

Novi Community Schools

Report to the Board of Education

June 30, 2017

To the Board of Education
Novi Community School District

We have recently completed our audit of the basic financial statements of Novi Community School District (the "School District") as of and for the year ended June 30, 2017. In addition to our audit report, we are providing the following results of the audit, informational items, and other comments and recommendations which impact the School District:

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We are grateful for the opportunity to be of service to Novi Community School District. We would also like to extend our thanks to Ms. Jill Minnick and Ms. Deanna Birrell and the entire business office for their assistance and preparedness during the audit. We recognize that preparing for the audit is carried out in addition to your staff's normal daily activities. Should you have any questions regarding the comments in this report, please do not hesitate to call.

Plante & Moran, PLLC

October 12, 2017

Results of the Audit

October 12, 2017

To the Board of Education
Novi Community School District

We have audited the financial statements of Novi Community School District (the "School District") as of and for the year ended June 30, 2017 and have issued our report thereon dated October 12, 2017. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility Under U.S. Generally Accepted Auditing Standards

As stated in our engagement letter dated June 8, 2017, 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 U.S. generally accepted accounting principles. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

As part of our audit, we considered the internal control of the School District. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters.

Our audit of the School District's financial statements has also been conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Under *Government Auditing Standards*, we are obligated to communicate certain matters that come to our attention related to our audit to those responsible for the governance of the School District, including compliance with certain provisions of laws, regulations, contracts, grant agreements, certain instances of error or fraud, illegal acts applicable to government agencies, and significant deficiencies in internal control that we identify during our audit. Toward this end, we issued a separate letter dated October 12, 2017 regarding our consideration of the School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters on July 25, 2017.

Significant Audit Findings

Qualitative Aspects of Accounting Practices

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the School District are described in Note I 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, 2017.

We noted no transactions entered into by the School District during the year for which there is a lack of authoritative guidance or consensus.

We noted no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

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 estimate affecting the financial statements was the School District's share of the MPSERS pension plan net pension liability recorded on the government-wide statements for the implementation of GASB Statement No. 68. The School District's estimate as of June 30, 2017 is approximately \$114,800,000, based on data received from the Office of Retirement Services. We evaluated the key factors and assumptions used to develop the accounting estimate in determining that it is reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements 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 the purpose 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.

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. We did not detect any misstatements as a result of audit procedures.

Significant Findings or Issues

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the School District, and business plans and strategies that may affect the risks of material misstatement with management each year prior to our retention as the School District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition of our retention.

As required by 2 CFR Part 200, we have also completed an audit of the federal programs administered by the School District. The results of that audit are provided to those charged with governance in our report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with 2 CFR Part 200 dated October 12, 2017.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 12, 2017.

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 School 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.

This information is intended solely for the use of the Board of Education and management of Novi Community School District and is not intended to be, and should not be, used by anyone other than these specified parties.

Very truly yours,

Plante & Moran, PLLC



Laura K. Claeys, CPA
Partner



Christopher Geck
Manager

Informational Items

Novi Community School District

Informational Items

Fund Balance Results

For the year ended June 30, 2017, the School District experienced an increase in fund balance of approximately \$1.0 million for the General Fund. As a result, at June 30, 2017, the General Fund fund balance is approximately \$10.2 million and equal to approximately 13.9 percent of General Fund expenditures, which is above the board goal for fund balance. As has been communicated in the past, the expenditures include the “pass-through” of State provided funds for the retirement system. If these expenditures are excluded from the computation of fund balance as a percentage of expenditures, the fund balance would represent 14.87 percent of the net expenditure amount. We commend the board and the administration for their careful consideration of balancing current needs with the long-term planning for the School District’s future needs. School districts throughout the state have been faced with an enormous amount of pressure. The cost to educate a child has outpaced the level of funding increases that districts are receiving each and every year - leaving districts with many tough decisions to make and opportunities to be creative in how they operate. We commend the Novi Community School District for making important and timely decisions in order to continue to provide the best possible education to its students while maintaining fiscal responsibility.

State Aid Funding

State Aid and the Foundation Allowance

State of Michigan funding for public schools continued to focus on several recurring themes for the fiscal year ended June 30, 2017: limited increases in the foundation allowance; additional funding boosts for districts at the minimum foundation; continued student count blending formula; and additional resources dedicated to assisting with funding the district’s retirement/postretirement healthcare obligation (MPERS). One change worth noting was the increase in the number of required school days to 180, up from 175 days, but without a change in the number of required hours of instruction. Many districts were already providing 180 days of instruction, and for those districts, the change did not have an impact.

2016-2017 Foundation: For the 2016-2017 fiscal year, the base foundation increased by \$60, from \$8,169 to \$8,229. The School District’s foundation allowance was increased to \$8,539. For comparison purposes, the School District’s foundation prior to the \$470 cut was \$8,799, meaning the current foundation is \$260/per pupil below the 2011 foundation allowance. If the \$311 per pupil foundation had been restored, using current School District enrollment, this would have represented an additional \$1.7 million in resources for the School District.

2017-2018 Foundation: For the 2017-2018 fiscal year, the base foundation, once again, increases by \$60. Using the pupil count from the June 2017 year end, this increase equates to an additional \$390,000 in funding. New for 2017-2018, an additional per pupil allocation, Section 22n, was created for students counted in high school. For those students, a new categorical providing additional funding of \$25 per pupil was created. This funding is not rolled into the foundation calculation.

Foundation Calculations for Hold Harmless Districts: Due to an inflationary cap on Hold Harmless District Foundation Allowances, which was put in statute along with the school funding reforms tied to Proposal A in 1994, Hold Harmless districts (currently foundation allowances greater than \$8,229) are capped. Last year, the State Aid Act provided funding under Section 20m, which allows the difference between each Hold Harmless district’s inflationary increase and the \$60 increase in the base foundation allowance to be allocated under a separate calculation. This supplemental payment allows Hold Harmless districts to receive the same minimum funding increase as other districts in 2016-2017. For 2017-2018, this allocation has been added back into the district’s foundation allowance, allowing full funding of the foundation for Hold Harmless districts.

Novi Community School District

Informational Items (Continued)

Pupil Membership Blend for 2016-2017 and 2017-2018: The method for counting students was the same for 2016-2017 and for 2017-2018. The funding formula uses calendar year counts with a weighting of 90 percent of the Fall count and 10 percent of the February count. 2016 calendar year counts were used for the 2016-2017 fiscal year funding and 2017 calendar year counts are used for the 2017-2018 fiscal year funding. One significant change for 2017-2018 was an enrollment count cap of .75 for students enrolled in a shared time program. As a result, the district cannot generate more than a .75 FTE for a student participating in a shared time program.

MPSERS Cost Support: Retirement system contributions are a significant part of a district's labor costs. The contribution rate the School District is required to pay continues to rise, though the growth rate has slowed. The School District has no ability to influence the rate and no choice regarding its participation in the program. To aid a district in meeting its obligation, the 2016-2017 State Aid Act continued to include funding to help pay for some of the increased cost. The categorical aid is formula driven using the School District's MPSERS payroll participation data. This funding is provided in two separate sections of the State Aid Act: Section 147a and Section 147c. The School District received a total of \$544,175 of 147a and \$4,822,344 of 147c categorical aid to help offset the impact of its retirement costs. Section 147c was designed to fund approximately 10 percent of covered payroll and does not increase district resources. Instead, the funding is recognized as revenue and then returned directly to the retirement system. In general terms, this means that the total cost of the retirement system contributions in 2016-2017, representing approximately 36 percent of covered payroll, is recognized as an expenditure in the School District's financial statements along with related revenue that was previously considered state support to the system. The net effect is that the School District is responsible for approximately a 26 percent contribution to the retirement system. The School District budgeted for additional state revenue and additional retirement expenditures in order to accommodate this funding mechanism, but may encounter some budget variances due to the fact the state revenue provided is based on prior year School District payroll information.

This retirement funding approach will continue into 2017-2018. However, there are key changes that will impact retirement contributions. The first is the fact that the assumed rate of return within the retirement plan will be decreasing to 7.5 percent from 8 percent. When this assumption is reduced, it has the net effect of increasing the value of the retirement obligation for the plan. This then increases the required contributions to fund the plan. A total of \$48 million has been provided in 147a to pay school districts to offset the impact of this change. Second, for staff hired on or after February 1, 2018, the default employee election will be into a defined contribution (DC) plan; however, an employee can elect the hybrid plan within a specified timeframe. District contributions and state support are also modified for employees electing the DC plan. This will create a change in the district's cost of the benefit for employees new to the retirement system in February 2018. Additional funding is provided under a new State Aid Act, Section 147e, to help support the shift to the new design.

Novi Community School District

Informational Items (Continued)

GASB Statement No. 75 - Postemployment Benefits Other Than Pensions (OPEB)

Effective for the School District's June 30, 2018 financial statements is GASB Statement No. 75, *Accounting and Financial Reporting for Postemployment Benefits Other Than Pensions*. This upcoming GASB addresses reporting by governments that provide postemployment benefits other than pensions (OPEB) to their employees and for governments that finance OPEB for employees of other governments. This OPEB standard will require the School District to recognize on the face of the government-wide financial statements its proportionate share of the net OPEB liability related to its participation in the MPSERS plan. The statement is expected to have a similar impact on the statement of net position as did GASB No. 68 when it was adopted in 2015. Just like GASB No. 68, it is not expected to have an impact on the modified accrual funds (General Fund), and should not impact the School District's budget process. The statement also enhances accountability and transparency through revised note disclosures and required supplementary (or supplemental) information (RSI).

IT Items

Cyber Security

Public schools are not exempt from cyberattacks in which systems and critical data are compromised. School systems store personal information of staff, underage students, and students' parents in addition to other confidential data. It is important that schools protect themselves from both external and internal threats whether they are intentional or accidental threats. For example, ransomware attacks are on the rise and gain media attention with their ability to cripple an organization, including schools and universities. It may be the hacks of large, multi-million dollar companies that we see exposed on the evening news, but public schools can be an enticing target with the amount of data and limited budget to protect themselves.

Here are some questions to think about regarding cybersecurity issues:

- Do you receive a lot of junk email?
- Are you allowed to access risky or unsafe websites?
- Have you attended any security awareness trainings?
- In the event of an incident, are you familiar with who should be contacted?
- Is there a plan in place in the event of a breach and student records are lost?

Because of the many access points within a school district's IT environment, continued assessment of cybersecurity issues is an essential part of the district's overall data security assessment.

Novi Community School District

Informational Items (Continued)

Federal Programs

Written Procedures for Grants - Required for District Federal Grant Participation

As part your annual single audit, we are required to assess the written procedures that exist related to the specific compliance requirements for the federal programs that are selected for testing. The Federal Uniform Guidance, which was effective during the 2014-2015 school year, outlines various requirements related to written procedures and policies. It is important for the School District to be aware of the comprehensive list of required written (board) policies and (administrative) procedures required for federal grant participation. These requirements are described in 2 CFR Part 200 and include the following:

- Written Cash Management Procedures [§200.302(b)(6)]: To implement the requirements of §200.305 payment
- Written Allowability Procedures [§200.302(b)(7)]: To determine the allowability of costs in accordance with Subpart E- Cost Principles
- Written Travel Policy [§200.474(b)]: To ensure costs incurred by employees for travel are reasonable and allowable
- Written Conflict of Interest Policy [§200.318(c)]*: To maintain standards of conduct covering conflicts of interest and governing the actions of its employees engaged in the selection, award, and administration of contracts
- Written Procurement Procedures [§200.319(c)]*: To ensure that all solicitations include the following requirements:
 - i. Incorporate clear and accurate descriptions of technical requirements for the material product or service to be procured
 - ii. Identify all requirements which must be fulfilled
 - iii. Ensure that all prequalified lists of persons, firms, or products which are used in acquiring goods and services are current and include enough qualified sources to ensure maximum open and free competition
- Written Procedures for Conducting Technical Evaluations of Proposals and Selecting Participants [§200.320(d)(3)]*: To maintain a method for evaluation proposals received

*In the Federal Register published on September 10, 2015 (Vol. 80, No. 175), the procurement procedures noted above were formally delayed via an initial two-year grace period. On May 17, 2017, the OMB extended the delay of implementation for an additional year. Therefore, the School District is not required to implement these requirements until July 1, 2018. However, if the extended delay is elected, the School District *must* document this in writing.

The School District should be aware that the aforementioned requirements for written procedures are more extensive in nature than those required for a financial statement audit, which focuses on key controls related to grants management. The Michigan Department of Education has indicated that districts that do not have the requisite written policies and procedures in place may be excluded from future participation in the grants program. In addition, absence of policies and procedures required under the Uniform Guidance could result in single audit findings.

Novi Community School District

Informational Items (Continued)

We encourage the School District to review its policies and procedures to ensure that the items listed above have been addressed and are easily accessible for use and in the event of a fiscal monitoring. Many, if not all, of the items may already be addressed in various forms throughout the School District's policies and procedures; however, it is important the School District be aware of where the written documentation resides. If any items are not currently addressed, we recommend the School District establish the required procedures and document them accordingly.

Procurement Methods

Procurement reform under the Uniform Guidance requires revisions to district purchasing policies and practices when using federal funds. In addition, the Uniform Guidance requires districts to maintain standards of conduct covering conflicts of interest and to maintain specific written procedures for procurement transactions and bid evaluation. The new procurement standards include the following five methods as outlined in 2 CFR Part 200:

- Micro-purchases [§200.320(a)]: acquisition of supplies or services that does not exceed the Micro-Purchase Threshold (outlined in §200.67 Micro-purchase)
- Small purchases [§200.320(b)*]: procurement of services, supplies, or other property that does not exceed the Simplified Acquisition Threshold (outlined in §200.88 Simplified Acquisition Threshold)
- Sealed bids [§200.320(c)*]: bids are publicly solicited for a fixed price contract and awarded to the lowest bidder

In order for sealed bidding to be feasible, the following conditions should be present [§200.320(c)(1)]:

- i. A complete, adequate, and realistic specification or purchase description is available
- ii. Two or more responsible bidders are willing and able to compete effectively for the business
- iii. The procurement lends itself to a firm fixed price contract and the selection of the successful bidder can be made principally on the basis of price.

If sealed bids are used, the following requirements apply [§200.320(c)(2)]:

- i. Bids must be solicited from an adequate number of known suppliers and the invitation for bids must be publicly advertised
- ii. The invitation for bids must define the items or services and include any specifications and pertinent attachments
- iii. All bids will be opened at the time and place prescribed in the invitation for bids
- iv. A firm fixed price contract award will be made in writing to the lowest responsive and responsible bidder
- v. Any or all bids may be rejected if there is a sound documented reason

Novi Community School District

Informational Items (Continued)

- Competitive proposals [§200.320(d)*]: offers are solicited for either a fixed price or cost-reimbursement contract. This method is typically used when it is not appropriate to use the sealed bids methods. The following requirements apply to this method:
 - i. Requests for proposals must be publicized and identify all evaluation factors
 - ii. Proposals must be solicited from an adequate number of qualified sources
 - iii. The non-federal entity must have a written method for conducting technical evaluations of the proposals received and for selecting recipients
 - iv. Contracts must be awarded to the responsible firm whose proposal is most advantageous to the program, with price and other factors considered
 - v. The non-federal entity may use competitive proposal procedures for qualifications-based procurement of architectural/engineering professional services whereby competitors' qualifications are evaluated and the most qualified competitor is selected
- Noncompetitive proposals [§200.320(f)]: procurement through solicitation of a proposal from only one source. This method may be used only when one or more of the following circumstances apply:
 - i. The item is available only from a single source
 - ii. The public exigency or emergency for the requirement will not permit a delay
 - iii. Authorized by the federal awarding agency or pass-through in response to a written request
 - iv. After solicitation of a number of sources, competition is determined inadequate

* Purchases made using either the small purchase, sealed bids, or competitive proposals methods should also consider any state and local purchasing requirements. The State of Michigan Bid Threshold (MCL 380.1274) would apply to purchases of goods. The School District cannot increase the mandated thresholds; however, school district policies could be more restrictive than the federal requirements. The School District should ensure that all relevant thresholds are considered when drafting and implementing policy revisions.

Provisions of the Uniform Guidance allowed entities to elect a delay in the adoption of the procurement provisions and for school districts, the required implementation date is July 1, 2018. The School District has elected the delay and is working to finalize policy and procedure revisions to comply with the new requirements.

Other Comments and Recommendations

Novi Community School District

Other Comments and Recommendations

We commend the business office, especially Deanna Birrell, for the assistance, responsiveness, and receptiveness displayed during the audit process. Her level of professionalism and that of the entire team ensured that the audit was completed in a timely fashion.

As the result of our audit procedures for the year ended June 30, 2017, we offer the following suggestions for your review and consideration:

- **Construction Transactions** - As previously discussed with the finance committee, the School District engaged another CPA firm to review the transactions associated with the Sinking Fund and the 2014 and 2016 Capital Projects Funds for the year ended June 30, 2017. Their agreed-upon procedures letter indicated all transactions were in compliance with Section 1212(1) (Sinking Fund) or Section 1351(a) (2014 & 2016 Capital Projects Funds) of the Revised School Code and the Revised Bulletin for School District Audits of Bonded Construction Funds and Sinking Funds in Michigan.
- **Segregation of Duties** - We offer the following recommendation to the School District as it relates to areas in which segregation of duties could be strengthened, but will need to be balanced with district resources and capacity:
 - Certain school district employees are "super users" for the finance system. They have access to nearly all levels of the financial system, which allows them to initiate transactions, add vendors, perform certain payroll tasks, and process transactions. The School District currently runs edit reports which will identify new transactions and/or changes made to system data in order to verify these changes are supported and approved. The School District also has other detective controls in place to mitigate the lack of segregation of duties caused by having this access. Additionally, we recommend that at least annually the levels of system access for all personnel be reviewed for (1) continued need and (2) changing responsibilities. As of the date of this letter, the School District has changed the super user access in order to segregate certain steps in the processing of transactions.
- **ACH/Wire Transfers** - As a result of our review of the School District's policies and controls surrounding the ACH and wire transfers, we offer the following recommendation to the School District to strengthen the control environment surrounding online banking:
 - Certain employees have the ability to add users to the School District's bank account without the need of a second approval. This ability may undermine the segregation of duties controls that are currently in place over ACH and wire transfers. We recommend that the School District utilize the controls currently offered by its bank, which would require a dual approval for any new user additions requests submitted to the bank. The School District currently has detective controls in place that would likely identify any unauthorized activity in a timely fashion; however, enabling this suggested preventive control would further enhance the School District's internal controls. As of the date of this letter, the School District has revised the approval process as it relates to adding new users to address this comment.
- **Information Technology (IT) Recommendations** - As a result of our review of the School District's policies and controls surrounding the IT environment, we offer the following recommendation:
 - **User Access Lockout** - The current settings of the network allow five invalid login attempts before a user ID is set to inactive. The counter resets automatically after 10 minutes. We recommend that once the number of invalid login attempts is reached, the user ID should be set as inactive until the user who is attempting to login contacts the IT administrator to verify identity prior to having the user ID reset and set to active.