

Management Report

for

Independent School District No. 281  
New Hope, Minnesota

June 30, 2018

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PRINCIPALS

Thomas A. Karnowski, CPA  
Paul A. Radosevich, CPA  
William J. Lauer, CPA  
James H. Eichten, CPA  
Aaron J. Nielsen, CPA  
Victoria L. Holinka, CPA/CMA  
Jaclyn M. Huegel, CPA

To the School Board and Management of  
Independent School District No. 281  
New Hope, Minnesota

We have prepared this management report in conjunction with our audit of Independent School District No. 281, Robbinsdale Area Schools' (the District) financial statements for the year ended June 30, 2018. 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  
January 7, 2019

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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, *GOVERNMENT AUDITING STANDARDS*, AND TITLE 2 U.S. CODE OF FEDERAL REGULATIONS PART 200, *UNIFORM ADMINISTRATIVE REQUIREMENTS, COST PRINCIPLES, AND AUDIT REQUIREMENTS FOR FEDERAL AWARDS (UNIFORM GUIDANCE)***

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, 2018. Professional standards require that we provide you with information about our responsibilities under auditing standards generally accepted in the United States of America, *Government Auditing Standards*, and the Uniform Guidance, 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, 2018:

- We have issued an unmodified opinion on the District's basic financial statements.
- We reported one deficiency in the District's internal control over financial reporting that we considered to be a significant deficiency. During our audit, we noted that the monthly cash reconciliations were not being completed in a timely and accurate manner.
- The results of our testing disclosed no instances of noncompliance required to be reported under *Government Auditing Standards*.
- We reported that the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the basic financial statements.
- We reported one matter involving the internal control over compliance and its operation that we consider to be a material weakness in our testing of major federal programs, which also resulted in a reportable instance of noncompliance with the types of compliance requirements that could have a direct and material effect on the District's major federal program.

The District did not have adequate internal control procedures over allowable costs/costs principles to ensure that all costs charged to the federal Title I program met the standard for an allowable cost as defined by Uniform Guidance. This resulted in salary and benefits costs for employees not working in the Title I program being recorded in the general ledger as Title I expenditures and included in reimbursement claims throughout the 2018 fiscal year. The District subsequently reviewed and corrected all salaries and benefits charged to the Title I program prior to completing its final reimbursement request and Schedule of Expenditures of Federal Awards for the year ended June 30, 2018.

- 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, 2018 in accordance with the financial reporting provisions of the Minnesota Department of Education (MDE) (regulatory basis of accounting). Our opinion was qualified for a limitation related to the completeness of cash receipts reported.

We reported one deficiency involving internal control 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 prenumbered receipts, prenumbered admission tickets for events, 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 MDE *Manual for Activity Fund Accounting*, in which we reported no findings.

## **FOLLOW-UP ON PRIOR YEAR FINDINGS AND RECOMMENDATIONS**

As a part of our audit of the District's financial statements for the year ended June 30, 2018, we performed procedures to follow-up on any findings and recommendations that resulted from our prior year audit. In the prior year, we reported the following findings that have been corrected by management:

- The District did not have documented written controls to ensure compliance with OMB Uniform Guidance cash management, allowable costs, subrecipient monitoring, and financial management standards. Written controls were established during the year ended June 30, 2018.
- In the prior year, 4 of 40 claims tested were not paid within the required statutory 35-day time period, and interest was not paid on the claims. All claims tested for the current year were paid within the 35-day statutory time period allowed.

## **OTHER COMMENTS AND RECOMMENDATIONS**

**Negative Lunch Account Balances** – During our audit, we noted that the District has significant receivables recorded in its Food Service Special Revenue Fund related to individual student lunch accounts with deficit balances. We recommend the District review its policies and internal controls regarding limitations and collections of negative lunch account balances. Negative lunch account balances should be evaluated for collectability, and accounts deemed uncollectable should be eliminated through a transfer from the General Fund.

**Unclaimed Property** – State statutes require government entities with unclaimed property held for more than three years to file an unclaimed property report and remit the unclaimed property to the state Commissioner of Commerce. During our audit, we noted several outstanding District checks issued more than three years ago. We recommend the District review its outstanding check listing and remit all unclaimed property to the Commissioner of Commerce at least annually.

## **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, 2018. However, the District implemented the following governmental accounting standards during the fiscal year ending June 30, 2018:

- Governmental Accounting Standards Board (GASB) Statement No. 85, *Omnibus 2017*, which addresses issues that have been identified during implementation and application of certain GASB statements.

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.

## **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:

General education revenue and certain other revenues are computed by applying an allowance per student to the number of students served by the District. Student attendance is accumulated in a state-wide database—MARSS. Because of the complexity of student accounting and because of certain enrollment options, student information is input by other school districts and the MARSS data for the current fiscal year is not finalized until after the District has closed its financial records. General education revenue and certain other revenues are computed using preliminary information on the number of students served in the resident district and also utilizing some estimates, particularly in the area of enrollment options.

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) and pension benefits. These obligations are calculated using actuarial methodologies primarily described in GASB Statement Nos. 68, 74, and 75. These actuarial calculations include significant assumptions, including projected changes, healthcare insurance costs, investment returns, retirement ages, proportionate share, and employee turnover.

The depreciation of capital assets involves estimates pertaining to useful lives.

The District's self-insured activities require the recording of liabilities 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.

#### **CORRECTED AND UNCORRECTED MISSTATEMENTS**

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. There were no misstatements detected as a result of audit procedures that were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

#### **DISAGREEMENTS WITH MANAGEMENT**

For purposes of this letter, a disagreement with management is a financial accounting, reporting, or auditing matter, whether or not resolved to our satisfaction, that could be significant to the financial statements or the auditor's report. We are pleased to report that no such disagreements arose during the course of our audit.

#### **DIFFICULTIES ENCOUNTERED IN PERFORMING THE AUDIT**

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

#### **MANAGEMENT REPRESENTATIONS**

We have requested certain representations from management that are included in the management representation letter dated January 7, 2019.

#### **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 the management's discussion and analysis and the pension and OPEB-related 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 accompanying the financial statements, and the separately issued Schedule of Expenditures of Federal Awards and the Uniform Financial Accounting and Reporting Standards (UFARS) Compliance Table, 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 statistical section, which accompany the financial statements but are not RSI. Such information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on it.

## FUNDING PUBLIC EDUCATION IN MINNESOTA

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.

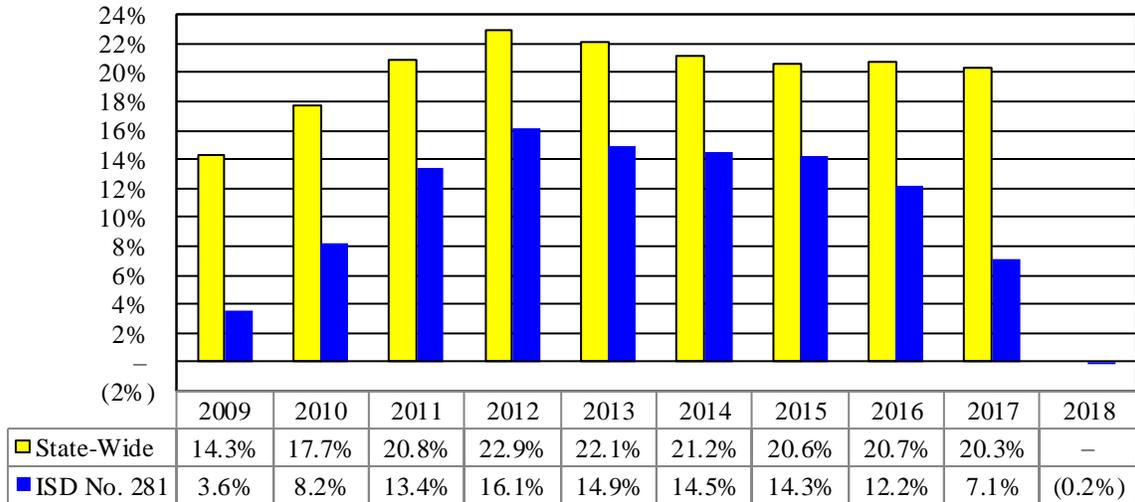
The table below presents a summary of the formula allowance for the past decade and as approved for the 2019 fiscal year. The amount of the formula allowance and the percentage change from year-to-year excludes temporary funding changes, the “roll-in” of aids that were previously funded separately, and changes that may vary dependent on actions taken by individual districts. The \$529 increase in 2015 was offset by changes to pupil weightings and the general education aid formula that resulted in an increase equivalent to approximately \$105, or 2.0 percent, state-wide.

Fiscal Year Ended June 30,	Formula Allowance	
	Amount	Percent Increase
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 %
2016	\$ 5,948	2.0 %
2017	\$ 6,067	2.0 %
2018	\$ 6,188	2.0 %
2019	\$ 6,312	2.0 %

## 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 2018.

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. We have also included the comparable percentages for your district.

During the economic downturn that began in 2008, the average unrestricted fund balance as a percentage of operating expenditures maintained by Minnesota school districts increased, peaking at 22.9 percent at the end of fiscal 2012. This trend reflected districts' efforts to limit budget cuts, retain educational programs, and maintain adequate operating cash flow during a period of uncertain funding. As the state's economic condition improved in subsequent years, this ratio has gradually decreased to 20.3 percent at the end of fiscal 2017.

The District's unrestricted operating fund balance as a percentage of operating expenditures was a deficit of 0.2 percent at the end of the current year, as compared to 7.1 percent at June 30, 2017. Statutory operating debt exists if this ratio reaches a deficit of 2.5 percent at year-end.

The table below shows a comparison of governmental fund revenue per ADM received by Minnesota school districts and your district. Revenues for all governmental funds are included, except for the Capital Projects – Building Construction and OPEB Debt Service Funds. Other financing sources, such as proceeds from sales of capital assets, insurance recoveries, bond sales, loans, and interfund transfers, are also excluded.

<b>Governmental Funds Revenue per Student (ADM) Served</b>								
	State-Wide		Seven-County Metro Area		ISD No. 281 – Robbinsdale Area Schools			
	2016	2017	2016	2017	2016	2017	2018	
<b>General Fund</b>								
Property taxes	\$ 1,777	\$ 1,933	\$ 2,342	\$ 2,516	\$ 2,802	\$ 2,985	\$ 2,864	
Other local sources	495	515	392	423	285	270	298	
State	9,271	9,386	9,357	9,387	9,404	9,483	9,773	
Federal	432	450	447	480	477	432	452	
Total General Fund	<u>11,975</u>	<u>12,284</u>	<u>12,538</u>	<u>12,806</u>	<u>12,968</u>	<u>13,170</u>	<u>13,387</u>	
<b>Special revenue funds</b>								
Food Service	548	561	545	557	603	621	622	
Community Service	591	628	692	733	692	773	809	
Debt Service Fund	<u>1,053</u>	<u>1,119</u>	<u>1,084</u>	<u>1,118</u>	<u>1,276</u>	<u>1,417</u>	<u>1,527</u>	
Total revenue	<u>\$ 14,167</u>	<u>\$ 14,592</u>	<u>\$ 14,859</u>	<u>\$ 15,214</u>	<u>\$ 15,539</u>	<u>\$ 15,981</u>	<u>\$ 16,345</u>	
ADM served per MDE School District Profiles Report (current year estimated)					<u>12,820</u>	<u>12,601</u>	<u>12,478</u>	
Note: Excludes the Capital Projects – Building Construction and OPEB Debt Service Funds.								
Source of state-wide and seven-county metro area data: School District Profiles Report published by the MDE								

ADM used in the table above is based on enrollments consistent with those used in the MDE School District Profiles Report, which includes extended time ADM, and may differ from the ADM reported in other tables.

The mix of local and state revenues vary from year to year, primarily based on funding formulas and the state’s financial condition. The mix of revenue components from district to district varies, due to factors such as the strength of property values, mix of property types, operating and bond referendums, enrollment trends, density of population, types of programs offered, and countless other criteria.

Changes in enrollment also impact comparisons in the table above and on the next page when revenue and expenditures are based on fixed costs, such as debt levies and principal and interest on outstanding indebtedness.

The District earned approximately \$204.0 million in the governmental funds reflected above in fiscal 2018, an increase of \$2.6 million (1.3 percent) from the prior year, or \$364 per ADM served.

General Fund property tax revenue decreased \$1.9 million, due to decreases in several components of the general tax levy. General Fund revenue from state sources was about \$2.5 million or \$290 per ADM higher than the prior year, resulting from the increase in the basic general education formula allowance discussed earlier as well as increases in special education funding and general education compensatory funding. Debt Service Fund revenue was \$1.2 million, or \$110 per ADM, higher than last year, primarily due to an increase in property taxes levied for debt service.

The following table reflects similar comparative data available from the MDE for all governmental fund expenditures, excluding the Capital Projects – Building Construction and OPEB Debt Service Funds. Other financing uses, such as bond refundings and transfers, are also excluded.

<b>Governmental Funds Expenditures per Student (ADM) Served</b>								
	State-Wide		Seven-County Metro Area		ISD No. 281 – Robbinsdale Area Schools			
	2016	2017	2016	2017	2016	2017	2018	
<b>General Fund</b>								
Administration and district support	\$ 960	\$ 991	\$ 958	\$ 996	\$ 806	\$ 1,079	\$ 951	
Elementary and secondary regular instruction	5,466	5,539	5,849	5,887	6,444	6,388	6,095	
Vocational education instruction	158	166	146	153	140	119	111	
Special education instruction	2,182	2,225	2,330	2,334	2,164	2,222	2,524	
Instructional support services	622	660	725	765	817	1,102	1,239	
Pupil support services	1,019	1,074	1,104	1,165	1,145	1,224	1,376	
Sites and buildings and other	890	906	847	870	1,112	1,199	1,327	
Total General Fund – noncapital	11,297	11,561	11,959	12,170	12,628	13,333	13,623	
General Fund capital expenditures	600	627	532	592	406	208	452	
Total General Fund	11,897	12,188	12,491	12,762	13,034	13,541	14,075	
<b>Special revenue funds</b>								
Food Service	542	550	539	545	598	666	642	
Community Service	577	611	676	713	689	760	836	
Debt Service Fund	1,522	1,359	1,453	1,323	1,278	1,520	1,518	
Total expenditures	<u>\$ 14,538</u>	<u>\$ 14,708</u>	<u>\$ 15,159</u>	<u>\$ 15,343</u>	<u>\$ 15,599</u>	<u>\$ 16,487</u>	<u>\$ 17,071</u>	
ADM served per MDE School District Profiles Report (current year estimated)					<u>12,820</u>	<u>12,601</u>	<u>12,478</u>	
Note: Excludes the Capital Projects – Building Construction and OPEB Debt Service Funds.								
Source of state-wide and seven-county metro area data: School District Profiles Report published by the MDE								

Expenditure patterns also vary from district to district for various reasons. Factors affecting the comparison include the growth cycle or maturity of the District, average employee experience, availability of funding, population density, and even methods of allocating costs. The differences from program to program reflect the District’s particular character, such as its community service programs, as well as the fluctuations from year to year for such things as capital expenditures.

The District spent approximately \$213.0 million in the governmental funds reflected above in fiscal 2018, an increase of \$5.2 million (2.5 percent) from the prior year, or \$584 per ADM served.

General Fund current expenditures were \$290 per ADM higher than last year, with the largest increase in the special education program area. General Fund capital expenditures also increased by \$244 per ADM from the prior year. Community Service Special Revenue Fund expenditures were \$76 per ADM higher than last year, due to increased staffing needs as a result of increased program participation.

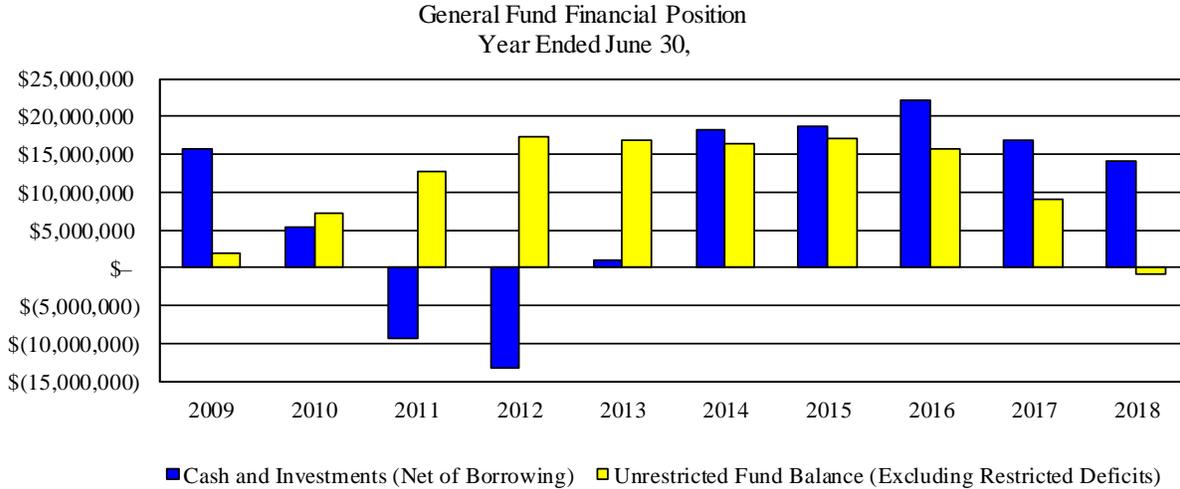
## SUMMARY

Funding for Minnesota school districts generally has not kept pace with inflation, despite recent enhancements to the basic general education state aid formula. This has often increased districts reliance on local revenue sources like voter-approved operating referenda and user fees to maintain programs. Many districts are also beginning to experience delays in collecting property tax revenues due to higher abatements, as more commercial property taxpayers are appealing the assessed values of brick-and-mortar facilities in light of the rapid evolution of e-commerce. School boards and district administrators continue to face many challenges in providing the best education within the limits of the resources available.

## FINANCIAL TRENDS OF YOUR DISTRICT

### GENERAL FUND FINANCIAL POSITION

The following graph displays the District's General Fund trends of financial position. Unrestricted fund balance and cash balance are two indicators of financial health.



The District ended fiscal year 2018 with a General Fund cash balance, net of interfund borrowing, of \$14,094,284, a decrease of \$2,870,723 from the previous year. The total fund balance of the District's General Fund was \$4,979,913 at year end, a decrease of \$8,579,837, compared to a decrease of \$4,620,901 projected in the final budget.

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

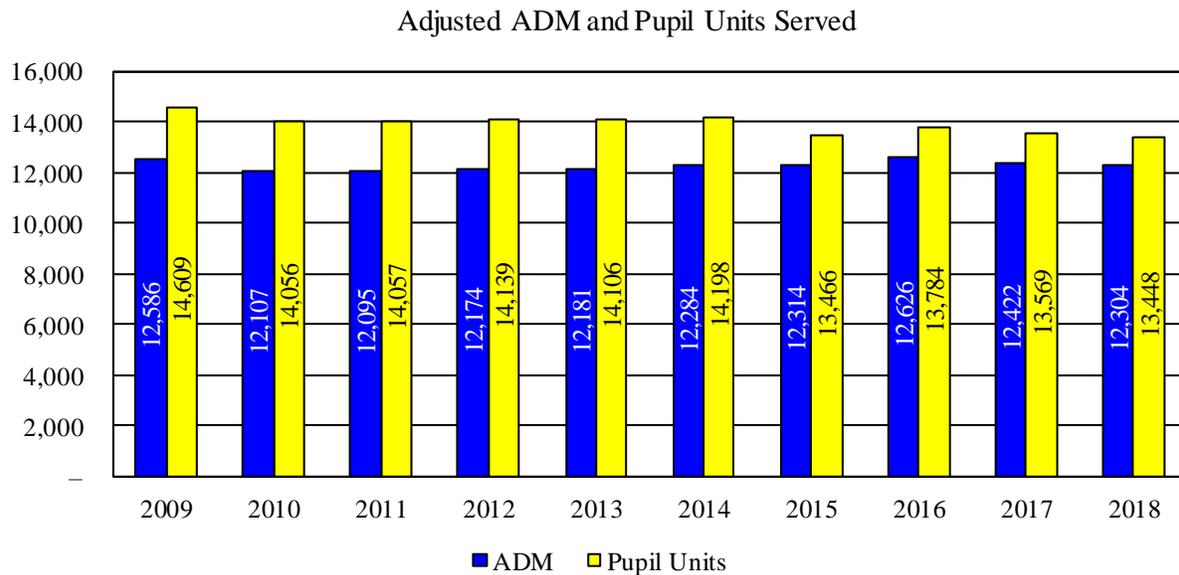
	June 30,				
	2014	2015	2016	2017	2018
Nonspendable fund balances	\$ 890,495	\$ 800,112	\$ 552,260	\$ 375,117	\$ 486,096
Restricted fund balances (1)	1,426,315	1,204,027	1,930,703	4,030,044	5,271,636
Unrestricted fund balances					
Assigned	1,231,939	930,246	1,839,081	873,292	-
Unassigned	15,087,416	16,158,352	13,914,464	8,281,297	(777,819)
<b>Total fund balance</b>	<b>\$ 18,636,165</b>	<b>\$ 19,092,737</b>	<b>\$ 18,236,508</b>	<b>\$ 13,559,750</b>	<b>\$ 4,979,913</b>
Unrestricted fund balances as a percentage of expenditures	<u>11.0%</u>	<u>11.0%</u>	<u>9.4%</u>	<u>5.4%</u>	<u>(0.4%)</u>
Unassigned fund balances as a percentage of expenditures	<u>10.1%</u>	<u>10.4%</u>	<u>8.3%</u>	<u>4.9%</u>	<u>(0.4%)</u>

(1) Includes any deficits in restricted fund balance accounts allowed to accumulate deficits under UFARS, which are part of unassigned fund balance on the accounting principles generally accepted in the United States of America-based financial statements.

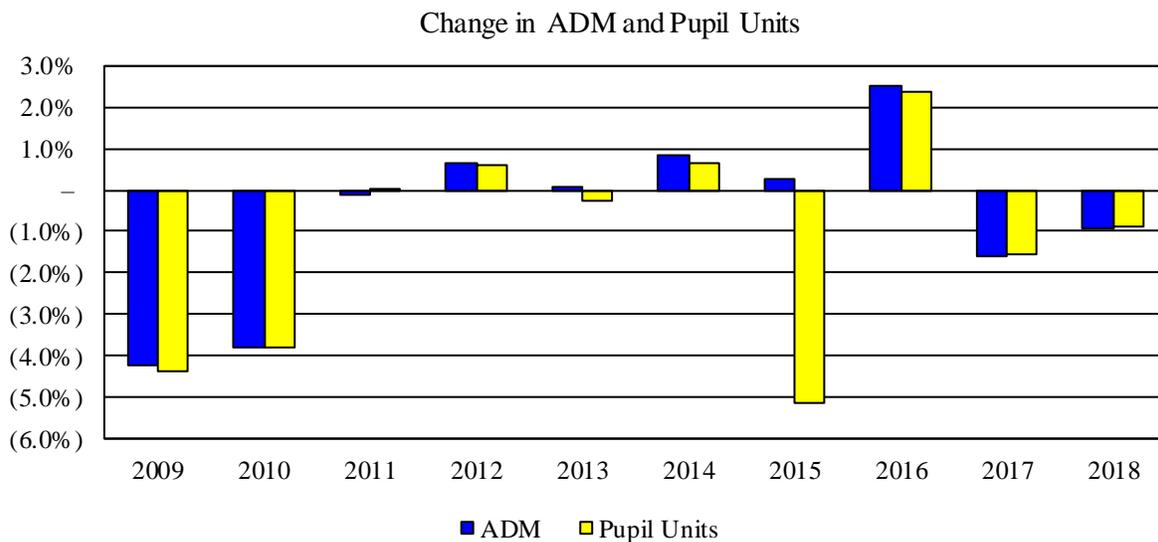
Unrestricted fund balances as a percentage of expenditures is one key measure of a school district's financial health. The resources represented by this fund balance are critical to a district's ability to maintain adequate cash flow throughout the year, to retain its programs, and to cushion against the impact of unexpected costs or funding shortfalls. At June 30, 2018, unrestricted fund balances in the General Fund represented a negative 0.4 percent of annual expenditures.

## AVERAGE DAILY MEMBERSHIP (ADM) AND PUPIL UNITS

The following graph presents the District's adjusted ADM and pupil units served for the past 10 years:



The following graph shows the rate of change in ADM served by the District from year to year, along with the change in the resulting pupil units:



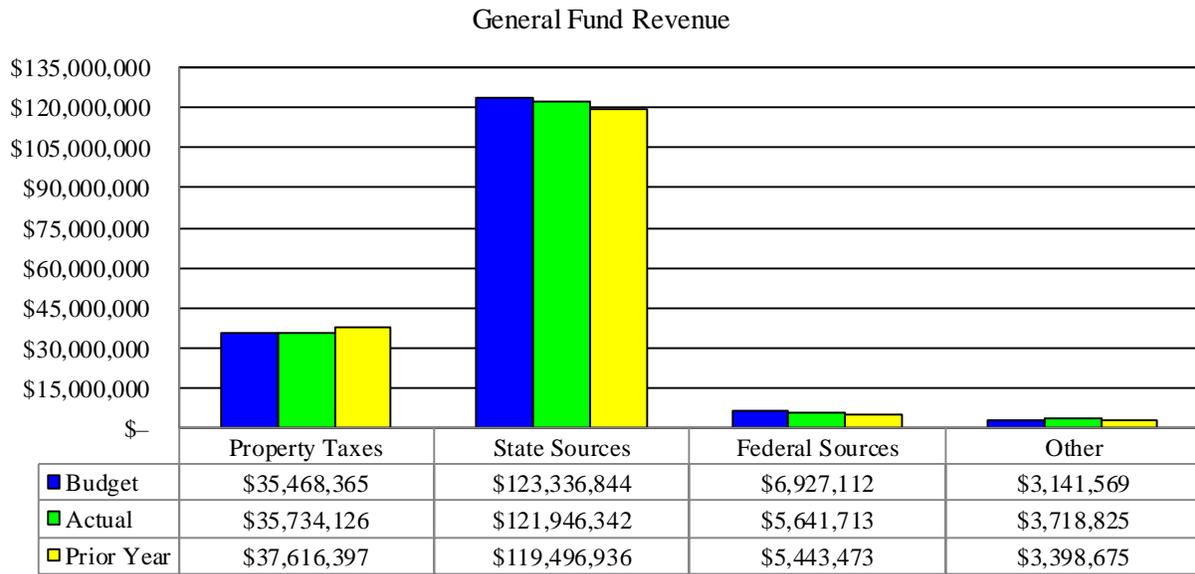
Note: The change in pupil units for 2015 includes the effect of legislative reductions to pupil units.

ADM is a measure of students attending class, which is then converted to pupil units (the base for determining revenue) using a statutory formula. Not only is the original budget based on ADM estimates, the final audited financial statements are based on updated, but still estimated, ADM since the counts are not finalized until around January of the following year. When viewing revenue budget variances, one needs to consider these ADM changes, the impact of the prior year final adjustments, which affect this year's revenue, and also the final adjustments caused by open enrollment gains and losses.

The District served an estimated adjusted ADM of 12,304 in 2018, a decrease of 118 from the previous year. The number of pupil units served by the District for fiscal 2018 was 13,448, a decrease of 121 (0.9 percent) from the prior year.

## GENERAL FUND REVENUE

The following graph summarizes the District's General Fund revenue for 2018:



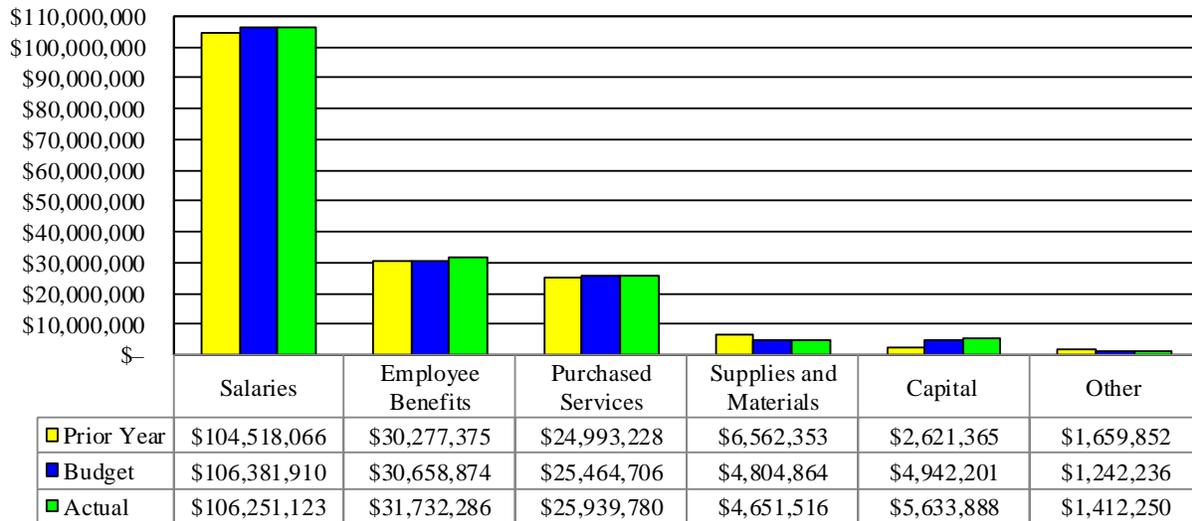
Total General Fund revenues were \$167,041,006 for the year ended June 30, 2018, which was \$1,832,884 (1.1 percent) under the final budget. Revenue from state sources was \$1,390,502 under budget, as the District received less general education aid than anticipated, as a result of declining enrollment. Revenue from federal sources was \$1,285,399 under budget, mainly in Title I and special education federal aids. Revenue from other local sources such as gifts, bequests, tuition, interest, and rental income, which are difficult to predict from year to year, was \$577,256 over budget.

General Fund total revenues were \$1,085,525 (0.7 percent) higher than the previous year. Revenue from property taxes decreased \$1,882,271, due to a decreased tax levy. Revenue from state sources was \$2,449,406 higher than the prior year, as a result of increases in the general education funding formula, special education funding, and general education compensatory aid. Revenue from federal sources was \$198,240 more than last year, mainly due to the District earning more in federal special education entitlements. Revenue from other local sources (including gifts, bequests, tuition, interest, and rental income) increased by \$320,150.

## GENERAL FUND EXPENDITURES

The following graph presents the District's General Fund expenditures for 2018:

General Fund Expenditures

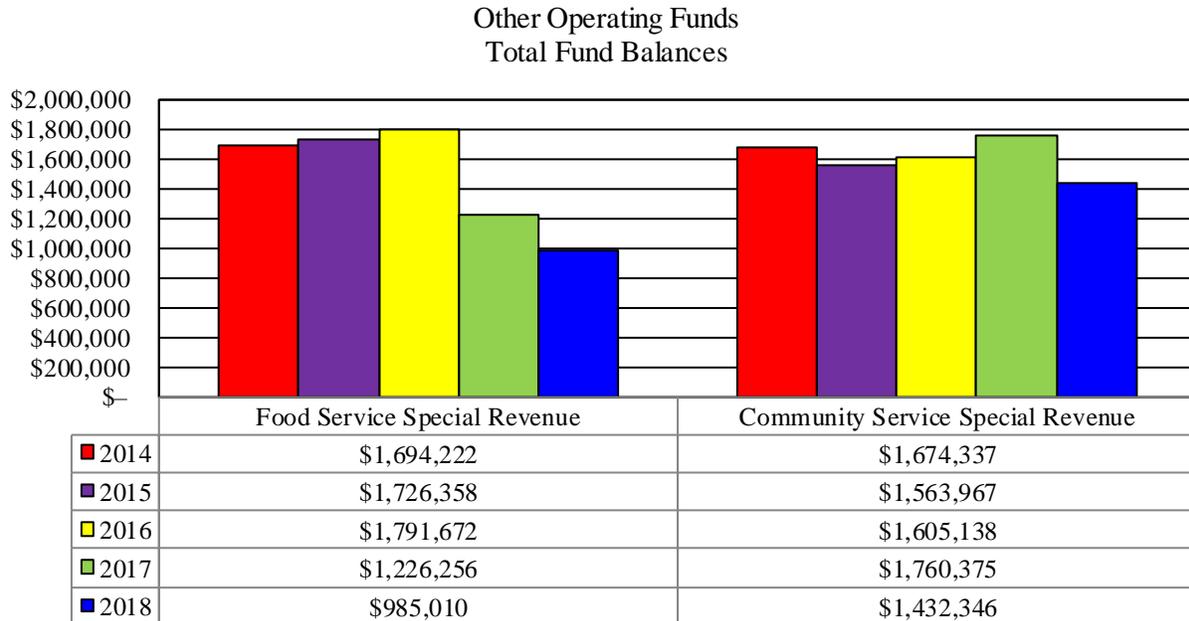


Total General Fund expenditures were \$175,620,843 for the year ended June 30, 2018, which was \$2,126,052 (1.2 percent) over the final budget. Employee benefits were over budget by \$1,073,412, as increases for health insurance were more than anticipated in the budget. Purchased services were \$475,074 over budget, mainly in sites and buildings. Capital expenditures were over budget by \$691,687, mainly due to a difference between the expected and actual progress of construction maintenance projects.

Total General Fund expenditures were \$4,988,604 (2.9 percent) more than the prior year. Salaries and benefits were \$3,187,968 higher than the previous year, due to increased staffing in special education, instructional support, and pupil support services programs, combined with inflationary increases to benefits. Supplies and materials were \$1,910,837 lower than the previous year, due to the District purchasing a significant amount of instructional technology supplies in the prior year. Capital expenditures increased by \$3,012,523 from the previous year, largely due to the timing of various construction projects taking place throughout the District.

## OTHER FUNDS OF THE DISTRICT

The following graph shows what is referred to as the other operating funds. The remaining nonoperating funds are only included in narrative form below, since their level of fund balance can fluctuate significantly due to such things as issuing and spending the proceeds of refunding or building bonds and, therefore, the trend of fund balance levels are not necessarily a key indicator of financial health. It does not mean that these funds cannot experience financial trouble or that their fund balances are unimportant.



### Food Service Special Revenue Fund

The Food Service Special Revenue Fund ended fiscal 2018 with a fund balance decrease of \$241,246, compared to a budgeted increase of \$8,793. Food service revenue of \$7,765,894 was under budget by \$154,375, mainly in federal meal reimbursements. Expenditures of \$8,007,190 exceeded budget by \$95,714, mainly in salaries and benefits, which were over budget by 589,077. This unfavorable variance was partially offset by a favorable variance in supplies and materials of \$462,234. The year-end fund balance of \$985,010 is equal to 12.3 percent of annual Food Service Special Revenue Fund expenditures.

### Community Service Special Revenue Fund

The Community Service Special Revenue Fund ended fiscal 2018 with a fund balance decrease of \$328,029, compared to a budgeted decrease of \$72,447. Revenues were \$10,097,388, which exceeded budget by \$550,143, mainly in tuition, fees, and state sources. Expenditures of \$10,425,417 exceeded budget by \$805,725, mainly in salaries and benefits. The year-end fund balance of \$1,432,346 represents 13.7 percent of current year expenditures.

### Capital Projects – Building Construction Fund

This fund experienced a fund balance decrease of \$309,682 in fiscal 2018, compared to a budgeted reduction of \$5,348,320. The District financed \$15.6 million of capital improvement costs utilizing the proceeds of bonds issued in the current year and certificates of participation issued in the prior year. The ending fund balance for fiscal 2018 was \$12,386,151, all of which is restricted for future capital improvements of various types.

## **Debt Service Fund**

The funding of debt service is controlled in accordance with each outstanding debt issue's financing plan, and the resources of the Debt Service Fund, are dedicated to payment of outstanding debt obligations of the District. As of June 30, 2018, the District has \$2,427,803 available for future debt service.

## **Internal Service Funds**

The District maintains two internal service funds established to finance the costs of its self-insured dental benefits and health benefits.

At June 30, 2018, the Self-Insured Dental Benefits Internal Service Fund had a net position of \$1,203,550 available to pay future dental benefits for the participating members of the District, including estimated claims payable of \$22,239 accrued at year-end. The cost of these benefits for fiscal 2018 was \$1,307,421.

At June 30, 2018, the Self-Insured Health Benefits Internal Service Fund had a deficit net position of \$377,451, including estimated claims payable of \$2,273,622 accrued at year-end. This represented a decline in net position of \$2,457,613, as the cost of health benefit claims for fiscal 2018 of \$18,484,823 exceeded the internal contributions of \$15,994,465 received from the District's governmental funds.

## **Post-Employment Benefits Trust Fund**

The District's Post-Employment Benefits Trust Fund ended the year with cash and investments of \$18.8 million and net position of \$18.3 million available to pay future OPEB. The assets in this fund represent the proceeds from the District's 2009 Taxable OPEB Bonds, which were contributed to an irrevocable trust the District established to finance its OPEB liabilities, and can only be used to pay future OPEB costs, which were estimated to be just under \$10.0 million at year-end.

## 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 two years:

	June 30,		Increase (Decrease)
	2018	2017	
Net position – governmental activities			
Total fund balances – governmental funds	\$ 22,211,223	\$ 31,547,525	\$ (9,336,302)
Total capital assets, net of depreciation	305,733,999	301,821,497	3,912,502
OPEB asset, net of deferments	8,491,701	8,470,648	21,053
Bonds, certificates of participation, and capital leases	(209,153,714)	(209,492,204)	338,490
PERA and TRA pensions, net of deferments	(193,505,326)	(147,505,323)	(46,000,003)
Other adjustments	(4,748,565)	(2,759,155)	(1,989,410)
	<u>\$ (70,970,682)</u>	<u>\$ (17,917,012)</u>	<u>\$ (53,053,670)</u>
Net position			
Net investment in capital assets	\$ 117,654,573	\$ 115,303,157	\$ 2,351,416
Restricted	11,038,463	9,768,518	1,269,945
Unrestricted	(199,663,718)	(142,988,687)	(56,675,031)
	<u>\$ (70,970,682)</u>	<u>\$ (17,917,012)</u>	<u>\$ (53,053,670)</u>

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 vacation payable, severance payable, net pension, and net OPEB liabilities.

Total net position decreased \$53,053,670 in fiscal 2018. The change in the District's proportionate share of the Public Employees Retirement Association's and the Teachers Retirement Association's state-wide pension liabilities and related deferments, along with the spend down of the General Fund unrestricted fund balances, were the primary causes of the \$56,675,031 decrease in unrestricted net position.

The District's net investment in capital assets increased \$2,351,416 this year. The change in this category of net position typically depends on the relationship of the rate at which the District is adding additional capital assets, the rate capital assets are being depreciated, and how that relates to the rate at which the District is repaying the debt issued to purchase or construct those assets.

The restricted portion of the District's net position increased \$1,269,945 in 2018, mainly due to an increase in the restriction for capital asset acquisition.

## LEGISLATIVE SUMMARY

The 2018 legislative session, falling in the second half of the state's fiscal biennium, was a short session in which only two major finance-related bills were passed, an omnibus bonding bill and an omnibus pensions bill. The following is a brief summary of specific legislative changes from the 2018 session or previous legislative sessions impacting Minnesota school districts in future years.

**Basic General Education Revenue** – The Legislature approved annual increases of 2 percent to the basic general education formula allowance for the 2018–2019 biennium. The per pupil allowance will increase \$124 to \$6,312 for fiscal year (FY) 2019.

**Compensatory Revenue** – The \$5 million previously allocated for compensatory pilot grants was permanently added to the allocation for regular compensatory revenue beginning in FY 2018. The portion of compensatory revenue required to be used for extended time activities will increase from 1.7 percent of total compensatory revenue for FY 2018 to 3.5 percent in FY 2019, and 3.5 percent plus the percentage change in the basic formula for FY 2020 and beyond.

**Early Learning** – The Legislature made a number of changes to early learning programs, including appropriating funding of \$71.75 million for the 2018–2019 biennium. Other changes include:

- The creation of a new School Readiness Plus (SR+) program for FY 2018 and FY 2019 only, with the following student eligibility requirements:
  - A child who is four years of age as of September 1, and who demonstrates one or more risk factors is eligible to participate in the program free of charge,
  - A child who is four years of age as of September 1, and who does not demonstrate any risk factors is eligible to participate on a fee-for-service basis, and
  - A district must adopt a sliding fee schedule for students not demonstrating risk factors, but must waive the fee for students unable to pay.
- Changing the Voluntary Pre-Kindergarten (VPK) cap from a limit on the total state aid entitlement to a limit on the number of participants, as follows:
  - A combined cap of 7,160 participants for VPK and SR+ for FY 2019, and
  - A cap of 3,160 participants for VPK for FY 2020 and later (SR+ program sunsets).
- All applications submitted in January to renew an existing VPK program will be funded first (3,160 slots). Applications for expanded VPK programs, and new VPK or SR+ programs will be ranked and approved based on various criteria. The number of new participants allowed in each new or expanded program will depend on how the programs are ranked.

**Long-Term Facilities Maintenance Revenue** – Long-term facilities maintenance revenue will increase from \$292 to \$380 per adjusted pupil unit (APU); multiplied by the lessor of one, or the ratio of the district's average building age to 35 years for FY 2019 and thereafter.

**School Building Bond Agricultural Tax Credit** – Effective for taxes beginning with the payable 2018 levy (FY 2019), a tax credit on all property classified as agricultural (excluding the house, garage, and one acre of an agricultural homestead) is provided equal to 40 percent of the tax on the property attributable to school district building bond levies. The legislative appropriation for this tax credit is \$34.8 million for FY 2019, \$45.2 million for FY 2020, and \$52.5 million for FY 2021.

**School Safety Grants** – The 2018 bonding bill included an appropriation of \$25 million for school safety grants to be funded from the state's General Fund for FY 2019. These grants may be used to design, construct, furnish, or equip school facilities, including renovating or expanding existing facilities. Grants will be awarded by the MDE on a first come – first served basis, up to a limit of \$500,000 for each qualifying school building. At least half the grants must be awarded to school districts outside of the metro area.

**Pension Benefit Reforms** – The 2018 pension bill included a number of reforms to the various defined benefit pension plans across the state, including the plans administered by the Teachers Retirement Association (TRA), St. Paul Teachers Retirement Fund Association (SPTRFA), and the Public Employees Retirement Association (PERA). The reforms include:

- Elimination of augmentation (annual percentage increases to pension benefits accrued by individuals leaving public service prior to retirement). For the TRA plan, augmentation is eliminated for all members after December 31, 2017, but does not eliminate augmentation previously credited to member accounts.
- Early retirement subsidies (augmentation an early retiree would have received had they waited until the normal retirement age to begin receiving the pension) are phased out.
- Post-retirement cost of living adjustments (COLAs) are reduced. For the TRA plan, the COLA was reduced from 2.0 percent to 1.0 percent for five years, with the rate increasing by 0.1 percent annually thereafter, to a maximum of 1.5 percent. For the SPTRFA plan, there will be no COLA increase for two years, and a 1.0 percent annual COLA thereafter. For the PERA plans, the COLA will be equal to 50.0 percent of the annual increase for Social Security, but not less than 0.5 percent and not more than 1.5 percent.
- For early retirees that retire on or after January 1, 2024, COLAs are deferred until the retiree reaches the normal retirement age.
- The rate of interest paid on refunds of employee contributions to former public employees was reduced from an annual rate of 4 percent to 3 percent.
- The actuarial assumption for investment rate of return was reduced to 7.5 percent for all plans.
- Employer contribution rates were increased for the TRA plan (a total increase of 1.25 percent phased in over a 6-year period beginning in FY 2019) and the SPTRFA plan (a total increase of 2.50 percent phased in over a 6-year period beginning in FY 2019). Employee contribution rates were also increased by 0.25 percent beginning in FY 2024 for the TRA plan and beginning in FY 2023 for the SPTRFA plan. The pension adjustment component of the general education aid formula was increased by an amount equal to the product of the salaries paid to members of these two plans times the district's pension adjustment rate for the fiscal year to help offset the cost of the employer contribution increases.

**Competitive Bidding Threshold** – Effective for contracts awarded on or after August 1, 2018, the dollar threshold at which Minnesota Statutes require the use of a sealed bidding process was raised from \$100,000 to \$175,000. This extends the dollar range for which contracts may be awarded using direct negotiation (obtaining two quotations) contracts between \$25,000 and \$175,000. By reference, this change also increased the dollar threshold at which public contractors' performance and payment bonds are required for contracts over \$175,000.

## ACCOUNTING AND AUDITING UPDATES

### **GASB Statement No. 83, *Certain Asset Retirement Obligations***

At times, state and local governments are required to take specific actions to retire certain tangible capital assets, such as the decommissioning of nuclear reactors, removal and disposal of wind turbines in wind farms, dismantling and removal of sewage treatment plants, and removal and disposal of x-ray machines. Obligations to retire certain tangible capital assets also arise from contracts or court judgments. Accounting and financial reporting standards exist for costs of the closure and post-closure care of municipal solid waste landfills, but those standards do not address retirement obligations associated with other types of tangible capital assets.

This statement addresses accounting and financial reporting for certain asset retirement obligations (AROs) that were not addressed in GASB standards by establishing uniform accounting and financial reporting requirements for these obligations. An ARO is a legally enforceable liability associated with the retirement of a tangible capital asset. A government that has legal obligations to perform future asset retirement activities related to its tangible capital assets should recognize a liability based on the guidance in this statement. The requirements of this statement are effective for reporting periods beginning after June 15, 2018.

### **GASB Statement No. 84, *Fiduciary Activities***

This statement is intended to enhance consistency and comparability of fiduciary activity reporting by state and local governments. It is also meant to improve the usefulness of fiduciary activity information primarily for assessing the accountability of governments in their roles as fiduciaries.

This statement establishes criteria for identifying fiduciary activities of all state and local governments. The focus of the criteria generally is on (1) whether a government is controlling the assets of the fiduciary activity and (2) the beneficiaries with whom a fiduciary relationship exists. An activity meeting the criteria should be reported in a fiduciary fund in the basic financial statements. This statement describes four fiduciary funds that should be reported, if applicable: (1) pension (and other employee benefit) trust funds, (2) investment trust funds, (3) private-purpose trust funds, and (4) custodial funds. Custodial funds generally should report fiduciary activities that are not held in a trust or equivalent arrangement that meets specific criteria. The requirements of this statement are effective for reporting periods beginning after December 15, 2018.

### **GASB Statement No. 87, *Leases***

A lease is a contract that transfers control of the right to use another entity's nonfinancial asset as specified in the contract for a period of time in an exchange or exchange-like transaction. Examples of nonfinancial assets include buildings, land, vehicles, and equipment. Any contract that meets this definition should be accounted for under the leases guidance, unless specifically excluded in this statement.

Governments enter into leases for many types of assets. Under the previous guidance, leases were classified as either capital or operating depending on whether the lease met any of four tests. In many cases, the previous guidance resulted in reporting lease transactions differently than similar nonlease financing transactions.

The goal of this statement is to better meet the information needs of users by improving accounting and financial reporting for leases by governments. It establishes a single model for lease accounting based on the principle that leases are financings of the right to use an underlying asset. This statement increases the usefulness of financial statements by requiring recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows of resources or outflows of resources based on the payment provisions of the contract.

Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset, and a lessor is required to recognize a lease receivable and a deferred inflow of resources, thereby enhancing the relevance and consistency of information about governments' leasing activities.

To reduce the cost of implementation, this statement includes an exception for short-term leases, defined as a lease that, at the commencement of the lease term, has a maximum possible term under the lease contract of 12 months (or less), including any options to extend, regardless of their probability of being exercised. Lessees and lessors should recognize short-term lease payments as outflows of resources or inflows of resources, respectively, based on the payment provisions of the lease contract. The requirements of this statement are effective for reporting periods beginning after December 15, 2019.

### ***GASB Statement No. 88, Certain Disclosures Related to Debt, Including Direct Borrowings and Direct Placements***

The primary objective of this statement is to improve the information that is disclosed in notes to government financial statements related to debt, including direct borrowings and direct placements. It also clarifies which liabilities governments should include when disclosing information related to debt.

The requirements of this statement will improve financial reporting by providing users of financial statements with essential information that currently is not consistently provided. In addition, information about resources to liquidate debt and the risks associated with changes in terms associated with debt will be disclosed. As a result, users will have better information to understand the effects of debt on a government's future resource flows.

This statement defines debt for purposes of disclosure in notes to financial statements as a liability that arises from a contractual obligation to pay cash (or other assets that may be used in lieu of cash) in one or more payments to settle an amount that is fixed at the date the contractual obligation is established. The statement requires that additional essential information related to debt be disclosed in notes to financial statements, including unused lines of credit; assets pledged as collateral for the debt; and terms specified in debt agreements related to significant events of default with finance-related consequences, significant termination events with finance-related consequences, and significant subjective acceleration clauses. It also requires that existing and additional information be provided for direct borrowings and direct placements of debt separately from other debt. The requirements of this statement are effective for reporting periods beginning after June 15, 2018.

### **Uniform Guidance, Micro-Purchase Threshold**

Under the Uniform Guidance for federal programs, a micro-purchase is one for goods or services that, due to its relatively low value, does not require the government to abide by many of its ordinary competitive procedures, including small business set-asides. Because the contract is theoretically, such a low amount, the contracting officer can pick virtually whatever company and product he or she wants to satisfy the procurement, so long as the price is reasonable. The standard micro-purchase threshold has been amended to increase the threshold to \$10,000, effective June 20, 2018. Entities are not required to increase the micro-purchase and simplified acquisition thresholds but, if they wish to do so, they must update their procurement policies and procedures to reflect the change in thresholds. They cannot retroactively make these changes effective prior to June 20, 2018.