE SCHOOL DISTRICT FINANCIAL HEALTH

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

State-Wide Unrestricted Operating Fund Balance
as a Percentage of Operating Expenditures



Note: State-wide information is not available for fiscal 2014.

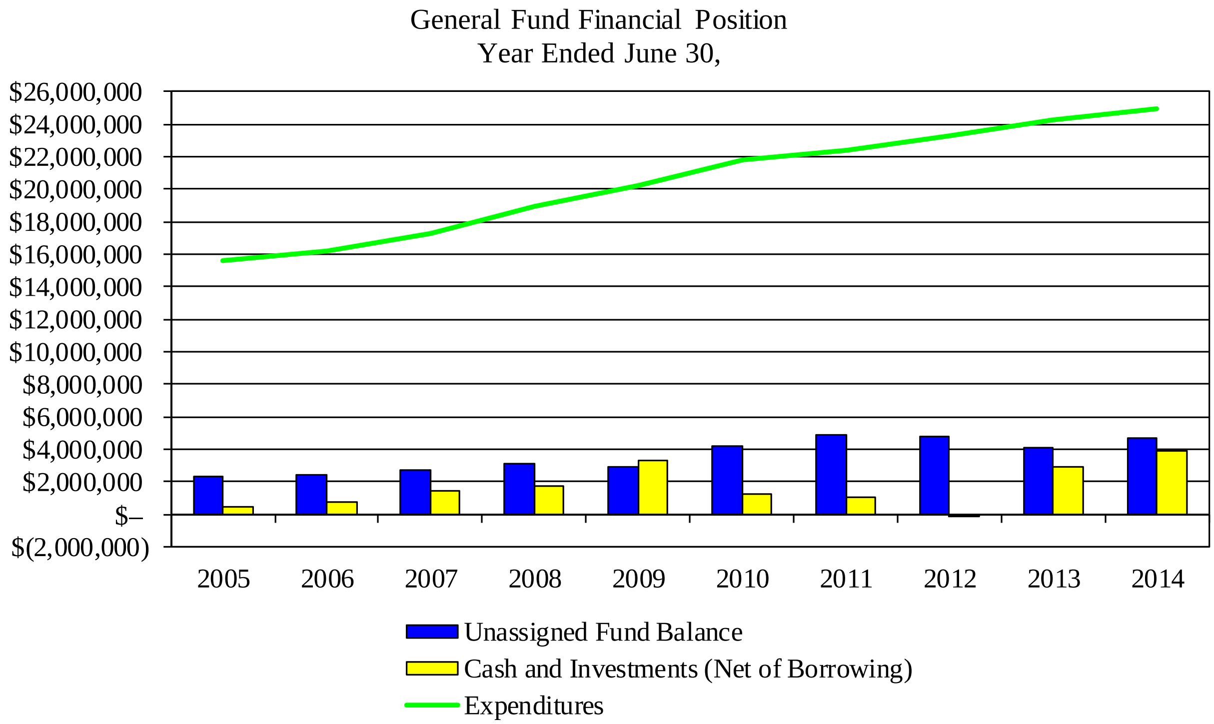
The calculation above reflects only the unrestricted fund balance of the General Fund, and the corresponding expenditures, which is the same method the state uses for the calculation of statutory operating debt (SOD). We have also included the comparable percentages for your district.

Even with limited funding increases, Minnesota school districts have generally been maintaining a higher unrestricted fund balance as a percentage of operating expenditures in recent years. This trend is the result of many factors, including districts reducing operating expenditures, adapting to funding restrictions, efforts to maintain fund balance for cash flow purposes, and in some cases community support in the form of operating referendums.

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 activity. Unassigned fund balance and cash balance are two indicators of financial health, while annual expenditures are often used to measure the size of the operation.



The District ended fiscal year 2014 with a General Fund cash and investments balance of $3,923,173 (net of borrowing and interfund receivables and payables), an increase of $1,036,595 from the previous year. This change was primarily due to the change in the metering of state aid payments. Unassigned fund balance at year-end was $4,642,898, an increase of $560,220.

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

	Year Ended June 30,				
	2010	2011	2012	2013	2014
Nonspendable fund balances	$ 11,115	$ 4,806	$ 106,799	$ 80,710	$ 9,922
Restricted fund balances	1,614,259	1,604,790	1,458,010	1,430,576	1,414,463
Assigned fund balances	–	–	–	110,661	–
Unassigned	4,186,226	4,909,422	4,785,805	4,082,678	4,642,898
Total fund balances	$ 5,811,600	$ 6,519,018	$ 6,350,614	$ 5,704,625	$ 6,067,283
Unassigned fund balances as a percentage of expenditures	19.2%	21.9%	20.6%	16.8%	18.6%
Cash and temporary investments (net of borrowing)	$ 1,266,203	$ 1,062,392	$ (150,730)	$ 2,886,578	$ 3,923,173

The table on the previous page reflects the total General Fund unassigned fund balance and percentages, which differs from those used in the previous discussion of state-wide fund balances, which are based on a state 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.

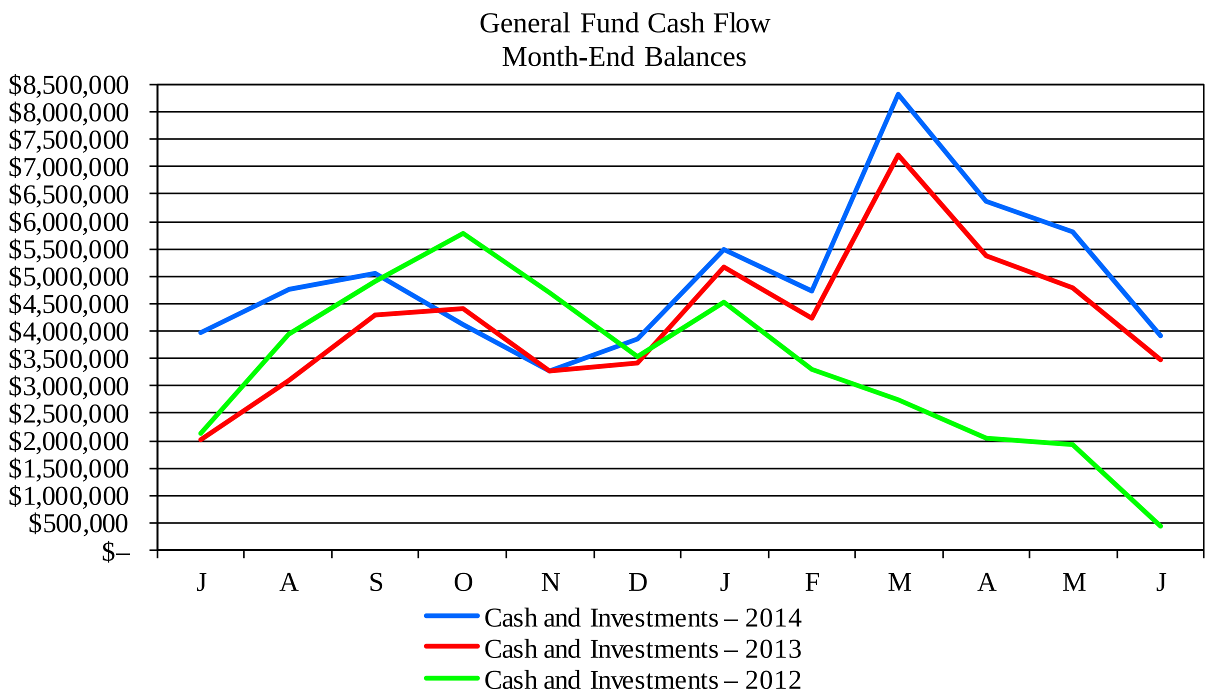
Fund balance as a percentage of expenditures is one key measure in assessing the financial health of the District. Maintaining an adequate fund balance is particularly important because of the limited availability of borrowing for the District and the need for the General Fund to be self-sustaining in its cash flow needs.

The fund balance remains healthy when compared to the level of district expenditures. The District's plan, based on current fund balance policy, is to maintain a minimum unassigned General Fund balance of 15 percent of the annual budget. At June 30, 2014, the District has exceeded that policy with an unassigned fund balance as a percentage of 2014 expenditures of 18.6 percent.

The restricted fund balance amounts listed in the table on the previous page mainly represent accumulated assets from capital-related transactions that are restricted for the payment of debt service or future capital-related projects.

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 (net of short-term cash flow borrowing) over the past three years:



The graph above shows the peaks and valleys of the General Fund cash and investments balance (net of borrowing and interfund balances) on a monthly basis. The swing between its high and low month-end cash balances was about $5 million for fiscal 2014. Changes in the state aid payment schedules significantly affect the cash flow of Minnesota school districts. As further described in the Legislative Summary section of this report, the metering of state aids normally paid on a 90–10 schedule has changed several times over the last few years, with the state holdback as high as 40 percent at one point in fiscal year 2012. At June 30, 2014, the metering of state aids was being paid on a 90–10 schedule.

General Fund Operations and Financial Position by Account

The following tables present comparative operating results for some of the accounts of the District's General Fund:

Secondary Education Account

	Year Ended June 30,				
	2010	2011	2012	2013	2014
Revenue and other financing sources	$ 3,892,238	$ 3,888,279	$ 4,225,045	$ 3,823,175	$ 3,391,004
Expenditures	3,807,382	3,872,245	3,967,802	4,135,016	3,471,081
Net change in fund balances	84,856	16,034	257,243	(311,841)	(80,077)
Fund balances					
Beginning of year	1,866,547	1,951,403	1,967,437	2,224,680	1,912,839
End of year	$ 1,951,403	$ 1,967,437	$ 2,224,680	$ 1,912,839	$ 1,832,762

This account experienced a net decrease in fund balance of $80,077 during fiscal 2014. This compares to a budgeted decrease of $223,105. Revenues exceeded budget by $34,136, while expenditures ended the year lower than budget by $108,892.

Total revenue and other financing sources in the Secondary Education Account of the General Fund totaled $3,391,004 for fiscal 2014, a decrease of $432,171 from the previous year, mainly due to shifting targeted services programs back to the local districts in fiscal 2014.

Special Education Account

	Year Ended June 30,				
	2010	2011	2012	2013	2014
Revenue and other financing sources	$ 18,218,537	$ 18,423,168	$ 17,867,527	$ 18,615,960	$ 20,660,172
Expenditures and other financing uses	17,271,862	17,694,715	18,152,937	18,895,373	20,084,109
Net change in fund balances	946,675	728,453	(285,410)	(279,413)	576,063
Fund balances					
Beginning of year	1,214,695	2,161,370	2,889,823	2,604,413	2,325,000
End of year	$ 2,161,370	$ 2,889,823	$ 2,604,413	$ 2,325,000	$ 2,901,063

This account experienced a net increase in fund balance of $576,063 during fiscal 2014, which compares to a budgeted increase in fund balance of $254,511 for the year. Most of this was due to the District receiving better than anticipated state special education aid for both the current year and the final payments for fiscal 2013.

Special Education Account revenues and other financing sources increased $2,044,212 in fiscal 2014 mostly due to an increase in students in these programs in fiscal 2014.

OTHER FUNDS OF THE DISTRICT

Internal Service Funds

The internal service funds are considered proprietary funds and are used to account for dental insurance offered by the District to its employees as a self-insured plan and post-employment employee benefits.

The following table presents comparative operating results for the District's internal service funds over the past five fiscal years:

	Year Ended June 30,				
	2010	2011	2012	2013	2014
Revenue	$ 449,384	$ 590,486	$ 553,360	$ 525,386	$ 552,460
Expenses	591,883	486,642	449,948	519,904	411,914
Change in net position	(142,499)	103,844	103,412	5,482	140,546
Net position					
Beginning of year	(571,875)	(714,374)	(610,530)	(507,118)	(501,636)
End of year	$ (714,374)	$ (610,530)	$ (507,118)	$ (501,636)	$ (361,090)

These funds experienced an increase in net position of $140,546 during fiscal 2014. This occurred mostly as a result of expenses being less than fiscal 2013 by $107,990, while revenue increased by $27,074.

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 governmental 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 financial statements provide information on the total cost of delivering educational services, including capital assets and long-term liabilities.

Theoretically, net position represents District resources available 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, this statement divides net position into three components: net investment in capital assets, restricted, and unrestricted. The following table presents a summarized reconciliation of the District's governmental fund balances to net position, and the separate components of net position for the last three years:

	As of June 30,		
	2012	2013	2014
Net position – governmental activities			
Total fund balances – governmental funds	$ 6,821,235	$ 6,011,062	$ 6,178,520
Total capital assets, net of depreciation	7,606,075	7,441,349	7,248,954
Total long-term debt	(8,004,419)	(7,790,080)	(7,590,332)
Internal Service Fund balance	(507,118)	(501,636)	(361,090)
Other items	2,944	435	(1,901)
Total net position – governmental activities	$ 5,918,717	$ 5,161,130	$ 5,474,151
Net position			
Net investment in capital assets	$ 425,952	$ 636,891	$ 560,535
Restricted	1,336,698	1,126,946	897,218
Unrestricted	4,156,067	3,397,293	4,016,398
Total net position	$ 5,918,717	$ 5,161,130	$ 5,474,151

Some of the District's fund balances translate into restricted net position by virtue of external restrictions (statutory restrictions) or by the nature of the fund they are in (e.g. Food Service Special Revenue Fund balance can only be spent for food service program costs). The unrestricted net position category consists mainly of the General Fund unrestricted fund balances, offset against noncapital long-term obligations such as severance payable.

Total net position increased $313,021 in fiscal 2014. Unrestricted net position increased by $619,105, which is consistent with the operating results of the General Fund.

LEGISLATIVE SUMMARY

The 2014 legislative session began with a projected budget excess for the remainder of the biennium of $1.09 billion, later revised upward to a projected excess of $1.23 billion in the February 2014 economic forecast. In addition to the bonding bill and supplemental budget typically addressed during an even-year short session, the projected excess enabled the Legislature to repay $246 million of K–12 education finance shifts and to replenish the state "Rainy Day Fund" budget reserve with the addition of $150 million. The supplemental budget adopted by the 2014 Legislature contained $54.0 million in additional state aid appropriations for K–12 education for fiscal year 2015, including a $25 increase to the basic general education formula allowance. The 2014 Legislature also adopted a number of technical corrections and modifications to the significant education funding changes adopted by the 2013 legislature.

The following is a brief summary of recent legislative changes and issues affecting the future funding of Minnesota school districts:

Basic General Education Revenue – The per pupil basic general education formula allowance for fiscal year (FY) 2015 was set to increase $504 to $5,806, with simultaneous changes to pupil weights and the general education formula structure reducing the increase to the equivalent of $80 per pupil state-wide. The 2014 Legislature approved an additional $25 increase, bringing the FY 2015 formula allowance to $5,831. This also increases the other aids linked to the formula allowance.

Pupil Unit Weights – Pupil unit weights for FY 2015 will change as follows:

	FY 2014	FY 2015
Pre-Kindergarten and Disabled Kindergarten	1.25	1.0
Part-Time Kindergarten (under 850 instruction hours)	0.612	0.55
All-Day Kindergarten (at least 850 instruction hours)	0.612	1.0
Grades 1–3	1.115	1.0
Grades 4–6	1.06	1.0
Grades 7–12	1.30	1.2

Other Changes to the General Education Formula – A number of other changes were made to general education formula for FY 2015, including:

- Marginal cost pupil units are eliminated and a new declining enrollment revenue component of general education aid is established equal to the decline in adjusted pupil units between the prior year and current year times 28 percent of the basic general education aid allowance.
- The extended time allowance increases from $4,601 to $5,017.
- The gifted and talented revenue allowance increases from $12 to $13.
- The revenue set aside for learning and development is converted to a flat amount per ADM of $299 per kindergarten student and $459 per student in Grades 1 through 6.
- The small schools allowance increases from $522.40 to $544, and the qualifying threshold decreases from 1,000 to 960 pupil units.
- Operating capital revenue increases from $73 per pupil unit + $100 times the building age index to $79 per pupil unit + $109 times the building age index.
- The equity revenue allowance increases from $75 to $80 for sliding scale, and from $46 to $50 for flat rate.
- The pension adjustment reduction to general education aid is eliminated, with districts having a below average pension adjustment guaranteed to receive a minimum of the state average gain from the elimination of the pension adjustment.
- Quality Compensation (Q Comp) revenue is rolled out of the general education formula and established as a separate categorical aid, and the transition revenue calculation is amended to adjust for the roll-out.
- General education revenue generated for all-day kindergarten may be used for programs to meet the needs of 3 and 4-year-olds within the district.

Special Education Funding Reform – State funding for special education is being transitioned to new funding formulas that will be effective beginning in FY 2016.

The funding formula for state special education aid remains the same through FY 2015. For FY 2016, special education will be the lesser of: 62 percent of old formula special education expenditures for the prior year; 50 percent of nonfederal special education expenditures for the prior year; or 56 percent of the amount calculated using a new pupil driven formula based on prior year data.

Beginning in FY 2015, special education tuition billing is changed so that the resident district is responsible for 90 percent of unfunded costs (versus 100 percent currently) and the serving district or charter school is responsible for 10 percent of unfunded costs for open-enrolled students. This does not apply to students placed by tuition agreement, or served by a charter school with at least 70 percent special education students.

Beginning in FY 2016, special education aid will be paid directly to cooperatives and intermediate districts, rather than flowing through the resident districts. Tuition bills will be reduced by the aid paid directly to these entities.

A new special education cross subsidy reduction aid was added for FY 2014 and FY 2015 only. Aid for FY 2015 will equal the lesser of $48 per ADM served or 2.27 percent of the amount generated for the district under the new pupil-based formula, with a state-wide limit of $30 million.

The formula for special education excess cost aid was simplified beginning in FY 2014 by basing the calculation on prior year data and excluding special education tuition receipts and expenditures. For FY 2016, excess cost aid will be the greater of: 56 percent of the difference between the district's unreimbursed nonfederal special education costs and 7 percent of the district's general education revenue; or 62 percent of the difference between the district's unreimbursed old formula special education costs and 2.5 percent of the district's general education revenue.

Teacher Development and Evaluation Aid – For FY 2015 only, school districts, intermediate districts, and charter schools not receiving Q Comp revenue are eligible for teacher development and evaluation aid equal to $302 times the number of full-time equivalent teachers employed on October 1 of the previous school year. The entitlement is limited to $10 million state-wide.

Alternative Learning Center (ALC) Reserve – ALC reserve requirements and tuition billing language was amended to clarify that the amount required to be reserved or paid to the serving district under tuition billing is at least 90 percent *but no more than 100 percent* of general education revenue, and that local optional revenue is not included in the calculation.

General Education Levy Reform – The following changes were made to various elements of the general education tax levy effective FY 2015:

- A uniform general education levy, known as the "student achievement levy," is reestablished. All districts may levy up to the student achievement rate, which is set to raise $20 million state-wide in FY 2015. Districts that levy less than the maximum permitted rate will be subject to a proportionate reduction in its general education aid.
- The equalization factor for operating capital is increased to offset the impact of the student achievement levy.
- Operating referendum revenue is converted from an amount based of resident marginal cost pupil units to an amount based on adjusted pupil units (APUs), due to the elimination of marginal cost pupil units. The separate alternative attendance adjustment is eliminated and rolled into the allowance per APU. The allowance per APU will be set so the total revenue prior to applicable caps is the same as under the old law.

- Districts are allowed to convert up to $300 per APU of existing voter-approved operating referendum revenue to board-approved. Districts with approved operating referendums of less than $300 per APU are permitted to authorize additional referendum revenue up to the $300 per APU limit. Operating referenda will be equalized based on a new, three-tiered formula.
- A new "Location Equity levy" was established, providing school districts with land in the seven-county metro area with authority for a location equity levy of $424 per APU. Districts with adjusted ADM of greater than 2,000 that do not qualify as metro districts are eligible for a location equity levy of $212 per APU. Both levies are equalized at $510,000. Districts may opt out of location equity revenue by a board vote taken by September 1 of the fiscal year preceding the fiscal year when the revenue takes effect (e.g. September 2013 for FY 2015 revenue). Beginning in FY 2016 (levy payable 2015), the name of this levy is changed from "Location Equity" to "Local Option"; does not require districts to have land in the seven-county metro area; and will no longer require a board resolution to opt out of the levy.

Safe Schools Levy – Beginning in FY 2015, the safe schools levy increases from $30 to $36 per pupil unit, with $4 of the increase representing new revenue and $2 to adjust for the changes to pupil weightings. Beginning in FY 2016, the levy allowance for intermediate districts increases from $10 to $15 per pupil unit. The use of this levy is expanded to include facility security enhancements, efforts to improve school climate, and mental health services.

Fund Transfers – The authority for school districts to transfer money from one fund or account to another, as long as the transfer does not increase state aid obligations or increase local property taxes, was extended through FY 2015. School boards may only approve such transfers after adopting a resolution stating that the transfer will not diminish instructional opportunities for students. This authorization excludes transfers from the food service or community service funds, and prohibits transfers from the reserved account for staff development through FY 2015.

Child Nutrition Program Aids – Beginning in FY 2015, state school lunch aid for reduced price lunch students increases from 12.5 cents per lunch to 52.5 cents, making lunches free for those students. State aid for school breakfasts for kindergarten students increases from 55 cents to $1.30, making school breakfasts free for all kindergarten students.

Early Childhood Family Education (ECFE) – Beginning in FY 2015, the ECFE formula is linked to the general education formula, equaling 2.3 percent of the basic general education allowance. For FY 2015, this increases the EFCE allowance from $120 to $134.11. New program requirements were also added related to the assessment of community needs for program services.

School Readiness – Beginning in FY 2015, the state-wide entitlement for school readiness will increase $2 million per year.

Early Learning Scholarships – State-wide funding for early learning scholarships increases $4.65 million for FY 2015 and $4.884 million for later years. The $5,000 limit on scholarships is eliminated beginning in FY 2015, and the Commissioner of Education is directed to establish a target for the average scholarship based on the results of a rate survey.

Community Education Reserve Limits – The limitations on the community education, early childhood family education, and school readiness reserve accounts and the associated aid and levy reductions have been repealed beginning in FY 2014.

Review and Comment – The estimated cost threshold at which facility projects are required to undergo review and comment was raised from $1.4 million to $2.0 million. Facility additions, remodeling, or maintenance projects funded entirely with certain revenue sources (general education, health and safety, alternative facilities, deferred maintenance, lease levies, or facilities bonding), and technology purchases funded with capital projects referendum, are exempted from review and comment. The consultation requirement for smaller projects was eliminated.

ACCOUNTING AND AUDITING UPDATES

GASB STATEMENT NO. 68, *ACCOUNTING AND FINANCIAL REPORTING FOR PENSIONS—AN AMENDMENT OF GASB STATEMENT NO. 27*

The primary objective of this statement is to improve accounting and financial reporting by state and local governments for pensions. This statement replaces the requirements of GASB Statement Nos. 27 and 50, as they relate to pensions that are provided through pension plans administered as trusts or equivalent arrangements that meet certain criteria. The requirements of GASB Statement Nos. 27 and 50 remain applicable for pensions that are not covered by the scope of this statement.

This statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expense/expenditures. In addition, this statement details the recognition and disclosure requirements for employers with liabilities (payables) to a defined benefit pension plan and for employers whose employees are provided with defined contribution pensions. This statement also addresses circumstances in which a nonemployer entity has a legal requirement to make contributions directly to a pension plan. This statement is effective for financial statements for fiscal years beginning after June 15, 2014. Earlier application is encouraged.

Included in this statement are major changes in how employers that participate in cost-sharing pension plans, such as TRA and PERA, account for pension benefit expenses and liabilities. In financial statements prepared using the economic resources measurement focus and accrual basis of accounting (government-wide and proprietary funds), a cost-sharing employer that does not have a special funding situation is required to recognize a liability for its proportionate share of the net pension liability of all employers with benefits provided through the pension plan. A cost-sharing employer is required to recognize pension expense and report deferred outflows of resources and deferred inflows of resources related to pensions for its proportionate share of collective pension expense and collective deferred outflows of resources and deferred inflows of resources related to pensions. In addition, the effects of (1) a change in the employer's proportion of the collective net pension liability and (2) differences during the measurement period between the employer's contributions and its proportionate share of the total of contributions from employers included in the collective net pension liability are required to be determined. These effects are required to be recognized in the employer's pension expense in a systematic and rational manner over a closed period equal to the average of the expected remaining service lives of all active and inactive employees that are provided with pensions through the pension plan.

CHANGES TO FEDERAL GRANT AUDIT REQUIREMENTS

In December 2013, the OMB issued *Uniform Administrative Requirements, Cost Principles, and Audit Requirements for Federal Audits*, which supersedes all or parts of eight OMB circulars; consolidating federal cost principles, administrative principles, and audit requirements in one document. The "Super Circular" includes a number of significant changes to the federal Single Audit process, including: an increase in dollar threshold for requiring a Single Audit from $500,000 to $750,000; changes to the thresholds and process used for determining major programs; reductions in the percentages of expenditures required to be covered by a Single Audit from 50 percent to 40 percent for high risk auditees and from 25 percent to 20 percent for low risk auditees; revised criteria for determining low-risk auditees; and an increase in the threshold for reporting questioned costs from $10,000 to $25,000. Auditees are required to implement the administrative requirements of the new Super Circular by December 26, 2014. The revised audit requirements will be effective for fiscal year 2016 district audits.

COSO INTERNAL CONTROL FRAMEWORK

The clarified auditing standards applicable to governmental audits incorporate a definition of internal control that is based on the internal control integrated framework developed and issued in 1992 by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). In May 2013, COSO issued an updated framework which supersedes the original after December 15, 2014. The new COSO framework retains the basic definition of internal control and its five components established in its original framework, along with the fundamental requirements to consider these five components and to use judgment when assessing and evaluating the effectiveness of a system of internal controls. The new COSO framework enhances and clarifies a number of concepts from the original framework to make it easier to use and apply. One of the more significant enhancements was the establishment of 17 principles, associated with the 5 components of internal control, intended to assist users in understanding the requirements of effective internal control and designing effective systems of internal control.

The 5 components of internal control and 17 underlying principles are as follows:

Control Environment –

1. Organization demonstrates a commitment to integrity and ethical values.
2. Governing body is independent from management and exercises oversight control.
3. Management establishes structure, reporting lines, authority, and responsibilities.
4. Organization demonstrates a commitment to the competence of individuals involved with internal control.
5. Organization holds individuals accountable for internal control responsibilities.

Risk Assessment –

6. Organization specifies clear objectives for the identification and assessment of risks.
7. Organization identifies and analyzes risk.
8. Organization assesses the potential for fraud risks.
9. Organization identifies and assesses significant changes that could impact internal control.

Control Activities –

10. Organization selects and develops control activities to mitigate risks.
11. Organization selects and develops general information technology (IT) controls.
12. Organization establishes and implements control policies and procedures.

Information and Communication –

13. Organization uses relevant, quality information to support internal control.
14. Organization communicates internal control information internally.
15. Organization communicates internal control information externally.

Monitoring –

16. Organization conducts ongoing and/or separate internal control evaluations.
17. Organization evaluates and communicates deficiencies to responsible parties for corrective action.

COSO defines an effective system of internal control as one that reduces to an acceptable level the risk of failing to achieve an organizational objective in the areas of operations, compliance, or reporting. According to the new framework, an organization can achieve effective internal control by applying all of the principles listed above. To achieve this, each of these five components and the relevant principles must be present and functioning, and the five components must operate in an integrated manner. Local governments should be reviewing their internal control systems to assure these principles have been incorporated and implemented.