

KUTZTOWN AREA SCHOOL DISTRICT

FINANCIAL AND COMPLIANCE REPORT

Year Ended June 30, 2014

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Herbein + Company, Inc.
2763 Century Boulevard
Reading, PA 19610
P: 610.378.1175
F: 610.378.0999
www.herbein.com

INDEPENDENT AUDITOR'S REPORT

To the Board of School Directors
Kutztown Area School District
Kutztown, Pennsylvania

Report on the Financial Statements

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Kutztown Area School District as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

Our responsibility is to express opinions on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Opinions

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Kutztown Area School District, as of June 30, 2014, and the respective changes in financial position and, where applicable, cash flows thereof for the year then ended in accordance with accounting principles generally accepted in the United States of America.

Other Matters

Required Supplementary Information

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis, budgetary comparison schedules for the general fund, and the schedule of funding progress - postemployment benefits plan be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about 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 do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Kutztown Area School District's basic financial statements. The schedule of expenditures of federal awards, as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, is presented for purposes of additional analysis and is not a required part of the basic financial statements.

The schedule of expenditures of federal awards is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedule of expenditures of federal awards is fairly stated in all material respects in relation to the basic financial statements as a whole.

Other Reporting Required by *Government Auditing Standards*

In accordance with *Government Auditing Standards*, we have also issued our report dated October 23, 2014, on our consideration of the District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Herbein + Company, Inc.

Reading, Pennsylvania
October 23, 2014

Kutztown Area School District

251 Long Lane | Kutztown, PA 19530-9722 | Tel: 610-683-7361 | Fax: 610-683-7230

David J. Miller, Business Administrator

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE FISCAL YEAR ENDED JUNE 30, 2014

The discussion and analysis of Kutztown Area School District's financial performance provides an overall review of the School District's financial activities for the fiscal year ended June 30, 2014. The intent of this discussion and analysis is to look at the School District's financial performance as a whole; readers should also review the basic financial statements and the notes to the financial statements to enhance their understanding of the School District's financial performance.

FINANCIAL HIGHLIGHTS

Revenues in the General Fund (the fund that reports most of the District's programs and services) exceeded the anticipated revenues in the budget by $725,137. This was primarily due to higher than anticipated: Real Estate Taxes; $300,565, Delinquent Real Estate Taxes; 130,706, Earned Income Tax: $139,900, Vocational Education; $79,387. Revenue areas below their budgeted amounts were: Investment Income; ($13,062), Transportation Subsidy; ($96,780), and Medical Access Payments; ($94,700), Social Security Subsidy ($29,127), Retirement Subsidy ($26,103). Spending and other uses (net of bond refinancing) in the General Fund was under budget primarily due to lower than budgeted operations and maintenance expenses. These variances in revenues and expenditures resulted in $391,548 being added to the fund balance.

The General Fund made transfers to the Food Service Fund for $56,070 and $36,514 in the years ended June 30, 2014 and 2013, respectively. In the past the Food Service Fund has not been self-supporting. Lunch prices have been increased, which has helped Food Service come closer to funding itself. Prices were raised in the 2012-2013 and 2011-2012 school years in accordance with revised federal regulations. Lunch prices will also rise in the upcoming school year.

A total of $1,645,000 was paid against the principal of General Obligation Bonds. In the previous year, the District also was able to refinance its' 2009 Bond Issue to achieve a cash flow savings of $256,025 and a corresponding net present value savings of $258,170. The balance of all bonds at the end of the year was $17,685,000.

The Capital Projects Fund at the end of the fiscal year June 30, 2014, had a fund balance of $1,210,952. Revenues included investment income of $329 and an intergovernmental transfer from the general fund of $975,929. Expenditures consisted of capital outlays; $813,899 and professional services of $41,957.

USING THE BASIC FINANCIAL STATEMENTS

This annual report consists of **two** distinct series of financial statements: the district-wide and the fund financials. The **district-wide** reports are designed to show the District as a sum of its significant fund activities. The **fund financial** statements provide the next level of detail. They focus on the individual parts of the District's operations in more detail than the district-wide statements.

Reporting the School District as a Whole (District-wide Financials)

Statement of Net Position and *Statement of Activities*

The view of the School District as a whole looks at all financial transactions and asks the question, "How did we do financially during fiscal year 2014?" The S*tatement of Net Position* and the S*tatement of Activities* answer this question. These statements include all assets and liabilities using the accrual basis of accounting similar to the accounting system used by most private sector companies. This basis of accounting takes into consideration all of the current year's revenues and expenses regardless of when cash was received or paid.

These two statements provide information for a long-term view of the School District's finances. They report the School District's net assets and changes in those assets. This change in net assets is important because it identifies whether the financial position of the School District has improved or diminished for the School District as a whole. The cause of this change may be the result of many factors, some financial, some not.

In the S*tatement of Net Position* and the S*tatement of Activities*, the School District is divided into two distinct activities:

> **Governmental Activities** – Most of the School District's programs and services are reported here including instruction, support services, operation and maintenance of plant, pupil transportation, and extracurricular activities. In the case of the Kutztown Area School District, the major funds included under governmental activities are the **General Fund,** and the **Capital Projects Fund**. There are no longer any non-major funds grouping under governmental activities. The **Athletic Fund** is now combined with the **General Fund** to satisfy the requirements of Governmental Accounting Standards Board Statement #54.
>
> **Business-Type Activity** – This service is provided on a charge for goods or services basis to recover all of the expenses of the goods or services provided. The **Food Service** enterprise fund is the only fund reported as a business activity for Kutztown Area School District.

Reporting the School District's Most Significant Funds

Fund Financial Statements

Fund Financial reports provide detailed information about the School District's major funds. The School District uses several funds to account for a multitude of financial transactions.

Governmental Funds – Most of the School District's activities are reported in governmental funds, which focus on how monies flow into and out of those funds and the balances left at fiscal year end for spending in future periods. These funds are reported using an accounting method called modified accrual, which measures cash and all other financial assets that can readily be converted to cash. The governmental fund statements provide a detailed short-term view of the School District's general government operations and the basic services it provides. Governmental fund information helps determine whether there are more or less financial resources that can be spent in the near future to finance educational programs. The same funds (Kutztown Area School District's General Fund, and Capital Projects Fund) are included in the Governmental Funds as are included in Governmental Activities. As stated previously, the Athletic Fund is now combined with the General Fund to comply with the requirements of GASB #54. *The relationship, or differences, between governmental activities (reported in the* Statement of Net Position *and the* Statement of Activities*) and the governmental funds is reconciled in the financial statements*.

Proprietary Funds – Proprietary Funds (in Kutztown Area School District's case this is only the food service fund) have historically operated as enterprise funds using the same basis of accounting as business-type activities; therefore, these statements will essentially match the information provided in the statements for the School District as a whole.

Fiduciary Funds – The District is the trustee, or fiduciary, for some Scholarship Funds and Activities Funds. All of the District's fiduciary activities are reported in separate Statements of Fiduciary Net Assets and Changes in Net Assets. We ***exclude*** these activities from the District's other financial statements because the District cannot use these assets to finance its operations.

FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

Table 1 provides a summary of Statement of Net Position as of June 30, 2014 compared to June 30, 2013.

Table 1
Fiscal Year Ended June 30, 2014 and 2013
Net Assets

	Governmental Activities		Business-type Activities		Total School District	
	2014	2013	2014	2013	2014	2013
Current & Other Assets	$ 11,599,187	$ 10,797,924	348,192	394,447	11,947,379	11,192,371
Net Capital Assets	29,275,457	28,500,612	200,966	152,854	29,476,423	28,653,466
Total Assets	**$ 40,874,644**	**$ 39,298,536**	**549,158**	**547,301**	**41,423,802**	**39,845,837**
Deferred Chrg on Bond Refund	741,785	827,448			741,785	827,448
Current & Other Liabilities	5,033,243	4,280,207	7,391	54,032	5,040,634	4,334,239
Long-Term Liabilities	17,667,165	18,565,283	14,926	13,250	17,682,091	18,578,533
Total Liabilities	**22,700,408**	**22,845,490**	**22,317**	**67,282**	**22,722,725**	**22,912,772**
Net Investment in Capital Assets	10,662,119	9,957,369	200,966	152,854	10,863,085	10,110,223
Net Assets-Restricted	1,222,691	1,090,550		-	1,222,691	1,090,550
Net Assets-Unrestricted	7,031,211	6,232,575	325,875	327,165	7,357,086	6,559,740
Total Net Position	**18,916,021**	**17,280,494**	**526,841**	**480,019**	**19,442,862**	**17,760,513**

Most of the District's net assets are invested in capital assets (building, land and equipment).

The results of this year's operations as a whole are reported in the *Statement of Activities*. All expenses are reported in the first column. Specific charges, grants, revenues and subsidies that directly relate to specific expense categories are represented to determine the final amount of the District's activities that are supported by other general revenues. The two largest general revenues are the Basic Education Subsidy provided by the State of Pennsylvania, and the local taxes assessed to community taxpayers.

Table 2 takes the information from that Statement, rearranges it slightly, so you can see the total revenues for the year.

Table 2
Fiscal Year Ended June 30, 2014 and 2013
Changes in Net Assets

	Governmental Activities		Business-type Activities		Total School District	
Revenues	**2014**	**2013**	**2014**	**2013**	**2014**	**2013**
Program Revenues :						
Charges for Services	$ 79,425	$ 67,941	383,382	435,016	462,807	502,957
Operating Grants & Contributions	3,927,831	3,612,842	276,501	268,348	4,204,332	3,881,190
Capital Grants & Contributions	257,582	262,480			257,582	262,480
General Revenues :					-	-
Property Taxes	19,649,357	19,501,205			19,649,357	19,501,205
Other Taxes	1,842,388	1,837,688			1,842,388	1,837,688
Grants, Subsidies & Contributions	3,236,657	3,153,035			3,236,657	3,153,035
Investment Earnings	21,277	23,264	457	570	21,734	23,834
Miscellaneous Income	105,583	24,410			105,583	24,410
Transfers	(56,071)	(36,514)	56,071	36,514	-	-
Total Revenues	29,064,029	28,446,351	716,411	740,448	29,780,440	29,186,799
Expenses						
Instruction	16,534,354	15,650,361		-	16,534,354	15,650,361
Instructional Student Support	2,778,435	2,476,584		-	2,778,435	2,476,584
Admin. & Fin'l Support Services	1,972,790	1,881,432		-	1,972,790	1,881,432
Oper. & Maint. Of Plant Svcs.	2,745,509	2,743,094		-	2,745,509	2,743,094
Pupil Transportation	1,143,117	1,182,047		-	1,143,117	1,182,047
Human Resources	178,998	148,493		-	178,998	148,493
Student Activities	571,458	562,886		-	571,458	562,886
Community Services	6,420	15,307		-	6,420	15,307
Interest on Long-Term Debt	707,771	782,247		-	707,771	782,247
Unallocated Depreciation Exp	789,650	789,697		-	789,650	789,697
Food Services		-	669,589	709,422	669,589	709,422
Total Expenses	27,428,502	26,232,148	669,589	709,422	28,098,091	26,941,570
Increase (decrease) in Net Assets	**$ 1,635,527**	**2,214,203**	**46,822**	**31,026**	**1,682,349**	**2,245,229**

Governmental Activities

The *Statement of Activities* reflects the cost of program services and the revenues (charges for services and sales, grants and contributions) offsetting those services. Table 3, for government activities, indicates the ***total cost*** of services and the ***net cost*** of services. The net cost represents the cost of these services that is supported by tax revenues and unrestricted state entitlements.

Table 3
Fiscal Year Ended June 30, 2014 and 2013
Governmental Activities

Functions/Programs	Total Cost of Services		Net Cost of Services	
	2014	2013	2014	2013
Instruction	16,534,354	15,650,361	$13,756,003	$13,124,411
Instructional Student Support	2,778,435	2,476,584	2,537,965	2,278,986
Administrative	2,151,788	2,021,581	2,012,958	1,917,537
Operation and Maintenance	2,745,509	2,743,094	2,604,002	2,628,842
Pupil Transportation	1,143,117	1,182,047	513,610	505,065
Student Activities	571,458	562,886	492,867	500,929
Community Services	6,401	15,307	6,401	15,307
Interest on Long-Term Debt	707,771	782,247	450,189	519,767
Refund of Prior Year Revenue	49	8,344	49	8,344
Unallocated Depreciation	789,650	789,697	789,650	789,697
Total Governmental Activities	**$27,428,532**	**$26,232,148**	**$23,163,694**	**$22,288,885**
Less:				
Unrestricted Grants & Subsidies			3,236,657	3,153,035
Total Needs from Local Taxes and Other Revenues			**$19,927,037**	**$19,135,850**

The dependence upon tax revenues for governmental activities is apparent. In fiscal year 2014, the costs of instructional activities were equal to 78 percent of taxes and other general revenues. Taxes and other general revenues fund 91 percent of all government activity expenses. The community, as a whole, is the primary support for Kutztown Area School District students.

Business-Type Activity

Table 4 reflects the activities of the Food Service Program, the only Business-type activity of the District. The Statement of Revenues, Expenses and Changes in Fund Net Assets for the proprietary fund will further detail the actual results of operations. The Kutztown Area School District's Food Service operation is not self-supporting; it requires assistance from the General Fund.

Table 4
Fiscal Year Ended June 30, 2014 and 2013
Business Type Activities

Functions/Programs	Total Cost of Services		Net Cost of Services	
	2014	2013	2014	2013
Food Services	$ 669,589	$ 708,752	$ 9,706	$ 5,388
Less:				
Investment Earnings,Gains (losses)			457	570
Total Business-type Activities			**$ 9,249**	**$ 4,818**

Major factors causing the increase in Net Cost of Services are an increase in salaries of 8%. Overall benefits were higher by 54% due to increasing retirement costs and the fact that an employee who had previously opted out of health care coverage is now taking the coverage. Revenues were lower by 11% due mostly to Vocational Technical students no longer eating lunch at our school and the fact that state mandated menu options do not seem to be favored by students. Non-operating revenues decreased by 21%. The General Fund transferred $56,071 and $36,514 to the Food Services Fund in 2014 and 2013 respectively. These transfers basically represent the net employee benefits for the Cafeteria Fund. The General Fund pays for these benefits and the expenditure for the Cafeteria portion is recognized as a transfer-out (expenditure) in the General Fund and a transfer-in (revenue) in the Cafeteria Fund.

THE SCHOOL DISTRICT'S FUNDS

The School District's governmental funds are accounted for using the *modified accrual* basis of accounting. **Total** governmental funds had revenues of $29,330,666 and expenditures and other financing sources/uses of $28,818,716. This increased the total fund balance by $511,950.

General Fund:

The positive net change in fund balance of $391,548 represents the revenues over the expenditures of Kutztown Area School Districts General Fund for the fiscal year ended June 30, 2014. This was primarily due to lower Debt Service, better than expected collections in current and delinquent taxes offset by increased labor and benefit costs. Lower maintenance costs also added to the increase. Transfers to the Capital Projects Fund was budgeted to complete some much needed capital projects at the High School and Middle School. The majority of financial transactions flow through this fund.

Capital Projects Fund:

The fund balance for the Capital Projects Fund increased by $120,402. This represents interest revenue of $329, transfer from the General Fund of $975,929 and expenditures of $855,856 primarily for a new boiler at the Middle School and various High School projects. Although the Capital Reserve Fund has a zero balance, future accounting treatment will group it with the Capital Projects Fund in accordance with Governmental Accounting Standards Board Statement 54.

Non-Major Governmental Funds:

The Athletic Fund that was previously listed under this category is now combined with the General Fund in accordance with Governmental Accounting Standards Board Statement 54.

General Fund Budgeting Highlights

During the fiscal year, the Board of School Directors (The Board) authorizes revisions to the original budget to accommodate differences from the original budget to the actual expenditures of the District.

Revenues exceeded the budget by $725,137. This was primarily due to greater than anticipated: Real Estate Taxes; $300,565, Delinquent Real Estate Taxes: $130,706, Earned Income Tax; $139,900, Vocational Ed; $79,387. Revenue items that were below budget, Investment Income; ($13,062), Transportation Subsidy; ($96,780), Medical Access Payments; ($94,700), Social Security Subsidy ($29,127), and Retirement Subsidy ($26,103). Some expenditures exceeded budgeted amounts, others were less than anticipated. Maintenance and Operations made up the largest savings with a positive variance of $334,199. These variances in revenues and expenditures resulted in $391,548 being added to the fund balance.

CAPITAL ASSETS AND DEBT ADMINISTRATION

Capital Assets

At the end of the 2014 fiscal year, the district had invested over $29 million in land, buildings, furniture and equipment, and vehicles. The value of the land is not the fair market, but rather the acquisition cost. Table 5 shows the breakdown of net capital assets. The increase in the totals is largely due to new additions net of depreciation expense.

Table 5
Capital Assets at June 30, 2014 and 2013 (Net of Depreciation)

	Governmental Activities		Business-Type Activity		Total	
	2014	2013	2014	2013	2014	2013
Land	$ 46,090	$ 46,090	-	-	46,090	46,090
Construction in Progress	501,005	62,510	-	-	501,005	62,510
Site Improvements	404,817	449,816	-	-	404,817	449,816
Bldg & Bldg Improvements	25,585,247	26,031,644	-	-	25,585,247	26,031,644
Furniture & Equipment	2,738,298	1,910,552	200,966	152,854	2,939,264	2,063,406
Totals	**$ 29,275,457**	**28,500,612**	**200,966**	**152,854**	**29,476,423**	**28,653,466**

Debt

As of July 1, 2013 the District had outstanding bonds of $19,330,000. During the year principal payments were made against these outstanding bonds in the amount of $1,645,000. As of June 30, 2014 outstanding bonds totaled $17,685,000. Table 6 shows the breakdown of these numbers.

Table 6
Outstanding Debt

	Balance July 1, 2013	Additions	Reductions	Balance June 30, 2014
GOB Series 2004	$ 380,000	-	380,000	-
GOB Series 2005	12,515,000	-	865,000	11,650,000
GOB Series 2013	6,435,000		400,000	6,035,000
Total	**$ 19,330,000**	**$ -**	**$ 1,645,000**	**$ 17,685,000**

Other obligations include accrued vacation pay and sick leave for specific employees of the District. More detailed information about our long-term liabilities is included in the Notes to the Financial Statements.

CURRENT ISSUES

1. Act 1 of 2006 - Tax Relief Act continues to have a significant impact on the operation of the School District. The Act restricts annual increase of real estate property tax to an inflation index and imposes an earlier more stringent and strenuous budget timeline for the school district. The exceptions to raise taxes above the Act 1 index were substantially diminished with the 2013-2014 fiscal year.

2. Special Education – Special Education costs increased by 8% in 2013-2014. They are in excess of $3.9 million and they remain a source of concern as more services become required for this segment of the school population. The government mandates which require and regulate these programs are largely unfunded.

3. Health Benefits – Health benefits trend rates continue to remain high. For 2014-2015 the rate increase is 3%. The Berks County Schools Health Insurance Consortium has become self-insured and continues to look at various ways to control costs. In addition, health insurance reform will take effect Jan. 1, 2015. This places several mandates and reporting requirements on employers. Health costs are expected to exceed the general rate of inflation for years to come.

4. Charter Schools – Charter School costs have increased significantly over the last ten years, from $44,237 in 2003-2004 to $749,946 in the 2013-2014 school year, an increase 1,595% since 2004. In response to this significant increase, the district has launched its own cyber charter school program to give students another option. This program will allow students to participate in all on-campus courses as well as access to all extracurricular activities. The cost per student is significantly less than tuition at an outside entity.

5. Retirement Rates – PSERS retirement contribution rates have increased from 1.15% in 2002-03 to an actual rate of 21.4% in 2014-15. This, in conjunction with increasing salary costs, has caused retirement costs to increase at double-digit rates. It is estimated that in the school year 2015-16 the PSERS contribution will increase to approximately 25.84%, which will greatly impact the expenditure budget.

6. Student Enrollment - The administration continues to monitor declining student enrollment and the impact that it may have on district operations. Staffing was adjusted in 2010-2011 and 2011-2012 in response to declining enrollment.

7. Our Vision - The school district continues to invest in programs that are designed to increase student achievement. The Kutztown Virtual Academy is took on a new look beginning with the 2012-2013 year. We have contracted with new providers with an eventual goal of operating our own program with a seamless transition between brick and mortar classes and cyber. Blended instruction will also be available as a student choice. The Read 180 program was made possible by ARRA funds a few years ago, it has the goal of improving reading proficiency and comprehension. We are focused on strengthening our computer network infrastructure and ability to support appropriate classroom use of technology afforded by a one-to-one program. Our professional employees continue to employ the Professional Learning Communities model as a continuous and on-going process to monitor student achievement and design programs to best meet the needs of students. This includes rewriting curriculum to the state standards and improving learning through remediation procedures that are in place at all grade levels.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

The financial report is designed to provide our citizens, taxpayers, customers, and investors and creditors with a general overview of the School District's finances and to show the School District's accountability for the money it receives. If you have questions about this report or need additional information, contact David J. Miller, Business Administrator and Board Treasurer, at Kutztown Area School District, 251 Long Lane, Kutztown, PA 19530.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF NET POSITION

June 30, 2014

	Governmental Activities	Business-Type Activities	Total
ASSETS			
Cash and Investments	$ 9,516,131	$ 320,229	$ 9,836,360
Taxes Receivable, Net	1,133,864	-	1,133,864
Internal Balances	20,235	(20,235)	-
Intergovernmental Receivables	903,174	33,003	936,177
Other Receivables, Net	177	-	177
Inventories	-	15,195	15,195
Prepaid Expenses	25,606	-	25,606
Capital Assets Not Being Depreciated:			
Land	46,090	-	46,090
Construction in Progress	501,005	-	501,005
Capital Assets, Net of Accumulated Depreciation:			
Site Improvements	404,817	-	404,817
Building and Building Improvements	25,585,247	-	25,585,247
Fixtures and Equipment	2,738,298	200,966	2,939,264
TOTAL ASSETS	40,874,644	549,158	41,423,802
DEFERRED OUTFLOWS OF RESOURCES			
Deferred Charge on Bond Refunding	741,785	-	741,785
LIABILITIES			
Accounts Payable	792,897	-	792,897
Accrued Salaries and Benefits	1,420,382	-	1,420,382
Payroll Deductions and Withholdings	723,893	-	723,893
Accrued Interest	197,201	-	197,201
Unearned Revenues	26,420	7,391	33,811
Noncurrent Liabilities			
Due Within One Year	1,872,450	-	1,872,450
Bonds Payable, Net	16,190,654	-	16,190,654
Long-Term Portion of Capital Lease Obligation	550,234	-	550,234
Long-Term Portion of Compensated Absences	363,846	-	363,846
Other Postemployment Benefit Obligation	562,431	14,926	577,357
TOTAL LIABILITIES	22,700,408	22,317	22,722,725
NET POSITION			
Net Investment in Capital Assets	10,662,119	200,966	10,863,085
Restricted	1,222,691	-	1,222,691
Unrestricted	7,031,211	325,875	7,357,086
TOTAL NET POSITION	$ 18,916,021	$ 526,841	$ 19,442,862

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF ACTIVITIES

For the Year Ended June 30, 2014

Functions/Programs	Expenses	Program Revenue: Charges for Services	Program Revenue: Operating Grants and Contributions	Program Revenue: Capital Grants and Contributions	Net (Expense) Revenue and Changes in Net Position: Governmental Activities	Net (Expense) Revenue and Changes in Net Position: Business-Type Activities	Net (Expense) Revenue and Changes in Net Position: Total
Governmental Activities:							
Instruction:							
Regular	$ 11,297,159	$ -	$ 1,185,943	$ -	$ (10,111,216)	$ -	$ (10,111,216)
Special	3,969,647	-	1,421,780	-	(2,547,867)	-	(2,547,867)
Vocational	1,093,778	-	133,388	-	(960,390)	-	(960,390)
Other Instructional Programs	169,520	-	37,240	-	(132,280)	-	(132,280)
Adult Education Programs	4,250	-	-	-	(4,250)	-	(4,250)
Total Instructional Services	16,534,354	-	2,778,351	-	(13,756,003)	-	(13,756,003)
Support Services:							
Pupil Personnel	899,562	-	75,740	-	(823,822)	-	(823,822)
Instructional Staff	1,490,409	-	116,414	-	(1,373,995)	-	(1,373,995)
Administration	1,599,985	-	102,307	-	(1,497,678)	-	(1,497,678)
Pupil Health	388,464	-	48,316	-	(340,148)	-	(340,148)
Business Services	347,635	-	22,653	-	(324,982)	-	(324,982)
Operation of Plant and Maintenance Services	2,745,509	47,980	93,527	-	(2,604,002)	-	(2,604,002)
Student Transportation Services	1,143,117	-	629,507	-	(513,610)	-	(513,610)
Human Resources	178,998	-	13,870	-	(165,128)	-	(165,128)
Other Support Services	25,170	-	-	-	(25,170)	-	(25,170)
Total Support Services	8,818,849	47,980	1,102,334	-	(7,668,535)	-	(7,668,535)
Noninstructional Services:							
Student Activities	571,458	31,445	47,146	-	(492,867)	-	(492,867)
Community Services	6,401	-	-	-	(6,401)	-	(6,401)
Interest on Long-Term Debt	707,771	-	-	257,582	(450,189)	-	(450,189)
Refund of Prior Year Revenue	49	-	-	-	(49)	-	(49)
Unallocated Depreciation	789,650	-	-	-	(789,650)	-	(789,650)
Total Noninstructional Services	2,075,329	31,445	47,146	257,582	(1,739,156)	-	(1,739,156)
Total Governmental Activities	27,428,532	79,425	3,927,831	257,582	(23,163,694)	-	(23,163,694)
Business-Type Activities:							
Food Services	669,589	383,381	276,502	-	-	(9,706)	(9,706)
Total Primary Government	$ 28,098,121	$ 462,806	$ 4,204,333	$ 257,582	(23,163,694)	(9,706)	(23,173,400)
General Revenues and Transfers							
General Revenues:							
Taxes:							
Property Taxes					19,649,387	-	19,649,387
Public Utility Realty, Earned Income and Mercantile Taxes					1,842,388	-	1,842,388
Grants, Subsidies, and Contributions Not Restricted for Specific Programs					3,236,657	-	3,236,657
Investment Earnings					21,277	457	21,734
Miscellaneous					105,583	-	105,583
Transfers					(56,071)	56,071	-
Total General Revenues and Transfers					24,799,221	56,528	24,855,749
Change in Net Position					1,635,527	46,822	1,682,349
Net Position - Beginning					17,280,494	480,019	17,760,513
Net Position - Ending					$ 18,916,021	$ 526,841	$ 19,442,862

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

BALANCE SHEET
GOVERNMENTAL FUNDS

June 30, 2014

	General	Capital Projects	Total Governmental Funds
ASSETS			
Cash and Investments	$ 8,779,404	$ 736,727	$ 9,516,131
Taxes Receivable, Net	1,154,768	-	1,154,768
Interfund Receivable	-	858,088	858,088
Intergovernmental Receivables	903,174	-	903,174
Other Receivables, Net	177	-	177
Prepaid Expenditures	25,606	-	25,606
TOTAL ASSETS	$ 10,863,129	$ 1,594,815	$ 12,457,944
LIABILITIES, DEFERRED INFLOWS, AND FUND BALANCES			
LIABILITIES			
Accounts Payable	$ 409,034	$ 383,863	$ 792,897
Accrued Salaries and Benefits	1,420,382	-	1,420,382
Payroll Deductions and Withholdings	723,893	-	723,893
Interfund Payable	837,853	-	837,853
Current Portion of Compensated Absences Payable	74,799	-	74,799
Unearned Revenues	26,420	-	26,420
TOTAL LIABILITIES	3,492,381	383,863	3,876,244
DEFERRED INFLOWS OF RESOURCES			
Unavailable Revenue - Property Taxes	883,200	-	883,200
FUND BALANCES			
Nonspendable for Prepaid Expenditures	25,606	-	25,606
Restricted Fund Balance	11,739	1,210,952	1,222,691
Committed Fund Balance:			
Future Capital Projects	1,600,486	-	1,600,486
Future PSERS Contributions	1,360,310	-	1,360,310
Amounts Due Career and Technology Center	181,533	-	181,533
Further Development of Virtual Academy	115,147	-	115,147
Assigned Fund Balance	753,128	-	753,128
Unassigned Fund Balance	2,439,599	-	2,439,599
TOTAL FUND BALANCES	6,487,548	1,210,952	7,698,500
TOTAL LIABILITIES, DEFERRED INFLOWS, AND FUND BALANCES	$ 10,863,129	$ 1,594,815	$ 12,457,944

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE GOVERNMENT-WIDE STATEMENT OF NET POSITION

June 30, 2014

Amounts reported for governmental activities in the statement of net position (page 3) are different because:

TOTAL FUND BALANCES - GOVERNMENTAL FUNDS (page 5)		$ 7,698,500
Capital assets used in governmental activities are not financial resources and therefore, are not reported as assets in governmental funds. The cost of the assets is $47,393,807 and the accumulated depreciation is $18,118,350.		29,275,457
Property taxes receivable will be collected this year, but are not available soon enough to pay for the current period's expenditures and therefore, are reported as unavailable revenue in the funds.		862,296
Long-term liabilities, including bonds payable and capital lease payable, are not due and payable in the current period and therefore, are not reported as liabilities in the funds. Long-term liabilities at year-end consist of:		
Bonds Payable	$ (17,685,000)	
Capital Lease Payable	(817,885)	
Accrued Interest on Long-term Debt	(197,201)	
Unamortized Bond Premium	(101,203)	
Unamortized Bond Discount	65,549	
Deferred Charge on Bond Refunding	741,785	
Long-Term Portion of Compensated Absences	(363,846)	
Postemployment Benefit Obligation	(562,431)	(18,920,232)
NET POSITION OF GOVERNMENTAL ACTIVITIES		$ 18,916,021

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS

For the Year Ended June 30, 2014

	General	Capital Projects	Total Governmental Funds
REVENUES			
Local Sources	$ 21,631,626	$ 329	$ 21,631,955
State Sources	7,381,937	-	7,381,937
Federal Sources	316,774	-	316,774
TOTAL REVENUES	29,330,337	329	29,330,666
EXPENDITURES			
Instructional Services	16,221,120	-	16,221,120
Support Services	8,648,620	131,240	8,779,860
Operation of Noninstructional Services	573,627	-	573,627
Capital Outlay	1,101,381	724,616	1,825,997
Debt Service			
Principal	1,928,496	-	1,928,496
Interest	620,315	-	620,315
Refund of Prior Year Revenue	49	-	49
TOTAL EXPENDITURES	29,093,608	855,856	29,949,464
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	236,729	(855,527)	(618,798)
OTHER FINANCING SOURCES (USES)			
Sale of Fixed Assets	85,438	-	85,438
Proceeds from Capital Lease	1,101,381	-	1,101,381
Operating Transfers In	-	975,929	975,929
Operating Transfers Out	(1,032,000)	-	(1,032,000)
TOTAL OTHER FINANCING SOURCES (USES)	154,819	975,929	1,130,748
NET CHANGE IN FUND BALANCES	391,548	120,402	511,950
FUND BALANCES - BEGINNING	6,096,000	1,090,550	7,186,550
FUND BALANCES - ENDING	$ 6,487,548	$ 1,210,952	$ 7,698,500

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES TO THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES

For the Year Ended June 30, 2014

Amounts reported for governmental activities in the statement of activities (page 4) are different because:		
NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS (Page 7)		$ 511,950
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.		
Capital Outlays	$ 2,012,598	
Loss on Disposal of Fixed Assets	(4,486)	
Less: Depreciation Expense	(1,233,267)	774,845
Because some property taxes will not be collected for several months after the District's year-end, they are not considered as "available" revenues in the governmental funds. Unavailable revenues increased (decreased) by this amount during the year.		(291,488)
Issuance of long-term debt provides current financial resources to governmental funds, while the repayment of the principal of long-term debt consumes the current financial resources of governmental funds. However, neither transaction has any effect on net position. Also, governmental funds report the effect of premiums, discounts, and similar items when debt is first issued, whereas these amounts are deferred and amortized in the statement of activities. The effect of these transactions in the statement of activities is shown below:		
Repayment of Bond Principal	1,645,000	
Repayment of Capital Lease	283,496	
Amortization of Bond Discount	(6,789)	
Amortization of Bond Premium	11,826	
Amortization of Deferred Charge on Bond Refunding	(85,663)	
Issuance of Capital Lease	(1,101,381)	746,489

KUTZTOWN AREA SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES TO THE GOVERNMENT-WIDE STATEMENT OF ACTIVITIES - CONTINUED

For the Year Ended June 30, 2014

Interest on long-term debt in the statement of activities differs from the amount reported in the governmental funds because interest is recognized as an expenditure in the funds when it is due, and thus requires the use of current financial resources. In the statement of activities, interest expense is recognized as the interest accrues, regardless of when it is due. The amount represents the difference between interest accrued and paid.	(19,584)
Postemployment benefits are recognized when they are paid on the fund statements. With the implementation of GASB #45, an estimated liability for future benefits due will be phased in over several years. This amount represents the difference between the estimated annual cost and the amount paid.	(92,828)
In the statement of activities, certain operating expenses - compensated absences (vacations and sick days) are measured by the amounts earned during the year. In the governmental funds; however, expenditures for these items are measured by the amount of financial resources used. This amount represents the difference between the amount earned versus the amount used.	6,143
CHANGE IN NET POSITION OF GOVERNMENTAL ACTIVITIES	$ 1,635,527

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF NET POSITION
PROPRIETARY FUND

June 30, 2014

	Enterprise Fund Food Service
ASSETS	
CURRENT ASSETS	
Cash and Investments	$ 320,229
Intergovernmental Receivables	33,003
Inventories	15,195
TOTAL CURRENT ASSETS	368,427
NONCURRENT ASSETS	
Furniture and Equipment, Net	200,966
TOTAL ASSETS	569,393
LIABILITIES	
CURRENT LIABILITIES	
Interfund Payable	20,235
Unearned Revenues	7,391
TOTAL CURRENT LIABILITIES	27,626
NONCURRENT LIABILITIES	
Other Postemployment Benefit Obligation	14,926
TOTAL LIABILITIES	42,552
NET POSITION	
Net Investment in Capital Assets	200,966
Unrestricted	325,875
TOTAL NET POSITION	$ 526,841

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF REVENUES, EXPENSES, AND CHANGES IN NET POSITION
PROPRIETARY FUND

For the Year Ended June 30, 2014

	Enterprise Fund Food Service
OPERATING REVENUES	
Food Service Revenue	$ 356,527
Other Operating Revenue	26,855
TOTAL OPERATING REVENUES	383,382
OPERATING EXPENSES	
Salaries	245,127
Employee Benefits	83,698
Purchased Services	4,580
Supplies	319,758
Depreciation	12,485
Repairs and Maintenance	2,708
Miscellaneous	1,233
TOTAL OPERATING EXPENSES	669,589
OPERATING LOSS	(286,207)
NONOPERATING REVENUES	
Local Sources - Earnings on Investments	457
State Sources	47,747
Federal Sources	228,754
TOTAL NONOPERATING REVENUES	276,958
LOSS BEFORE TRANSFERS	(9,249)
Operating Transfers In	56,071
CHANGE IN NET POSITION	46,822
NET POSITION - BEGINNING	480,019
NET POSITION - ENDING	$ 526,841

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF CASH FLOWS
PROPRIETARY FUND

For the Year Ended June 30, 2014

	Enterprise Fund Food Service
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash Received from Users	$ 385,497
Cash Payments to Employees for Services	(317,132)
Cash Payments to Suppliers for Goods and Services	(339,484)
NET CASH USED BY OPERATING ACTIVITIES	(271,119)
CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES	
State Sources	45,154
Federal Sources	161,193
Operating Transfers In	56,071
NET CASH PROVIDED BY NONCAPITAL FINANCING ACTIVITIES	262,418
CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES	
Capital Asset Purchases	(60,597)
CASH FLOWS FROM INVESTING ACTIVITIES	
Earnings on Investments	457
NET DECREASE IN CASH AND CASH EQUIVALENTS	(68,841)
CASH AND CASH EQUIVALENTS - BEGINNING OF YEAR	389,070
CASH AND CASH EQUIVALENTS - END OF YEAR	$ 320,229

See accompanying notes.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF CASH FLOWS - CONTINUED
PROPRIETARY FUND

For the Year Ended June 30, 2014

	Enterprise Fund Food Service
Reconciliation of Operating Loss to Net Cash Used by Operating Activities:	
Operating Loss	$ (286,207)
Adjustments to Reconcile Operating Loss to Net Cash Used by Operating Activities:	
Depreciation	12,485
Donated Commodities Used	37,798
Changes in Assets and Liabilities:	
Inventories	(3,006)
Accounts Payable	(45,997)
Accrued Salaries and Benefits	(2,760)
Interfund Balances	12,777
Unearned Revenues	2,115
Other Liabilities	1,676
Total Adjustments	15,088
NET CASH USED BY OPERATING ACTIVITIES	$ (271,119)

NONCASH NONCAPITAL FINANCING ACTIVITIES

During the year, the District used $37,798 of commodities from the U.S. Department of Agriculture.

KUTZTOWN AREA SCHOOL DISTRICT

STATEMENT OF NET POSITION
FIDUCIARY FUND

June 30, 2014

	Agency Fund Student Activities
ASSETS	
CURRENT ASSETS	
Cash and Investments	$ 72,175
TOTAL ASSETS	$ 72,175
LIABILITIES	
CURRENT LIABILITIES	
Other Current Liabilities	$ 72,175
TOTAL LIABILITIES	$ 72,175

See accompanying notes.

The Kutztown Area School District is a combination of three boroughs and three townships; the boroughs of Kutztown, Lyons, and Lenhartsville and the townships of Maxatawny, Greenwich, and Albany.

The Kutztown Area School District (the "District") is a unit established, organized, and empowered by the Commonwealth of Pennsylvania for the express purpose of carrying out, on the local level, the commonwealth's obligation to public education, as established by the constitution of the commonwealth and by the School Law Code of the same (Article II; Act 150, July 8, 1968).

As specified under the School Law Code of the Commonwealth of Pennsylvania, this and all other school districts of the state "shall be and hereby are vested as, bodies corporate, with all necessary powers to carry out the provisions of this act" (Article II, Section 211).

The District is governed by a board of nine school directors who are residents of the School District and who are elected every two years, on a staggered basis, for a four-year term. The board of school directors has the power and duty to establish, equip, furnish, and maintain a sufficient number of elementary, secondary and other schools necessary to educate every person residing in such district, between the ages of six and twenty-one years, who may attend.

The superintendent is the chief administrative officer and chief instructional officer of the board and the District and is responsible for the execution of all actions of the board. Subject to the policies and direction of the board, the superintendent is responsible for the administration and operation of the public school system and oversees all matters pertaining to instruction. The superintendent manages the District with the assistance of the assistant superintendent, the business administrator, the director of personnel, the director of curriculum and information, as well as the building principals.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

As required by generally accepted accounting principles, the financial statements of the reporting entity include those of the District (the primary government) and its component units.

The District used guidance contained in generally accepted accounting principles to evaluate the possible inclusion of related entities (authorities, boards, etc.) within its reporting entity. The criteria used by the District for inclusion are financial accountability and the nature and significance of the relationships. In determining financial accountability in a given case, the District reviews the applicability of the following criteria. The District is financially accountable for:

- Organizations that make up the legal District entity.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

A. Reporting Entity - continued

- Legally separate organizations if District officials appoint a voting majority of the organizations' governing body and the District is able to impose its will on the organization, or if there is a potential for the organization to provide specific financial benefits to, or impose specific financial burdens on, the District as defined below.

  Impose its will - If the District can significantly influence the programs, projects or activities of, or the level of services performed or provided by, the organization.

  Financial benefit or burden - exists if the District (1) is entitled to the organization's resources; (2) is legally obligated or has otherwise assumed the obligation to finance the deficits of, or provide support to, the organization; or (3) is obligated in some manner for the debt of the organization.

- Organizations that are fiscally dependent on the District. Fiscal dependency is established if the organization is unable to adopt its budget, levy taxes, set rates or charges, or issued bonded debt without approval by the District.

Based on the foregoing criteria, the District has determined it has no component units.

Governments commonly enter into special arrangements with each other to provide or obtain needed services. A common type of such an arrangement is a joint venture. In addition to joint ventures, governments also enter into contracts to plan for and address certain activities for their mutual benefits; i.e., a jointly governed organization. The District has one of each of these relationships:

Joint Venture: The District is a participating member of the Berks Career and Technology Center. See Note 10 for details of involvement and financial information of the joint venture.

Jointly Governed Organizations: The District is a participating member of the Berks County Intermediate Unit (BCIU). The BCIU is run by a joint committee consisting of members from each participating district. No participating district appoints a majority of the joint committee. The board of directors of each participating district must approve BCIU's annual operating budget.

The BCIU is a self-sustaining organization that provides services for fees to participating districts. As such, the District has no ongoing financial interest or responsibility in the BCIU. The BCIU contracts with participating districts to supply special education services, computer services, and to act as a conduit for certain federal programs.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

B. Basis of Presentation - Government-Wide Financial Statements

Government-wide financial statements (i.e., the statement of net position and the statement of activities) display information about the reporting entity, except for its fiduciary activities. All fiduciary activities are reported only in the fund financial statements. The government-wide statements include separate columns for the governmental and business-type activities of the primary government, as well as any discretely presented component units. Governmental activities, which normally are supported by taxes, intergovernmental revenues, and other nonexchange transactions are reported separately from business-type activities which rely to a significant extent, on fees and charges for support. Likewise, the primary government is reported separately from the legally separate component units for which the primary government is financially accountable.

Governmental activities are supported by taxes and intergovernmental revenues while business-type activities are supported by user charges and fees. The statement of activities demonstrates the level to which the direct expenses of a given function to the District are offset by the program revenues related to that function. Direct expenses are those that are directly related to and clearly identified with a function. Program revenues include charges to customers or others who purchase, use or directly benefit from services or goods provided by a given function or grants and contributions that are restricted to meet the operational or capital requirements of a function. Other items not includable in program revenues are reported as general revenues.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are the contributions made to any component units from the District's governmental funds and transfers between governmental funds and business-type and fiduciary funds. Elimination of these contributions would distort the direct costs and program revenues reported for the various functions concerned.

C. Basis of Presentation - Fund Financial Statements

The fund financial statements provide information about the government's funds, including its fiduciary funds. Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds. The emphasis of fund financial statements is on major governmental and enterprise funds, each displayed in a separate column. All remaining governmental funds are aggregated and reported as nonmajor funds. Major individual governmental and enterprises funds are reported as separate columns in the fund financial statements.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

C. Basis of Presentation - Fund Financial Statements - continued

The District Reports the Following Major Governmental Funds:

***General Fund*:** This fund is established to account for resources devoted to financing the general services that the District performs. Intergovernmental revenues and other sources of revenue used to finance the fundamental operations of the District are included in this fund. The fund is charged with all costs of operating the District for which a separate fund has not been established.

Capital Projects Fund: This fund is established to account for financial resources to be used for the acquisition or construction of major capital equipment and facilities (other than those financed by proprietary funds).

The District has the Following Major Enterprise Fund:

Food Service Fund: This fund accounts for all revenues, food purchases, and costs and expenses for the food service program. The food service fund is the District's only major enterprise fund where the intent of the governing body is that the costs of providing food services are covered by user charges and subsidies received.

Additionally, the District Reports the Following Fund Type:

Fiduciary Funds: The District's fiduciary fund is the activity fund, an agency fund. Agency funds are custodial in nature (assets equal liabilities) and do not involve measurement of results of operations.

During the course of operations, the government has activity between funds for various purposes. Any residual balances outstanding at year-end are reported as due from/to other funds and advances to/from other funds. While these balances are reported in fund financial statements, certain eliminations are made in the preparation of the government-wide financial statements. Balances between the funds included in governmental activities (i.e., the governmental and internal service funds) are eliminated so that only the net amount is included as internal balances in the governmental activities column. Similarly, balances between the funds included in business-type activities (i.e., the enterprise funds) are eliminated so that only the net amount is included as internal balances in the business-type activities column.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

C. Basis of Presentation - Fund Financial Statements - continued

Further, certain activity occurs during the year involving transfers of resources between funds. In fund financial statements these amounts are reported at gross amounts as transfers in/out. While reported in fund financial statements, certain eliminations are made in the preparation of the government-wide financial statements. Transfers between the funds included in governmental activities are eliminated so that only the net amount is included as transfers in the governmental activities column. Similarly, balances between the funds included in business-type activities are eliminated so that only the net amount is included as transfers in the business-type activities column.

D. Measurement Focus and Basis of Accounting

The accounting and financial reporting treatment is determined by the applicable measurement focus and basis of accounting. Measurement focus indicates the type of resources being measured such as *current financial resources* or *economic resources*. The basis of accounting indicates the timing of transactions or events for recognition in the financial statements.

The government-wide financial statements are reported using the *economic resources measurement focus*, and the *accrual basis of accounting*. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

The governmental fund financial statements are reported using the *current financial resources measurement focus* and the *modified accrual basis of accounting*. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences, and claims and judgments, are recorded only when payment is due. General capital asset acquisitions are reported as expenditures in governmental funds. Issuance of long-term debt and acquisitions under capital leases are reported as other financing sources.

Property taxes, licenses, and interest associated with the current fiscal period is considered to be susceptible to accrual and so has been recognized as revenue of the current fiscal period. Expenditure-driven grants are recognized as revenue when the qualifying expenditures have been incurred and all other eligibility requirements have been met, and the amount is received during the period or within the availability period for this revenue source (within 60 days of year-end). All other revenue items are considered to be measurable and available only when cash is received by the government.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

D. Measurement Focus and Basis of Accounting - continued

The proprietary fund is reported using the *economic resources measurement focus* and the *accrual basis of accounting*. The agency fund has no measurement focus but utilizes the *accrual basis of accounting* for reporting its assets and liabilities.

E. Budgetary Information

1. Budgetary Basis of Accounting

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for the general fund in accordance with the PA School Code of 1949, as amended. Budgetary control is legally maintained at the function level within the General Fund. The PA School Code allows the District board to make budgetary transfers between major function and major object codes only within the last nine months of the fiscal year, unless there is a two-thirds majority of the school directors approving the transfer.

All budget amounts presented in the accompanying financial statements have been adjusted for legally authorized revisions of the annual budget during the year. Appropriations, except unexpended grant appropriations and encumbrances, lapse at the end of each fiscal year.

No budget has been adopted for the capital projects funds.

F. Assets, Liabilities, Deferred Inflows/Outflows of Resources, and Net Position/Fund Balance

1. Cash and Investments

Investments are reported at fair value (generally based on quoted market prices).

The District's reporting entity considers all highly-liquid investments with a maturity of three months or less when purchased to be cash equivalents.

2. Receivables/Payables

Activity between funds that is representative of lending/borrowing arrangements outstanding at the end of the year are referred to as "interfund receivables/payables." Any residual balances outstanding between the governmental and business-type activities are reported in the government-wide financial statements as "internal balances."

3. Inventories and Prepaid Items

On government-wide financial statements, inventories are presented at the lower of cost or market on a first-in, first-out basis and are expensed when used.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

F. Assets, Liabilities, Deferred Inflows/Outflows of Resources, and Net Position/Fund Balance - continued

3. Inventories and Prepaid Items - continued

Inventories of the governmental funds, consisting principally of textbooks and instructional supplies, are not valued since it is the policy of the District to charge these items to expense upon acquisition.

Inventories of the Enterprise Fund consisting of food and paper supplies are carried at cost, using the first-in, first-out method. Federal donated commodities are valued at their fair market value as determined by the U.S. Department of Agriculture at the date of donation. The inventories on hand at June 30, 2014, consist of the following:

Purchased food and supplies	$ 5,686
Donated commodities	9,509
	$ 15,195

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both the government-wide and fund financial statements. The cost of prepaid items is recorded as expenditures/expenses when consumed rather than when purchased.

4. Capital Assets, Depreciation, and Amortization

The District generally capitalizes assets with cost of $2,500 or more as purchase and construction outlays occur. Management has elected to include certain homogeneous asset categories with individual assets less than $2,500 as composite groups for financial reporting purposes. Assets purchased or constructed with long-term debt may be capitalized regardless of the threshold established. The costs of normal maintenance and repairs that do not add to the asset value or materially extend useful lives are not capitalized. Capital assets, including those of component units, are depreciated using the straight-line method. When capital assets are disposed, the cost and applicable accumulated depreciation are removed from the respective accounts, and the resulting gain or loss is recorded in operations.

Estimated useful lives, in years, for depreciable assets are as follows:

Assets	Years
Site improvements	10 - 50
Buildings and improvements	10 - 50
Fixtures and equipment	5 - 20

Interest costs incurred during the construction phase of capital assets are capitalized when incurred by proprietary funds and similar component units on debt where proceeds were used to finance the construction of assets.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

F. Assets, Liabilities, Deferred Inflows/Outflows of Resources, and Net Position/Fund Balance - continued

5. Deferred Outflows/Inflows of Resources

In addition to assets, the statement of financial position will sometimes report a separate section for deferred outflows of resources. This separate financial statement element, *deferred outflows of resources*, represents a consumption of net position that applies to a future period(s) and so will *not* be recognized as an outflow of resources (expense/expenditure) until then. The District has one item that qualifies for reporting in this category, which is a deferred charge on bond refunding reported in the government-wide statement of net position. A deferred charge on refunding results from the difference in the carrying value of refunded debt and its reacquisition price. This amount is deferred and amortized over the shorter of the life of the refunded or refunding debt.

In addition to liabilities, the statement of financial position will sometimes report a separate section for deferred inflows of resources. This separate financial statement element, *deferred inflows of resources,* represents an acquisition of net position that applies to a future period(s) and so will not be recognized as an inflow of resources (revenue) until that time. The government has only one type of item, which arises only under a modified accrual basis of accounting, that qualifies for reporting in this category. Accordingly, the item, *unavailable revenue*, is reported only in the governmental funds balance sheet. The governmental funds report unavailable revenues from one source - property taxes. These amounts are deferred and recognized as an inflow of resources in the period that the amounts become available.

6. Unearned Revenues

Revenues that are received but not earned are unearned revenues in the government-wide and enterprise funds financial statements. Unearned revenues arise when resources are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the District has legal claim to the resources, the liability for unearned revenue is removed from the respective statement of net position/balance sheet and revenue is recognized.

7. Net Position Flow Assumptions

Sometimes the government will fund outlays for a particular purpose from both restricted (e.g., restricted bond or grant proceeds) and unrestricted resources. In order to calculate the amounts to report as restricted - net position and unrestricted - net position in the government-wide and proprietary fund financial statements, a flow assumption must be made about the order in which the resources are considered to be applied.

It is the government's policy to consider restricted resources to have been depleted before unrestricted resources are applied.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

F. Assets, Liabilities, Deferred Inflows/Outflows of Resources, and Net Position/Fund Balance - (continued)

8. Fund Balance Flow Assumptions

Sometimes the government will fund outlays for a particular purpose from both restricted and unrestricted resources (the total of committed, assigned, and unassigned fund balance). In order to calculate the amounts to report as restricted, committed, assigned, and unassigned fund balance in the governmental fund financial statements a flow assumption must be made about the order in which the resources are considered to be applied. The District's policy places no restrictions on the order of the unrestricted fund balances used. The order of the unrestricted fund balances used for disbursements is at the discretion of the business manager.

9. Fund Balance Policies

Fund balance of governmental funds is reported in various categories based on the nature of any limitations requiring the use of resources for specific purposes. The government itself can establish limitations on the use of resources through either a commitment (committed fund balance) or an assignment (assigned fund balance).

The committed fund balance classification includes amounts that can be used only for the specific purposes determined by a formal action of the government's highest level of decision-making authority. The board of directors is the highest level of decision-making authority for the government that can, by adoption of a resolution prior to the end of the fiscal year, commit fund balance. Once adopted, the limitation imposed by the resolution remains in place until a similar action is taken (the adoption of another resolution) to remove or revise the limitation.

Amounts in the assigned fund balance classification are intended to be used by the government for specific purposes but do not meet the criteria to be classified as committed. The board of directors may assign fund balance. Unlike commitments, assignments generally only exist temporarily. In other words, an additional action does not normally have to be taken for the removal of an assignment. Conversely, as discussed above, an additional action is essential to either remove or review a commitment.

The unassigned fund balance of the general fund at the end of each fiscal year-end shall not be less than five percent of the following year's projected budgeted expenditures. In any fiscal year where the District is unable to maintain this minimum reservation of fund balance as required in this section, the District shall not budget any amount of unassigned fund balance for the purpose of balancing the general fund budget until this level is achieved.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

G. Revenues and Expenditures/Expense

1. Program Revenues

Amounts reported as program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions (including special assessments) that are restricted to meeting the operations or capital requirements of a particular function or segment. All taxes and other internally dedicated resources are reported as general revenues rather than as program revenues.

2. Compensated Absences

Sick Pay

Under the District's various bargaining agreements and plans, professional employees and administrators accumulate unused sick days without limitation. These unused sick days may be accumulated for future illnesses and are not vested. Upon retirement, professional employees are paid for unused sick days at the rate of $25/day. Upon retirement each administrator/supervisor shall be eligible to continue on the District's hospitalization plan, at District expense, for a period of time, as calculated below, or receive compensation for unused sick days as described below. Each retiring administrator/supervisor has the option of choosing one of the benefit plans outlined below, either: Hospitalization Plan Benefit or Pay for Unused Sick Days Benefit.

Option to Continue on District's Hospitalization Plan

Upon retirement each administrator/supervisor shall be eligible to continue on the District's hospitalization plan, at District expense, for a period of time calculated as follows:

1. Coverage will be calculated based on one (1) month for every six (6) days of unused sick leave.

2. Any remaining days, after the calculation of (1) above, shall be allocated at the rate of seventy-five dollars ($75.00) per each day of unused sick leave (upon retirement) toward the purchase of coverage for a hospitalization plan.

3. The maximum length of hospitalization paid for the District will be two (2) years.

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - CONTINUED

G. Revenues and Expenditures/Expense - continued

2. Compensated Absences - Continued

Option to Receive Compensation for Unused Sick Days

Upon the retirement of an administrator/supervisor, such individual shall receive compensation for each accumulated sick day at the rate of $75.00 per day for each unused sick day up to a maximum of 120 days.

Vacation Leave

Unused vacation leave can be accumulated by administrators/supervisors to a maximum of 30 days. Administrators/supervisors may receive full payment for up to 30 days of unused vacation days upon retirement. The District maintains records of all employees' accumulated vacation days.

Retirement Benefits

Upon notification to the District that the next school year shall be the final year of service prior to retirement, a professional employee will receive an increment equivalent to $100 per year of service up to a maximum of $3,500. All service must have been in the Kutztown Area School District.

The District records this benefit on a pay as you go basis.

3. Proprietary Funds Operating and Nonoperating Revenues and Expenses

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the food service fund are charges to customers for meals and services provided. Operating expenses for proprietary funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

H. Other Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures. Accordingly, actual results could differ from those estimates.

NOTE 2 - CASH AND CASH EQUIVALENTS AND INVESTMENTS

The deposit and investment policy of the District adheres to state statutes. There were no deposits or investment transactions during the year that were in violation of either the state statutes or the policy of the District.

The breakdown of total cash and investments at June 30, 2014 is as follows:

Cash	$ 3,301,836
Pooled cash and investments	4,035,384
Investments	2,571,315
	$ 9,908,535

Cash

Custodial Credit Risk - Deposit

Custodial credit risk is the risk that in the event of a bank failure, the government's deposits may not be returned to it. The District does not have a policy for custodial credit risk. As of June 30, 2014, the carrying amount of the District's deposits was $3,301,836 and the bank balance was $3,380,937. Of the bank balance, $250,000 was covered by federal depository insurance, and $3,130,937 was exposed to custodial credit risk but covered by the collateralization requirements in accordance with Act 72.

A portion of the District's deposits are in the Pennsylvania School District Liquid Asset Fund (PSDLAF). Although not registered with the Securities and Exchange Commission and not subject to regulatory oversight, the funds act like money market mutual funds in that their objective is to maintain a stable net asset value of $1 per share, is rated by a nationally recognized statistical rating organization, and is subject to an independent annual audit.

Investments

Under Section 440.1 of the Public School Code of 1949, as amended, the District is permitted to invest funds in the following types of investments:

Obligations of (a) the United States of America or any of its agencies or instrumentalities backed by the full faith and credit of the United States of America, (b) the Commonwealth of Pennsylvania or any of its agencies or instrumentalities backed by the full faith and credit of the commonwealth, or (c) any political subdivision of the Commonwealth of Pennsylvania or any of its agencies or instrumentalities backed by the full faith and credit of the political subdivision.

Deposits in savings accounts, time deposits or share accounts of institutions insured by the Federal Deposit Insurance Corporation to the extent that such accounts are so insured and, for any amounts above the insured maximum, provided that approval collateral as provided by law therefore, shall be pledged by the depository.

NOTE 2 - CASH AND CASH EQUIVALENTS AND INVESTMENTS - CONTINUED

As of June 30, 2014, the District had the following investments:

	Maturities	Fair Value
Certificates of Deposit	12 - 24 months	$ 2,571,315
PA School District Liquid Asset Fund		4,035,384
		$ 6,606,699

Although not registered with the Securities and Exchange Commission and not subject to regulatory oversight, PSDLAF funds act like money market mutual funds in that their objective is to maintain a stable net asset value of $1 per share, is rated by a nationally recognized statistical rating organization and is subject to an independent annual audit.

Interest Rate Risk
The District does not have a formal investment policy that limits investment maturities as a means of managing its exposure to fair value losses arising from increasing interest rates.

Credit Risk
The District has no investment policy that would limit its investment choices to certain credit ratings. As of June 30, 2014, the District's investments were rated as:

Investment	Standard & Poor's
PA School District Liquid Asset Fund	AAA

Concentration of Credit Risk
The District places no limit on the amount the District may invest in any one issuer. As of June 30, 2014, the District did not have any investments subject to concentration of credit risk.

Custodial Credit Risk
For an investment, custodial credit is the risk that, in the event of the failure of the counterparty, the District will not be able to recover the value of its investments or collateral security that are in the possession of an outside party. The District has no investment subject to custodial credit risk.

NOTE 3 - TAXES RECEIVABLE AND UNAVAILABLE REVENUE

The District has five independently elected tax collectors. Assessed values are established by the County Board of Assessment. All taxable real property was assessed at $678,851,200. The District's tax rate for the year ended June 30, 2014 was $29.2465 per $1,000 of assessed valuation. The schedule for real estate taxes levied for each fiscal year is as follows:

July 1	Levy date
July 1 - August 31	2% discount period
September 1 - October 31	Face payment period
November 1 - January 14	10% penalty period
January 15	Lien date

The District, in accordance with generally accepted accounting principles, recognized the delinquent and unpaid taxes receivable reduced by an allowance for uncollectible taxes as determined by administration. A portion of the net amount estimated to be collectible which was measurable and available within 60 days was recognized as revenue and the balance unavailable in the fund financial statements.

The balances at June 30, 2014 are as follows:

	Gross Taxes Receivable	Allowance for Uncollectible Taxes	Net Estimated to be Collectible	Tax Revenue Recognized	Unavailable Revenues
Real estate tax	$ 1,045,212	$ 20,904	$ 1,024,308	$ 141,108	$ 883,200
Transfer tax	13,167	-	13,167	13,167	-
Earned income tax	83,252	-	83,252	83,252	-
Other misc. tax	13,137	-	13,137	13,137	-
	$ 1,154,768	$ 20,904	$ 1,133,864	$ 250,664	$ 883,200

NOTE 4 - INTERGOVERNMENTAL RECEIVABLES

The following schedule represents intergovernmental receivables at June 30, 2014:

	General Fund	Proprietary Fund
Commonwealth of PA - Retirement	$ 400,335	$ -
Commonwealth of PA - Social Security	57,213	-
Commonwealth of PA - Food Nutrition Service	-	33,003
Commonwealth of PA - Rental Subsidy	145,828	
Other Local Education Agencies	13,149	-
Federal Subsidies - ARRA Race to the Top	530	-
Federal Subsidies - IDEA	282,982	-
Federal Subsidies - IDEA Preschool	938	-
Federal Subsidies - ACCESS Administration	2,199	-
	$ 903,174	$ 33,003

NOTE 5 - CHANGES IN CAPITAL ASSETS

Capital asset balances and activity for the year ended June 30, 2014 were as follows:

Governmental Activities

	Beginning Balance	Increase	(Reclass) Decrease	Ending Balance
Capital assets not being depreciated:				
Land	$ 46,090	$ -	$ -	$ 46,090
Construction-in-progress	62,510	501,005	(62,510)	501,005
Totals not be depreciated	108,600	501,005	(62,510)	547,095
Capital assets being depreciated:				
Site improvements	1,115,653	5,415	-	1,121,068
Buildings and building improvements	40,666,416	283,773	-	40,950,189
Fixtures and equipment	4,376,699	1,284,915	(886,159)	4,775,455
Totals being depreciated	46,158,768	1,574,103	(886,159)	46,846,712
Less accumulated depreciation for:				
Site improvements	665,837	50,414	-	716,251
Buildings and building improvements	14,634,772	730,170	-	15,364,942
Fixtures and equipment	2,466,147	452,683	(881,673)	2,037,157
Total accumulated depreciation	17,766,756	1,233,267	(881,673)	18,118,350
TOTAL CAPITAL ASSETS BEING DEPRECIATED, NET	28,392,012	340,836	(4,486)	28,728,362
GOVERNMENTAL ACTIVITIES, CAPITAL ASSETS, NET	$ 28,500,612	$ 841,841	$ (66,996)	$ 29,275,457

Business-Type Activities

Capital assets being depreciated:				
Furniture and equipment	$ 665,494	$ 60,597	$ -	$ 726,091
Accumulated depreciation for:				
Furniture and equipment	512,640	12,485	-	525,125
BUSINESS-TYPE ACTIVITIES CAPITAL ASSETS, NET	$ 152,854	$ 48,112	$ -	$ 200,966

NOTE 5 - CHANGES IN CAPITAL ASSETS - CONTINUED

Depreciation expense was charged to the functions/programs of the governmental activities of the primary government as follows:

Instructional	$ 278,142
Support Services	164,542
Operation of Noninstructional Services	933
Unallocated	789,650
TOTAL DEPRECIATION EXPENSE - GOVERNMENTAL ACTIVITIES	$ 1,233,267

NOTE 6 - LONG-TERM LIABILITIES

Long-term liabilities except for compensated absences were:

General Obligation Bond - Series of 2013:
The District is liable for general obligation bonds dated May 15, 2013 in the original principal amount of $6,435,000. Principal maturities occur on August 15 through the year 2022. Interest rates range from 0.25% to 2.00%. The proceeds of this Bond were used to advance refund the General Obligation Bonds - Series 2009 and to pay debt issuance costs. The refunding resulted in a net annual cash flow savings of $256,025 with a corresponding net present value savings of $258,170. $ 6,035,000

General Obligation Bond - Series of 2005:
The District is liable for general obligation bonds dated April 1, 2005 in the original principal amount of $18,015,000. Principal maturities occur on March 15 through the year 2024. Interest rates range from 2.60% to 5.00%. The proceeds of this Bond were used to currently refund the General Obligation Bonds - Series 1999 and to pay debt issuance costs. 11,650,000

Total Bonds Payable $ 17,685,000

NOTE 6 - LONG-TERM LIABILITIES - CONTINUED

Capital Leases

Capital lease liabilities are as follows:

Capitalized lease obligation for computers, with annual payments of $283,496, with final payment due in July, 2016. The lease has an effective rate of 1.94 percent.	$ 817,885

The amount of capitalized lease equipment included on the balance sheet at June 30, 2014 is:

Cost	$ 1,101,381
Accumulated depreciation	(137,673)
Net Book Value	$ 963,708

The future annual payments required to amortize all outstanding debt and obligations, except for compensated absences for the years ending June 30 are as follows:

	General Obligation Bond Series of 2005	General Obligation Bond Second Series of 2013	Total Principal	Interest	Capital Lease Obligation
2015	$ 895,000	$ 635,000	$ 1,530,000	$ 594,293	$ 267,651
2016	940,000	640,000	1,580,000	546,034	272,832
2017	990,000	645,000	1,635,000	493,729	277,402
2018	1,030,000	655,000	1,685,000	445,991	-
2019	1,070,000	670,000	1,740,000	393,179	-
2020 - 2024	6,725,000	2,790,000	9,515,000	1,056,816	-
	$ 11,650,000	$ 6,035,000	$ 17,685,000	$ 3,530,042	$ 817,885

NOTE 6 - LONG-TERM LIABILITIES - CONTINUED

Long-term liability balance and activity, except for postemployment benefits, for the year ended June 30, 2014 was as follows:

	Beginning Balance	Additions	Reductions	Ending Balance	Amounts Due Within One Year
Governmental Activities					
General Obligation Debt:					
Bonds payable	$ 19,330,000	$ -	$ 1,645,000	$ 17,685,000	$ 1,530,000
Less deferred amounts:					
For issuance discounts	(72,338)	-	(6,789)	(65,549)	-
For issuance premiums	113,029	-	11,826	101,203	-
Subtotal	19,370,691	-	1,650,037	17,720,654	1,530,000
Other Liabilities:					
Capital lease payable	-	1,101,381	283,496	817,885	267,651
Compensated absences	441,362	-	2,717	438,645	74,799
TOTAL GOVERNMENTAL LONG-TERM LIABILITIES	$ 19,812,053	$ 1,101,381	$ 1,936,250	$ 18,977,184	$ 1,872,450

Payments on bonds and capital leases payable are made by the general fund. The compensated absence liabilities will be liquidated by the general fund. Total interest paid during the year ended June 30, 2014 was $620,315.

Defeased Debt

During the year ended June 30, 2013, the District issued General Obligation Bonds, Series of 2013 in the amount of $6,435,000, that were used to advance refund the balance of the General Obligation Bonds, Series of 2009. The advance refunding met the requirements of an in-substance debt defeasance and the bonds were removed from the District's long-term liabilities.

As of June 30, 2014, outstanding general obligation bonds of the District in the amount of $5,575,000 were considered to be defeased with a related $5,666,440 (market value at June 30, 2014) held in escrow funds.

NOTE 7 - EMPLOYEE RETIREMENT PLANS

Multi-Employer Defined Pension Plan

Plan Description

The District contributes to a governmental cost-sharing, multiple-employer defined pension plan administered by the Commonwealth of Pennsylvania Public School Employees Retirement System (PSERS). Benefit provisions of the Plan are established under the provisions of the PSERS Code (Act No. 96 of October 2, 1975) and may be amended by an act of the Pennsylvania State Legislature. The Plan provides retirement, disability, and death benefits, legislatively mandated ad hoc cost-of-living adjustments, and healthcare insurance premium assistance to qualifying plan members and beneficiaries. It also provides for refunds of a member's accumulated contribution upon termination of a member's employment in the public school sector. PSERS issues a publicly available financial report that includes financial statements for the Plan. That report may be obtained by writing to PSERS, PO Box 125, Harrisburg, PA 17108-0125. The publication is also available on the PSERS website at www.psers.state.pa.us/publications/cafr/index.htm.

Funding Policy

The contribution policy is set by the Code and requires contributions by active employees and by participating employers. Active members who joined the System prior to July 22, 1983, contribute at 5.25 percent (Membership Class TC) or at 6.50 percent (Membership Class TD) of the member's qualifying compensation. Members joining PSERS on or after July 22, 1983 and who were active or inactive as of July 1, 2001, contribute at 6.25 percent (Membership Class TC) or at 7.50 percent (Membership Class TD) of the member's qualifying compensation. Members joining PSERS after June 30, 2001 contribute at 7.50 percent (automatic Membership Class TD). For all new hires and for members who elected Class TD membership, the higher contribution rates began with service rendered on or after January 1, 2002. Members joining PSERS on or after July 1, 2011, contribute a 7.5 percent (Membership Class TE) or at 10.30 percent (Membership Class TF). Both membership classes TE and TF contain a "shared risk" which allows for an increase in the contribution percentage up to an additional 2.00 percent based on market results.

The contributions required of participating employers are based on an actuarial valuation and are expressed as a percentage of annual covered payroll during the period for which the amount is determined. For the fiscal year ended June 30, 2014, the rate of employer contributions was 16.93 percent of covered payroll. The 16.93 percent rate is composed of a pension contribution, 16.00 percent of pension benefits and 0.93 percent for healthcare insurance premium assistance. The District's contributions to PSERS for the years ended June 30, 2014, 2013, and 2012 were $2,274,561, $1,619,723, and $1,164,715, respectively.

403(b) Tax Shelter Plan

The District has established a 403(b) tax shelter plan permitting the establishment of accounts for school employees to voluntarily set aside monies to supplement their retirement income. All school employees are eligible to participate. The District does not contribute to the Plan.

NOTE 8 - POSTEMPLOYMENT BENEFITS PLAN

Plan Description

Kutztown Area School District administers a single-employer defined benefit healthcare plan (the Retiree Health Plan). The Plan provides lifetime healthcare insurance for eligible retirees and their spouses through the District's health insurance plan, which covers both active and retired members. Benefit provisions are established through negotiation with the District and the unions representing the District's employees. The Retiree Health Plan does not issue a publicly available financial report.

Funding Policy

Contribution requirements are negotiated between the District and union representatives. The required contribution is based on pay as you go financing. For all employees with 30 years of PSERS service or upon superannuation retirement (age 60 with 30 years of service, age 62 with one year of service, or 35 years of service regardless of age), the retired plan member pays the premium determined for the purpose of COBRA. The retired plan member may elect to continue coverage for themselves and their dependents until the retired plan member reaches Medicare age. For the fiscal year ended June 30, 2014, the District contributed $262,338 to the Plan related to retirees.

Annual OPEB Cost and Net OPEB Obligation

The District's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with the parameters of GASB Statement 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal cost each year and amortize any unfunded actuarial liabilities (or funding excess) over a period not to exceed thirty years. The following table shows the components of the District's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District's net OPEB obligation:

Annual required contribution	$ 382,121
Interest on net OPEB obligation	19,314
Adjustment to annual required contribution	(34,163)
Annual OPEB Cost	367,272
Contributions made	(272,768)
Increase in net OPEB obligation	94,504
Net OPEB obligation - beginning of year	482,853
Net OPEB obligation - end of year	$ 577,357

NOTE 8 - POSTEMPLOYMENT BENEFITS PLAN - CONTINUED

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the Plan, and the net OPEB obligation was as follows:

Fiscal Year Ended	Annual OPEB Cost	Percentage of Annual OPEB Cost Contributed	Net OPEB Obligation
6/30/2014	$ 367,272	74.3%	$ 577,357
6/30/2013	374,836	70.0%	482,853
6/30/2012	323,353	72.3%	370,355

Funded Status and Funding Progress

As of July 1, 2012, the most recent actuarial valuation date, the plan was unfunded. The actuarial accrued liability for benefits was $3,025,606, and the actuarial value of assets was $0, resulting in an unfunded actuarial accrued liability (UAAL) of $3,025,606. The covered payroll (annual payroll of active employees covered by the Plan) was $12,006,662, and the ratio of the UAAL to the covered payroll was 25.2 percent.

Actuarial valuations of an ongoing plan involve estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the Plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The schedule of funding progress, presented as required supplementary information following the notes to the financial statements, presents information about actuarial value of plan assets and actuarial accrued liabilities for benefits.

Actuarial Methods and Assumptions

Projections of benefits for financial reporting purposes are based on the substantive Plan (the Plan as understood by the employer and the plan members) and include the types of benefits provided at the time of each valuation and the historical pattern of sharing of benefit costs between the employer and plan members to that point. The actuarial methods and assumptions used include techniques that are designed to reduce the effects of short-term volatility in actuarial accrued liabilities and the actuarial value of assets, consistent with the long-term perspective of the calculations.

In the July 1, 2012 actuarial valuation, the entry age actuarial cost method was used. The actuarial assumptions included a 4.0 percent investment rate of return (net of administrative expenses) and an annual healthcare cost trend rate of 7.0 percent initially, decreasing 1.0 percent per year to an ultimate rate of 5 percent in 2015 and later. The unfunded actuarial accrued liability is being amortized at the end of the year based on level dollar and a twenty-year open amortization period.

NOTE 9 - INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS

The following is a summary of interfund receivables and payables at June 30, 2014:

	Interfund Receivables	Interfund Payables
General Fund	$ -	$ 837,853
Capital Projects Fund	858,088	-
Proprietary Fund - Food Service	-	20,235
	$ 858,088	$ 858,088

Interfund receivables and payables exist as a result of a time lag between dates when payments between funds are made. All will be paid within one year.

Interfund transfers are summarized as follows:

	Operating Transfers In	Operating Transfers Out
General Fund	$ -	$ 1,032,000
Capital Projects Fund	975,929	-
Proprietary Fund - Food Service	56,071	-
	$ 1,032,000	$ 1,032,000

Transfers are generally made to subsidize food service fund costs and to reserve for future capital needs.

NOTE 10 - JOINT VENTURE

The District is a participating member of the Berks Career & Technology Center. The Berks Career & Technology Center is controlled and governed by a joint board, which is composed of representative school board members of the participating schools. Direct oversight of Berks Career & Technology Center operations is the responsibility of the joint board. The District's share of annual operating and capital costs for Berks Career & Technology Center fluctuates based on the percentage of enrollment. The District's share for the 2013/14 year was $567,555.

NOTE 10 - JOINT VENTURE - CONTINUED

Berks Career Vocational Technical School Authority issued General Obligation Bonds and lent the proceeds to Berks Career & Technology Center. The proceeds are being used to renovate and build an addition to Berks Career & Technology Center's facilities. Each member district adopted a resolution approving the project and the project's maximum cost. Under the amended Articles of Agreement, each member district is required to pay from current revenues its annual share of the sublease rental based on the District's share of taxable real estate to the total market valuation of the taxable real estate of all participating school districts. The District's share for the 2013/14 year was $111,168.

Summary financial information as of June 30, 2013 (the most recent information available) is as follows:

Berks Career & Technology Center (Governmental Activities)	
Total Assets and Deferred Outflows of Resources	$ 32,748,687
Total Liabilities	16,457,162
Total Net Position	$ 16,291,525

Separate financial statements of the Berks Career & Technology Center have been prepared and are available.

NOTE 11 - RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. Significant losses are covered by commercial insurance for all major programs except for workers' compensation, for which the District retains risk of loss. The District monitors its insured programs and increases insurance coverage as needed. Settlement amounts have not exceeded insurance coverage for the current year or the three prior years. The District has no unfunded liability.

The District is a member of the School Districts Insurance Consortium (SDIC) for workers' compensation coverage. SDIC is comprised of 80 member school districts which jointly self-assume their workers' compensation liabilities. Even though the member school districts contribute to SDIC's insurance fund, they remain individually liable for their own workers' compensation claims. The members of SDIC are required to participate in any deficiencies of SDIC and are subject to periodic assessments, as required. At June 30, 2014, there was no unfunded liability.

NOTE 12 - CONTINGENT LIABILITIES AND COMMITMENTS

The District receives federal, state, and local funding through a number of programs. Payments made by these sources under contractual agreements are provisional and subject to redetermination based on filing reports and audits of those reports. Final settlements due from or to these sources are recorded in the year in which the related services are performed. Any adjustments resulting from subsequent examinations are recognized in the year in which the results of such examinations become known. District officials do not expect any significant adjustments as a result of these examinations.

The District has a commitment related to a billing issue with the Berks Career & Technology Center for $181,533 as of June 30, 2014. This liability is payable in annual installments beginning in the 2011/2012 school year and ending 2018/2019.

During the year, the District awarded a contract for $573,000 for middle school boiler room upgrades. Included in capital project funds are costs totaling $463,658 related to this contract, leaving a commitment remaining of $109,342.

NOTE 13 - FUND BALANCE

Details of the District's governmental fund balance reporting and policy can be found in Note 1, *Summary of Significant Accounting Policies.* Fund balance classifications for the year ended June 30, 2014 were as follows:

General Fund
The general fund has a nonspendable fund balance of $25,606, restricted fund balance for the athletic department of $11,739, committed funds of $1,600,486 for future capital projects, $1,360,310 for future PSERS contributions, $181,533 for amounts due to the Berks Career & Technology Center, and $115,147 for further development of Kutztown Virtual Academy and assigned fund balance of $753,128 to balance the 2014/15 budget and unassigned fund balance of $2,439,599. The commitments were authorized by the board of school directors' motion to set aside resources for specific purposes.

Capital Projects Fund
The capital projects fund has restricted funds of $1,210,952 comprised of surplus monies transferred from the general fund for the acquisition or construction of capital facilities and qualifying capital assets as authorized by Municipal Code P.L. 145 Act of April 30, 1943.

NOTE 14 - NEW ACCOUNTING PRONOUNCEMENTS

The Government Accounting Standards Board (GASB) has issued the following standards which have not yet been implemented:

- Statement No. 68, *Accounting and Financial Reporting for Pensions*, which is required to be implemented by the year ended June 30, 2015. The objective of this statement is to improve accounting and financial reporting by governments for pensions. This statement establishes standards for measuring and recognizing liabilities, deferred outflows of resources, deferred inflows of resources, and expenditures. This statement also enhances note disclosure and required supplementary information for government pension plans. This pronouncement applies to employers that have a legal obligation to make contributions directly to a pension plan.

- Statement No. 71, *Pension Transition for Contributions Made Subsequent to the Measurement Date* - an amendment of GASB Statement No. 68 will be implemented at the same time of implementation of 68.

Although the District has not yet completed the analyses necessary to determine the financial statement impact of these new pronouncements, it does believe the new standards will have a negative impact on the District's net position.

REQUIRED SUPPLEMENTARY INFORMATION

KUTZTOWN AREA SCHOOL DISTRICT

BUDGETARY COMPARISON SCHEDULE FOR THE GENERAL FUND

For the Year Ended June 30, 2014

REVENUES	Budgeted Amount Original	Budgeted Amount Final	Actual (GAAP) Basis	Variances Final to Actual
REVENUES				
Local Sources	$ 20,894,030	$ 20,894,030	$ 21,631,626	$ 737,596
State Sources	7,326,671	7,326,671	7,381,937	55,266
Federal Sources	384,499	384,499	316,774	(67,725)
TOTAL REVENUES	28,605,200	28,605,200	29,330,337	725,137
EXPENDITURES				
EXPENDITURES - INSTRUCTION				
Regular Programs - Elementary/Secondary	11,444,604	11,444,604	11,006,041	438,563
Special Programs - Elementary/Secondary	4,200,435	4,200,435	3,950,481	249,954
Vocational Education Programs	1,150,238	1,150,238	1,091,622	58,616
Other Instructional Programs - Elementary/Secondary	190,156	190,156	168,726	21,430
Adult Education Programs	4,904	4,904	4,250	654
TOTAL INSTRUCTION	16,990,337	16,990,337	16,221,120	769,217
SUPPORT SERVICES				
Pupil Personnel	945,902	945,902	893,711	52,191
Instructional Staff	1,547,497	1,547,497	1,467,186	80,311
Administration	1,411,748	1,411,748	1,574,308	(162,560)
Pupil Health	339,692	339,692	387,183	(47,491)
Business	345,916	345,916	342,046	3,870
Operation and Maintenance of Plant Services	2,919,530	2,919,530	2,585,331	334,199
Student Transportation Services	1,244,328	1,244,328	1,195,473	48,855
Central Services	154,269	154,269	178,212	(23,943)
Other Support Services	28,000	28,000	25,170	2,830
TOTAL SUPPORT SERVICES	8,936,882	8,936,882	8,648,620	288,262
OPERATION OF NONINSTRUCTIONAL SERVICES				
Student Activities	576,192	576,192	567,226	8,966
Community Services	19,650	19,650	6,401	13,249
TOTAL OPERATION OF NONINSTRUCTIONAL SERVICES	595,842	595,842	573,627	22,215
Capital Outlay	-	-	1,101,381	(1,101,381)
Debt Service	2,265,289	2,265,289	2,548,811	(283,522)
Refund of Prior Year Revenues	-	-	49	(49)
TOTAL EXPENDITURES	28,788,350	28,788,350	29,093,608	(305,258)
EXCESS OF REVENUES OVER EXPENDITURES	(183,150)	(183,150)	236,729	419,879

See note to required supplementary information.

KUTZTOWN AREA SCHOOL DISTRICT

BUDGETARY COMPARISON SCHEDULE FOR THE GENERAL FUND - CONTINUED

For the Year Ended June 30, 2014

	Budgeted Amount		Actual	Variances Final to
	Original	Final	(GAAP) Basis	Actual
OTHER FINANCING SOURCES (USES)				
Sale of Fixed Assets	500	500	85,438	84,938
Proceeds from Capital Lease	-	-	1,101,381	1,101,381
Operating Transfers Out	(1,032,000)	(1,032,000)	(1,032,000)	-
TOTAL OTHER FINANCING SOURCES (USES)	(1,031,500)	(1,031,500)	154,819	1,186,319
REVENUES AND OTHER FINANCING SOURCES OVER (UNDER) EXPENDITURES AND OTHER FINANCING USES	$ (1,214,650)	$ (1,214,650)	391,548	$ 1,606,198
FUND BALANCE - BEGINNING OF YEAR			6,096,000	
FUND BALANCE - END OF YEAR			$ 6,487,548	

See note to required supplementary information.

KUTZTOWN AREA SCHOOL DISTRICT

SCHEDULE OF FUNDING PROGRESS - POSTEMPLOYMENT BENEFITS PLAN

	Actuarial Valuation Date	Actuarial Value of Assets (a)	Actuarial Accrued Liability (AAL) - Entry Age (b)	Unfunded AAL (UAAL) (b - a)	Funded Ratio (a / b)	Covered Payroll (c)	UAAL as a Percentage of Covered Payroll ((b - a) / c)
Governmental Activities	7/1/2012	$ -	$ 2,996,213	$ 2,996,213	0.00%	N/A	N/A
	7/1/2010	-	2,550,079	2,550,079	0.00%	N/A	N/A
	7/1/2008	-	2,701,230	2,701,230	0.00%	N/A	N/A
Business-type Activities	7/1/2012	-	29,393	29,393	0.00%	N/A	N/A
	7/1/2010	-	21,656	21,656	0.00%	N/A	N/A
	7/1/2008	-	61,973	61,973	0.00%	N/A	N/A
Total	7/1/2012	-	3,025,606	3,025,606	0.00%	$ 12,006,662	25.2%
	7/1/2010	-	2,571,735	2,571,735	0.00%	11,992,719	21.4%
	7/1/2008	-	2,763,203	2,763,203	0.00%	N/A	N/A

See note to required supplementary information.

KUTZTOWN AREA SCHOOL DISTRICT

NOTE TO REQUIRED SUPPLEMENTARY INFORMATION

For the Year Ended June 30, 2014

BUDGETARY DATA

The budget for the general fund is adopted on the modified accrual basis of accounting which is consistent with generally accepted accounting principles.

SUPPLEMENTARY INFORMATION

KUTZTOWN AREA SCHOOL DISTRICT

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the Year Ended June 30, 2014

Grantor/Program Title	Source Code	Federal CFDA Number	Federal Pass-Through Grantor's Number	Program or Award Amount	Grant Period Beginning/ Ending Date	Total Received for Year	Accrued or (Unearned) Revenue at July 1, 2013	Revenue Recognized	Expenditures	Accrued or (Unearned) Revenue at June 30, 2014
U.S. Department of Education										
Passed through the State Department of Education:										
Title I Grants to Local Educational Agencies	I	84.010	013-14-0215	$ 235,576	07/01/13-09/30/14	$ 237,492	$ -	$ 235,576	$ 235,576	$ (1,916)
Title I Grants to Local Educational Agencies	I	84.010	013-13-0215	265,390	07/01/12-09/30/13	88,089	66,601	21,488	21,488	-
Total Title I						325,581	66,601	257,064	257,064	(1,916)
Improving Teacher Quality State Grants	I	84.367	020-14-0215	52,307	07/01/13-09/30/14	52,307	-	52,099	52,099	(208)
Passed through the Berks County Intermediate Unit:										
Special Education Cluster (IDEA)										
Special Education - Grants to States	I	84.027	N/A	282,982	07/01/13-06/30/14	-	-	282,982	282,982	282,982
Special Education - Grants to States	I	84.027	N/A	291,915	07/01/12-06/30/13	161,547	161,547	-	-	-
Special Education - Preschool Grants	I	84.173	N/A	938	07/01/13-06/30/14	-	-	938	938	938
Special Education - Preschool Grants	I	84.173	N/A	1,405	07/01/12-06/30/13	1,405	1,405	-	-	-
Total Special Education Cluster (IDEA)						162,952	162,952	283,920	283,920	283,920
ARRA Race to the Top - Phase III	I	84.413A	N/A	14,505	12/22/11-12/22/15	8,320	8,320	530	530	530
TOTAL U. S. DEPARTMENT OF EDUCATION						549,160	237,873	593,613	593,613	282,326
U.S. Department of Health and Human Services										
Passed through the Pennsylvania Department of Welfare:										
Medical Assistance Program	I	93.778	N/A	N/A	07/01/13-06/30/14	5,412	-	7,611	7,611	2,199
Medical Assistance Program	I	93.778	N/A	N/A	07/01/12-06/30/13	1,204	1,204	-	-	-
TOTAL U. S. DEPARTMENT OF HEALTH AND HUMAN SERVICES						6,616	1,204	7,611	7,611	2,199
U.S. Department of Agriculture										
Child Nutrition Cluster										
Passed through the State Department of Education:										
School Breakfast Program	I	10.553	N/A	N/A	07/01/13-06/30/14	17,375	-	20,796	20,796	3,421
School Breakfast Program	I	10.553	N/A	N/A	07/01/12-06/30/13	384	384	-	-	-
National School Lunch Program	I	10.555	N/A	N/A	07/01/13-06/30/14	143,434	-	170,161	170,161	26,727
Passed through the PA Department of Agriculture:										
National School Lunch Program	I	10.555	N/A	N/A	07/01/13-06/30/14	41,447	(5,860)	37,798	37,798	(9,509)
TOTAL CHILD NUTRITION CLUSTER AND U. S. DEPARTMENT OF AGRICULTURE						202,640	(5,476)	228,755	228,755	20,639
TOTAL FEDERAL AWARDS						$ 758,416	$ 233,601	$ 829,979	$ 829,979	$ 305,164

KUTZTOWN AREA SCHOOL DISTRICT

NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

For the Year Ended June 30, 2014

NOTE 1 - BASIS OF ACCOUNTING

The accompanying schedule of expenditures of federal awards is presented using the accrual basis of accounting, which is the same basis used for the basic financial statements.

NOTE 2 - FOOD COMMODITIES

Nonmonetary assistance is reported in the schedule at the fair market value of the commodities received and disbursed. At June 30, 2014, the District had $9,509 of food commodity inventory.

Herbein + Company, Inc.
2763 Century Boulevard
Reading, PA 19610
P: 610.378.1175
F: 610.378.0999
www.herbein.com

Independent Auditor's Report on Internal Control over Financial Reporting and on Compliance and Other Matters Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards*

To the Board of School Directors
Kutztown Area School District
Kutztown, Pennsylvania

We have audited, in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Kutztown Area School District, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the Kutztown Area School District's basic financial statements and have issued our report thereon dated October 23, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the Kutztown Area School District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Kutztown Area School District's internal control. Accordingly, we do not express an opinion on the effectiveness of the Kutztown Area School District's internal control.

A *deficiency in internal control* exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct misstatements on a timely basis. A *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit attention by those charged with governance.

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or, significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Kutztown Area School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the entity's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the entity's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Herbein + Company, Inc.

Reading, Pennsylvania
October 23, 2014

Herbein + Company, Inc.
2763 Century Boulevard
Reading, PA 19610
P: 610.378.1175
F: 610.378.0999
www.herbein.com

Independent Auditor's Report on Compliance for Each Major Program
and on Internal Control Over Compliance Required by OMB Circular A-133

To the Board of School Directors
Kutztown Area School District
Kutztown, Pennsylvania

Report on Compliance for Each Major Federal Program

We have audited Kutztown Area School District's compliance with the types of compliance requirements described in the *OMB Circular A-133 Compliance Supplement* that could have a direct and material effect on each of the Kutztown Area School District's major federal programs for the year ended June 30, 2014. The Kutztown Area School District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the Kutztown Area School District's major federal programs based on our audit of the types of compliance requirements referred to above. We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Kutztown Area School District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the Kutztown Area School District's compliance.

Opinion on Each Major Federal Program

In our opinion, the Kutztown Area School District complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

Report on Internal Control Over Compliance

Management of the Kutztown Area School District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the Kutztown Area School District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of the Kutztown Area School District's internal control over compliance.

A *deficiency in internal control over compliance* exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. A *material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. A *significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Herbein + Company, Inc.

Reading, Pennsylvania
October 23, 2014

KUTZTOWN AREA SCHOOL DISTRICT

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For the Year Ended June 30, 2014

Section I - Summary of Auditor's Results

Financial Statements

Type of Auditor's Report Issued:	Unmodified	
Internal Control Over Financial Reporting:		
Material weakness(es) identified?	____ yes	X no
Significant deficiency(ies) identified not considered to be material weaknesses?	____ yes	X none reported
Noncompliance material to financial statements noted?	____ yes	X no

Federal Awards

Internal Control Over Major Programs:		
Material weakness(es) identified?	____ yes	X no
Significant deficiency(ies) identified not considered to be material weaknesses?	____ yes	X none reported
Type of Auditor's Report Issued on Compliance for Major Programs:	Unmodified	
Any audit findings disclosed that are required to be reported in accordance with Circular A-133, Section .510(a)?	____ yes	X no

Identification of Major Program(s):

CFDA Number(s)	Name of Federal Program or Cluster
Child Nutrition Cluster	
10.555	National School Lunch Program
10.553	School Breakfast Program

Dollar Threshold used to distinguish between Type A and Type B Programs: $300,000

Auditee qualified as low-risk auditee? X yes ____ no

KUTZTOWN AREA SCHOOL DISTRICT

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

For the Year Ended June 30, 2014

Section II - Financial Statement Findings

There were no financial statements findings reported.

Section III - Federal Award Findings and Questioned Costs

There were no federal award findings or questioned costs reported.

KUTZTOWN AREA SCHOOL DISTRICT

STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS

For the Year Ended June 30, 2014

FEDERAL FUNDS REPORTING

National School Lunch Program CFDA 10.555; passed through the Pennsylvania Department of Education; Grant Period 7/1/12-6/30/13
School Breakfast Program CFDA 10.553; passed through the Pennsylvania Department of Education; Grant Period 7/1/12-6/30/13 - Special tests - verification requirements - significant deficiency in internal control over compliance and significant deficiency instance of noncompliance.

Criteria
Title 7 CFR 245 covers eligibility requirements for all programs within the Child Nutrition Cluster. Title 7 CFR 245.6a requires that the local education agency must verify eligibility of children in a sample of household applications approved for free and reduced price meal benefits for that school year. The local educational agency must select an allowable sample and complete the verification efforts no later than November 15 of each school year. Based on the verification activities, the education agency must make appropriate modifications to the eligibility determinations made initially.

Condition
Upon examining documentation of the verification process, it was noted that two applications for which the eligibility status should have been verified as change from Free to Reduced was instead verified as No change - Free. An additional application for which the eligibility status should have been verified as change from Free to Reduced was instead verified as change from Free to Paid; however, the change was never made in the point of sale system.

Questioned Costs
Known questioned costs less than $10,000.

Context
From a District-wide population of 1,468 students with 57 applications approved as free and 56 applications approved as reduced price, four of the approved applications were selected for verification. Of the four that were verified, three had no changes and one had a change in eligibility from free to paid which was never made.

Cause
The District did not have written policies covering the verification process. Further, there was no supervisory review of the verification process and documentation was not consistently done. Both factors caused a breakdown in internal controls that led to the actual inappropriate classification of three participant families consisting of eight students in aggregate.

Effect
Participants receiving NSLP program benefits at a free rate when they should have been receiving at a reduced rate. Additionally there were improper payments from a federal program as the local education agency was reimbursed more than what was appropriate.

KUTZTOWN AREA SCHOOL DISTRICT

STATUS OF PRIOR YEAR FINDINGS AND QUESTIONED COSTS

For the Year Ended June 30, 2014

Recommendation

We recommend the following:

1. The District establish written policies covering eligibility for free and reduced price meals including the verification process for use by all schools as well as at the District office. Those policies should include approval of eligibility by more than a single person. Training should be conducted on these policies.

2. The District should consider a more formal review program for NSLP operations at the individual school level. As appropriate, the review function could be expanded to cover all programs of the Child Nutrition Cluster.

Current Status of Corrective Action Plan

The recommendation was adopted and no similar findings were noted in the current year.