

**FRANKLIN-MCKINLEY
SCHOOL DISTRICT**

ANNUAL FINANCIAL REPORT

JUNE 30, 2012

FRANKLIN-MCKINLEY SCHOOL DISTRICT

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FINANCIAL SECTION

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INDEPENDENT AUDITOR'S REPORT

Governing Board
Franklin-McKinley School District
San Jose, California

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of the Franklin-McKinley School District (the District) as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the District's management. 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; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2011-2012*, issued by the California Education Audit Appeals Panel as regulations. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to previously present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of the Franklin-McKinley School District, as of June 30, 2012, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated November 30, 2012, 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 the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis on page 4 through 13 and budget comparison schedule on page 51 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's financial statements. The Schedule of Expenditures of Federal Awards, as required by *Office of Management and Budget Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations* (Circular A-133) and other supplementary information listed in the table of contents are presented for purposes of additional analysis and are not a required part of the financial statements. Such information is the responsibility of management and was derived from and relates directly to the underlying accounting and other records used to prepare the financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the supplementary information is fairly stated in all material respects in relation to the financial statements as a whole.



Palo Alto, California
November 30, 2012

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

This section of Franklin-McKinley School District's (the District) annual financial report presents our discussion and analysis of the District's financial performance during the fiscal year that ended on June 30, 2012. Please read it in conjunction with the District's financial statements, which immediately follow this section.

OVERVIEW OF THE FINANCIAL STATEMENTS

The Financial Statements

The financial statements presented herein include all of the activities of the District using the integrated approach as prescribed by GASB Statement Number 34 (The Statement).

The Government-Wide Financial Statements present the financial picture of the District from the economic resources measurement focus using the accrual basis of accounting. They present governmental activities. These statements include all assets of the District (including capital assets) as well as all liabilities (including long-term debt). Additionally, certain eliminations have occurred as prescribed by the Statement in regards to interfund activity, payables, and receivables.

The Fund Financial Statements include statements for each of the three categories of activities: governmental, proprietary, and fiduciary.

- The Governmental Activities are prepared using the current financial resources measurement focus and modified accrual basis of accounting.
- The Proprietary Activities are prepared using the economic resources measurement focus and the accrual basis of accounting.
- The Fiduciary Activities are agency funds, which only report a balance sheet and do not have a measurement focus.

Reconciliation of the Fund Financial Statements to the Government-Wide Financial Statements is provided to explain the differences created by the integrated approach.

The Primary unit of the government is the District.

FINANCIAL HIGHLIGHTS OF THE PAST YEAR

The District's primary source of operating revenue is based on a revenue limit calculation as required by the State of California. The revenue limit is determined by multiplying the District's base revenue limit times the average daily attendance (ADA) for the year. During 2011-2012, the District's base revenue limit per ADA before any deficit or reduction totaled \$6,211.12. This funding level represents an increase of \$137.00 per ADA or a 2.24% increase over the prior year's base revenue limit. Due to the State budget shortage, the State applied deficit and other revenue limit adjustments to the base revenue limit. The deficit is 20.602% or \$1,279.61 per ADA. The funded revenue limit per ADA after deficit and other adjustments is \$4,931.51. The District converted Fair Middle School to Bridges Academy as a dependent Charter School in 2010-11. Bridges Academy is funded through the Block Grant and the funding is part of district's revenue limit source. The total funded ADA including

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

Bridges of 9,838 resulted in a total revenue limit of \$47.4 million of the General Fund revenues for fiscal year 2011-2012.

The recommended reserves for a district our size equals 3% of General Fund expenditures and other financing uses. The Board of Trustees passed a resolution on June 14, 2011 to maintain a minimum unassigned fund balance of 5% of the District's General Fund annual operating expenditures. If a fund balance drops below 4%, it shall be recovered at a rate of 1% minimally each year. This policy will be revisited each year. At June 30, 2012, the District's available reserves totaled \$6,598,315 consisting of \$4,333,717 in unassigned fund balance and \$2,264,598 reserved for economic uncertainties. This reserve amount is equal to 8.74% of General Fund expenditures and other financing uses.

REPORTING THE DISTRICT AS A WHOLE

The Statement of Net Assets and the Statement of Activities

The Statement of Net Assets and the Statement of Activities report information about the District as a whole and about its activities. These statements include all assets and liabilities of the District using the accrual basis of accounting, which is similar to the accounting used by most private-sector companies. All of the current year's revenues and expenses are taken into account regardless of when cash is received or paid.

These two statements report the District's net assets and changes in them. Net assets are the difference between assets and liabilities, one way to measure the District's financial health, or financial position. Over time, increases or decreases in the District's net assets are one indicator of whether its financial health is improving or deteriorating. Other factors to consider are changes in the District's property tax base and the condition of the District's facilities.

The differences between revenues and expenses are the District's operating results. Since the Board's responsibility is to provide services to our students and not to generate profit as commercial entities do, one must consider other factors when evaluating the overall health of the District. The quality of the education and the safety of our schools will likely be an important component in this evaluation.

In the Statement of Net Assets and the Statement of Activities, we present the governmental activities, all of the District's services are reported in this category. This includes the education of kindergarten through grade eight students, the operation of the different educational programs and the on-going effort to improve and maintain buildings and sites. Property taxes, state income taxes, user fees, interest income, federal, state and local grants, as well as certificates of participation and general obligation bonds, finance these activities.

REPORTING THE DISTRICT'S MOST SIGNIFICANT FUNDS

Fund Financial Statements

The fund financial statements provide detailed information about the most significant funds - not the District as a whole. Some funds are required to be established by State law and by debt covenants. However, management establishes many other funds to help it control and manage money for particular purposes or to show that it is meeting legal responsibilities for using certain taxes, grants, and other money that it receives from the U.S. and State Departments of Education.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2012

Governmental funds - Most activities are reported in governmental funds, which focus on how money flows into and out of those funds and the balances left at year-end available 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 District's general government operations and the basic services it provides. Governmental fund information helps one determine whether there are more or fewer financial resources that can be spent in the near future to finance educational programs. As the name suggests, these funds record governmental type activities.

Proprietary funds - When the District charges users for the services it provides, whether to outside customers or to other departments within the District, these services are generally reported in proprietary funds. Proprietary funds are reported in the same way that all activities are reported in the Statement of Net Assets and the Statement of Revenues, Expenses and Changes in Net Assets. We use internal service funds to report activities that provide supplies and services for the District's other programs and activities - such as the District's Self-Insurance Fund. The internal service funds are reported with governmental activities in the government-wide financial statements.

THE DISTRICT AS TRUSTEE

Reporting the District's Fiduciary Responsibilities

The District is the trustee, or fiduciary, for funds held on behalf of others, like our funds for associated student body activities. The District's fiduciary activities are reported in the Statements of Fiduciary Net Assets. We exclude these activities from the District's other financial statements because the District cannot use these assets to finance its operations. The District is responsible for ensuring that the assets reported in these funds are used for their intended purposes.

THE DISTRICT AS A WHOLE

Net Assets

The District's net assets were \$52.1 and \$50.9 million for the fiscal years ended June 30, 2012, and 2011, respectively. Of these amounts, \$3.3 and \$2.2 million were unrestricted for the combined governmental funds for each respective year. Restricted net assets are reported separately to show legal constraints from debt covenants and enabling legislation that limit the Board's ability to use those net assets for day-to-day operations. Our analysis below focuses on the net assets (Table 1) and change in net assets (Table 2) of the District's governmental activities.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

Table 1

(Amounts in millions)

	Governmental Activities	
	2012	2011
Current and other assets	\$ 57.1	\$ 43.5
Capital assets	114.0	104.2
Total Assets	171.1	147.7
Current liabilities	21.2	11.8
Current portion of long-term debt	6.7	4.8
Long-term debt	91.1	80.2
Total Liabilities	119.0	96.8
Net assets		
Invested in capital assets, net of related debt	37.5	39.1
Restricted	11.3	9.6
Unrestricted	3.3	2.2
Total Net Assets	\$ 52.1	\$ 50.9

The \$3.3 million and \$2.2 million for fiscal years 2012 and 2011 in unrestricted net assets of governmental activities represent the accumulated results of all past years' operations. It means that if we had to pay off all of our bills at those year-end dates, including all of our non-capital liabilities (compensated absences as an example); we would have \$3.3 million and \$2.2 million left from governmental activities for fiscal years 2012 and 2011, respectively.

Current assets in 2012 increased by \$13.6 million and current liabilities increased by \$9.4 from 2011 mainly due to the district's issuance of a cross fiscal year TRAN in 2011-12 but not in 2010-11. The cross fiscal year TRAN was issued in February 2012 with a payback schedule of August 2012. The available cash and current liabilities are more at June 2012 compared with June 2011 due to the unpaid balance of TRAN. Long-term debt increased by \$12.8 million mainly due to the new issuance of the Election of 2010 General Obligation Bond, Series B. Net Assets increased by \$1.2 million to \$52.1 million in 2012 from \$50.09 million in 2011 mainly due to a slightly higher fund balance in General Fund and Non Major Governmental Funds.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS

JUNE 30, 2012

Changes in Net Assets

The results of this year's operations for the District as a whole are reported in the Statement of Activities. Table 2 takes the information from the Statement, rounds off the numbers, and rearranges them slightly so you can see our total revenues and expenses for the year.

Table 2

(Amounts in millions)	Governmental Activities	
	2012	2011
Revenues		
Charges for services	\$ 0.3	\$ 0.2
Operating grants and contributions	20.9	21.0
General revenues:		
Property tax, federal revenue and state revenue limit sources	66.6	67.0
Other general revenues	5.0	3.8
Total Revenues	92.9	92.0
Expenses		
Instruction related	64.4	64.5
Student support services	9.2	8.1
Administration	6.3	8.6
Maintenance and operations	7.0	7.5
Debt Service	4.5	3.7
Other	0.3	0.5
Total Expenses	91.7	92.9
Change in Net Assets	1.2	(0.9)
Net assets - beginning	50.9	51.8
Net assets - ending	\$ 52.1	\$ 50.9

Governmental Activities

As reported in the Statement of Activities, the cost of all of our governmental activities was \$91.7 and \$92.9 million for 2012 and 2011, respectively. However, the amount that our taxpayers ultimately financed for these activities through local taxes and other unrestricted revenue sources was only \$70.4 and \$71.7 million for 2012 and 2011. The cost paid by those who benefited from the programs was \$0.3 and \$0.2 million for 2012 and 2011, or by other governments and organizations who subsidized certain programs with grants and contributions of \$20.9 and \$21.0 million for 2012 and 2011. We paid for the "public benefit" portion of our governmental activities, with general revenue sources, primarily property taxes, in both years.

In Table 3, we have presented the net cost of each of the District's largest functions. Net cost shows the financial burden that was placed on the District's taxpayers by each of these functions. Providing this information allows our citizens to consider the cost of each function in comparison to the benefits they believe are provided by that function.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

Table 3

(Amounts in millions)

	Net Cost	
	2012	2011
Instruction	\$ 46.0	\$ 44.5
Instruction related	5.0	5.1
Pupil services	2.7	2.5
Administration	5.9	8.1
Maintenance	6.8	7.3
Interest on long-term obligation	4.5	3.7
Other	(0.4)	0.5
Totals	\$ 70.5	\$ 71.7

THE DISTRICT'S FUNDS

As the District completed this year, our governmental funds reported a combined fund balance of \$35 million, which was an increase of \$4.3 million from last year. The primary reason for the increase is related to the Building Fund. The district issued a General Obligation bond in April 2012 in the amount of \$15 million. Most of fund will disbursed during fiscal year 2012-2013 and after.

GENERAL FUND BUDGETARY HIGHLIGHTS

The Education Code requires that all local educational agencies adopt a budget by July 1, and then twice a year submit to their District Business Advisory Services in the County Offices of Education interim financial reports. The interim reports reflect updates to the District budget as grants are awarded and as the District revises its budget to reflect changes in revenues and expenditures. The final amendment to the budget was adopted in June 2012.

The District prepared the fiscal year 2011-2012 original adoption budget when the carryovers from fiscal year 2010-2011 were not known. The carryovers, however, were included in the fiscal year 2011-2012 final and thus the final budget was higher than the original adopted budget. The District's final budget is adjusted based on the estimated revenue and expenditures at the time of the fiscal year 2012-2013 adoption budget was prepared. At the end of the fiscal year, however, unspent revenues for some categorical programs will be deferred to the new fiscal year. A schedule showing the District's original and final budget amounts compared with actual final amounts is provided in the required supplementary information, succeeding the financial statement section.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

CAPITAL ASSET AND DEBT ADMINISTRATION

Capital Assets

The District's net capital assets include land, buildings, furniture, and equipment. At June 30, 2012, the District had \$114.01 million in capital assets, representing a net increase of \$9.76 million over \$104.25 million in 2011.

Table 4

(Amounts in millions)	Governmental Activities	
	2012	2011
Capital Assets		
Land	\$ 1.57	\$ 1.57
Construction in progress	17.31	2.73
Buildings and improvements	124.97	124.97
Furniture and equipment	5.78	5.67
Total Assets	149.63	134.94
Accumulated Depreciation		
Buildings and improvements	32.30	27.16
Furniture and equipment	3.32	3.53
Total Accumulated Depreciation	35.62	30.69
Net Capital Assets		
Land	1.57	1.57
Construction in progress	17.31	2.73
Buildings and improvements	92.67	97.81
Furniture and equipment	2.47	2.14
Total	\$ 114.01	\$ 104.25

Some of the highlights of this year's construction program include:

- Projects that are under construction:
 - McKinley Two Story
 - Modernization projects at following sites:
Meadow, Hellyer, Success, Bridges and Sylvandale
 - Technology Infrastructure at different sites
 - Security Safety projects at following sites:
McKinley, Santee, Meadow, Franklin, Stonegate, Hellyer, Bridges and Sylvandale
 - Environmental Review projects at following sites:
Santee, Kennedy, Franklin and Hellyer
- Projects that under design:
 - New school at Franklin

Refer to Capital Assets Note 4 in the financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

Long-Term Obligations

At the end of this year, the District had \$97.74 million in outstanding long-term liabilities versus \$84.97 million last year, an increase of \$12.77 million. Long-term obligations consisted of:

Table 5

(Amounts in millions)	Governmental Activities	
	2012	2011
General obligation bonds	\$ 80.75	\$ 69.91
Accretion to date	5.00	4.08
Cost of defeasance	(0.52)	(0.57)
Bond premium	3.46	2.95
Certificates of participation	5.17	5.38
Postemployment benefits	0.18	-
Accumulated vacation - net	0.34	0.34
Early retirement incentive	3.36	2.88
Totals	\$ 97.74	\$ 84.97

The District's obligations include compensated absences payable, general obligation bonds, certificates of participation, postemployment benefits and early retirement incentive.

The District's general obligation bonds have been assigned an insured rating of "AA-" with an underlying rating of "A+". The State limits the amount of general obligation debt that non-unified districts can issue to 1.25 percent of the assessed value of all taxable property within the District's boundaries. The District's outstanding general obligation debt of \$80.75 million is below this \$82.07 million statutorily-imposed limit.

We present more detailed information regarding our long-term obligations in Note 9 of the financial statements.

ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The majority of the District's unrestricted general fund revenues are derived from State and Local income sources through revenue limit, property taxes, and other state funding. The State of California's severe revenue and budget shortfalls for the last few years has put tremendous pressure on the District's general fund. The District will continue to monitor the budget situation and be poised to make additional adjustments as may be required to remain fiscally sound. The District has been on a steady course of continuous improvement in academic achievement, closing the achievement gap, improving its facilities, and meeting the priorities of the School Board and community. It is imperative that the District continue this course of success.

The General Fund ending fund balance increased by \$2.2 million in 2011-12 and increased by \$2.7 million in 2010-11 primarily as a result of one-time infusion of federal funds and cuts in expenditures that have been made. This means that the District has been strategic and prudent in managing its fiscal affairs during this very difficult time and is in a better position to handle the bumps in the road still to come.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

MANAGEMENT'S DISCUSSION AND ANALYSIS JUNE 30, 2012

The 2012-13 Budget Act for the State of California assumes passage of Governor Brown's tax initiative, which will appear on the November ballot as Proposition 30. The Schools and Local Public Safety Protection Act is expected to generate \$8 billion in additional revenue to help close a \$15.7 billion deficit and build a reserve of nearly \$1 billion. If Governor Brown's tax initiative fails, the Budget Act requires mid-year trigger cuts averaging \$441 per ADA. Given the significance of the possible trigger cuts, the District has identified the need to reduce the school year by up to 20 days. The election was held November 6, 2012 and Proposition 30 was approved by 54.1% of the voters in California. As a result the trigger cuts referred to above will not be implemented for the 2012-13 fiscal year. The District's General Fund ending fund balance has increased \$4.9 million over the last two years which will provide a small financial cushion in dealing with an unknown financial outlook in future years.

The District construction and modernization program is supported by a \$30 million bond issue which has been augmented by the passage of an additional \$50 million bond authorization approved in November 2010. Individual school needs have been prioritized and construction schedules developed to effectively utilize these funds to modernize our schools.

CONTACTING THE DISTRICT'S FINANCIAL MANAGEMENT

This financial report is designed to provide our citizens, taxpayers, and customers and investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information, please contact Timothy McClary, Deputy Superintendent, Business Services, or Joanne Chin, Director of Fiscal Services, Franklin-McKinley School District, at 645 Wool Creek Dr., San Jose, CA 95112.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

STATEMENT OF NET ASSETS

JUNE 30, 2012

	<u>Governmental Activities</u>
ASSETS	
Deposits and investments	\$ 36,690,271
Receivables	17,783,721
Prepaid expenses	491,534
Deferred charges	1,827,928
Stores inventories	98,387
Other current assets	186,656
Capital assets not depreciated	18,877,839
Capital assets, net of accumulated depreciation	95,133,883
Total Assets	<u>171,090,219</u>
LIABILITIES	
Accounts payable	8,899,590
Interest payable	1,369,214
Deferred revenue	794,316
Claims liability	96,863
Current loans	10,060,000
Current portion of long-term obligations	6,676,992
Noncurrent portion of long-term obligations	91,065,474
Total Liabilities	<u>118,962,449</u>
NET ASSETS	
Invested in capital assets, net of related debt	37,503,767
Restricted for:	
Legally restricted	3,616,474
Special revenue	1,382,651
Debt service	5,341,791
Capital projects	655,554
Self insurance programs	364,876
Unrestricted	3,262,657
Total Net Assets	<u>\$ 52,127,770</u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

STATEMENT OF ACTIVITIES FOR THE YEAR ENDED JUNE 30, 2012

Functions/Programs	Expenses	Program Revenues		Net (Expenses) Revenues and Changes in Net Assets
		Charges for Services and Sales	Operating Grants and Contributions	Governmental Activities
Governmental Activities:				
Instruction	\$ 56,175,660	\$ 29,243	\$ 10,123,532	\$ (46,022,885)
Instruction-related activities:				
Supervision of instruction	2,044,311	19	1,514,431	(529,861)
Instructional library, media, and technology	743,919	12	762,852	18,945
School site administration	5,496,579	881	969,434	(4,526,264)
Pupil services:				
Home-to-school transportation	2,295,830	-	1,679,841	(615,989)
Food services	5,370,769	23,803	4,480,846	(866,120)
All other pupil services	1,493,895	318	260,717	(1,232,860)
Administration:				
Data processing	1,062,205	-	-	(1,062,205)
All other administration	5,278,573	1,109	451,324	(4,826,140)
Plant services	7,019,440	11	247,094	(6,772,335)
Enterprise services	6,589	-	-	(6,589)
Interest on long-term obligations	4,477,810	-	-	(4,477,810)
Other outgo	205,885	287,162	398,069	479,346
Total Governmental Activities	\$ 91,671,465	\$ 342,558	\$ 20,888,140	(70,440,767)
General revenues and subventions:				
Property taxes, levied for general purposes				20,995,260
Property taxes, levied for debt service				7,035,175
Taxes levied for other specific purposes				1,309,093
Federal and state aid not restricted to specific purposes				36,972,239
Interest and investment earnings				290,525
Interagency revenues				33,446
Miscellaneous				5,026,842
				<u>71,662,580</u>
Change in Net Assets				1,221,813
Net Assets - Beginning				50,905,957
Net Assets - Ending				<u>\$ 52,127,770</u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

GOVERNMENTAL FUNDS BALANCE SHEET JUNE 30, 2012

	General Fund	Building Fund	Bond Interest and Redemption Fund	Non Major Governmental Funds	Total Governmental Funds
ASSETS					
Deposits and investments	\$ 6,354,256	\$ 22,052,618	\$ 6,705,560	\$ 1,314,274	\$ 36,426,708
Receivables	16,828,308	26,351	5,445	923,330	17,783,434
Due from other funds	233,962	136	-	155,542	389,640
Prepaid expenditures	481,534	-	-	-	481,534
Stores inventories	36,709	-	-	61,678	98,387
Total Assets	<u>\$ 23,934,769</u>	<u>\$ 22,079,105</u>	<u>\$ 6,711,005</u>	<u>\$ 2,454,824</u>	<u>\$ 55,179,703</u>
LIABILITIES AND FUND BALANCES					
Liabilities:					
Accounts payable	\$ 3,993,440	\$ 4,723,495	\$ -	\$ 182,655	\$ 8,899,590
Due to other funds	156,909	-	-	233,964	390,873
Other current liabilities	10,060,000	-	-	-	10,060,000
Deferred revenue	794,316	-	-	-	794,316
Total Liabilities	<u>15,004,665</u>	<u>4,723,495</u>	<u>-</u>	<u>416,619</u>	<u>20,144,779</u>
Fund Balances:					
Nonspendable	543,243	-	-	61,678	604,921
Restricted	1,788,546	17,355,610	6,711,005	1,976,527	27,831,688
Unassigned	6,598,315	-	-	-	6,598,315
Total Fund Balances	<u>8,930,104</u>	<u>17,355,610</u>	<u>6,711,005</u>	<u>2,038,205</u>	<u>35,034,924</u>
Total Liabilities and Fund Balances	<u>\$ 23,934,769</u>	<u>\$ 22,079,105</u>	<u>\$ 6,711,005</u>	<u>\$ 2,454,824</u>	<u>\$ 55,179,703</u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET TO THE STATEMENT OF NET ASSETS JUNE 30, 2012

Total Fund Balance - Governmental Funds		\$ 35,034,924
Amounts Reported for Governmental Activities in the Statement of Net Assets are Different Because:		
Capital assets used in governmental activities are not financial resources and therefore, are not reported as assets in governmental funds.		
The cost of capital assets is	\$ 149,627,859	
Accumulated depreciation is	<u>(35,616,137)</u>	
Net Capital Assets		114,011,722
Expenditures related to debt issuances are recognized in the governmental fund's statement of revenues, expenditures and changes in fund balance but are deferred on the government-wide statements and amortized over the life of the related debt.		1,827,928
In governmental funds, unmatured interest on long-term obligations is recognized in the period when it is due. On the government-wide financial statements, unmatured interest on long-term obligations is recognized when it is incurred.		(1,369,214)
An internal service fund is used by the District's management to charge the costs of the dental and vision insurance program to the individual funds. The assets and liabilities of the internal service fund are included with governmental activities.		364,876
Long-term obligations, including bonds payable, are not due and payable in the current period and, therefore, are not reported as liabilities in the funds. Long-term obligations at year-end consist of:		
Bonds payable	88,698,565	
Certificates of participation	5,165,000	
Early retirement incentive	3,364,040	
Postemployment benefits	179,795	
Compensated absences (vacations)	<u>335,066</u>	
Total Long-Term Obligations		(97,742,466)
Total Net Assets - Governmental Activities		<u>\$ 52,127,770</u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

GOVERNMENTAL FUNDS

STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES FOR THE YEAR ENDED JUNE 30, 2012

	General Fund	Building Fund	Bond Interest and Redemption Fund	Nonmajor Governmental Funds	Total Governmental Funds
REVENUES					
Revenue limit sources	\$ 47,637,909	\$ -	\$ -	\$ -	\$ 47,637,909
Federal sources	6,464,286	-	188,720	4,296,119	10,949,125
Other State sources	18,239,347	-	67,602	359,001	18,665,950
Other local sources	7,175,665	98,812	6,981,234	1,383,294	15,639,005
Total Revenues	79,517,207	98,812	7,237,556	6,038,414	92,891,989
EXPENDITURES					
Current					
Instruction	52,633,389	-	-	-	52,633,389
Instruction-related activities:					
Supervision of instruction	1,911,059	-	-	-	1,911,059
Instructional library, media and technology	695,429	-	-	-	695,429
School site administration	5,138,303	-	-	-	5,138,303
Pupil services:					
Home-to-school transportation	2,146,184	-	-	-	2,146,184
Food services	40	-	-	5,020,653	5,020,693
All other pupil services	1,396,520	-	-	-	1,396,520
Administration:					
Data processing	992,969	-	-	-	992,969
All other administration	4,042,049	-	-	233,959	4,276,008
Plant services	7,264,549	-	-	-	7,264,549
Facility acquisition and construction	-	14,231,802	-	337,504	14,569,306
Other outgo	205,885	-	-	-	205,885
Debt service					
Principal	215,000	-	4,155,000	-	4,370,000
Interest and other	676,281	71,208	2,895,461	2,192	3,645,142
Total Expenditures	77,317,657	14,303,010	7,050,461	5,594,308	104,265,436
Excess (Deficiency) of Revenues Over Expenditures	2,199,550	(14,204,198)	187,095	444,106	(11,373,447)
Other Financing Sources (Uses)					
Other sources	-	15,000,000	698,517	-	15,698,517
NET CHANGE IN FUND BALANCES	2,199,550	795,802	885,612	444,106	4,325,070
Fund Balance - Beginning	6,730,554	16,559,808	5,825,393	1,594,099	30,709,854
Fund Balance - Ending	\$ 8,930,104	\$ 17,355,610	\$ 6,711,005	\$ 2,038,205	\$ 35,034,924

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES TO THE STATEMENT OF ACTIVITIES FOR THE YEAR ENDED JUNE 30, 2012

Net Change in Fund Balances of Governmental Funds **\$ 4,325,070**
Amounts Reported for Governmental Activities in the Statement of Activities are Different Because:

Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures, however, for governmental activities, those costs are shown in the statement of net assets and allocated over their estimated useful lives as annual depreciation expenses in the statement of activities. This is the amount by which capital outlays exceed depreciation in the period.

Capital outlays	\$ 15,320,947	
Depreciation expense	<u>(5,559,894)</u>	9,761,053

Proceeds received from sale of general obligation bonds, are recorded as revenues in the governmental funds but increase long-term debt on the statement of net assets, and does not affect the statement of activities. (15,000,000)

Cost of issuance of the general obligation bonds is recorded as an expenditure in the governmental funds but is recorded as a deferred charge on the statement of net assets and does not affect the statement of activities. 280,006

Principal payments made on long-term obligations are expenditures in the governmental funds when due, however, on the government-wide statement of net assets, the payments reduce the obligations and do not affect the statement of activities. The following payments were made on long-term obligations during the year:

General obligation bonds	4,155,000	
Certificates of participation	<u>215,000</u>	4,370,000

In the governmental funds, interest expenditure includes those amounts due for payment during the year. In the statement of activities, interest expense includes the change in interest payable, additional accreted interest on bonds payable, and amortization of deferred charges and bond premiums as follows:

Change in interest payable	(268,319)	
Amortization of bond premium	187,672	
Additional accreted interest	(911,975)	
Amortization of defeasance cost	(57,531)	
Amortization of cost of issuance	<u>(120,052)</u>	(1,170,205)

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

RECONCILIATION OF THE GOVERNMENTAL FUNDS STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCES TO THE STATEMENT OF ACTIVITIES (CONTINUED) FOR THE YEAR ENDED JUNE 30, 2012

Bond premium is a revenue source in the governmental funds, but is recorded as a liability on the statement of net assets.	(698,517)
Supplemental employee retirement obligations are not recognized in the governmental funds but are recognized as a long-term obligation on the statement of net assets.	(1,201,535)
The annual payment of the supplemental employee retirement obligations was expensed in the governmental funds but it reduces the liability in the government-wide statement of net assets and does not impact the statement of activities.	720,835
Compensated absences are recorded in the governmental funds only to the extent that they are paid from current financial resources, while the accrued balances are recorded as long-term obligations in the statement of net assets. The net increase or decrease in the vacation accrual is recorded in the statement of activities. Vacation used was more than the amounts earned.	700
Addition to the post employment benefits was not recognized in the governmental funds. However, it is recognized as expenses in the statement of activities and increases liabilities in the statement of net assets.	(195,861)
Payments to the retiree benefits are recorded as an expenditure in the governmental funds when paid. However, on the government-wide statement of net assets, the payments reduce the obligations and do not affect the statement of activities.	16,066
An internal service fund is used by the District's management to charge the costs of the dental and vision insurance program to the individual funds. The increase in net assets of the internal service fund is reported with governmental activities.	<u>14,201</u>
Change in Net Assets of Governmental Activities	<u><u>\$ 1,221,813</u></u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

PROPRIETARY FUND STATEMENT OF NET ASSETS JUNE 30, 2012

	<u>Governmental Activities - Internal Service Fund</u>
ASSETS	
Current Assets	
Deposits and investments	\$ 263,563
Receivables	287
Due from other funds	1,233
Prepaid expenses	10,000
Other current assets	<u>186,656</u>
Total Current Assets	<u>461,739</u>
LIABILITIES	
Current Liabilities	
Claim liabilities	<u>96,863</u>
Total Current Liabilities	<u>96,863</u>
NET ASSETS	
Restricted	<u>364,876</u>
Total Net Assets	<u><u>\$ 364,876</u></u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

**PROPRIETARY FUND
STATEMENT OF REVENUES, EXPENSES, AND CHANGES
IN NET ASSETS
FOR THE YEAR ENDED JUNE 30, 2012**

	Governmental Activities - Internal Service Fund
OPERATING REVENUES	
In-District contribution	\$ 1,389,931
OPERATING EXPENSES	
Other operating cost	1,377,019
Operating Income	<u>12,912</u>
NONOPERATING REVENUES	
Interest income	<u>1,289</u>
Change in Net Assets	14,201
Total Net Assets - Beginning	350,675
Total Net Assets - Ending	<u><u>\$ 364,876</u></u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

PROPRIETARY FUND STATEMENT OF CASH FLOWS FOR THE YEAR ENDED JUNE 30, 2012

	Governmental Activities - Internal Service Fund
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from user charges	\$ 1,365,697
Cash payments for insurance claims	(1,389,381)
Net cash used for operating activities	(23,684)
CASH FLOWS FROM INVESTING ACTIVITIES	
Interest on investments	1,380
Net decrease in cash and cash equivalents	(22,304)
Cash and cash equivalents - Beginning	285,867
Cash and cash equivalents - Ending	\$ 263,563
RECONCILIATION OF OPERATING LOSS TO NET CASH USED IN OPERATING ACTIVITIES:	
Operating income	\$ 12,912
Changes in assets and liabilities:	
Due from other fund	(1,233)
Other current assets	(23,001)
Claims liabilities	(12,362)
NET CASH USED IN OPERATING ACTIVITIES	\$ (23,684)

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

**FIDUCIARY FUND
STATEMENT OF NET ASSETS
JUNE 30, 2012**

	Student Body Agency Funds
ASSETS	
Deposits and investments	<u><u>\$ 189,368</u></u>
LIABILITIES	
Due to student groups	<u><u>\$ 189,368</u></u>

The accompanying notes are an integral part of these basic financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

NOTE 1 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Financial Reporting Entity

The Franklin-McKinley School District was organized in January 1948 under the laws of the State of California. The District operates under a locally elected five-member Board form of government and provides educational services to grades kindergarten - eighth as mandated by the State and Federal agencies. The District operates 14 elementary schools and two middle schools one of which operates as a conversion charter school.

A reporting entity is comprised of the primary government, component units, and other organizations that are included to ensure the financial statements are not misleading. The primary government of the District consists of all funds, departments, boards, and agencies that are not legally separate from the District. For Franklin-McKinley School District, this includes general operations, food service, and student related activities of the District.

Component Units

Component units are legally separate organizations for which the District is financially accountable. Component units may also include organizations that are fiscally dependent on the District, in that the District approves their budget, the issuance of their debt or the levying of their taxes. In addition, component units are other legally separate organizations for which the District is not financially accountable but the nature and significance of the organization's relationship with the District is such that exclusion would cause the District's financial statements to be misleading or incomplete. For financial reporting purposes, the component unit discussed below has a financial and operational relationship which meets the reporting entity definition criteria of the Governmental the financial statements of the District. The component unit, although a legally separate entity, is reported in the financial statements using the blended presentation method as if it were part of the District's operations because the governing board of the component unit is essentially the same as the governing board of the District.

Charter School The District has an approved Charter for the Bridges Academy Charter School pursuant to Education Code Section 47605. The Bridge Academy Charter School is operated by the District, and its financial activities are presented in the General Fund. The District receives revenue on behalf of the Charter School which it passes on to the Charter.

Basis of Presentation - Fund Accounting

The accounting system is organized and operated on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulations, restrictions, or limitations. The District's funds are grouped into three broad fund categories: governmental, proprietary, and fiduciary.

Governmental Funds Governmental funds are those through which most governmental functions typically are financed. Governmental fund reporting focuses on the sources, uses, and balances of current financial resources. Expendable assets are assigned to the various governmental funds according to the purposes for which they may or must be used. Current liabilities are assigned to the fund from which they will be paid. The difference between governmental fund assets and liabilities is reported as fund balance. The following are the District's major and non-major governmental funds:

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Major Governmental Funds

General Fund The General Fund is the chief operating fund for all districts. It is used to account for the ordinary operations of the District. All transactions except those accounted for in another fund are accounted for in this fund.

As the District has not taken formal action to commit the flexed revenue, the revenue would be considered to be available for general educational purposes, resulting in Fund 14, Deferred Maintenance, being combined with the General Fund for presentation in these audited financial statements. However, the District considers Fund 14, Deferred Maintenance, fund balance to be insignificant, and therefore is not combined with the General Fund for presentation in the audited financial statements.

Building Fund The Building Fund exists primarily to account separately for proceeds from sale of bonds and the acquisition of major governmental capital facilities and buildings.

Bond Interest and Redemption Fund The Bond interest and Redemption Fund is used to account for the accumulation of resources for, and the repayment of, district bonds, interest, and related costs.

Non-Major Governmental Funds

Special Revenue Funds The Special Revenue funds are established to account for the proceeds from specific revenue sources (other than trusts, major capital projects, or debt service) that are restricted or committed to the financing of particular activities and that compose a substantial portion of the inflows of the fund. Additional resources that are restricted, committed, or assigned to the purpose of the fund may also be reported in the fund.

Cafeteria Fund The Cafeteria Fund is used to account separately for federal, State, and local resources to operate the food service program (*Education Code* Sections 38090-38093) and is used only for those expenditures authorized by the governing board as necessary for the operation of the District's food service program (*Education Code* Sections 38091 and 38100).

Deferred Maintenance Fund The Deferred Maintenance Fund is used to account separately for state apportionments and the District's contributions for deferred maintenance purposes (*Education Code* Sections 17582-17587) and for items of maintenance approved by the State Allocation Board.

Capital Project Funds The Capital Project funds are used to account for and report financial resources that are restricted, committed, or assigned to the acquisition or construction of major capital facilities and other capital assets (other than those financed by proprietary funds and trust funds).

Capital Facilities Fund The Capital Facilities Fund is used primarily to account separately for monies received from fees levied on developers or other agencies as a condition of approving a development (*Education Code* Sections 17620-17626. Expenditures are restricted to the purposes specified in *Government Code* Sections 65970-65981 or to the items specified in agreements with the developer (*Government Code* Section 66006).

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

County School Facilities Fund The County School Facilities Fund is established pursuant to *Education Code* Section 17070.43 to receive apportionments from the 1998 State School Facilities Fund (Proposition 1A), the 2002 State School Facilities Fund (Proposition 47), or the 2004 State School Facilities Fund (Proposition 55) authorized by the State Allocation Board for new school facility construction, modernization projects, and facility hardship grants, as provided in the Leroy F. Greene School Facilities Act of 1998 (*Education Code* Section 17070 et seq.).

Special Reserve Fund for Capital Outlay Projects The Special Reserve Fund for Capital Outlay Projects exists primarily to provide for the accumulation of General Fund monies for capital outlay purposes (*Education Code* Section 42840).

Proprietary Funds Proprietary fund reporting focuses on the determination of operating income, changes in net assets, financial position, and cash flows. The District applies all GASB pronouncements, as well as the Financial Accounting Standards Board pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements. Proprietary funds are classified as enterprise or internal service. The District operates only an internal service fund.

Internal Service Fund Internal service funds may be used to account for any activity for which services are provided to other funds of the District on a cost reimbursement basis. The District operates a dental and vision program that is accounted for in the internal service fund.

Fiduciary Funds Fiduciary funds are used to account for assets held in trustee or agent capacity for others that cannot be used to support the district's own programs. The fiduciary fund category is split into four classifications: pension trust funds, investment trust funds, private-purpose trust funds, and agency funds. The key distinction between trust and agency funds is that trust funds are subject to a trust agreement that affects the degree of management involvement and the length of time that the resources are held. The District operates agency funds which account for student body activities (ASB).

Basis of Accounting - Measurement Focus

Government-Wide Financial Statements The government-wide financial statements are prepared using the economic resources measurement focus and the accrual basis of accounting. This is the same approach used in the preparation of the proprietary fund financial statements, but differs from the manner in which governmental fund financial statements are prepared.

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each governmental function. Direct expenses are those that are specifically associated with a service, program, or department and are therefore, clearly identifiable to a particular function. The District does not allocate indirect expenses to functions in the Statement of Activities, except for depreciation. Program revenues include charges paid by the recipients of the goods or services offered by the programs and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues are presented as general revenues. The comparison of program revenues and expenses identifies the extent to which each program or business segment is self-financing or draws from the general revenues of the District. Eliminations have been made to minimize the double counting of internal activities.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Net assets should be reported as restricted when constraints placed on net asset use are either externally imposed by creditors (such as through debt covenants), grantors, contributors, or laws or regulations of other governments or imposed by law through constitutional provisions or enabling legislation.

Fund Financial Statements Fund financial statements report detailed information about the District. The focus of governmental and proprietary fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Non-major funds are aggregated and presented in a single column. The internal service fund is presented in a single column on the face of the proprietary fund statements.

Governmental Funds All governmental funds are accounted for using the flow of current financial resources measurement focus and the modified accrual basis of accounting. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. The statement of revenues, expenditures, and changes in fund balance reports on the sources (revenues and other financing sources) and uses (expenditures and other financing uses) of current financial resources. This approach differs from the manner in which the governmental activities of the government-wide financial statements are prepared. Governmental fund financial statements, therefore, include reconciliations with brief explanations to better identify the relationship between the government-wide financial statements, prepared using the economic resources measurement focus and the accrual basis of accounting, and the governmental fund financial statements, prepared using the flow of current financial resources measurement focus and the modified accrual basis of accounting.

Proprietary Funds Proprietary funds are accounted for using the flow of economic resources measurement focus and the accrual basis of accounting. All assets and all liabilities associated with the operation of this fund are included in the statement of net assets. The statement of changes in fund net assets presents increases (revenues) and decreases (expenses) in net total assets. The statement of cash flows provides information about how the District finances and meets the cash flow needs of its proprietary fund.

Fiduciary Funds Fiduciary funds are accounted for using the flow of economic resources measurement focus and the accrual basis of accounting. Fiduciary funds are excluded from the government-wide financial statements because they do not represent resources of the District.

Revenues – Exchange and Non-Exchange Transactions Revenue resulting from exchange transactions, in which each party gives and receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenue is recorded in the fiscal year in which the resources are measurable and become available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter, to be used to pay liabilities of the current fiscal year. Generally, available is defined as collectible within 45 or 60 days. However, to achieve comparability of reporting among California districts and so as not to distort normal revenue patterns, with specific respect to reimbursement grants and corrections to State-aid apportionments, the California Department of Education has defined available for districts as collectible within one year. The following revenue sources are considered to be both measurable and available at fiscal year-end: State apportionments, interest, certain grants, and other local sources.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Non-exchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, certain grants, entitlements, and donations. Revenue from property taxes is recognized in the fiscal year in which the taxes are received. Revenue from certain grants, entitlements, and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied. Eligibility requirements include time and purpose restrictions. On a modified accrual basis, revenue from non-exchange transactions must also be available before it can be recognized.

Deferred Revenue Deferred revenue arises when potential revenue does not meet both the "measurable" and "available" criteria for recognition in the current period or when resources are received by the District prior to the incurrence of qualifying expenditures. In subsequent periods, when both revenue recognition criteria are met, or when the District has a legal claim to the resources, the liability for deferred revenue is removed from the balance sheet and revenue is recognized.

Expenses/Expenditures On the accrual basis of accounting, expenses are recognized at the time they are incurred. The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable, and typically paid within 90 days. Principal and interest on long-term obligations, which has not matured, are recognized when paid in the governmental funds as expenditures. Allocations of costs, such as depreciation and amortization, are not recognized in the governmental funds but are recognized in the government-wide statements.

Cash and Cash Equivalents

The District's cash and cash equivalents are considered to be cash on hand, demand deposits, and short-term investments with original maturities of three months or less from the date of acquisition. Cash equivalents also include cash with county treasury balances for purposes of the statement of cash flows.

Investments

Investments held at June 30, 2012, with original maturities greater than one year are stated at fair value. Fair value is estimated based on quoted market prices at year-end. Fair values of investments in county and State investment pools are determined by the program sponsor.

Prepaid Expenditures

Prepaid expenditures (expenses) represent amounts paid in advance of receiving goods or services. The District has the option of reporting an expenditure in governmental funds for prepaid items either when purchased or during the benefiting period. The District has chosen to report the expenditures when incurred.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Stores Inventories

Inventories consist of expendable food and supplies held for consumption. Inventories are stated at cost, on the weighted average basis. The costs of inventory items are recorded as expenditures in the governmental funds and expenses in the proprietary funds when used.

Capital Assets and Depreciation

The accounting and reporting treatment applied to the capital assets associated with a fund are determined by its measurement focus. Capital assets are long-lived assets of the District. The District maintains a capitalization threshold of \$10,000. The District does not possess any infrastructure. Improvements are capitalized; the costs of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized, but are expensed as incurred.

When purchased, such assets are recorded as expenditures in the governmental funds and capitalized in the government-wide statement of net assets. The valuation basis for capital assets is historical cost, or where historical cost is not available, estimated historical cost based on replacement cost. Donated capital assets are capitalized at estimated fair market value on the date donated.

Depreciation is computed using the straight-line method. Estimated useful lives of the various classes of depreciable capital assets are as follows: buildings, 20 to 50 years; improvements, 5 to 50 years; equipment, 2 to 15 years.

Interfund Balances

On fund financial statements, receivables and payables resulting from short-term interfund loans are classified as "interfund receivables/payables". These amounts are eliminated in the governmental and business-type activities columns of the statement of net assets, except for the net residual amounts due between governmental and business-type activities, which are presented as internal balances.

Compensated Absences

Compensated absences are accrued as a liability as the benefits are earned. The entire compensated absence liability is reported on the government-wide statement of net assets. For governmental funds, the current portion of unpaid compensated absences is recognized upon the occurrence of relevant events such as employee resignations and retirements that occur prior to year-end that have not yet been paid with expendable available financial resources. These amounts are reported in the fund from which the employees who have accumulated leave are paid.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Sick leave is accumulated without limit for each employee at the rate of one day for each month worked. Leave with pay is provided when employees are absent for health reasons; however, the employees do not gain a vested right to accumulated sick leave. Employees are never paid for any sick leave balance at termination of employment or any other time. Therefore, the value of accumulated sick leave is not recognized as a liability in the District's financial statements. However, credit for unused sick leave is applicable to all classified school members who retire after January 1, 1999. At retirement, each member will receive .004 year of service credit for each day of unused sick leave. Credit for unused sick leave is applicable to all certificated employees and is determined by dividing the number of unused sick days by the number of base service days required to complete the last school year, if employed full-time.

Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities, and long-term obligations are reported in the government-wide and proprietary fund financial statements. In general, governmental fund payables and accrued liabilities that, once incurred, are paid in a timely manner and in full from current financial resources are reported as obligations of the governmental funds.

However, claims and judgments, compensated absences, special termination benefits, and contractually required pension contributions that will be paid from governmental funds are reported as a liability in the governmental fund financial statements only to the extent that they are due for payment during the current year. Bonds, capital leases, and other long-term obligations are recognized as liabilities in the governmental fund financial statements when due.

Deferred Issuance Costs, Premiums and Discounts

In the government-wide financial statements and in the proprietary fund type financial statements, long-term obligations are reported as liabilities in the applicable governmental activities, or proprietary fund statement of net assets. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the life of the bonds using the straight-line method.

Fund Balances – Governmental Funds

As of June 30, 2012, fund balances of the governmental funds are classified as follows:

Nonspendable – amounts that cannot be spent either because they are in nonspendable form or because they are legally or contractually required to be maintained intact.

Restricted – amounts that can be spent only for specific purposes because of constitutional provisions or enabling legislation or because of constraints that are externally imposed by creditors, grantors, contributors, or the laws or regulations of other governments.

Committed – amounts that can be used only for specific purposes determined by a formal action of the governing board. The governing board is the highest level of decision-making authority for the District. Commitments may be established, modified, or rescinded only through resolutions or other action as approved by the governing board.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Assigned – amounts that do not meet the criteria to be classified as restricted or committed but that are intended to be used for specific purposes. Under the District's adopted policy, only the governing board or assistant superintendent of business services may assign amounts for specific purposes.

Unassigned – all other spendable amounts.

Spending Order Policy

When an expenditure is incurred for purposes for which both restricted and unrestricted fund balance is available, the District considers restricted funds to have been spent first. When an expenditure is incurred for which committed, assigned, or unassigned fund balances are available, the District considers amounts to have been spent first out of committed funds, then assigned funds, and finally unassigned funds, as needed, unless the governing board has provided otherwise in its commitment or assignment actions.

Minimum Fund Balance Policy

In fiscal year 2010-2011, the governing board adopted a minimum fund balance policy for the General Fund in order to protect the district against revenue shortfalls or unpredicted on-time expenditures. The policy requires a Reserve for Economic Uncertainties consisting of unassigned amounts equal to no less than 5 percent of General Fund expenditures and other financing uses.

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the District or through external restrictions imposed by creditors, grantors, or laws or regulations of other governments. The District first applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the District, these revenues are primarily interfund insurance premiums. Operating expenses are necessary costs incurred to provide the good or service that is the primary activity of the fund. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Interfund Activity

Exchange transactions between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds and after non-operating revenues/expenses in proprietary funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented in the financial statements. Interfund transfers are eliminated in the governmental and business-type activities columns of the statement of activities.

Estimates

The preparation of the financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results may differ from those estimates.

Budgetary Data

The budgetary process is prescribed by provisions of the California Education Code and requires the governing board to hold a public hearing and adopt an operating budget no later than July 1st of each year. The District governing board satisfied these requirements. The adopted budget is subject to amendment throughout the year to give consideration to unanticipated revenue and expenditures primarily resulting from events unknown at the time of budget adoption with the legal restriction that expenditures cannot exceed appropriations by major object account.

The amounts reported as the original budgeted amounts in the budgetary statements reflect the amounts when the original appropriations were adopted. The amounts reported as the final budgeted amounts in the budgetary statements reflect the amounts after all budget amendments have been accounted for. For purposes of the budget, on behalf payments have not been included as revenue and expenditures.

Property Tax

Secured property taxes attach as an enforceable lien on property as of January 1. Taxes are payable in two installments on November 1 and February 1 and become delinquent on December 10 and April 10, respectively. Unsecured property taxes are payable in one installment on or before August 31. The County of Santa Clara bills and collects the taxes on behalf of the District. Local property tax revenues are recorded when received.

New Accounting Pronouncements

In November 2010, the GASB issued Statement No. 61, *The Financial Reporting Entity: Omnibus-an amendment of GASB Statement No. 14 and No. 34*. The objective of this Statement is to improve financial reporting for a governmental financial reporting entity. The requirements of Statement No. 14, *The Financial Reporting Entity*, and the related financial reporting requirements of Statement No. 34, *Basic Financial Statements-and Management's Discussion and Analysis-for State and Local Governments*, were amended to better meet user needs and to address reporting entity issues that have arisen since the issuance of those Statements. The provisions of this Statement are effective for financial statements for periods beginning after June 15, 2012. Early implementation is encouraged.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

In June 2011, the GASB issued Statement No. 63, *Financial Reporting of Deferred Outflows of Resources, Deferred Inflows of Resources, and Net Position*. This Statement provides financial reporting guidance for deferred outflows of resources and deferred inflows of resources. Concepts Statement No. 4, *Elements of Financial Statements*, introduced and defined those elements as a consumption of net assets by the government that is applicable to a future reporting period, and an acquisition of net assets by the government that is applicable to a future reporting period, respectively. Previous financial reporting standards do not include guidance for reporting those financial statement elements, which are distinct from assets and liabilities.

Concepts Statement 4 also identifies net position as the residual of all other elements presented in a statement of financial position. This Statement amends the net asset reporting requirements in Statement No. 34, *Basic Financial Statements—and Management's Discussion and Analysis—for State and Local Governments*, and other pronouncements by incorporating deferred outflows of resources and deferred inflows of resources into the definitions of the required components of the residual measure and by renaming that measure as net position, rather than net assets. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2011. Earlier implementation is encouraged.

In March 2012, the GASB issued Statement No. 65, *Items Previously Reported as Assets and Liabilities*. This Statement establishes accounting and financial reporting standards that reclassify, as deferred outflows of resources or deferred inflows of resources, certain items that were previously reported as assets and liabilities and recognizes, as outflows of resources or inflows of resources, certain items that were previously reported as assets and liabilities. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012. Earlier application is encouraged. Earlier implementation is encouraged.

In March 2012, the GASB issued Statement No. 66, *Technical Corrections—2012—an amendment of GASB Statements No. 10 and No. 62*. The objective of this Statement is to improve accounting and financial reporting for a governmental financial reporting entity by resolving conflicting guidance that resulted from the issuance of two pronouncements, Statements No. 54, *Fund Balance Reporting and Governmental Fund Type Definitions*, and No. 62, *Codification of Accounting and Financial Reporting Guidance Contained in Pre-November 30, 1989 FASB and AICPA Pronouncements*. The provisions of this Statement are effective for financial statements for periods beginning after December 15, 2012. Earlier implementation is encouraged.

In June 2012, the GASB issued Statement No. 68, *Accounting and Financial Reporting for Pensions—an amendment of Statement No. 27*. The primary objective of this Statement is to improve accounting and financial reporting by state and local governments for pensions. It also improves information provided by State and local governmental employers about financial support for pensions that is provided by other entities. This Statement results from a comprehensive review of the effectiveness of existing standards of accounting and financial reporting for pensions with regard to providing decision-useful information, supporting assessments of accountability and inter-period equity, and creating additional transparency. This Statement is effective for fiscal years beginning after June 15, 2014. Earlier implementation is encouraged.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

NOTE 2 – DEPOSITS AND INVESTMENTS

Summary of Deposits and Investments

Deposits and investments as of June 30, 2012, are classified in the accompanying financial statements as follows:

Governmental activities	\$ 36,426,708
Proprietary activities	263,563
Fiduciary activities	189,368
Total Deposits and Investments	<u>\$ 36,879,639</u>

Deposits and investments as of June 30, 2012, consist of the following:

Cash on hand and in banks	\$ 189,368
Cash in revolving	25,000
Investments	36,665,271
Total Deposits and Investments	<u>\$ 36,879,639</u>

Policies and Practices

The District is authorized under California Government Code to make direct investments in local agency bonds, notes, or warrants within the State; U.S. Treasury instruments; registered State warrants or treasury notes; securities of the U.S. Government, or its agencies; bankers acceptances; commercial paper; certificates of deposit placed with commercial banks and/or savings and loan companies; repurchase or reverse repurchase agreements; medium term corporate notes; shares of beneficial interest issued by diversified management companies, certificates of participation, obligations with first priority security; and collateralized mortgage obligations.

Investment in County Treasury - The District is considered to be an involuntary participant in an external investment pool as the District is required to deposit all receipts and collections of monies with their County Treasurer (Education Code Section 41001). The fair value of the District's investment in the pool is reported in the financial statements based upon the District's pro-rata share of the fair value provided by the County Treasurer for the entire portfolio (in relation to the amortized cost of that portfolio). The balance available for withdrawal is based on the accounting records maintained by the County Treasurer, which is recorded on the amortized cost basis.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

General Authorizations

Limitations as they relate to interest rate risk and concentration of credit risk are indicated in the schedules below:

Authorized Investment Type	Maximum Remaining Maturity	Maximum Percentage of Portfolio	Maximum Investment in One Issuer
Local Agency Bonds, Notes, Warrants	5 years	None	None
Registered State Bonds, Notes, Warrants	5 years	None	None
U.S. Treasury Obligations	5 years	None	None
U.S. Agency Securities	5 years	None	None
Banker's Acceptance	180 days	40%	30%
Commercial Paper	270 days	25%	10%
Negotiable Certificates of Deposit	5 years	30%	None
Repurchase Agreements	1 year	None	None
Reverse Repurchase Agreements	92 days	20% of base	None
Medium-Term Corporate Notes	5 years	30%	None
Mutual Funds	N/A	20%	10%
Money Market Mutual Funds	N/A	20%	10%
Mortgage Pass-Through Securities	5 years	20%	None
County Pooled Investment Funds	N/A	None	None
Local Agency Investment Fund (LAIF)	N/A	None	None
Joint Powers Authority Pools	N/A	None	None

Credit Risk

Credit risk is the risk that an issuer of an investment will not fulfill its obligation to the holder of the investment. The District's investments with the Treasurer of the County of Santa Clara is not rated.

Interest Rate Risk

Interest rate risk is the risk that changes in market interest rates will adversely affect the fair value of an investment. Generally, the longer the maturity of an investment, the greater the sensitivity of its fair value to changes in market interest rates. The District manages its exposure to interest rate risk by depositing substantially all of its funds in the County Treasury Pool. The fair value of the deposits with County Treasurer at June 30, 2012 was \$36,804,965 and the weighted average maturity of the pool was 1.293 years.

Custodial Credit Risk - Deposits

Custodial risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District does not have a policy for custodial credit risk for deposits. However, the California Government Code requires that a financial institution secure deposits made by state or local governmental units by pledging securities in an undivided collateral pool held by a depository regulated under state law. The District has no significant custodial credit risk.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

NOTE 3 - RECEIVABLES

Receivables at June 30, 2012, consist of intergovernmental grants, entitlements, interest and other local sources. All receivables are considered collectible in full.

	General Fund	Building Fund	Bond Interest and Redemption Fund	Non-Major Governmental Funds	Total	Proprietary Fund
Federal Government						
Categorical aid	\$ 582,503	\$ -	\$ -	\$ 781,527	\$ 1,364,030	\$ -
State Government						
Apportionment	11,979,080	-	-	-	11,979,080	-
Categorical aid	3,337,362	-	-	55,692	3,393,054	-
Lottery	717,186	-	-	-	717,186	-
Local Government						
Interest and other local	212,177	26,351	5,445	86,111	330,084	287
Total	<u>\$ 16,828,308</u>	<u>\$ 26,351</u>	<u>\$ 5,445</u>	<u>\$ 923,330</u>	<u>\$ 17,783,434</u>	<u>\$ 287</u>

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

NOTE 4 - CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2012, was as follows:

	Balance July 1, 2011	Additions	Deductions	Balance June 30, 2012
Governmental Activities				
Capital Assets Not Being Depreciated:				
Land	\$ 1,565,500	\$ -	\$ -	\$ 1,565,500
Construction in Progress	2,732,003	14,580,336	-	17,312,339
Total Capital Assets Not Being Depreciated	4,297,503	14,580,336	-	18,877,839
Capital Assets Being Depreciated:				
Buildings and Improvements	124,978,857	68	11,097	124,967,828
Furniture and Equipment	5,665,649	740,543	624,000	5,782,192
Total Capital Assets Being Depreciated	130,644,506	740,611	635,097	130,750,020
Total Capital Assets	134,942,009	15,320,947	635,097	149,627,859
Less Accumulated Depreciation:				
Buildings and Improvements	27,169,069	5,142,798	11,097	32,300,770
Furniture and Equipment	3,522,271	417,096	624,000	3,315,367
Total Accumulated Depreciation	30,691,340	5,559,894	635,097	35,616,137
Governmental Activities Capital Assets, Net	\$ 104,250,669	\$ 9,761,053	\$ -	\$ 114,011,722

Under the terms of agreement of the Certificates of Participations described in Note 9, the George Shirakawa, Sr. Elementary School has been pledged as collateral for the full balance due on the Certificates of Participation.

Depreciation expense was charged as a direct expense to governmental functions as follows:

Governmental Activities

Instruction	\$ 3,542,271
Supervision of instruction	133,252
Instructional library, media, and technology	48,490
School site administration	358,276
Home-to-school transportation	149,646
Food services	350,076
All other pupil services	97,375
Enterprise activities	6,589
All other general administration	298,151
Data processing	69,236
Plant maintenance and operations	506,532
Total Depreciation Expenses Governmental Activities	\$ 5,559,894

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

NOTE 5 – INTERFUND TRANSACTIONS

Interfund Receivables/Payables (Due From/Due To)

Interfund receivable and payable balances at June 30, 2012, between major and nonmajor governmental funds are as follows:

Due To	Due From				Total
	General Fund	Building Fund	Non-Major Governmental Funds	Proprietary Funds	
General Fund	\$ -	\$ 136	\$ 155,540	\$ 1,233	\$ 156,909
Non-Major Governmental Funds	233,962	-	2	-	233,964
Total	<u>\$ 233,962</u>	<u>\$ 136</u>	<u>\$ 155,542</u>	<u>\$ 1,233</u>	<u>\$ 390,873</u>

All balances resulted from the time lag between the date that (1) interfund goods and services are provided or reimbursable expenditures occur, (2) transactions are recorded in the accounting system, and (3) payments between funds are made.

NOTE 6 – ACCOUNTS PAYABLE

Accounts payable at June 30, 2012, consists of the following:

	General Fund	Building Fund	Non-Major Governmental Funds	Total
Vendor payables	\$ 2,196,330	\$ 4,716,638	\$ 179,134	\$ 7,092,102
State apportionment	786,783	-	-	786,783
Salaries and benefits	1,010,327	6,857	3,521	1,020,705
Total	<u>\$ 3,993,440</u>	<u>\$ 4,723,495</u>	<u>\$ 182,655</u>	<u>\$ 8,899,590</u>

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

NOTE 7 – DEFERRED REVENUE

Deferred revenue at June 30, 2012, consists of the following:

	General Fund
Federal financial assistance	\$ 40,864
Other local	753,452
Total	<u>\$ 794,316</u>

NOTE 8 - TAX AND REVENUE ANTICIPATION NOTES (TRANS)

At July 1, 2011, the District had outstanding Tax and Revenue Anticipation Notes in the amount of \$3,769,500, which matured on August 1, 2011. On July 1, 2011, the District issued \$9,950,000 Tax and Revenue Anticipation Notes bearing interest at two percent. Interest and principal were due and payable on February 1, 2012.

On February 09, 2012, the District issued \$10,060,000 Tax and Revenue Anticipation Notes bearing interest at 2.5 percent. Interest and principal were due and payable by January 31, 2013. The notes were issued to supplement cash flows. The outstanding balance for these notes was \$10,060,000.

Changes in the outstanding liabilities for the Tax and Revenue Anticipation Notes are as follows:

Issue Date	Rate	Maturity Date	Outstanding July 1, 2011	Additions	Payments	Outstanding June 30, 2012
7/1/2011	0.70%	8/31/2011	\$ 3,769,500	\$ -	\$ 3,769,500	\$ -
7/1/2011	2.00%	2/1/2012	-	9,950,000	9,950,000	-
2/9/2012	2.50%	1/1/2013	-	10,060,000	-	10,060,000
			<u>\$ 3,769,500</u>	<u>\$ 9,950,000</u>	<u>\$ 13,719,500</u>	<u>\$ 10,060,000</u>

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

NOTE 9 – LONG-TERM OBLIGATIONS

Long-Term Obligation Summary

The changes in the District's long-term obligations during the year consist of the following:

	Balance July 1, 2011	Additions	Deductions	Balance June 30, 2012	Due in One Year
General obligation bonds	\$ 73,997,260	\$ 15,911,975	\$ 4,155,000	\$ 85,754,235	\$ 5,008,781
Loss on bond refunding	(575,313)	-	(57,531)	(517,782)	(57,531)
Bond premiums	2,951,267	698,517	187,672	3,462,112	187,672
Certificates of participation	5,380,000	-	215,000	5,165,000	225,000
Accumulated vacation - net	335,766	-	700	335,066	335,066
Postemployment benefits	-	195,861	16,066	179,795	16,862
Early retirement incentive	2,883,340	1,201,535	720,835	3,364,040	961,142
	<u>\$ 84,972,320</u>	<u>\$ 18,007,888</u>	<u>\$ 5,237,742</u>	<u>\$ 97,742,466</u>	<u>\$ 6,676,992</u>

The Bond Interest and Redemption Fund makes payments on the general obligation bonds with local property tax revenues. The General Fund or the Capital Facilities Fund, make payments for the Certificates of Participation. The accumulated vacation will be paid by the fund for which the employee worked.

Bonded Debt

In fiscal year 2005-2006, the District issued \$6.95 million in General Obligation Bonds with interest rates ranging from 3.25 to 5.25 percent to advance refund \$7.12 million of outstanding 2001 Series A and B bonds. The net proceeds of \$7,488,308 were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for partial future debt service payments on the 2001 Series A and B bonds. As a result, the 2001 Series A and B bonds are considered to be partially defeased and the liability for those bonds has been removed from the District's statement of net assets. The trust account assets and the liability for the defeased bonds are not included in the District's financial statements. At June 30, 2012, \$0 of the 2001 Series A and \$4.67 million of the 2001 Series B bonds outstanding are considered defeased.

In fiscal year 2008-2009, the District issued \$7.34 million in General Obligation Bonds with an interest rates ranging from 3.50 to 5.00 percent to advance refund \$6.72 million of outstanding 2004 Series A bond. The net proceeds of \$7,415,375 were used to purchase U.S. government securities. Those securities were deposited in an irrevocable trust with an escrow agent to provide for partial future debt service payments on the 2004 Series A bond. As a result, the 2004 Series A bond is considered to be partially defeased and the liability for this bond has been removed from the District's statement of net assets. The trust account assets and the liability for the defeased portion of the bond is not included in the District's financial statements. At June 30, 2012, \$6.73 million of the 2004 Series A bonds outstanding are considered defeased.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

The outstanding general obligation bonded debt is as follows:

Issue Date	Maturity Date	Interest Rate	Original Issue	Bonds Outstanding July 1, 2011	Issued/ Accreted	Redeemed	Bonds Outstanding June 30, 2012
1999	2018	4.25-5.00%	\$ 4,990,000	\$ 2,070,000	\$ -	\$ 325,000	\$ 1,745,000
2002	2027	2.70-6.00%	8,999,326	8,024,956	416,032	525,000	7,915,988
2003	2028	3.00-4.90%	5,498,794	859,516	45,800	75,000	830,316
2004	2016	2.38-2.93%	3,500,047	2,106,467	49,607	630,000	1,526,074
2003	2015	1.25-5.00%	7,675,000	2,785,000	-	720,000	2,065,000
2004	2018	2.00-5.00%	14,755,000	7,790,000	-	1,180,000	6,610,000
2005	2030	3.50-5.00%	15,999,162	7,488,011	41,604	225,000	7,304,615
2006	2029	3.25-5.25%	6,950,000	6,905,000	-	-	6,905,000
2008	2033	3.50-4.00%	14,000,000	13,675,000	-	-	13,675,000
2009	2021	3.50-5.00%	7,340,000	7,040,000	-	475,000	6,565,000
2011	2036	5.25-11.98%	15,163,985	15,253,310	358,932	-	15,612,242
2012	2036	3.00-4.00%	15,000,000	-	15,000,000	-	15,000,000
				<u>\$ 73,997,260</u>	<u>\$ 15,911,975</u>	<u>\$ 4,155,000</u>	<u>\$ 85,754,235</u>

Debt Service Requirements to Maturity

The bonds mature through 2036 as follows:

Fiscal Year	Principal	Interest to Maturity	Total
2013	\$ 5,008,781	\$ 3,078,430	\$ 8,087,211
2014	5,403,318	3,832,900	9,236,218
2015	4,798,487	3,456,131	8,254,618
2016	4,522,102	3,318,346	7,840,448
2017	4,282,012	3,110,220	7,392,232
2018-2022	15,021,842	14,903,004	29,924,846
2023-2027	19,323,175	8,945,400	28,268,575
2028-2032	10,371,727	4,226,225	14,597,952
2033-2036	12,024,870	1,172,025	13,196,895
Subtotal	<u>80,756,314</u>	<u>\$ 46,042,681</u>	<u>\$ 126,798,995</u>
Accretion to date	4,997,921		
Total	<u>\$ 85,754,235</u>		

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Certificates of Participation

In April 2002, the District issued certificates of participation (Certificates) in the amount of \$13 million through the California School Boards Association Finance Corporation at interest rates ranging from 3.0 to 4.5 percent. In November 2004, \$6.5 million in Certificates were called, paid off and removed from long-term debt. Interest rates on the remaining unpaid Certificates ranged from 3.0 to 4.4 percent with an original maturity through 2028.

The certificates mature through 2028 as follows:

Year Ending June 30,	Principal	Interest	Total
2013	\$ 225,000	\$ 248,405	\$ 473,405
2014	230,000	238,393	468,393
2015	240,000	227,518	467,518
2016	255,000	215,953	470,953
2017	265,000	203,794	468,794
2018-2022	1,535,000	803,125	2,338,125
2023-2027	1,960,000	368,000	2,328,000
2028	455,000	11,375	466,375
Total	<u>\$ 5,165,000</u>	<u>\$ 2,316,563</u>	<u>\$ 7,481,563</u>

Accumulated Unpaid Employee Vacation

The long-term portion of accumulated unpaid employee vacation for the District at June 30, 2012, amounted to \$335,066.

Postemployment Benefits

The District provides postemployment health care benefits, in accordance with District employment contracts, to two employees who retired from the District in 2006. The District contributes 100 percent of the amount of premiums incurred by the retirees. Expenditures for post-employment benefits are recognized on a pay-as-you-go basis, as retirees' premiums are paid. During the year, expenditures of \$16,066 were recognized for retirees' health care benefits.

The approximate accumulated future liability for the District at June 30, 2012, amounts to \$179,795. This amount was calculated based upon the two retirees receiving benefits multiplied by the District payment in effect at June 30, 2012, multiplied by the number of years of payments remaining.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Early Retirement Incentives

In the 2010-11 and 2011-12, the District provided a Supplemental Early Retirement Incentives Program to eligible employees.

The incentive payments through the end of the contract are as follows:

Year ending June 30,	Incentive Payments
2013	\$ 961,142
2014	961,142
2015	961,142
2016	240,307
2017	240,307
Total	<u>\$ 3,364,040</u>

NOTE 10 – FUND BALANCES

Fund balances are composed of the following elements:

	General	Building Fund	Bond Interest and Redemption Fund	Non-Major Governmental Funds	Total
Nonspendable					
Revolving cash	\$ 25,000	\$ -	\$ -	\$ -	\$ 25,000
Stores inventories	36,709	-	-	61,678	98,387
Prepaid expenditures	481,534	-	-	-	481,534
Total Nonspendable	<u>543,243</u>	<u>-</u>	<u>-</u>	<u>61,678</u>	<u>604,921</u>
Restricted					
Legally restricted programs	1,788,546	-	-	1,320,973	3,109,519
Capital projects	-	17,355,610	-	655,554	18,011,164
Debt services	-	-	6,711,005	-	6,711,005
Total Restricted	<u>1,788,546</u>	<u>17,355,610</u>	<u>6,711,005</u>	<u>1,976,527</u>	<u>27,831,688</u>
Unassigned					
Reserve for economic uncertainties	2,264,598	-	-	-	2,264,598
Remaining unassigned	4,333,717	-	-	-	4,333,717
Total Unassigned	<u>6,598,315</u>	<u>-</u>	<u>-</u>	<u>-</u>	<u>6,598,315</u>
Total	<u>\$ 8,930,104</u>	<u>\$ 17,355,610</u>	<u>\$ 6,711,005</u>	<u>\$ 2,038,205</u>	<u>\$ 35,034,924</u>

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

NOTE 11 - RISK MANAGEMENT

Property and Liability

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. During fiscal year ending June 30, 2012, the District contracted with Santa Clara County Schools Insurance Group for property and liability insurance coverage. Settled claims have not exceeded this commercial coverage in any of the past three years. There has not been a significant reduction in coverage from the prior year.

Workers' Compensation

The District participates in the Santa Clara County Schools Insurance Group (the JPA) public entity risk pool for the workers' compensation, and property liability coverage.

Coverage provided by Santa Clara County Schools Insurance Group for property and liability and workers' compensation is as follows:

<u>Insurance Program / Company Name</u>	<u>Type of Coverage</u>	<u>Limits</u>
<u>Workers' Compensation Program</u>		
Santa Clara County Schools Insurance Group	Workers' Compensation	\$ 1,000,000
<u>Property and Liability Program</u>		
Santa Clara County Schools Insurance Group	General	\$ 1,000,000
	Automobile	\$ 1,000,000
	Property	\$ 250,000,000

Claims Liabilities

The District records an estimated liability for its Dental and Vision self-insurance programs. Claims liabilities are based on estimates of the ultimate cost of reported claims (including future claim adjustment expenses) and an estimate for claims incurred, but not reported based on historical experience.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Unpaid Claims Liabilities

The self-insurance fund establishes a liability for both reported and unreported events, which includes estimates of both future payments of losses and related claim adjustment expenses. The following represent the changes in approximate aggregate liabilities for the District from July 1, 2010 to June 30, 2012.

	Dental and Vision
Liability Balance, July 1, 2010	\$ 103,102
Claims and changes in estimates	1,437,904
Claims payments	(1,431,781)
Liability Balance, July 1, 2011	109,225
Claims and changes in estimates	1,170,932
Claims payments	(1,377,020)
Liability Balance, June 30, 2012	\$ (96,863)
Assets available to pay claims at June 30, 2012	\$ 461,739

NOTE 12 – EMPLOYEE RETIREMENT SYSTEMS

Qualified employees are covered under multiple-employer retirement plans maintained by agencies of the State of California. Certificated employees are members of the State Teachers' Retirement System (CalSTRS) and classified employees are members of the Public Employees' Retirement System (CalPERS).

CalSTRS

Plan Description

The District contributes to the California State Teachers' Retirement System (CalSTRS); a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalSTRS. The plan provides retirement and disability benefits, annual cost-of-living adjustments and survivor benefits to beneficiaries. Benefit provisions are established by State statutes, as legislatively amended, within the State Teachers' Retirement Law. STRS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalSTRS annual financial report may be obtained from CalSTRS, 7667 Folsom Blvd., Sacramento, CA 95826.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS JUNE 30, 2012

Funding Policy

Active plan members are required to contribute 8.0 percent of their salary and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by CalSTRS Teachers' Retirement Board. The required employer contribution rate for fiscal year 2011-2012 was 8.25 percent of annual payroll. The contribution requirements of the plan members are established by State statute. The District's contributions to CalSTRS for the fiscal years ending June 30, 2012, 2011, and 2010, were \$3,117,630, \$3,232,183, and \$3,570,351, respectively, and equal 100 percent of the required contributions for each year.

CalPERS

Plan Description

The District contributes to the School Employer Pool under the California Public Employees' Retirement System (CalPERS); a cost-sharing multiple-employer public employee retirement system defined benefit pension plan administered by CalPERS. The plan provides retirement and disability benefits, annual cost-of-living adjustments, and survivor benefits to plan members and beneficiaries. Benefit provisions are established by State statutes, as legislatively amended, within the Public Employees' Retirement Laws. CalPERS issues a separate comprehensive annual financial report that includes financial statements and required supplementary information. Copies of the CalPERS' annual financial report may be obtained from the CalPERS Executive Office, 400 P Street, Sacramento, CA 95811.

Funding Policy

Active plan members are required to contribute 7.0 percent of their salary and the District is required to contribute an actuarially determined rate. The actuarial methods and assumptions used for determining the rate are those adopted by the CalPERS Board of Administration. The required employer contribution rate for fiscal 2011-2012 was 10.923 percent of covered payroll. The contribution requirements of the plan members are established by State statute. The District's contribution to CalPERS for the fiscal years ending June 30, 2012, 2011, and 2010 was \$1,134,327, \$1,092,989, and \$1,066,911, respectively.

Tax Deferred Annuity (TDA)

As established by Federal law, all public sector employees who are not members of their employer's existing retirement system (CalSTRS or CalPERS) must be covered by Social Security or an alternative plan. For the District's employees not covered under CalPERS or CalSTRS, the District use Social Security as an alternative plan. Contributions made by the District and an employee vest immediately. The District contributes 6.2 percent of an employee's gross earnings. An employee is required to contribute 6.2 percent of his or her gross earnings to the pension plan through December 31, 2010 and 4.2% through June 30, 2012.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

On Behalf Payments

The State of California makes contributions to CalSTRS on behalf of the District. These payments consist of State General Fund contributions to CalSTRS in the amount of \$1,831,082, \$1,668,546, and \$1,846,626, for fiscal years 2012, 2011 and 2010, respectively. Those amounts represent 4.855 percent of annual payroll as of June 30, 2012, 4.267 percent of annual payroll as of June 30, 2011 and 4.517 for fiscal year ending June 30, 2010. Under accounting principles generally accepted in the United States of America, these amounts are to be reported as revenues and expenditures. Accordingly, these amounts have been recorded in these financial statements. On behalf payments have been excluded from the calculation of available reserves, and have not been included in the budget or actual amounts reported in the General Fund Budgetary Schedule.

NOTE 13 - COMMITMENTS AND CONTINGENCIES

Grants

The District received financial assistance from Federal and State agencies in the form of grants. The disbursement of funds received under these programs generally requires compliance with terms and conditions specified in the grant agreements and are subject to audit by the grantor agencies. Any disallowed claims resulting from such audits could become a liability of the general fund or other applicable funds. However, in the opinion of management, any such disallowed claims will not have a material adverse effect on the overall financial position of the District at June 30, 2012.

Litigation

The District is involved in various litigation arising from the normal course of business. In the opinion of management and legal counsel, the disposition of all litigation pending is not expected to have a material adverse effect on the overall financial position of the District at June 30, 2012.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

Construction Commitments

As of June 30, 2012, the District had the following commitments with respect to the unfinished capital projects:

Capital Project	Remaining Construction Commitment	Expected Date of Completion
Technology Infrastructure IT	\$ 293,081	06/30/13
Bridges Academy Security Safety	363,418	09/30/12
Cornerstone Modernization	2,658,058	08/03/12
Dahl Security Safety	7,961	08/31/12
Franklin Security Safety	46,238	08/03/12
Hellyer Modernization	1,735,431	08/03/12
Kennedy Security Safety	351,142	07/31/12
Lairon School Modernization	566,368	08/03/12
Mckinley Security Safety	83,418	08/31/12
Mckinley Two Story	1,410,565	08/03/12
Meadows Security Safety	1,958,407	08/03/12
Santee Security Safety	267,385	08/31/12
Shirakawa New Construction and Security Safety	145,994	08/31/12
Stonegate School Security Safety	874,268	08/03/12
Success Academy Modernization	487,498	08/03/12
Sylvandale Modernization	459,976	08/31/12
Transportation Security Safety	11,719	08/31/12
Windmill Two Story	315,844	08/31/12
Windmill Security Safety	5,500	08/31/12
	<u>\$ 12,042,271</u>	

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2012

NOTE 14 - PARTICIPATION IN PUBLIC ENTITY RISK POOLS, JOINT POWER AUTHORITIES AND OTHER RELATED PARTY TRANSACTIONS

The District is a member of the Santa Clara County Schools Insurance Group (SCCSIG) public entity risk pool and the East Valley Transportation (EVT) joint powers authority (JPA). The District pays an annual premium to the applicable entity for its health, workers' compensation, and property liability coverage and to provide transportation services for special education students. The relationships between the District, the pool, and the JPA are such that they are not component units of the District for financial reporting purposes.

These entities have budgeting and financial reporting requirements independent of member units and their financial statements are not presented in these financial statements; however, fund transactions between the entities and the District are included in these statements. The District has appointed one board member to the Governing Board of each of these two authorities. During the year ended June 30, 2012, the District made payments of \$457,582 and \$172,485 to SCCSIG and EVT, respectively. Audited financial statements are generally available from the respective entities.

NOTE 15 – SUBSEQUENT EVENTS

On July 2, 2012, the District issued \$8,820,000 Tax and Revenue Anticipation Notes bearing interest at 2.0 percent. Interest and principal were due and payable by February 1, 2013. The notes were sold to supplement cash flows.

REQUIRED SUPPLEMENTARY INFORMATION

FRANKLIN-MCKINLEY SCHOOL DISTRICT

GENERAL FUND BUDGETARY COMPARISON SCHEDULE FOR THE YEAR ENDED JUNE 30, 2012

	Budgeted Amounts		Actual ¹	Variances - Favorable (Unfavorable) Final to Actual
	Original	Final		
REVENUES				
Revenue limit sources	\$48,337,563	\$47,549,016	\$ 47,637,909	\$ 88,893
Federal sources	6,033,633	6,610,030	6,464,286	(145,744)
Other state sources	14,346,379	16,164,227	16,408,265	244,038
Other local sources	4,513,452	6,312,068	7,175,665	863,597
Total Revenues	<u>73,231,027</u>	<u>76,635,341</u>	<u>77,686,125</u>	<u>1,050,784</u>
EXPENDITURES				
Current				
Certificated salaries	38,127,881	38,502,023	38,563,175	(61,152)
Classified salaries	9,756,532	9,408,432	9,406,915	1,517
Employee benefits	14,092,573	14,456,091	14,238,492	217,599
Books and supplies	2,163,174	2,445,408	2,123,323	322,085
Services and operating expenditures	10,099,547	10,080,310	9,999,450	80,860
Other outgo	217,669	24,655	(28,077)	52,732
Capital outlay	-	-	710,541	(710,541)
Debt service				
Principal	215,000	215,000	215,000	-
Interest and other	257,758	257,758	257,756	2
Total Expenditures	<u>74,930,134</u>	<u>75,389,677</u>	<u>75,486,575</u>	<u>(96,898)</u>
NET CHANGE IN FUND BALANCES	<u>(1,699,107)</u>	<u>1,245,664</u>	<u>2,199,550</u>	<u>953,886</u>
Fund Balance - Beginning	<u>6,730,554</u>	<u>6,730,554</u>	<u>6,730,554</u>	<u>-</u>
Fund Balance - Ending	<u>\$ 5,031,447</u>	<u>\$ 7,976,218</u>	<u>\$ 8,930,104</u>	<u>\$ 953,886</u>

¹ On behalf payments of \$1,831,082 are not included in the actual revenues and expenditures or the budgeted revenues and expenditures.

SUPPLEMENTARY INFORMATION

FRANKLIN-MCKINLEY SCHOOL DISTRICT

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS FOR THE YEAR ENDED JUNE 30, 2012

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number	Pass-Through Entity Identifying Number	Federal Expenditures
U.S. DEPARTMENT OF EDUCATION			
Direct Grant:			
Global Student Learning Passport	84.215K	¹	107,438
Passed through California Department of Education (CDE):			
No Child Left Behind Act:			
Title I, Part A, Basic Grants Low-Income and Neglected	84.010	14981	\$ 2,701,599
Title II, ARRA Enhancing Education Through Technology	84.386	¹	10,595
Title II, Part A, Improving Teacher Quality Local Grants	84.367	14341	756,742
Title II, Part D, Enhancing Education Through Technology	84.318	14334	11,171
Title III, Limited English Proficient Student Program	84.365	10084	559,257
Educational Jobs Fund	84.410	25152	515,847
Individuals with Disabilities Education Act			
Basic Local Assistance	84.027	13379	1,542,921
Preschool Grant	84.173	13430	70,008
Preschool Local Entitlement	84.027A	13682	121,461
IDEA Mental Health Allocation Plan, Part B, Sec 611	84.027	14468	66,568
Preschool Staff Development	84.173A	13431	680
Total U.S. Department of Education			<u>6,464,287</u>
U.S. DEPARTMENT OF AGRICULTURE			
Passed through California Department of Education (CDE):			
Child Nutrition Act:			
National School Lunch Program	10.553	13390	3,180,143
Basic School Breakfast	10.553	13525	2,116
Especially Needy Breakfast	10.553	13526	881,114
Fair Market Value of Commodities ²	10.558	13389	287,293
Meal Supplement	10.556	13527	232,746
Total U.S. Department of Agriculture			<u>4,583,412</u>
Total Expenditures of Federal Awards			<u>\$ 11,047,699</u>

¹ Pass-Through Entity Identifying Number not available.

² Not included in the District's financial statements.

See accompanying note to supplementary information.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

LOCAL EDUCATION AGENCY ORGANIZATION STRUCTURE JUNE 30, 2012

ORGANIZATION

The Franklin-McKinley School District was established in 1948 and consists of an area comprising approximately 10 square miles. The District operates 14 elementary schools and two middle schools one of which operates as a conversion charter school.

GOVERNING BOARD

<u>MEMBER</u>	<u>OFFICE</u>	<u>TERM EXPIRES</u>
John Lindner	President	2012
George Sanchez	Vice President	2012
Buu Thai	Clerk	2014
Keith Nguyen	Member	2014
Rudy Rodriguez	Member	2014

ADMINISTRATION

<u>NAME</u>	<u>TITLE</u>
Dr. John R. Porter, Jr.	District Superintendent
Timothy W. McClary	Deputy Superintendent, Business Services
Alicia Henderson	Acting Assistant Superintendent, Educational Services
Rudy Herrera	Deputy Superintendent, Human Resources
Joanne Chin	Director, Fiscal Services

See accompanying note to supplementary information.

FRANKLIN-MCKINLEY SCHOOL DISTRICT**SCHEDULE OF AVERAGE DAILY ATTENDANCE
FOR THE YEAR ENDED JUNE 30, 2012**

	Second Period Report	Annual Report
ELEMENTARY		
Kindergarten	983	984
First through third	3,141	3,142
Fourth through sixth	3,184	3,181
Seventh and eighth	1,205	1,204
Home and hospital	1	1
Special education	238	238
Extended year program	10	10
Total Elementary	8,763	8,760
CHARTER SCHOOL		
Classroom-Based seventh and eighth	619	620
Non-classroom-Based seventh and eighth	1	1
Total Charter School	620	621

See accompanying note to supplementary information.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

SCHEDULE OF INSTRUCTIONAL TIME FOR THE YEAR ENDED JUNE 30, 2012

Grade Level	1982-83	Reduced	1986-87	Reduced	2011-12	Number of Days	Status
	Actual	Actual	Minutes	Minutes	Actual	Traditional	
Minutes	Minutes	Requirement	Requirement	Minutes	Calendar		
Kindergarten	31,680	30,800	36,000	33,600	36,000	180	In compliance
Grade 1	46,816	45,516	50,400	47,040	53,210	180	In compliance
Grade 2	46,816	45,516	50,400	47,040	53,210	180	In compliance
Grade 3	46,816	45,516	54,000	47,040	53,210	180	In compliance
Grade 4	50,688	49,280	54,000	50,400	54,610	180	In compliance
Grade 5	50,688	49,280	54,000	50,400	54,610	180	In compliance
Grade 6	50,688	49,280	54,000	50,400	54,610	180	In compliance
Grade 7	50,688	49,280	54,000	50,400	55,950	180	In compliance
Grade 8	50,688	49,280	54,000	50,400	55,950	180	In compliance

CHARTER SCHOOL

Grade Level	1982-83	Reduced	1986-87	Reduced	2011-12	Number of Days	Status
	Actual	Actual	Minutes	Minutes	Actual	Traditional	
Minutes	Minutes	Requirement	Requirement	Minutes	Calendar		
Grade 7	50,688	49,280	54,000	50,400	58,352	180	In compliance
Grade 8	50,688	49,280	54,000	50,400	58,352	180	In compliance

See accompanying note to supplementary information.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

**RECONCILIATION OF ANNUAL FINANCIAL AND BUDGET REPORT WITH
AUDITED FINANCIAL STATEMENTS
FOR THE YEAR ENDED JUNE 30, 2012**

There were no adjustments to the Unaudited Actual Financial Report, which require reconciliation to the audited financial statements as of June 30, 2012.

See accompanying note to supplementary information.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

SCHEDULE OF FINANCIAL TRENDS AND ANALYSIS FOR THE YEAR ENDED JUNE 30, 2012

	(Budget) 2013 ¹	2012 ³	2011	2010
GENERAL FUND				
Revenues	\$ 73,699,089	\$ 77,686,125	\$ 77,975,746	\$ 79,874,099
Expenditures	74,571,232	75,486,575	75,267,699	82,397,750
Other uses and transfers out	-	-	-	250,000
Total Expenditures and Other Uses	74,571,232	75,486,575	75,267,699	82,647,750
INCREASE (DECREASE) IN FUND BALANCE	\$ (872,143)	\$ 2,199,550	\$ 2,708,047	\$ (2,773,651)
ENDING FUND BALANCE	\$ 8,057,961	\$ 8,930,104	\$ 6,730,554	\$ 4,022,507
AVAILABLE RESERVES ²	\$ 5,726,171	\$ 6,598,315	\$ 5,445,529	\$ 3,124,641
AVAILABLE RESERVES AS A PERCENTAGE OF TOTAL OUTGO	7.68%	8.74%	7.23%	3.78%
LONG-TERM OBLIGATIONS	\$ 91,065,474	\$ 97,742,466	\$ 84,972,320	\$ 69,670,066
AVERAGE DAILY ATTENDANCE AT P-2 ⁴	9,332	9,383	9,584	9,612

The General Fund balance has increased by \$4,907,597 over the past two years. The fiscal year 2012-2013 budget projects a decrease of \$872,143. For a district this size, the State recommends available reserves of at least 3 percent of total General Fund expenditures, transfers out, and other uses (total outgo).

The District has incurred two operating surplus in the past three years but anticipates incurring an operating deficit during the 2012-2013 fiscal year. Total long-term obligations have increased by \$28,072,400 over the past due to new bond issuances in the past two fiscal years.

Average daily attendance has decreased by 229 over the past two years. The District anticipates a decrease of 51 ADA during fiscal year 2012-2013.

¹ Budget 2013 is included for analytical purposes only and has not been subjected to audit.

² Available reserves consist of all unassigned fund balances including all amounts reserved for economic uncertainties contained with the General Fund.

³ On-behalf payments of \$1,831,082, \$1,668,546, and \$1,846,626, in the General Fund have been excluded from revenues, expenditures and the calculation of available reserves percentage for fiscal years ending June 30, 2012, 2011, and 2010, respectively.

⁴ Average daily attendance includes District and charter schools ADA.

See accompanying note to supplementary information.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

SCHEDULE OF CHARTER SCHOOLS JUNE 30, 2012

<u>Name of Charter School</u>	<u>Included in Audit Report</u>
Bridges Academy	Yes
Cornerstone Academy Preparatory School	No
Rocketship Mosaic Elementary Charter School	No
Voices College-Bound Language Academy	No

See accompanying note to supplementary information.

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FRANKLIN-MCKINLEY SCHOOL DISTRICT

NON-MAJOR GOVERNMENTAL FUNDS COMBINING BALANCE SHEET JUNE 30, 2012

	Cafeteria Fund	Deferred Maintenance Fund	Capital Facilities Fund
ASSETS			
Deposits and investments	\$ 735,569	\$ 82,680	\$ 449,116
Receivables	919,167	129	3,983
Due from other funds	45	-	155,495
Stores inventories	61,678	-	-
Total Assets	<u>\$ 1,716,459</u>	<u>\$ 82,809</u>	<u>\$ 608,594</u>
LIABILITIES AND FUND BALANCES			
Liabilities:			
Accounts payable	\$ 182,655	\$ -	\$ -
Due to other funds	233,962	-	2
Total Liabilities	<u>416,617</u>	<u>-</u>	<u>2</u>
Fund Balances:			
Nonspendable	61,678	-	-
Restricted	1,238,164	82,809	608,592
Total Fund Balance	<u>1,299,842</u>	<u>82,809</u>	<u>608,592</u>
Total Liabilities and Fund Balances	<u>\$ 1,716,459</u>	<u>\$ 82,809</u>	<u>\$ 608,594</u>

See accompanying note to supplementary information.

County School Facilities Fund	Special Reserve Capital Outlay Fund	Total Non-Major Governmental Funds
\$ 11,055	\$ 35,854	\$ 1,314,274
17	34	923,330
-	2	155,542
-	-	61,678
<u>\$ 11,072</u>	<u>\$ 35,890</u>	<u>\$ 2,454,824</u>

\$ -	\$ -	\$ 182,655
-	-	233,964
-	-	416,619

-	-	61,678
11,072	35,890	1,976,527
<u>11,072</u>	<u>35,890</u>	<u>2,038,205</u>

<u>\$ 11,072</u>	<u>\$ 35,890</u>	<u>\$ 2,454,824</u>
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FRANKLIN-MCKINLEY SCHOOL DISTRICT

NON-MAJOR GOVERNMENTAL FUNDS COMBINING STATEMENT OF REVENUES, EXPENDITURES, AND CHANGES IN FUND BALANCE FOR THE YEAR ENDED JUNE 30, 2012

	Cafeteria Fund	Deferred Maintenance Fund	Capital Facilities Fund
REVENUES			
Federal sources	\$ 4,296,119	\$ -	\$ -
Other state sources	359,001	-	-
Other local sources	798,317	582	250,367
Total Revenues	5,453,437	582	250,367
EXPENDITURES			
Current			
Instruction-related activities:			
Pupil services:			
Food services	5,020,653	-	-
Administration:			
All other administration	233,959	-	-
Facility acquisition and construction	-	-	3,799
Interest and other	-	-	2
Total Expenditures	5,254,612	-	3,801
NET CHANGE IN FUND BALANCES	198,825	582	246,566
Fund Balance - Beginning	1,101,017	82,227	362,026
Fund Balance - Ending	\$ 1,299,842	\$ 82,809	\$ 608,592

See accompanying note to supplementary information.

County School Facilities Fund	Special Reserve Capital Outlay Fund	Total Non-Major Governmental Funds
\$ -	\$ -	\$ 4,296,119
-	-	359,001
78	333,950	1,383,294
78	333,950	6,038,414
-	-	5,020,653
-	-	233,959
-	333,705	337,504
-	2,190	2,192
-	335,895	5,594,308
78	(1,945)	444,106
10,994	37,835	1,594,099
\$ 11,072	\$ 35,890	\$ 2,038,205

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTE TO SUPPLEMENTARY INFORMATION JUNE 30, 2012

Schedule of Expenditures of Federal Awards

The accompanying Schedule of Expenditures of Federal Awards includes the Federal grant activity of the District and is presented on the modified accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of the United States Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the financial statements.

The following schedule provides reconciliation between revenues reported on the Statement of Revenues, Expenditures, and Changes in Fund Balances and the related expenditures reported on the Schedule of Expenditures of Federal Awards.

Description	CFDA Number	Amount
Total Federal Revenues From the Statement of Revenues, Expenditures and Changes in Fund Balances:		\$ 10,949,125
Federal Reimbursement of Qualified School Construction	Not Available	(188,719)
Fair Market Value of Commodities	10.555	287,293
Total Schedule of Expenditures of Federal Awards		<u>\$ 11,047,699</u>

Local Education Agency Organization Structure

This schedule provides information about the District's boundaries and schools operated, members of the governing board, and members of the administration.

Schedule of Average Daily Attendance (ADA)

Average daily attendance (ADA) is a measurement of the number of pupils attending classes of the District. The purpose of attendance accounting from a fiscal standpoint is to provide the basis on which apportionments of State funds are made to school districts. The schedule provides information regarding the attendance of students at various grade levels and in different programs.

Schedule of Instructional Time

The District has received incentive funding of increasing instructional time as provided by the Incentives for Longer Instructional Day. This schedule presents information on the amount of instructional time offered by the District and whether the District complied with the provisions of Education Code Section 46201.

Reconciliation of Annual Financial and Budget Report with Audited Financial Statements

This schedule provides the information necessary to reconcile the fund balance of all funds reported on the Unaudited Actual Financial Report to the audited financial statements.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

NOTE TO SUPPLEMENTARY INFORMATION JUNE 30, 2012

Schedule of Financial Trends and Analysis

This schedule discloses the District's financial trends by displaying past years' data along with current budget information. These financial trend disclosures are used to evaluate the District's ability to continue as a going concern for a reasonable period of time.

Schedule of Charter Schools

This schedule lists all Charter Schools chartered by the Franklin-McKinley School District and displays information for each Charter School on whether or not the Charter School is included in the Franklin-McKinley School District audit.

Non-major Governmental Funds – Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balance

The Non-major Governmental Funds Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balance is included to provide information regarding the individual funds that have been included in the Non-Major Governmental Funds column on the Governmental Funds Balance Sheet and Statement of Revenues, Expenditures and Changes in Fund Balance.

INDEPENDENT AUDITOR'S REPORTS



**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***

Governing Board
Franklin-McKinley School District
San Jose, California

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Franklin-McKinley School District as of and for the year ended June 30, 2012, which collectively comprise Franklin-McKinley School District's basic financial statements and have issued our report thereon dated November 30, 2012. 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.

Internal Control Over Financial Reporting

Management of Franklin-McKinley School District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Franklin-McKinley School District's internal control over financial reporting as a basis for designing our auditing procedures 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 Franklin-McKinley School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Franklin-McKinley School District's internal control over financial reporting.

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 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.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined previously. However, we identified certain deficiencies in internal control over financial reporting, described in the accompanying schedule of findings and questioned costs 2012-1 that we consider to be significant deficiencies in internal control over financial reporting. 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.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Franklin-McKinley 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*.

This report is intended solely for the information and use of the governing board, management, the California Department of Education, the State Controller's Office, Federal awarding agencies, and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Wassinek, Trine, Day & Co., LLP

Palo Alto, California
November 30, 2012



**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH
REQUIREMENTS THAT COULD HAVE A DIRECT AND MATERIAL
EFFECT ON EACH MAJOR PROGRAM AND ON INTERNAL CONTROL
OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133**

Governing Board
Franklin-McKinley School District
San Jose, California

Compliance

We have audited Franklin-McKinley School District's compliance with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) *Circular A-133 Compliance Supplement* that could have a direct and material effect on each of Franklin-McKinley School District's major Federal programs for the year ended June 30, 2012. Franklin-McKinley 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. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major Federal programs is the responsibility of Franklin-McKinley School District's management. Our responsibility is to express an opinion on Franklin-McKinley School District's compliance based on our audit.

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 Franklin-McKinley 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. Our audit does not provide a legal determination of Franklin-McKinley School District's compliance with those requirements.

In our opinion, Franklin-McKinley School District complied, in all material respects, with the 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, 2012.

Internal Control Over Compliance

The management of Franklin-McKinley School District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to Federal programs. In planning and performing our audit, we considered Franklin-McKinley School District's internal control over compliance with the requirements that could have a direct and material effect on a major Federal program to determine the auditing procedures for the purpose of expressing our opinion on compliance 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 Franklin-McKinley 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.

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 that might be deficiencies, significant deficiencies or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of the governing board, management, the California Department of Education, the State Controller's Office, Federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.



Palo Alto, California
November 30, 2012



INDEPENDENT AUDITOR'S REPORT ON STATE COMPLIANCE

Governing Board
Franklin-McKinley School District
San Jose, California

We have audited Franklin-McKinley School District's compliance with the requirements as identified in the *Standards and Procedures for Audit of California K-12 Local Educational Agencies*, applicable to Franklin-McKinley School District's government programs as noted below for the year ended June 30, 2012. Compliance with the requirements referred to above is the responsibility of Franklin-McKinley School District's management. Our responsibility is to express an opinion on Franklin-McKinley School District's compliance based on our audit.

We conducted our audit 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 the *Standards and Procedures for Audits of California K-12 Local Educational Agencies 2011-2012* require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the compliance requirements referred to above that could have a material effect on the applicable government programs noted below. An audit includes examining, on a test basis, evidence about Franklin-McKinley 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 opinions. Our audit does not provide a legal determination of Franklin-McKinley School District's compliance with those requirements.

In our opinion, Franklin-McKinley School District complied, in all material respects, with the compliance requirements referred to above that are applicable to the government programs noted below that were audited for the year ended June 30, 2012.

In connection with the audit referred to above, we selected and tested transactions and records to determine the Franklin-McKinley School District's compliance with the State laws and regulations applicable to the following items:

	Procedures in Audit Guide	Procedures Performed
Attendance Accounting:		
Attendance reporting	8	Yes
Teacher Certification and Misassignments	3	Yes
Kindergarten continuance	3	Yes
Independent study	23	Yes
Continuation education	10	Not Applicable
Instructional Time:		
School districts	6	Yes
County offices of education	3	Not Applicable

	Procedures in Audit Guide	Procedures Performed
Instructional Materials:		
General requirements	8	Yes
Ratios of Administrative Employees to Teachers	1	Yes
Classroom Teacher Salaries	1	Yes
Early Retirement Incentive	4	Not Applicable
Gann Limit Calculation	1	Yes
School Accountability Report Card	3	Yes
Public Hearing Requirement - Receipt of Funds	1	Yes
Juvenile Court Schools	8	Not Applicable
Exclusion of Pupils - Pertussis Immunization	2	Yes
Class Size Reduction Program (including in charter schools):		
General requirements	7	Yes
Option one classes	3	Yes
Option two classes	4	Not Applicable
Districts or charter schools with only one school serving K-3	4	Not Applicable
After School Education and Safety Program:		
General requirements	4	Yes
After school	5	Yes
Before school	6	Not Applicable
Charter Schools:		
Contemporaneous records of attendance	3	Yes
Mode of instruction	1	Yes
Non classroom-based instruction/independent study	15	No
Determination of funding for non classroom-based instruction	3	No
Annual instruction minutes classroom based	4	Yes

We did not perform testing for non classroom-based instruction/independent study and determination of funding for non classroom-based instruction because ADA generated from this program is below testing threshold.

This report is intended solely for the information and use of the governing board, management, the California Department of Education, the State Controller's Office, the California Department of Finance, Federal awarding agencies, and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

Vavrinek, Trine, Day & Co., LLP

Palo Alto, California
November 30, 2012

SCHEDULE OF FINDINGS AND QUESTIONED COSTS

FRANKLIN-MCKINLEY SCHOOL DISTRICT

SUMMARY OF AUDITOR'S RESULTS FOR THE YEAR ENDED JUNE 30, 2012

FINANCIAL STATEMENTS

Type of auditor's report issued:	<u>Unqualified</u>
Internal control over financial reporting:	
Material weaknesses identified?	<u>No</u>
Significant deficiencies identified?	<u>Yes</u>
Noncompliance material to financial statements noted?	<u>No</u>

FEDERAL AWARDS

Internal control over major programs:	
Material weaknesses identified?	<u>No</u>
Significant deficiencies identified?	<u>None reported</u>
Type of auditor's report issued on compliance for major programs:	<u>Unqualified</u>
Any audit findings disclosed that are required to be reported in accordance with Section .510(a) of OMB Circular A-133?	
Identification of major programs:	<u>No</u>

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
<u>84.027,84.027A,84.173,84.173A</u>	<u>Special Education Cluster</u>
<u>84.365</u>	<u>Title III, Limited English Proficient Student Program</u>
<u>84.410</u>	<u>Educational Job Fund</u>

Dollar threshold used to distinguish between Type A and Type B programs:	<u>\$ 331,431</u>
Auditee qualified as low-risk auditee?	<u>Yes</u>

STATE AWARDS

Type of auditor's report issued on compliance for all State programs:	<u>Unqualified</u>
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FRANKLIN-MCKINLEY SCHOOL DISTRICT

FINANCIAL STATEMENT FINDINGS FOR THE YEAR ENDED JUNE 30, 2012

The following findings represent instances of noncompliance and/or questioned costs relating to State program laws and regulations. The findings have been coded as follows:

<u>Five Digit Code</u>	<u>AB 3627 Finding Type</u>
30000	Internal Control

2012-1 STUDENT BODY ACCOUNTS AT SITE (30000)

Criteria or Specific Requirements

The internal controls over the financial reporting of the Associated Student Body (ASB) accounts should include policies and procedures over the timely deposits of its cash collections.

Condition

During our visit at one of the school sites, we noted that the number of days between receipt and deposit was over a month.

Questioned Costs

None.

Context

All site cash collections and all cash collected from ASB activities.

Effect

Cash collections not deposited in the bank are subject to theft and misappropriation.

Cause

The policies and procedures outlined by the District for the cash deposit were not being completely followed.

Recommendation

We recommend District to enforce procedures at the affected school sites to ensure that all cash collections are deposited in a timely manner.

District Response

The district provided every principal a FCMAT Accounting Manual for Student Body. The Business Office staff will visit all schools to train site personnel with the procedures and address the issues raised in the audit.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

**FEDERAL AWARDS FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2012**

None reported.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

**STATE AWARDS FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2012**

None reported.

FRANKLIN-MCKINLEY SCHOOL DISTRICT

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS FOR THE YEAR ENDED JUNE 30, 2012

Except as specified in previous sections of this report, summarized below is the current status of all audit findings reported in the prior year's schedule of financial statement findings.

Financial Statement Findings

2011-1 Code 30000

Student Body Accounts at Site

Finding

During our visit at Sylvandale and Meadows schools, we noted that for fund raising activities, the sites did not prepare revenue potential forms. In addition, we noted that student council minutes were also not prepared for Sylvandale.

Recommendation

We recommend the District to enforce procedures at the affected school site to ensure that all fund raising activities cash collections should be reconciled against a sales expectation calculation formulated in what is referred to as revenue potential form. For student council minutes, we recommend the affected school site to compile minutes every time the student council meets noting topics discussed and other pertinent detailed information that was discussed during the student council meeting.

Current Status

Implemented.

Federal Awards Findings

None reported.

State Awards Findings

None reported.