

# **Novi Community School District**

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**Report to the Board of Education**

**June 30, 2014**

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" or the "District") as of and for the year ended June 30, 2014. In addition to our audit report, we are providing the following required audit communication, information items, and other comments and recommendations which impact the District.

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We are grateful for the opportunity to be of service to Novi Community School District. We also express our appreciation to the entire business office staff for the courtesy and cooperation extended to us during the course of the engagement. If there are any questions about your financial reports or the above comments, we are happy to discuss them at your convenience.

*Plante & Moran, PLLC*

October 22, 2014

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, 2014 and have issued our report thereon dated October 22, 2014. 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 May 14, 2014, 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 22, 2014 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.

We are also obligated to communicate certain matters related to our audit to those responsible for the governance of the School District, including certain instances of error or fraud and significant deficiencies in internal control that we identify during our audit. In certain situations, *Government Auditing Standards* require disclosure of illegal acts to applicable government agencies. If such illegal acts were detected during our audit, we would be required to make disclosures regarding these acts to applicable government agencies. No such disclosures were required.

### **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 May 14, 2014.

### **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 1 to the financial statements.

No new accounting policies were adopted and the application of existing policies was not changed during 2014.

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

There are 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. There were no significant balances, amounts, or disclosures in the financial statements based on sensitive management estimates.

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***

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 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.

***Management Representations***

We have requested certain representations from management that are included in the management representation letter dated October 22, 2014.

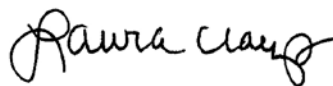
***Management Consultations with Other Independent Accountants***

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 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



Christopher Geck

## **Informational Items**

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# Novi Community School District

## Informational Items

These items have been discussed with the administration and are presented here for your information as the policy-making body of the School District.

### State Aid Funding

**State Aid and the Foundation Allowance** - The fiscal year ended June 30, 2014 saw continued focus on several recurring themes in school funding by the State of Michigan: limited increases in the foundation allowance; additional funding boosts for districts at the Minimum Foundation; additional resources dedicated to assisting with funding the districts' retirement/post-retirement health care obligation (MPSERS); and resources for best practice and student performance. While districts experienced an increase in the foundation, the increases still have not replaced the \$470 per pupil cut experienced in 2011-2012.

**2013-2014 Foundation** - For the 2013-2014 fiscal year, the School District's foundation allowance was increased to \$8,359. For comparison purposes, the School District's foundation prior to the \$470 cut in fiscal 2011 was \$8,799, meaning the current foundation is \$440/per pupil below the 2011 foundation allowance.

**2014-2015 Foundation** - Based on the new State Aid Act, your School District will receive a \$50 increase in its foundation allowance, representing an increase of 0.5 percent, to \$8,409 per pupil.

**Best Practice** - Instead of mandating certain activities, the governor identified many educational initiatives shortly after taking office and has used best practice funding to provide resources when a district performs the identified activities. Each year the list of criteria is modified and if a district chooses to, they must meet the criteria in order to receive the funding. The amount provided in 2013-2014 was maintained at the same level as in 2012-2013 - \$52 per pupil. In 2013-2014, to qualify for this incentive, the School District was required to meet seven of eight identified best practice initiatives. Your School District qualified for the \$52/pupil in 2013-2014 which resulted in \$331,618 of incentive dollars. For 2014-2015, the per pupil allocation was reduced to \$50/pupil and now requires the School District to meet seven of nine best practice criteria.

**MPSERS Cost Support** - The contribution rate the School District is required to pay continues to rise. The School District has no ability to influence the rate and no choice regarding its participation in the program. Recognizing the costs are increasing under the current system, the 2013-2014 and 2014-2015 State Aid Acts 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 - 147a and 147c. The School District received a total of \$534,445 of 147a and \$1,977,440 of 147c categorical aid to help offset the impact of the increase in the retirement costs.

# **Novi Community School District**

## **Informational Items (Continued)**

The 2014-2015 State Aid Act continues this MPSERS cost support categoricals. The School District Section 147c was designed to fund approximately 4 percent of 2013-2014 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 2013-2014, representing approximately 29 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 an approximate 25 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 continues into 2014-2015, along with an additional retirement categorical, 147d, which will operate similarly and in addition to 147c. The net effect of all these changes for 2014-2015 is that the School District's net out-of-pocket contribution will increase to an estimated 25.78 percent, up about 1 percent from the previous year, but the total cost of the retirement system will have grown to an estimated 34.54 percent.

### **Other State Aid Act Changes Impacting 2014-2015**

The amendments to the State Aid Act made several other changes impacting school districts. Several changes we identified that could impact the School District include:

**Change in District Required Filing Dates** – Currently, the School District must submit its audit report and its FID report to the Michigan Department of Education (MDE) by November 15. Beginning with the 2015 fiscal year, the reports will be due to the MDE on October 15. This significant acceleration will require districts and auditors to carefully plan the closing of the school district's books, the completion of the audit, and meetings with the Board of Education to ensure the 2015 filing deadlines are met. There has continued to be legislative discussion as to whether October 15 is a realistic date for filing, but for now it is law. We will continue to keep you apprised of any changes in this area. Also included in this accelerated filing date is certain information related to student counts, which will impact your pupil accounting personnel.



# Novi Community School District

## Informational Items (Continued)

### Accounting Items

#### **GASB Statement No. 68 - Pension Standards**

*Accounting and Financial Reporting for Pensions* is effective for the School District's June 30, 2015 financial statements. Statement No. 68 requires governments providing defined benefit pensions to recognize their unfunded pension benefit obligation as a liability for the first time, and to more comprehensively and comparably measure the annual costs of pension benefits. Due to the School District's participation in the Michigan Public School Employees' Retirement System (MPSERS), the School District will be required to report the School District's share of the MPSERS pension plan net pension liability in the basic financial statements (at the government-wide level and in proprietary funds - but not in governmental funds). While the School District has a very small share of the statewide net pension liability (less than 1 percent), the obligation the School District will record will be significant. Most of the needed data required to record this liability will come from the retirement system using the plan's September 30, 2014 fiscal year-end financial information. Changes in the net pension liability will generally be reported as pension expense at the government-wide level and in proprietary funds. Currently, the unfunded liability associated with retiree health care is not included in the computation, but will likely be added in the future. The Statement also enhances accountability and transparency through revised note disclosures and required supplementary information (RSI).

Some factors to focus on as the School District prepares for adoption of this standard include:

- The Office of Retirement Services is working on an implementation plan to assist districts in obtaining needed information.
- Since the obligation is so significant, documentation showing the calculation is accurate will need to be developed and audited. The current plan is the Auditor General's office will perform needed tests on most of the information and the information will be made available to the school district.
- For virtually all districts, once the obligation is included in the financial statements, it is likely the government-wide financial statements will report a negative net position. The State and bond rating agencies understand this fact and it should not adversely affect the assessment of the School District's financial position, as both agencies have been considering this obligation for quite some time in their assessments of districts and other agencies.
- As stated above, the adoption of the standard will not impact the MPSERS expenditures reported in the General Fund and will not impact General Fund fund balance.
- Disclosures regarding the plan and data related to the plan will be significantly expanded in the School District's financial statements.

# **Novi Community School District**

## **Informational Items (Continued)**

Once the plan's fiscal year is ended and the audit of the MPSERS plan is completed by the State of Michigan, we will have a clearer picture of the total net pension liability and the School District's proportionate share. At that time we will work closely with the School District, ORS, the Michigan Department of Education, and the Auditor General to ensure all the needed information is in place to make the adoption as smooth as possible.

### **Written Procedures for Grants - Required for District Federal Grant Participation**

As part of your single audit, annually, the auditors are required to assess the written procedures that exist related to the specific compliance requirements for the federal programs that are selected for testing. It is important for the School District to be aware of the comprehensive list of required written procedures required for federal grant participation. The Michigan Department of Education continues to emphasize the importance of maintaining adequate written procedures for grants, as discussed in the 2012-2013 Accounting and Audit Alert. The department has added example procedures to the Office of Audits website for reference.

These requirements are described in 34 CFR Part 80, 2 CFR Part 215, and OMB Circular A-133 Compliance Supplement Part 6 and include the following:

- Financial management systems
- Payments
- Allowable costs
- Period of availability
- Matching or cost sharing (if applicable)
- Program income (if applicable)
- Procurement
- Equipment and real property (if applicable)
- Supplies
- Copyrights (if applicable)
- Subawards to debarred and suspended parties
- Monitoring and reporting program performance (if applicable)
- Financial reporting
- Retention and access requirements for records
- In addition, districts should also have written procedures for:
  - Cash management
  - Conflict of interest
  - Payroll
  - Federal timekeeping

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 focus 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.

# Novi Community School District

## Informational Items (Continued)

We encourage the School District to review its procedures and the documentation of such 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. The procedure itself is not required to be specific to federal grants as long as it has applicability to the grants as well. Many, if not all, of the items may already be addressed in various different 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. The MDE has made sample procedures available on its website to either be used as a guide or implemented as provided. These provided procedures are viewed as "safe harbor" and the MDE will accept its approved documents as demonstrated compliance with the rules. The documents can be located at [www.michigan.gov/mde](http://www.michigan.gov/mde) on the Office of Audits webpage.

### New Rules Governing Management of Federal Programs

In December 2013, the Office of Management and Budget (OMB) issued long-awaited reforms to the compliance requirements that must be followed by non-federal entities receiving federal funding. All school districts receiving federal dollars will need to understand the changes made as a result of these reforms and may be required to make some changes to your internal procedures, processes, and controls.

These reforms impact three key areas of federal grants management:

1. **Audit Requirements** - For fiscal years beginning on or after January 1, 2015 (fiscal year ending June 30, 2016 for Michigan schools), the threshold for obtaining a federal awards audit will increase from the current threshold of \$500,000 of annual federal spending to \$750,000. There will also be significant changes to the criteria for qualifying as a low-risk auditee and a reduction in the number of major programs required to be tested for some districts.

The School District has historically been above the new \$750,000 threshold. However, from time to time, depending upon the level of federal spending, the School District may drop below the audit requirement threshold and monitoring of federal program expenditures will be important to ensure compliance with the audit requirement.

2. **Cost Principles** - Effective December 26, 2014, the grant reforms related to cost principles go into effect. Not only were certain changes made to allowable costs under this new guidance, but there were significant changes in the area of time and effort reporting and indirect costs. The State of Michigan will have a significant impact on how these changes will be applied to Michigan schools, as they often have different requirements than the federal government in this area.

# Novi Community School District

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## Informational Items (Continued)

- 3. Administrative Requirements** - Also effective December 26, 2014, non-federal entities receiving federal funding must adhere to new rules related to administering federal awards. Most notably, these requirements may impact the School District's procurement systems, including maintaining written conflict of interest policies and disclosures as well as updated grants management policies and procedures. The MDE has indicated that failure to adhere to these rules could result in the disqualification for participation in federal programs through the MDE. Please note, these requirements are more stringent than those required under your federal program audit, which focuses on key controls versus overall process.

These revisions are clearly the most significant changes to occur to federal grants management in recent history. School districts receiving federal funding will need to carefully digest these changes as the application of these changes will need to be assessed on a district-by-district basis. Plante & Moran, PLLC has many school district grants experts in these rules who will be working closely with the Michigan Department of Education regarding these changes and can assist you in understanding the changes and how they impact the School District. During the spring of 2014, we provided two webinars on the grants management changes. Those webinars are archived and available at no charge on our website to assist districts in increasing their understanding of the changes. As we continue to delve into these new rules, we will keep you informed and updated.

## **Other Comments and Recommendations**

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# Novi Community School District

## Other Comments and Recommendations

We commend the business office, especially Carmen Jaroslowski, 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, 2014, 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 for the year ended June 30, 2014. Their agreed-upon procedures letter indicated all transactions were in compliance with Section 1212(1) 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. These reports should be reviewed by individuals other than those who can make changes. 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.
- **Wire Transfers and ACH Transactions** - As the use of technology increases between organizations, many more vendors are requesting funds to be remitted via ACH or wire transfer. The School District currently only makes regular electronic transfers between their own accounts and ACH payments to the Michigan Public Schools Employees' Retirement System (and the IRS). We recommend the School District review their policies related to wire transfers and consider if any policy changes are needed as the volume of electronic activity increases over time. A key control around wire transfers is making sure appropriate authorization/approval is received prior to the wire being executed. The control associated with these wires is usually achieved by having another person beyond the one initiating the transaction provide authorization/approval before the transaction is executed. Most organizations use this control, but after the wires are already completed. We recommend the School District review the timing of approvals and determine if changes in this control should be implemented in order to prevent wires from being initiated and made to the wrong locations. Our understanding is the bank has already been contacted about implementing this control.

# Novi Community School District

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## Other Comments and Recommendations (Continued)

- **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 recommendations.
  - **User Access Review** - We noted that management does not review user access to systems. We recommend that management implement a process to review user access at least annually. This is best achieved when the review is performed by someone other than IT (as they administer access). Access reports should be provided by IT to each supervisor or human resources for review of access. Any exceptions should be clearly documented with IT remediation.
  - **User Access** - 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.