

October 23, 2013

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, 2013 and have issued our report thereon dated October 23, 2013. 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 2, 2013, 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 23, 2013 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 2, 2013.

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.

As described in Note 1, the School District changed accounting policies related to the implementation of Governmental Accounting Standards Board Nos. 62, 63, and 65. Accordingly, the accounting change has been retrospectively applied to prior periods presented as if the policy had always been used.

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

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. Management has corrected all such misstatements.

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 23, 2013.

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.

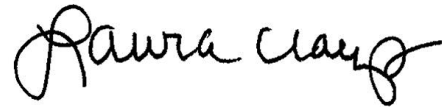
To the Board of Education
Novi Community School District

October 23, 2013

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

A handwritten signature in black ink that reads "Laura Claeys". The signature is written in a cursive style with a large initial "L" and a long, sweeping underline.

Laura K. Claeys

A handwritten signature in black ink that reads "Christopher Geck". The signature is written in a cursive style with a large initial "C" and a long, sweeping underline.

Christopher Geck

Informational Items

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.

Redefining State Aid and the Foundation Allowance - The fiscal year ended June 30, 2013 was the second year under a redefined funding approach for Michigan schools. While the foundation allowance concept continues, changes in the funding strategy significantly impacted your School District's 2012-2013 funding level and, with some modifications, those changes carry forward into 2013-2014. The three changes are a permanent reduction of the School District's foundation allowance, use of an incentive payment concept (best practice and student performance), and an additional categorical to aid in paying for the significantly increased cost of the retirement system (MPSERS).

- **Foundation Allowance** - After receiving a per pupil foundation reduction of \$470 in 2011-2012, for the 2012-2013 fiscal year the School District's foundation allowance was \$8,329. For the 2013-2014 fiscal year, the base foundation increases by \$30 to \$8,359. This increase represents a 0.4 percent increase in the foundation allowance funding.
- **Best Practices** - The governor identified many educational initiatives shortly after taking office. One key initiative was the concept of encouraging best practices. This concept was built into the State Aid Act for the first time in 2011-2012. This concept continued into 2012-2013 and 2013-2014. For 2012-2013, the concept of funding best practices included new initiative criteria listed in the State Aid Act. The amount provided \$52 per pupil in 2012-2013 and 2013-2014. To qualify for this incentive, the School District is required to meet seven of eight identified best practice initiatives. These incentives are not guaranteed past the 2013-2014 year. A new best practice item has been added to include the addition of new items to a district's dashboard requesting revenue and expenditure projections for 2014-2015, a list of all debt service obligations by project, anticipated debt payments for fiscal year 2013-2014, and total outstanding debt. Your School District qualified for the \$52 per pupil funding in 2012-2013, and this amounted to \$331,618. It is expected you will apply for and receive the best practice funding for 2013-2014.
- **MPSERS Cost Support** - As the board is well aware, the contribution rate the School District is required to pay has continued 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 2012-2013 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. The School District received \$806,027 in categorical aid to help offset the impact of the increase in the retirement costs, under what is termed Section 147a categorical funding. The 2013-2014 State Aid Act continues this MPSERS cost support categorical, but at a lower level. The impact of this reduced support was \$44 per pupil.

Novi Community School District

Informational Items (Continued)

In addition, near the end of the 2012-2013 fiscal year, the State determined that additional support the State was paying into the retirement system would now be distributed to the School District via their State Aid Status report, and then remitted by the School District, in the exact same amount, to the Office of Retirement Services. This is termed the Section 147c categorical funding and amounted to \$763,451. This payment represents approximately 4 percent of covered payroll and does not increase School 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, 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. This retirement funding approach continues into 2013-2014. The School District budgeted for additional State revenue and additional retirement expenditures in order to accommodate this funding mechanism.

Close attention should be paid to these two categorical items (Sections 147a and 147c) as they represent support for the retirement system. If they are not appropriated in the future and the plan is not changed, the required contributions for the School District to this plan will undoubtedly increase.

Other State Aid Act Changes Impacting 2013-2014

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:

- **Pupil Count Weighting** - School District membership blend will be based on a 90/10 split. The funding will be based on 90 percent of the October pupil count and 10 percent of the following February pupil count. This means when the initial fiscal year budget is prepared, 100 percent of student counts and, therefore, foundation revenue is not known, since the February count will not yet have occurred.

In addition, for the first time, if a student moves to another school district after the count date, the receiving district can claim a pro-rata share of the count with the "sending" district having a like reduction. The tracking of students has become exponentially more complex and now involves reporting and coordination through the Intermediate School District and the State of Michigan. Since the reporting and changes for student movement occurs after the October count, the October pupil count will not be "final" until the following spring, thereby increasing the complexity the School District faces in estimating revenue each year.

- **Online Learning** - New in 2013-2014, the School District must offer online learning to students in grades 5-12. A student can enroll in up to two courses per term, semester, trimester, etc. The cost of each course is capped at 1/12th of the foundation amount per semester.

Novi Community School District

Informational Items (Continued)

Grant Related Items

Fiscal Monitoring - The Michigan Department of Education (MDE) continues to focus on the grants fiscal monitoring process. This process focuses on the financial aspects of grants management with an emphasis on control procedures assessments in the key compliance areas of the grant. These actions continue as part of the increased federal emphasis for pass-through entities (the State of Michigan) to improve their monitoring efforts. To assist districts in their compliance efforts, the State has issued a self-evaluation checklist which will allow districts to identify areas which may require additional attention. In addition, the MDE has developed sample written compliance procedures for districts to consider when improving the quality of documentation maintained by the School District. We highly recommend the School District obtain the checklist and the sample procedures (located on the MDE website) and self-assess their processes and documentation against the types of items the MDE is focused upon.

Written Procedures for Grants

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

Novi Community School District

Informational Items (Continued)

The School District should be aware the written procedures are more extensive in nature than the written documentation required for a financial statement audit, which focuses on key controls related to grants management.

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. 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. It is important the School District be aware of where the documentation resides to cover the items listed above. The MDE has been performing Federal Program Fiscal Monitoring and will request these procedures when on site. If any items are not currently addressed, we recommend the School District evaluate putting procedures in place and document them accordingly. The MDE has placed sample policies on their website which can be used as either a guide or implemented as provided. Please note the MDE views these as "safe harbor" and will accept their approved documents as demonstrated compliance with the rules. The documents can be located at www.michigan.gov/mde and then navigate to the Office of Audits webpage.

GASB Statement No. 68, Pension Standards

In June 2012, the GASB issued GASB Statement No. 68, *Accounting and Financial Reporting for Pensions*, which will be 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 difference between the School District's share of the MPSERS pension plan net assets and the pension obligation liability as an asset or liability in the basic financial statements (at the government-wide level and in proprietary funds - but not in governmental funds). This will be called the "net pension liability" or "net pension asset." The data required to record this liability will come from the retirement system. 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 may be added in the future. The statement also enhances accountability and transparency through revised note disclosures and required supplemental information (RSI).

Other Comments and Recommendations

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, 2013, we offer the following suggestions for your review and consideration:

- **Federal Grant Compliance - Child Nutrition Grant** - The School District is required to perform Annual Onsite Reviews at each building by February 1 of each year. We recommend that the School District ensure the reviews are being performed timely by maintaining a tracking sheet for each building that has been visited.
- **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:
 - 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.
- **Cash Handling and Wire Transfers**
 - **Cash Deposits at School Buildings** - At one of the school buildings, we noted that funds are received, tallied, and prepared for deposit by the same individual. The teacher that remits the funds to the building secretary signs a log book indicating the amount remitted to the secretary; however, no receipt is provided to the teacher in case of any subsequent discrepancies between the actual deposit and amount actually remitted to the secretary occur. We recommend the School District implement a system whereby all individuals remitting funds to building secretaries are provided with a receipt that is signed by both the individual remitting the funds and the secretary that collects it and prepares the deposit.
 - **Intradistrict Transfers** - At one of the school buildings, we noted that the secretary collects "pay to participate" funds after the beginning of school year registration period. In general, the secretary does not count the cash and log in the receipt if it will be transferred to the High School Athletic Department. Once received by the Athletic Department, the cash is logged and counted. We recommend the School District implement a receipt log of all cash collected so that there is a proper tracking mechanism as cash is transferred between schools, departments, etc. and then ultimately deposited into the bank.

Novi Community School District

Other Comments and Recommendations (Continued)

- **Wire Transfers** - Organizations are using wire transfers more frequently to move money between various accounts as well as to pay certain vendors. 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 made to the wrong locations.
- **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. We have been informed that the School District plans to provide a listing of employees and access rights to human resources on an annual basis commencing during fiscal year 2014.
 - **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. It is our understanding these recommendations will be addressed in December.
 - **Password Complexity - Network** - Network passwords are not set to expire. We recommend that network passwords be set to expire every 30 days and that the same password cannot be used more than once over a one-year period. We also recommend that the minimum required password length be increased. It is our understanding these recommendations will be addressed in December.