



**SHELTER ISLAND
UNION FREE SCHOOL DISTRICT**

FINANCIAL STATEMENTS AND
SUPPLEMENTARY SCHEDULES WITH
INDEPENDENT AUDITOR'S REPORTS

June 30, 2012

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
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INDEPENDENT AUDITOR'S REPORT

To the Board of Education
Shelter Island Union Free School District
Shelter Island, New York

We have audited the accompanying financial statements of the governmental activities, each major fund and the fiduciary funds of the Shelter Island Union Free School District (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 the financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, 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 fiduciary funds of the Shelter Island Union Free School District, as of June 30, 2012, and the respective changes in financial position 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 16, 2012, on our consideration of the Shelter Island Union Free School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements 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 management's discussion and analysis, budgetary comparison information and the schedule of funding progress - other postemployment benefits on pages 3 through 14 and 42 through 44, respectively, 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 Shelter Island Union Free School District's basic financial statements. The other supplementary information on pages 45 through 48 is not a required part of the basic financial statements but is supplementary information required by the New York State Education Department. The other supplementary information has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we express no opinion on it.

Cullen & Danowski, LLP

November 16, 2012

**SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS**

The Shelter Island Union Free School District's (District) discussion and analysis of the financial performance provides an overall review of the District's financial activities for the fiscal year ended June 30, 2012. The intent of this discussion and analysis is to look at the District's financial performance as a whole. This should be read in conjunction with the financial statements, which immediately follow this section.

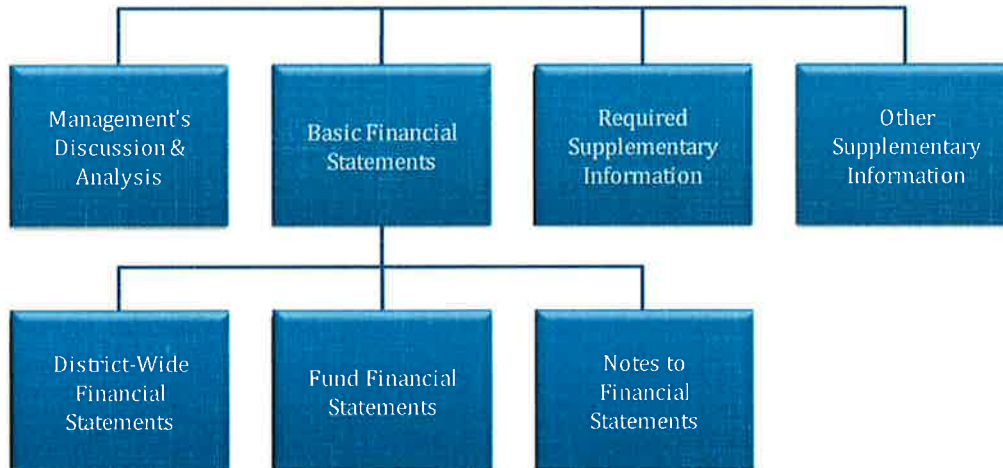
1. FINANCIAL HIGHLIGHTS

Key financial highlights for fiscal year 2012 are as follows:

- The District's total net assets, as reflected in the district-wide financial statements, decreased by \$1,060,017 or 15.63% to \$5,721,785.
- The general fund's total fund balance, as reflected in the fund financial statements, increased by \$249,604 or 10.29% to \$2,674,490.
- On May 15, 2012, the voters of the District approved the issuance of serial bonds in the amount of \$2,837,000 to finance various building improvements and the installation of a new generator and related lighting system improvements.

2. OVERVIEW OF THE FINANCIAL STATEMENTS

This annual report consists of four parts – management's discussion and analysis (MD&A), the basic financial statements, required supplementary information, and other supplementary information. The basic financial statements consist of district-wide financial statements, fund financial statements, and notes to the financial statements. A graphic display of the relationship of these statements follows:



A. District-Wide Financial Statements

The district-wide financial statements present the governmental activities of the District and are organized to provide an understanding of the fiscal performance of the District as a whole in a manner similar to a private sector business. There are two district-wide financial statements - the Statement of Net Assets and the Statement of Activities. These statements provide both an aggregate and long-term view of the District's finances.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

These statements utilize the accrual basis of accounting. This basis of accounting recognizes the financial effects of events when they occur, without regard to the timing of cash flows related to the events.

The Statement of Net Assets

The Statement of Net Assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Increases or decreases in net assets may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The Statement of Activities

The Statement of Activities presents information showing the change in net assets during the fiscal year. All changes in net assets are recorded at the time the underlying financial event occurs. Therefore, revenues and expenses are reported in the statement for some items that will result in cash flow in future fiscal periods.

B. Fund Financial Statements

The fund financial statements provide more detailed information about the District's funds, not the District as a whole. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The District also uses fund accounting to ensure compliance with finance-related legal requirements. The funds of the District are reported in the governmental funds and the fiduciary funds.

Governmental Funds

These statements utilize the modified accrual basis of accounting. This basis of accounting recognizes revenues in the period that they become measurable and available. It recognizes expenditures in the period that they become measurable, funded through available resources and payable within a current period.

Governmental funds are used to account for essentially the same functions reported as governmental activities in the district-wide financial statements. However, the governmental fund financial statements focus on shorter term inflows and outflows of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year for spending in future years. Consequently, the governmental fund statements provide a detailed short-term view of the District's operations and the services it provides.

Because the focus of governmental funds is narrower than that of district-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the district-wide financial statements. By doing so, you may better understand the long-term impact of the District's near-term financing decisions. Both the governmental fund Balance Sheet and the governmental fund Statement of Revenues, Expenditures, and Changes in Fund Balance provide a reconciliation to facilitate this comparison between governmental funds and governmental activities.

The District maintains four individual governmental funds: general fund, special aid fund, school lunch fund and capital projects fund, each of which is considered to be a major fund and is presented separately in the fund financial statements.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Fiduciary Funds

Fiduciary funds are used to account for assets held by the District in its capacity as agent or trustee and utilize the accrual basis of accounting. All of the District's fiduciary activities are reported in a separate Statement of Fiduciary Net Assets. The fiduciary activities have been excluded from the District's district-wide financial statements because the District cannot use these assets to finance its operations.

3. FINANCIAL ANALYSIS OF THE DISTRICT AS A WHOLE

A. Net Assets

The District's total net assets decreased by \$1,056,242 between fiscal year 2012 and 2011. A summary of the District's Statements of Net Assets are as follows:

	<u>2012</u>	<u>2011</u>	<u>Increase (Decrease)</u>	<u>Percentage Change</u>
Current and Other Assets	\$ 3,864,140	\$ 4,177,147	\$ (313,007)	(7.49)%
Capital Assets, Net	5,840,029	5,314,820	525,209	9.88 %
Total Assets	<u>9,704,169</u>	<u>9,491,967</u>	<u>212,202</u>	<u>2.24 %</u>
Current and Other Liabilities	1,062,986	901,942	161,044	17.86 %
Long-Term Liabilities	823,641	599,631	224,010	37.36 %
Net Other Postemployment Benefits Obligation	<u>2,095,757</u>	<u>1,208,592</u>	<u>887,165</u>	<u>73.40 %</u>
Total Liabilities	<u>3,982,384</u>	<u>2,710,165</u>	<u>1,272,219</u>	<u>46.94 %</u>
Net Assets				
Investment in Capital Assets, Net of Related Debt	5,840,029	5,314,820	525,209	9.88 %
Restricted	1,393,139	1,289,928	103,211	8.00 %
Unrestricted (Deficit)	<u>(1,511,383)</u>	<u>177,054</u>	<u>(1,688,437)</u>	<u>(953.63)%</u>
Total Net Assets	<u>\$ 5,721,785</u>	<u>\$ 6,781,802</u>	<u>\$ (1,060,017)</u>	<u>(15.63)%</u>

Current and other assets decreased by \$313,007, as compared to the prior year. The decrease is evidenced by a reduction in the District's cash balances, offset by increases in receivables.

Capital assets, net increased by \$525,209, as compared to the prior year. This increase is primarily due to capital outlays for building improvements / site improvements and equipment purchases in excess of depreciation. The accompanying Notes to Financial Statements, Note 8 "Capital Assets" provides additional information.

Current and other liabilities increased by \$161,044, as compared to the prior year. This increase is primarily due to increases in accounts payable and accrued liabilities offset by decreases in amounts due to other governments and to the teachers' retirement system, as well as a decrease in deferred revenues. In the current year, accrued liabilities included amounts related to retirement incentives. The District did not have similar accruals in the prior year.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Long-term liabilities increased by \$224,010, as compared to the prior year. This increase is primarily the result of increases in workers' compensation and termination benefits liabilities, offset by a decrease in the compensated absences liability.

Net other postemployment benefits (OPEB) obligation increased by \$887,165, as compared to the prior year. This increase was the result of the current year unfunded OPEB costs on the full accrual basis of accounting in excess of the amount reflected in the governmental funds on the modified accrual basis (pay as you go). Under the current NYS laws, there is no provision to fund this obligation by any other means than "pay as you go" method. The accompanying Notes to Financial Statements, Note 13 "Postemployment Benefits", provides additional information.

The investment in capital assets, net of related debt, relates to the investment in capital assets at cost such as land; construction in progress; buildings and improvements; site improvements; and, furniture and equipment, net of depreciation and related debt. This number increased over the prior year as follows:

	Increase (Decrease)
Capital asset additions - total	\$ 736,702
Depreciation expense	(211,493)
	\$ 525,209

The restricted net assets in the amount of \$1,393,139 relates to the District's reserves. This number increased over the prior year by \$103,211 principally due to the transfer into the reserves in the amount of \$386,352 and interest earnings of \$519, net of appropriation of reserves in the amount of \$283,660 to fund the 2011-12 budget and budget revisions.

The unrestricted net assets (deficit) in the amount of \$(1,511,383) relates to the balance of the District's net assets. This number decreased from the prior year by \$1,688,437.

The District's total net assets decreased by \$1,056,242 or 15.57%; \$5,725,560 at June 30, 2012, compared to \$6,781,802 at June 30, 2011.

B. Changes in Net Assets

The results of this year's operations as a whole are reported in the Statement of Activities in a programmatic format in the accompanying financial statements. In the accompanying financial statements STAR (school tax relief) revenue is included in the other tax items line. However, in this MD&A, STAR revenue has been combined with property taxes. A summary of these statements for the years ended June 30, 2012 and 2011 are as follows:

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

	2012	2011	Increase (Decrease)	Percentage Change
Revenues				
Program Revenues				
Charges for Services	\$ 53,688	\$ 53,833	\$ (145)	(0.27)%
Operating Grants	252,277	244,771	7,506	3.07 %
General Revenues				
Property Taxes and STAR	8,727,490	8,600,123	127,367	1.48 %
State Sources	392,389	461,568	(69,179)	(14.99)%
Other	173,065	88,102	84,963	96.44 %
Total Revenues	<u>9,598,909</u>	<u>9,448,397</u>	<u>150,512</u>	1.59 %
Expenses				
General Support	1,776,599	2,163,325	(386,726)	(17.88)%
Instruction	8,413,894	7,375,080	1,038,814	14.09 %
Pupil Transportation	267,307	311,705	(44,398)	(14.24)%
Community Service	24,760	11,143	13,617	100.00 %
Debt Service - Interest	5,519	9,766	(4,247)	(43.49)%
Food Service Program	170,847	150,103	20,744	13.82 %
Total Expenses	<u>10,658,926</u>	<u>10,021,122</u>	<u>637,804</u>	6.36 %
Decrease in Net Assets	<u>\$ (1,060,017)</u>	<u>\$ (572,725)</u>	<u>\$ (487,292)</u>	85.08 %

The District's revenues increased by \$150,512 or 1.59%, as compared to 2011. This increase is attributable to increases in property taxes and STAR and other revenues offset by a decrease in State sources. Property taxes and STAR were increased in 2012 to fund increases in appropriations in the 2011-12 budget. The increase in other revenues is due to the District receiving additional Medicare Part D reimbursements and additional reimbursements for the 2010-11 summer handicapped program. The District did not receive similar reimbursements in the prior year. The decrease in State sources is primarily due to decreases in excess cost aid and BOCES aid.

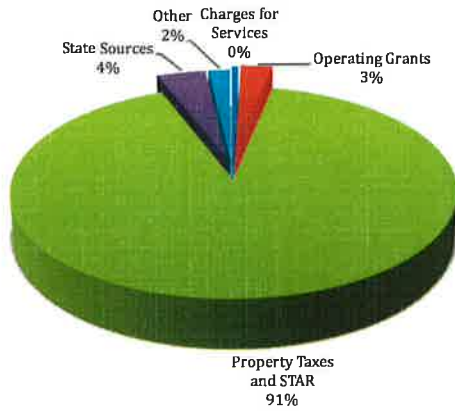
The District's expenses for the year increased by \$637,804 or 6.36%, as compared to 2011. The increase was primarily due to increases in instruction offset by decreases in general support and pupil transportation. The increase in instruction was due to salary increases, compensated absence payouts and retirement incentives combined with an increase in related employee benefits. In the prior year, general support included retirement payouts. The District did not have similar payouts in 2012. In addition, the decrease in general support reflects staff changes in administration. The decrease in transportation was the result of consolidating routes.

As indicated on the pie charts that follow, real property taxes and STAR is the largest component of revenues recognized (i.e., 91% of the total for both years). Instructional expenses is the largest category of expenses incurred (i.e., 79% and 74% of the total for the years 2012 and 2011, respectively).

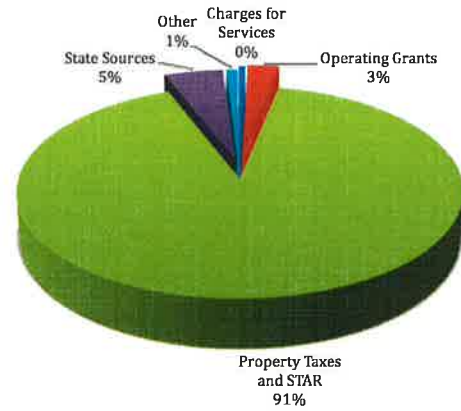
**SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

A graphic display of the distribution of revenues for the two years follows:

June 30, 2012

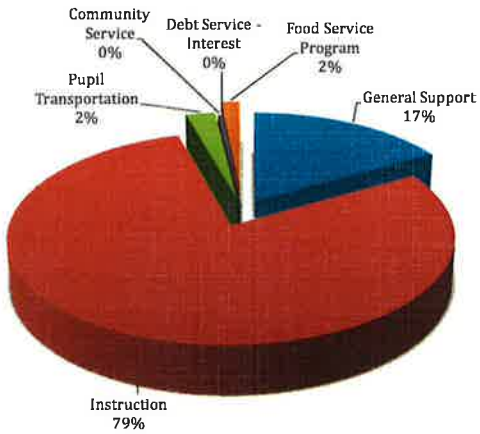


June 30, 2011

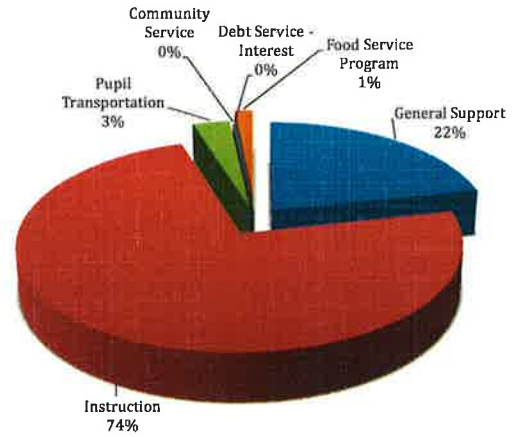


A graphic display of the distribution of expenses for the two years follows:

June 30, 2012



June 30, 2011



SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

4. FINANCIAL ANALYSIS OF THE DISTRICT'S FUNDS

At June 30, 2012, the District's governmental funds reported a combined fund balance of \$2,477,751 which is a decrease of \$472,088 from the prior year. A summary of the change in fund balance by fund is as follows:

	<u>2012</u>	<u>2011</u>	<u>Operating Changes</u>
General Fund			
Nonspendable: Advances	\$	\$ 14,618	\$ (14,618)
Restricted			
Unemployment insurance	149,388	69,355	80,033
Retirement contribution	249,801	199,707	50,094
Employee benefit accrued liability	464,484	493,911	(29,427)
Capital	529,466	337,889	191,577
Assigned:			
Appropriated fund balance	325,000	325,000	-
Unappropriated fund balance	44,624	44,564	60
Unassigned:			
Unassigned: Fund balance	911,727	939,842	(28,115)
	<u>2,674,490</u>	<u>2,424,886</u>	<u>249,604</u>
School Lunch Fund			
Nonspendable: Inventory	2,515	2,174	341
Assigned: Unappropriated fund balance	8,211		8,211
Unassigned: Fund balance (deficit)		(14,618)	14,618
	<u>10,726</u>	<u>(12,444)</u>	<u>23,170</u>
Capital Projects Fund			
Restricted: Capital		189,066	(189,066)
Assigned: Unappropriated fund balance		348,331	(348,331)
Unassigned: Fund balance (deficit)	(207,465)		(207,465)
	<u>(207,465)</u>	<u>537,397</u>	<u>(744,862)</u>
Total Fund Balance	<u>\$ 2,477,751</u>	<u>\$ 2,949,839</u>	<u>\$ (472,088)</u>

A. General Fund

The net change in the general fund – fund balance is an increase of \$249,604 (compared to an increase of \$8,149 in fiscal 2011), as revenues and other financing sources of \$9,482,360 exceeded expenditures and other financing uses of \$9,232,756.

Revenues increased by \$285,109 (3.10%) over fiscal 2011 totals primarily due to increases in property taxes, miscellaneous revenue and operating transfers in, offset by a decrease in state and federal sources. Property taxes were increased to fund increases in appropriations in the 2011-12 budget. The increase in miscellaneous revenue was the result of an increase in Medicare Part D reimbursements and additional reimbursement for the 2010-11 summer handicapped program, as previously mentioned. Operating transfers in the current year included a transfer from the capital projects fund for unspent capital reserve funds related to the completed roof project. In the prior year, the District did not have a similar transfer.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Expenditures and other financing uses increased by \$43,654 or 4.75% over fiscal 2011 totals. This increase was primarily in instruction and employee benefits offset by decreases in general support, pupil transportation and operating transfers out. The increase in instruction was due to salary increases and retirement payouts. The District did not have similar payouts in 2011. Employee benefits increased due to increases in salaries, increases in contribution rates for the retirement systems and increases in health insurance premiums. The decrease in general support reflects staff changes in administration. The decrease in transportation was the result of consolidating routes. In the prior year, operating transfers out included a \$219,000 transfer to the capital projects fund to finance a portion of the project F.I.T. capital project. The District did not make a similar transfer in 2012.

Nonspendable advances is used to reserve for loans to other funds that are not expected to be paid within a current period. This amount decreased by \$14,618 from the prior year due to the District providing additional funding from the general fund to subsidize the lunch program.

As part of the District's 2011-12 budget, the District planned on appropriating restricted reserves to fund a portion of the budget. Based on the 2011-12 budget \$20,000 was appropriated from the unemployment reserve and \$100,000 from the retirement contribution reserve. In addition during 2011-12, the District appropriated \$163,660 from the employee benefit accrued liability reserve to fund compensated absences payouts.

In June 2012, the Board of Education approved funding to replenish and in some instances increase these restricted reserves and transferred \$100,000 to the unemployment insurance reserve; \$150,000 to the retirement contribution reserve; and \$134,000 to the employee benefit accrued liability reserve. The increase in the capital reserve related to the transfer from the capital projects fund of unspent capital reserve monies for the completed roof project. The reserves also earned \$519 in interest.

In May 2006, the voters of the District authorized the creation of a capital reserve for \$2,000,000 to be funded for a period of five years. During the 2011-12 fiscal year, the reserve earned interest of \$159. The total amount paid into the reserve was \$1,767,000. During 2011-12, the District completed the roof project that was funded by the capital reserve. The unspent funds of \$189,066 were transferred back into the reserve. This resulted in an increase of \$189,225 in the reserves. The remaining balance of this reserve in the amount of \$527,114 is available for future capital projects.

In May 2011, the voters of the District authorized the creation of a capital reserve for \$10,000,000 to be funded over a period of 20 years. The reserve is to be used for renovations to the portion of the school known as the F.I.T. Center. Funding of the reserve is from surplus monies remaining in the general fund each year as received by the District from the Town of Shelter Island (revenues net of expenditures to operate the Center). During 2011-12 fiscal year, the District transferred \$2,338 into the reserve. In addition, the reserve earned \$14 in interest. At June 30, 2012 the reserve has a balance of \$2,352.

B. School Lunch Fund

The net change in the school lunch fund – fund balance is an increase of \$23,170, which was the operating profit of the school lunch fund. The fund is dependent on a transfer from the general fund.

**SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)**

C. Capital Projects Fund

The net change in the capital projects fund – fund balance is a decrease of \$744,862, due to expenditures incurred during the year on capital projects, primarily the F.I.T. Center, and the transfer to the general fund previously discussed.

On May 15, 2012, the voters approved capital projects for various building improvements and the installation of a new generator. The work is anticipated to be completed in 2013. The District issued \$2,837,000 in serial bonds in July 2012, to finance the project.

5. GENERAL FUND BUDGETARY HIGHLIGHTS

A. 2011-12 Budget

The District's general fund adopted budget for the year ended June 30, 2012 was \$9,640,614. This amount was increased by encumbrances carried forward from the prior year in the amount of \$44,564 and budget revisions in the amount of \$341,294 for a total final budget of \$10,026,472.

The budget was funded through a combination of revenues and designated fund balance. The majority of this funding source was \$8,727,224 in estimated property taxes and STAR.

B. Change in General Fund's Unassigned Fund Balance (Budget to Actual)

The general fund's unassigned fund balance is the component of total fund balance that is the residual of prior years' excess revenues over expenditures, net of transfers to reserves and appropriations to fund the subsequent year's budget. It is this balance that is commonly referred to as the "fund balance". The change in this balance demonstrated through a comparison of the actual revenues and expenditures for the year compared to budget follows:

Opening, Unassigned Fund Balance	\$ 939,842
Fund Balance Appropriated for Budget Revision	(154,767)
Revenues Over Budget	263,879
Expenditures and Encumbrances Under Budget	749,092
Net Change in Nonspendable Fund Balance	14,618
Transfers to Restricted Reserves	(575,418)
Interest Earned on Restricted Reserves	(519)
Appropriated for the June 30, 2013 Budget	<u>(325,000)</u>
Closing, Unassigned Fund Balance	<u><u>\$ 911,727</u></u>

Opening, Unassigned Fund Balance

The \$939,842 shown in the table is the portion of the District's June 30, 2011 fund balance that was retained as unassigned fund balance.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Fund Balance Appropriated for Budget Revision

The District appropriated an additional \$154,767 of unassigned fund balance during 2011-12 to fund the budget for the year ended June 30, 2012 for unanticipated contingent expenditures for retirement payouts and transfer to the school lunch fund to subsidize the lunch program.

Revenues Over Budget

The 2011-12 final budget for revenues was \$9,218,481. Actual revenues received for the year were \$9,482,360. The excess of actual revenue over estimated or budgeted revenue was \$263,879. This change contributes directly to the change to the general fund unassigned fund balance from June 30, 2011 to June 30, 2012. The surplus in revenues is primarily due to the District receiving more than anticipated in miscellaneous revenues and operating transfers in.

Expenditures and Encumbrances Under Budget

The 2011-12 final budget for expenditures was \$10,026,472. Actual expenditures as of June 30, 2012 were \$9,232,756 and outstanding encumbrances were \$44,624. Combined, the expenditures plus encumbrances for 2011-12 were \$9,277,380. The final budget was under expended by \$749,092. This under expenditure is primarily within general support, pupil transportation and employee benefit codes of the budget.

Net Change in Nonspendable Fund Balance

The decrease of \$14,618 reflects the decrease in nonspendable advances. This decrease similarly decreased the unassigned portion of the general fund – fund balance at June 30, 2012.

Transfers to Restricted Reserves

Monies transferred from budget lines within the general fund operating budget into the reserves do not affect the combined reserved, assigned and unassigned fund balance unless, and until these monies are actually expended. The transfers do, however, reduce the District's discretion regarding the use of these transferred monies, and thus, reduce the unassigned fund balance by the amount of the transfers.

The (\$575,418) shown in the previous table is made up of the following transfers: \$100,000 to the unemployment insurance reserve; \$150,000 to the retirement contribution reserve; \$134,000 to the employee benefit accrued liability reserve; and \$191,418 to the capital reserve.

Interest Earned in Restricted Reserves

This amount represents interest earned in the reserves as follows:

Reserve for:		
Unemployment insurance	\$	33
Retirement contribution		94
Employee benefit accrued liability		233
Capital		159
		<u>519</u>
	\$	<u>519</u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

Appropriated Fund Balance

The District has chosen to use \$325,000 of its available June 30, 2012 fund balance to partially fund its 2012-13 approved operating budget. As such, the June 30, 2012 unassigned fund balance must be reduced by the amount shown above.

Closing Unassigned Fund Balance

Based upon the summary changes shown in the above table, the District will begin the 2012-13 fiscal year with an unassigned fund balance of \$911,727. This is a reduction of \$28,115 from the unassigned fund balance from the prior year as of June 30, 2012. This unassigned portion is in excess of the permissible 4.0% statutory maximum. The District is in the process of formulating a plan to reduce the unassigned fund balance to be within the permissible limit. This plan will address funding its reserves to a fiscally prudent level and addressing the capital needs of the District.

6. CAPITAL ASSETS AND DEBT ADMINISTRATION

A. Capital Assets

At June 30, 2012, the District had invested in a broad range of capital assets, as indicated in the table below. The net increase in capital assets is due to capital additions less depreciation recorded for the year ended June 30, 2012. A summary of the District's capital assets, net of depreciation at June 30, 2012 and 2011 is as follows:

	2012	2011	Increase (Decrease)
Land	\$ 25,200	\$ 25,200	\$ -
Construction in progress	207,465	900,485	(693,020)
Buildings and improvements	4,993,173	3,870,796	1,122,377
Site improvements	239,945	185,301	54,644
Furniture and equipment	374,246	333,038	41,208
Capital assets, net	\$ 5,840,029	\$ 5,314,820	\$ 525,209

The increase in buildings and improvements is due to the completion of the following capital projects:

- Project F.I.T.
- Roof replacement
- Handicap access doors

B. Debt Administration

The District has no outstanding debt obligations at June 30, 2012. However, on July 26, 2012, the District issued serial bonds in the amount of \$2,837,000, which are due June 15, 2029 and bear interest rates ranging from 2.750% to 3.375%. The bonds were issued to finance various building improvements and the installation of a new generator and related lighting system improvements.

The District's latest underlying, long-term credit rating from Moody's Investors Service, Inc. is Aa2. The District's total outstanding indebtedness of \$2,837,000 does not exceed its debt limit of \$305,278,021, which is 10% of the full valuation of the taxable real property within the District.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
MANAGEMENT'S DISCUSSION AND ANALYSIS
(Continued)

7. ECONOMIC FACTORS AND NEXT YEAR'S BUDGET

The general fund budget, the only fund with a legally adopted budget, as approved by the voters on May 15, 2012, for the year ending June 30, 2013, is \$9,739,303. This is an increase of \$98,689 or 1.02% over the previous year's budget. The increase is principally in the instructional program and debt service areas of the budget.

The District budgeted non-property tax revenues at a \$47,873 increase over the prior year's estimate. This increase is principally due to an estimated increase in state aid. The assigned, appropriated fund balance applied to the June 30, 2013 budget in the amount of \$325,000 remained the same as the previous year. In addition, the District reduced amounts appropriated from restricted reserves by \$120,000. A property tax increase of 1.96% was needed to meet the revenue shortfall and cover the increase in projected expenditures.

Chapter 97 of the 2011 Laws of New York limits the increase in the property tax levy of school districts to the lesser of 2% or the rate of inflation effective for the 2012-13 fiscal year. There are additional statutory adjustments in the law. School districts may override the tax levy limit by presenting to the voters a budget that requires a tax levy that exceeds the statutory limit. However, that budget must be approved by 60% of the votes cast. Based on the new law, the District's tax levy cap was 2.26%. The District's 1.96% increase in the levy was within the tax levy cap.

8. CONTACTING THE DISTRICT

This financial report is designed to provide the reader with a general overview of the District's finances and to demonstrate the District's accountability for the funds it receives. Requests for additional information can be directed to:

Mr. Michael Hynes
Superintendent
Shelter Island Union Free School District
33 North Ferry Road
Box 2015
Shelter Island, New York 11964

SHELTER ISLAND UNION FREE SCHOOL DISTRICT

Statement of Net Assets

June 30, 2012

ASSETS	
Cash	\$ 3,266,719
Receivables	
Accounts receivable	846
Due from other funds	34,253
Due from state and federal	196,493
Due from other governments	39,910
Other assets	323,403
Inventory	2,516
Capital assets:	
Not being depreciated	232,665
Being depreciated, net of accumulated depreciation	<u>5,607,364</u>
 Total Assets	 <u><u>\$ 9,704,169</u></u>
 LIABILITIES	
Payables	
Accounts payable	\$ 320,688
Accrued liabilities	222,517
Due to other governments	197
Due to teachers' retirement system	445,175
Due to employees' retirement system	51,515
Compensated absences payable	21,136
Deferred credits	
Deferred revenues	1,758
Long-term liabilities	
Due and payable within one year	
Compensated absences payable	148,155
Termination benefits	200,250
Due and payable after one year	
Compensated absences payable	316,496
Workers' compensation liabilities	49,521
Termination benefits	109,219
Net other postemployment benefits obligation	<u>2,095,757</u>
 Total Liabilities	 <u><u>3,982,384</u></u>
 NET ASSETS	
Investment in capital assets, net of related debt	5,840,029
Restricted	1,393,139
Unrestricted (deficit)	<u>(1,511,383)</u>
 Net Assets	 <u><u>5,721,785</u></u>
 Total Liabilities and Net Assets	 <u><u>\$ 9,704,169</u></u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT

Statement of Activities

For The Year Ended June 30, 2012

	Expenses	Program Revenues		Net (Expense) Revenue and Changes in Net Assets
		Charges for Services	Operating Grants	
PROGRAMS/FUNCTIONS				
General support	\$ 1,776,599	\$	\$	\$ (1,776,599)
Instruction	8,413,894	350	230,803	(8,182,741)
Pupil transportation	267,307			(267,307)
Community service	24,760			(24,760)
Debt service - interest	5,519			(5,519)
Food service program	170,847	53,338	21,474	(96,035)
	<u>\$ 10,658,926</u>	<u>\$ 53,688</u>	<u>\$ 252,277</u>	<u>(10,352,961)</u>
Total Functions and Programs				
GENERAL REVENUES				
Real property taxes				8,545,400
Other tax items				182,992
Use of money and property				3,739
Miscellaneous				168,424
State sources				<u>392,389</u>
				<u>9,292,944</u>
Total General Revenues				
Change in Net Assets				(1,060,017)
Total Net Assets - Beginning of Year				<u>6,781,802</u>
Total Net Assets - End of Year				<u>\$ 5,721,785</u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Balance Sheet - Governmental Funds
June 30, 2012

	General	Special Aid	School Lunch	Capital Projects	Total Governmental Funds
ASSETS					
Cash	\$ 3,112,835	\$ 9,627	\$ 105,334	\$ 38,923	\$ 3,266,719
Receivables					
Accounts receivable	812		34		846
Due from other funds	457,923				457,923
Due from state and federal	23,565	171,673	1,255		196,493
Due from other governments	39,910				39,910
Inventory			2,516		2,516
Total Assets	<u>\$ 3,635,045</u>	<u>\$ 181,300</u>	<u>\$ 109,139</u>	<u>\$ 38,923</u>	<u>\$ 3,964,407</u>
LIABILITIES					
Payables					
Accounts payable	\$ 222,140	\$ 3,377		\$ 95,171	\$ 320,688
Accrued liabilities	220,589		1,928		222,517
Due to other funds		177,923	94,530	151,217	423,670
Due to other governments			197		197
Due to teachers' retirement system	445,175				445,175
Due to employees' retirement system	51,515				51,515
Compensated absences payable	21,136				21,136
Deferred credits					
Deferred revenues			1,758		1,758
Total Liabilities	<u>960,555</u>	<u>181,300</u>	<u>98,413</u>	<u>246,388</u>	<u>1,486,656</u>
FUND BALANCES (DEFICIT)					
Nonspendable:					
Inventory			2,515		2,515
Restricted:					
Unemployment insurance	149,388				149,388
Retirement contribution	249,801				249,801
Employee benefit accrued liability	464,484				464,484
Capital	529,466				529,466
Assigned:					
Appropriated fund balance	325,000				325,000
Unappropriated fund balance	44,624		8,211		52,835
Unassigned:					
Fund balance (deficit)	911,727			(207,465)	704,262
Total Fund Balances (Deficit)	<u>2,674,490</u>	<u>-</u>	<u>10,726</u>	<u>(207,465)</u>	<u>2,477,751</u>
Total Liabilities and Fund Balances	<u>\$ 3,635,045</u>	<u>\$ 181,300</u>	<u>\$ 109,139</u>	<u>\$ 38,923</u>	<u>\$ 3,964,407</u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Reconciliation of the Governmental Funds Balance Sheet
to the Statement of Net Assets
June 30, 2012

Total Governmental Fund Balances		\$ 2,477,751
Amounts reported for governmental activities in the Statement of Net Assets are different because:		
Cash held by third-party administrator is treated as a long-term asset and included in net assets.		323,403
The cost of building and acquiring capital assets (land, buildings, equipment) financed from the governmental funds are reported as expenditures in the year they are incurred, and the assets do not appear on the Balance Sheet. However, the Statement of Net Assets includes those capital assets among the assets of the District as a whole, and their original costs are expensed annually over their useful lives.		
Original cost of capital assets	10,517,320	
Accumulated depreciation	<u>(4,677,291)</u>	5,840,029
Long-term liabilities are not due and payable in the current period and, therefore, are not reported as liabilities in the governmental funds. Long-term liabilities at year end consist of:		
Compensated absences payable	(464,651)	
Workers' compensation liabilities	(49,521)	
Termination benefits	(309,469)	
Net other postemployment benefits obligation	<u>(2,095,757)</u>	<u>(2,919,398)</u>
Total Net Assets		<u>\$ 5,721,785</u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Statement of Revenues, Expenditures
and Changes in Fund Balances - Governmental Funds
For The Year Ended June 30, 2012

	General	Special Aid	School Lunch	Capital Projects	Total Governmental Funds
REVENUES					
Real property taxes	\$ 8,545,400	\$	\$	\$	\$ 8,545,400
Other tax items	182,992				182,992
Charges for services	350				350
Use of money and property	3,739				3,739
Miscellaneous	168,424				168,424
State sources	392,389	76,382	1,344		470,115
Federal sources		154,421	15,133		169,554
Surplus food			4,997		4,997
Sales - school lunch			53,338		53,338
Total Revenues	9,293,294	230,803	74,812	-	9,598,909
EXPENDITURES					
General support	1,507,099				1,507,099
Instruction	5,058,180	256,263			5,314,443
Pupil transportation	267,307				267,307
Community service	28,120				28,120
Employee benefits	2,223,293		7,608		2,230,901
Debt service					
Interest	5,519				5,519
Cost of sales			161,812		161,812
Capital outlay				555,796	555,796
Total Expenditures	9,089,518	256,263	169,420	555,796	10,070,997
Excess (Deficiency) of Revenues Over Expenditures	203,776	(25,460)	(94,608)	(555,796)	(472,088)
OTHER FINANCING SOURCES AND (USES)					
Operating transfers in	189,066	25,460	117,778		332,304
Operating transfers (out)	(143,238)			(189,066)	(332,304)
Total Other Financing Sources and (Uses)	45,828	25,460	117,778	(189,066)	-
Net Change in Fund Balances	249,604	-	23,170	(744,862)	(472,088)
Fund Balances (Deficit)					
- Beginning of Year	2,424,886		(12,444)	537,397	2,949,839
- End of Year	<u>\$ 2,674,490</u>	<u>\$ -</u>	<u>\$ 10,726</u>	<u>\$ (207,465)</u>	<u>\$ 2,477,751</u>

SHELTER ISLAND UNION FREE 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 \$ (472,088)

Amounts reported for governmental activities in the Statement of Activities are different because:

Long-Term Revenue and Expense Differences

Certain expenditures in the governmental funds requiring the use of current financial resources (amounts paid) are being held by a third-party administrator. This is the amount by which other assets - cash held by third-party administrator decreased in the period. \$ (1,964)

Certain expenditures in the governmental funds requiring the use of current financial resources (amounts paid) may exceed the amounts incurred during the year, resulting in a reduction of the long-term liability and an increase in net assets.

Decrease in compensated absences 91,938

In the Statement of Activities, certain operating expenses do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds.

Increase in workers' compensation liabilities	(6,478)	
Increase in termination benefits	(309,469)	
Increase in net other postemployment benefits obligation	<u>(887,165)</u>	
		(1,113,138)

Capital Related Differences

Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, for governmental activities those costs are capitalized and shown in the Statement of Net Assets and allocated over their useful lives as annual depreciation expenses in the Statement of Activities. This is the amount by which capital outlays exceeded depreciation in the period.

Capital outlays	736,702	
Depreciation expense	<u>(211,493)</u>	
		<u>525,209</u>

Change in Net Deficit of Governmental Activities \$ (1,060,017)

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Statement of Fiduciary Net Assets -
Fiduciary Funds
June 30, 2012

	Agency	Private Purpose Trust
ASSETS		
Cash	\$ 75,187	\$ 32,586
Due from other funds	5,266	
Total Assets	\$ 80,453	\$ 32,586
 LIABILITIES		
Extraclassroom activity balances	\$ 43,526	\$
Due to other funds	34,253	5,266
Other liabilities	2,674	
Total Liabilities	\$ 80,453	5,266
 NET ASSETS		
Reserved for scholarships		27,320
Total Liabilities and Net Assets		\$ 32,586

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Statement of Changes in Fiduciary Net Assets -
Fiduciary Funds
For The Year Ended June 30, 2012

	Private Purpose Trust
ADDITIONS	
Contributions	\$ 8,030
Investment earnings	
Interest	23
Total Additions	8,053
 DEDUCTIONS	
Scholarships and awards	26,489
Change in Net Assets	(18,436)
Net Assets - Beginning of Year	45,756
Net Assets - End of Year	\$ 27,320

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Shelter Island Union Free School District (District) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) for governmental units. The Governmental Accounting Standards Board (GASB) is the standard-setting body for establishing governmental accounting and financial reporting principles. Significant accounting principles and policies used by the District are as follows:

A. Reporting Entity

The District is governed by the laws of New York State. The District is an independent entity governed by an elected Board of Education consisting of seven members. The President of the Board serves as the chief fiscal officer and the Superintendent is the chief executive officer. The Board is responsible for, and controls all activities related to public school education within the District. Board members have authority to make decisions, power to appoint management, and primary accountability for all fiscal matters.

The financial reporting entity is based on criteria set forth by GASB Statement No. 14, *The Financial Reporting Entity* and No. 39, *Determining Whether Certain Organizations are Component Units*. The financial reporting entity consists of the primary government, organizations for which the primary government is financially accountable and other organizations for which the nature and significance of their relationship with the primary government are such that exclusion would cause the reporting entity's financial statements to be misleading or incomplete.

The accompanying financial statements present the activities of the District. The District is not a component unit of another reporting entity. The decision to include a potential component unit in the District's reporting entity is based on several criteria including legal standing, fiscal dependency, and financial accountability. Based on the application of these criteria, there are no other entities which would be included in the District's reporting entity as a component unit. However, the following is included in the District's financial statements:

Extraclassroom Activity Funds

The extraclassroom activity funds of the District represent funds of the students of the District. The Board of Education exercises general oversight of these funds. The extraclassroom activity funds are independent of the District with respect to its financial transactions and the designation of student management. The District reports these assets held by it as agent for the extraclassroom organizations in the Statement of Fiduciary Net Assets - Fiduciary Fund. Separate audited financial statements of the extraclassroom activity funds can be found at the District's Business Office.

B. Joint Venture

The District is a component district in the Board of Cooperative Educational Services of Eastern Suffolk (BOCES). A BOCES is a voluntary, cooperative association of school districts in a geographic area that share planning, services, and programs which provide educational and support activities. BOCES are organized under Section §1950 of the Education Law. A BOCES Board is considered a corporate body. Members of a BOCES Board are nominated and elected by their component member boards in accordance with provisions of Section §1950 of the Education Law. All BOCES property is held by the BOCES Board as a corporation under Section §1950(6). In addition, BOCES Boards also are considered municipal corporations to permit them to contract with other municipalities on a cooperative basis under Section

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

§119-n(a) of the General Municipal Law. A BOCES budget is comprised of separate budgets for administrative, program, and capital costs. Each component district's share of administrative and capital cost is determined by resident public school district enrollment as defined in Education Law, Section §1950(4)(b)(7). There is no authority or process by which a school district can terminate its status as a BOCES component. In addition, component school districts pay tuition or a service fee for programs in which its students participate.

C. Basis of Presentation

District-Wide Financial Statements

The Statement of Net Assets and the Statement of Activities present information about the overall governmental financial activities of the District, except for fiduciary activities. Eliminations have been made to minimize the double counting of interfund transactions. Governmental activities generally are financed through taxes, state aid, intergovernmental revenues, and other exchange and nonexchange transactions. Operating grants include operating-specific and discretionary (either operating or capital) grants.

The Statement of Net Assets presents the financial position of the District at fiscal year end. The Statement of Activities presents a comparison between program expenses and revenues for each function of the District's governmental activities. Direct expenses are those that are specifically associated with a program or function and, therefore, are clearly identifiable to a particular function. Employee benefits are allocated to functional areas in proportion to the payroll expended for those areas. Program revenues include (a) charges paid by the recipients of goods or services offered by the programs and (b) grants, contributions, and other revenues that are restricted to meeting the operational or capital requirements of a particular program. Revenues that are not classified as program revenues, including real property taxes and state aid, are presented as general revenues.

Fund Financial Statements

The fund financial statements provide information about the District's funds, including fiduciary funds. Separate statements for each fund category, governmental and fiduciary, are presented. The emphasis of fund financial statements is on major governmental funds as defined by GASB, each displayed in a separate column. The District's financial statements reflect the following major fund categories:

Governmental Funds:

General Fund - is the general operating fund and is used to account for all financial transactions except those required to be accounted for in another fund.

Special Aid Fund - is used to account for the proceeds of specific revenue sources such as federal and state grants that are legally restricted to expenditures for specified purposes. These legal restrictions may be imposed by either governments that provide the funds or outside parties.

School Lunch Fund - is used to account for the activities of the school lunch operations.

Capital Projects Fund - is used to account for the financial resources used for acquisition, construction, or major repair of capital facilities.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Fiduciary Funds – are used to account for activities in which the District acts as trustee or agent for resources that belong to others. These activities are not included in the district-wide financial statements, because their resources do not belong to the District, and are not available to be used. There are two classes of fiduciary funds:

Agency Funds - These funds are strictly custodial in nature and do not involve the measurement of results of operations. Assets are held by the District as agent for various student groups or extraclassroom activity funds and for payroll or employee withholding.

Private Purpose Trust Funds - These funds are used to account for trust arrangements in which principal and income benefits annual third party awards and scholarships for students. Established criteria govern the use of the funds and members of the District or representatives of the donors may serve on committees to determine who benefits.

D. Basis of Accounting and Measurement Focus

The district-wide and fiduciary fund financial statements are reported on the accrual basis of accounting using the economic resources measurement focus. Revenues are recorded when earned and expenses are recorded at the time liabilities are incurred, regardless of when the related cash transaction takes place. Nonexchange transactions, in which the District gives or receives value without directly receiving or giving equal value in exchange, include real property taxes, grants and donations. On an accrual basis, revenue from real property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants and donations is recognized in the fiscal year in which all eligibility requirements have been satisfied and the related expenditures are incurred.

The fund statements are reported on the modified accrual basis of accounting using the current financial resources measurement focus. Revenues are recognized when measurable and available. The District considers all revenues reported in the governmental funds to be available if the revenues are collected within 180 days after the end of the fiscal year, except for real property taxes, which are considered to be available if they are collected within 60 days after the end of the fiscal year. Expenditures are recorded when the related fund liability is incurred, except for principal and interest on general long-term debt, claims and judgments, compensated absences, and other postemployment benefits, which are recognized as expenditures to the extent they have matured. General capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

E. Real Property Taxes

Calendar

Real property taxes are levied annually by the Board no later than November 1st and become a lien on December 1st. Taxes are collected by the Town of Shelter Island and remitted to the District from December to June.

Enforcement

Uncollected real property taxes are subsequently enforced by Suffolk County in June.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

F. Restricted Resources

When an expense is incurred for purposes for which both restricted and unrestricted net assets are available, the District's policy concerning which to apply first varies with the intended use, and with associated legal requirements, many of which are described elsewhere in these Notes to Financial Statements.

G. Interfund Transactions

The operations of the District include transactions between funds. These transactions may be temporary in nature, such as with interfund borrowings. The District typically loans resources between funds for the purpose of providing cash flow. These interfund receivables and payables are expected to be repaid within one year. Permanent transfers of funds include transfers to provide financing or other services. This includes the transfer of unrestricted general fund revenues to finance various programs that the District must account for in other funds in accordance with budgetary authorizations.

In the district-wide statements, the amounts reported on the Statement of Net Assets for interfund receivables and payables represent amounts due between different fund types (governmental activities and fiduciary funds). Eliminations have been made for all interfund receivables and payables between the funds, with the exception of those due from or to the fiduciary funds.

The governmental funds report all interfund transactions as originally recorded. Interfund receivables and payables are netted on the accompanying governmental funds balance sheet when it is the District's practice to settle these amounts at a net balance based upon the right of legal offset.

A detailed disclosure by individual fund for interfund receivables, payables, transfers in and transfers out activity is provided subsequently in these Notes to Financial Statements.

H. Use of Estimates

The preparation of 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 reported amount of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported revenues and expenses during the reporting period. Accordingly, actual results could differ from those estimates. Estimates and assumptions are made in a variety of areas, including compensated absences, other postemployment benefits, workers' compensation liabilities, potential contingent liabilities and useful lives of long-lived assets.

I. Cash and Cash Equivalents/Investments

Cash and cash equivalents consist of cash on hand, bank deposits and investments with a maturity date of three months or less from date of acquisition.

Investments are reported at fair value, based on quoted market prices.

J. Receivables

Receivables are shown net of an allowance for uncollectibles, if any. However, no allowance for uncollectibles has been provided since it is believed that such allowance would not be material.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

K. Inventories

Inventories of food in the school lunch fund are recorded at cost on a first-in, first-out basis or in the case of surplus food donated by the U.S. Department of Agriculture, at the Government's assigned value, which approximates market. These inventories are accounted for on the consumption method. A reserve for inventory has been recognized to indicate that this does not constitute available spendable resources.

Purchases of inventorable items in other funds are recorded as expenditures at the time of purchase, and are considered immaterial in amount.

L. Other Assets

Other assets represent amounts on deposit that are being held by a third-party administrator for workers' compensation claims.

M. Capital Assets

Capital assets are reflected in the district-wide financial statements. Capital assets are reported at actual cost, when the information is available, or estimated historical cost based on professional third-party information. Donated assets are reported at estimated fair market value at the date of donation.

All capital assets, except land and construction in progress, are depreciated on a straight line basis over their estimated useful lives. Capitalization thresholds, the dollar value above which asset acquisitions are added to the capital asset accounts, and estimated useful lives of capital assets as reported in the district-wide statements are as follows:

	<u>Capitalization Threshold</u>	<u>Estimated Useful Life</u>
Buildings and improvements	\$ 10,000	50 years
Site improvements	10,000	50 years
Furniture and equipment	500	5-20 years

N. Deferred Revenues

Deferred revenues in the governmental funds arise when potential revenues do not meet both the measurable and available criteria for recognition in the current period. Deferred revenues also arise when resources are received by the District before it has a legal claim to them, as when grant monies are received prior to the incurrence of qualifying expenditures. In subsequent periods, when both recognition criteria are met, or when the District has legal claim to the resources, the liability for deferred revenues is removed and revenues are recognized.

O. Termination Benefits

Termination benefits consists of retirement incentives as specified in collective bargaining agreements. Upon retirement, resigned or death, employees may contractually receive a payment based on this retirement incentive. The liability is calculated in accordance with GASB Statement No. 47 *Accounting for Termination Benefits*. In the fund financial statements only, the amount of matured liabilities is accrued within the general fund based upon expendable and available resources.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

P. Vested Employee Benefits – Compensated Absences

Compensated absences consist of unpaid accumulated sick leave and vacation time.

Sick leave eligibility and accumulation is specified in collective bargaining agreements and in individual employment contracts. Upon retirement, resignation or death, employees may contractually receive a payment based on unused accumulated sick leave.

Vacation eligibility and accumulation is specified in collective bargaining agreements and in individual employment contracts. Some earned benefits may be forfeited if not taken within varying time periods.

Consistent with GASB Statement No. 16, *Accounting for Compensated Absences*, the liability has been calculated using the vesting method and an accrual for that liability is included in the district-wide financial statements. The compensated absences liability is calculated based on the pay rates in effect at year-end.

In the fund financial statements only the amount of matured liabilities is accrued within the general fund based upon expendable and available financial resources.

Q. Other Benefits

Eligible District employees participate in the New York State Teachers' Retirement System or the New York State Employees' Retirement System.

In addition to providing pension benefits, the District provides postemployment health insurance coverage and survivor benefits for retired employees and their survivors. Collective bargaining agreements determine if District employees are eligible for these benefits if they reach normal retirement age while working for the District. Health care benefits are provided through plans whose premiums are based on the benefits paid during the year. The cost of providing post-retirement benefits is shared between the District and the retired employee. The District accounts for these postemployment benefits in accordance with GASB Statement No. 45 (GASB 45) *Accounting and Financial Reporting by Employers for Postemployment Benefits Other Than Pensions*. The District recognizes the cost of providing health insurance by recording its share of insurance premiums as an expenditure in the general fund, in the year paid. In the District-wide statements, postemployment costs are measured and disclosed using the accrual basis of accounting.

R. Short-Term Debt

The District may issue revenue anticipation notes (RAN) and tax anticipation notes (TAN), in anticipation of the receipt of revenues. These notes are recorded as a liability of the fund that will actually receive the proceeds from the issuance of the notes. The RANs and TANs represent a liability that will be extinguished by the use of expendable, available resources of the fund.

The District may issue bond anticipation notes (BAN), in anticipation of proceeds from the subsequent sale of bonds. These notes are recorded as current liabilities of the funds that will actually receive the proceeds from the issuance of bonds. State law requires that BANs issued for capital purposes be converted to long-term financing within five years after the original issue date.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

S. Accrued Liabilities and Long-Term Obligations

Payables, accrued liabilities and long-term obligations are reported in the district-wide financial statements. In the governmental funds, payables and accrued liabilities are paid in a timely manner and in full from current financial resources. Claims and judgments, and compensated absences that will be paid from governmental funds, are reported as a liability in the fund financial statements only to the extent that they have matured. Bonds and other long-term obligations that will be paid from governmental funds are recognized as a liability in the fund financial statements when due.

Long-term obligations represent the District's future obligations or future economic outflows. The liabilities are reported as due and payable within one year or due and payable after one year in the Statement of Net Assets.

T. Equity Classifications

District-Wide Statements

In the district-wide statements there are three classes of net assets:

Investment in capital assets, net of related debt – consists of net capital assets (cost less accumulated depreciation) reduced by outstanding balances of related debt obligations from the acquisitions, construction and improvements of those assets.

Restricted net assets – reports net assets when constraints placed on the assets 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.

Unrestricted net assets – reports all other net assets that do not meet the definition of the above two classifications and are deemed to be available for general use by the District.

Fund Statements

The fund statements report fund balance classifications according to the relative strength of spending constraints placed on the purpose for which resources can be used, as follows:

Nonspendable – Consists of amounts that are inherently nonspendable in the current period either because of their form or because they must be maintained intact, including prepaid items, inventories, long-term portions of loans, receivables, financial assets held for resale and principal of an endowment. The District's nonspendable fund balance consists of inventory that is not in spendable form.

Restricted – Consists of amounts that are subject to externally enforceable legal purpose restrictions imposed by creditors, grantors, contributors, or laws and regulations of other governments; or through constitutional provisions or enabling legislation. Restricted fund balances, generally referred to as reserves in accordance with New York State law, are created to satisfy legal restrictions, plan for future expenditures or relate to resources not available for general use or appropriation. These reserve funds are established through Board action or voter approval and a separate identity must be maintained for each reserve. Earnings on the invested resources become part of the respective reserve funds; however, separate bank accounts are not necessary for each reserve fund. Fund balance reserves currently in use by the District include the following:

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Unemployment Insurance Reserve

Unemployment Insurance Reserve (GML §6-m) is used to pay the cost of reimbursement to the State Unemployment Insurance Fund for payments made to claimants where the employer has elected to use the benefit reimbursement method. The reserve may be established by Board action and is funded by budgetary appropriations and such other funds as may be legally appropriated. Within sixty days after the end of any fiscal year, excess amounts may either be transferred to another reserve or the excess applied to the appropriations of the next succeeding fiscal year's budget. If the District elects to convert to tax (contribution) basis, excess resources in the fund over the sum sufficient to pay pending claims may be transferred to any other reserve fund. This reserve is accounted for in the general fund.

Retirement Contribution Reserve

Retirement Contribution Reserve (GML §6-r) is used for the purpose of financing retirement contributions. The reserve must be accounted for separate and apart from all other funds and a detailed report of the operation and condition of the fund must be provided to the Board. The reserve is accounted for in the general fund.

Employee Benefit Accrued Liability Reserve

Reserve for Employee Benefit Accrued Liability (GML §6-p) is used to reserve funds for the payment of accrued employee benefit due an employee upon termination of the employee's service. This reserve may be established by a majority vote of the Board, and is funded by budgetary appropriations and such other reserves and funds that may be legally appropriated. The reserve is accounted for in the general fund.

Capital Reserve

Capital Reserve (Education Law §3651) is used to pay the cost of any object or purpose for which bonds may be issued. The creation of a capital reserve fund requires authorization by a majority of the voters establishing the purpose of the reserve; the ultimate amount, its probable term and the source of the funds. Expenditure may be made from the reserve only for a specific purpose further authorized by the voters. The form for the required legal notice for the vote on establishing and funding the reserve and the form of the proposition to be placed on the ballot are set forth in §3651 of the Education Law. The reserve is accounted for in the general fund.

Assigned – Consists of amounts that are subject to a purpose constraint that represents an intended use established by the District's Board of Education. The purpose of the assignment must be narrower than the purpose of the general fund, and in funds other than the general fund, assigned fund balance represents the residual amount of fund balance. Assigned fund balance includes an amount appropriated to partially fund the subsequent year's budget. Assigned fund balance also includes encumbrances not classified as restricted at the end of the fiscal year.

Unassigned – represents the residual classification for the District's general fund and could report a surplus or deficit. NYS Real Property Tax Law §1318, restricts the unassigned fund balance of the general fund to an amount not greater than 4% of the subsequent year's budget. In funds other than the general fund, the unassigned classification should be used only to report a deficit fund balance resulting from overspending for specific purposes for which amounts had been restricted or assigned.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Fund Balance Classification

Any portion of fund balance may be applied or transferred for a specific purpose by law, voter approval if required by law or by formal action of the Board of Education if voter approval is not required. Amendments or modification to the applied or transferred fund balance must also be approved by formal action of the Board of Education.

The Board of Education shall delegate the authority to assign fund balance, for encumbrance purposes, to the person(s) to whom it has delegated the authority to sign purchase orders.

In circumstances where an expenditure is incurred for a purpose for which amounts are available in multiple fund balance classifications (that is restricted, assigned or unassigned) the expenditure is to be spent first from the restricted fund balance to the extent appropriated by either budget vote or board approved budget revision and then from the assigned fund balance to the extent that there is an assignment and then from the unassigned fund balance.

2. EXPLANATION OF CERTAIN DIFFERENCES BETWEEN THE GOVERNMENTAL FUND STATEMENTS AND THE DISTRICT-WIDE STATEMENTS

Due to the differences in the measurement focus and basis of accounting used in the governmental fund statements and the district-wide statements, certain financial transactions are treated differently. The basic financial statements contain a full reconciliation of these items. The differences result primarily from the economic resource measurement focus of the Statement of Activities, compared with the current financial resource measurement focus of the governmental funds.

A. Total Fund Balances of Governmental Funds vs. Net Assets of Governmental Activities

Total fund balances of the District's governmental funds differ from "net assets" of governmental activities reported in the Statement of Net Assets. This difference primarily results from the additional long-term economic focus of the Statement of Net Assets versus the solely current financial resources focus of the governmental fund Balance Sheet.

B. Statement of Revenues, Expenditures and Changes in Fund Balance vs. Statement of Activities

Differences between the Statement of Revenues, Expenditures and Changes in Fund Balance and the Statement of Activities fall into one of three broad categories.

Long-Term Revenue and Expense Differences

Long-term revenue differences arise because governmental funds report revenues only when they are considered "available", whereas the Statement of Activities reports revenues when earned. Differences in long-term expenses arise because governmental funds report on a modified accrual basis, whereas the accrual basis of accounting is used on the Statement of Activities.

Capital Related Differences

Capital related differences include the difference between proceeds from the sale of capital assets reported on fund statements and the gain or loss on the sale of assets as reported on the Statement of Activities, and the difference between recording an expenditure for the purchase of capital items in the fund statements and depreciation expense on those items as recorded in the Statement of Activities.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Long-Term Debt Transaction Differences

Long-term debt transaction differences occur because the issuance of long-term debt provides current financial resources to governmental funds, but is recorded as a liability in the Statement of Net Assets. In addition, both interest and principal are recorded as expenditures in the fund statements when due and payable, whereas interest expense is recorded in the Statement of Activities as it accrues, and principal payments are recorded as a reduction of liabilities in the Statement of Net Assets.

3. STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY

A. Budgets

The District administration prepares a proposed budget for approval by the Board of Education for the general fund, the only fund with a legally adopted budget.

The voters of the District approved the proposed appropriation budget for the general fund.

Appropriations are adopted at the program line item level.

Appropriations established by the adoption of the budget constitute a limitation on expenditures (and encumbrances) that may be incurred. Appropriations lapse at the end of the fiscal year unless expended or encumbered. Encumbrances will lapse if not expended in the subsequent year. Appropriations authorized for the current year are increased by the planned use of specific reserves, and budget amendments approved by the Board of Education as a result of selected new revenue sources not included in the original budget (when permitted by law). These supplemental appropriations may occur subject to legal restrictions, if the Board approves them because of a need that exists which was not determined at the time the budget was adopted. The following supplemental appropriations occurred during the year:

Contingent expenditures funded by:

Unassigned fund balance for retirement incentives and transfer to school lunch fund	\$ 154,767
Restricted fund balance - employee benefit accrued liability - for retirement payouts	163,660
Donation - field trips and various programs	<u>22,867</u>
	<u>\$ 341,294</u>

Budgets are adopted annually on a basis consistent with GAAP. Appropriations authorized for the year are increased by the amount of encumbrances carried forward from the prior year.

Budgets are established and used for individual capital project funds expenditures as approved by a special referendum of the District's voters. The maximum project amount authorized is based primarily upon the cost of the project, plus any requirements for external borrowings, not annual appropriations. These budgets do not lapse and are carried over to subsequent fiscal years until the completion of the projects.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

B. Encumbrances

Encumbrance accounting is used for budget control and monitoring purposes and is reported as a part of the governmental funds. Under this method, purchase orders, contracts and other commitments for the expenditure of monies are recorded to reserve applicable appropriations. Outstanding encumbrances as of year-end are presented as part of other assigned, unappropriated fund balance, unless classified as restricted or committed, and do not represent expenditures or liabilities. These commitments will be honored in the subsequent period. Related expenditures are recognized at that time, as the liability is incurred or the commitment is paid.

C. Unassigned Fund Balance

The District's unassigned fund balance was in excess of the New York State Real Property Tax Law §1318 limit, which restricts it to an amount not greater than 4% of the District's budget for the upcoming school year. The District is in the process of formulating a plan to reduce the unassigned fund balance to be within the permissible limit. This plan will address funding its reserves to a fiscally prudent level and addressing the capital needs of the District.

D. Over expenditure of Certain Appropriations

Certain general fund appropriations were over expended. These were in the following appropriation categories of the budget: general support, instruction, community services, and operating transfers out. The general fund budget in total was not over expended.

E. Capital Projects Fund

The capital projects fund had a deficit fund balance of \$207,465. This will be funded when the District obtains permanent financing for its current construction project.

4. DEPOSITS WITH FINANCIAL INSTITUTIONS AND INVESTMENTS

The District's investment policies are governed by state statutes and District policy. Resources must be deposited in Federal Deposit Insurance Corporation (FDIC) insured commercial banks or trust companies located within the state. Permissible investments include obligations of the U.S. Treasury and U.S. Agencies, repurchase agreements and obligations of New York State or its localities. Collateral is required for demand and time deposits and certificates of deposit not covered by FDIC insurance. Obligations that may be pledged as collateral are obligations of the United States and its Agencies and obligations of New York State and its municipalities. Investments are stated at fair value.

Custodial credit risk is the risk that in the event of a bank failure, the District's deposits may not be returned to it. GASB directs that deposits be disclosed as exposed to custodial credit risk if they are not covered by depository insurance and the deposits are as follows:

- A. Uncollateralized,
- B. Collateralized by securities held by the pledging financial institution, or
- C. Collateralized by securities held by the pledging financial institution's trust department or agent but not in the District's name.

None of the District's aggregate bank balances, not covered by depository insurance, were exposed to custodial credit risk as described above at year end.

The District did not have any investments at year-end or during the year. Consequently, the District was not exposed to any material interest rate risk or foreign currency risk.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

Investment pool:

The District participates in a multi-municipal cooperative investment pool agreement pursuant to New York State General Municipal Law Article 5-G, §119-O, whereby it holds a portion of the investments in cooperation with other participants. The investments are highly liquid and are considered to be cash equivalents.

Total investments of the cooperative as of year-end are \$218,514,350, which consisted of \$123,620,189 in repurchase agreements, \$4,500,216 in U.S. Government guaranteed securities, \$40,393,945 in U.S. Treasury Securities and \$50,000,000 in collateralized bank deposits.

The amount of \$2,865 is included as cash in the general fund.

The above amounts represent the cost of the investment pool shares, and are considered to approximate market value. The investment pool is categorically exempt from the New York State collateral requirements. Additional information concerning the cooperative is presented in the annual report of New York Class – Board of Cooperative Educational Services of Putnam / Northern Westchester, 200 BOCES Drive, Yorktown Heights, New York 10596-4399.

5. PARTICIPATION IN BOCES

During the year ended June 30, 2012, the District was billed \$266,925 for BOCES administrative and program costs. The District's share of BOCES aid amounted to \$62,557. Financial statements for the BOCES are available from the BOCES administrative offices at 201 Sunrise Highway, Patchogue, New York 11772.

6. DUE FROM STATE AND FEDERAL

Due from other governments at June 30, 2012 consisted of:

General Fund	
New York State Aid - excess cost aid	\$ 23,565
Special Aid Fund	
Federal and state grants	171,673
School Lunch Fund	
Federal and state food service program reimbursements	<u>1,255</u>
	<u>\$ 196,493</u>

7. DUE FROM OTHER GOVERNMENTS

Due from other governments at June 30, 2012 consisted of:

General Fund	
BOCES aid	\$ 28,021
Medicare Part D	10,987
Town of Shelter Island - interest on property taxes	<u>902</u>
	<u>\$ 39,910</u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

8. CAPITAL ASSETS

Capital asset balances and activity for the year ended June 30, 2012 were as follows:

	Balance June 30, 2011	Additions	Reductions	Balance June 30, 2012
Governmental activities				
Capital assets not being depreciated				
Land	\$ 25,200	\$	\$	\$ 25,200
Construction in progress	900,485	580,695	(1,273,715)	207,465
Total capital assets not being depreciated	<u>925,685</u>	<u>580,695</u>	<u>(1,273,715)</u>	<u>232,665</u>
Capital assets being depreciated				
Buildings and improvements	7,786,770	1,283,366		9,070,136
Site improvements	269,420	67,764		337,184
Furniture and equipment	1,029,960	78,592	(231,217)	877,335
Total capital assets being depreciated	<u>9,086,150</u>	<u>1,429,722</u>	<u>(231,217)</u>	<u>10,284,655</u>
Less accumulated depreciation for:				
Buildings and improvements	3,915,974	160,989		4,076,963
Site improvements	84,119	13,120		97,239
Furniture and equipment	696,922	37,384	(231,217)	503,089
Total accumulated depreciation	<u>4,697,015</u>	<u>211,493</u>	<u>(231,217)</u>	<u>4,677,291</u>
Total capital assets, being depreciated, net	<u>4,389,135</u>	<u>1,218,229</u>	<u>-</u>	<u>5,607,364</u>
Capital assets, net	<u>\$ 5,314,820</u>	<u>\$ 1,798,924</u>	<u>\$ (1,273,715)</u>	<u>\$ 5,840,029</u>

Depreciation expense was charged to governmental functions as follows:

General support	\$ 5,245
Instruction	204,821
Food service program	<u>1,427</u>
Total depreciation expense	<u>\$ 211,493</u>

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

9. INTERFUND TRANSACTIONS

Interfund balances and activities at June 30, 2012, are as follows:

	Interfund			
	Receivable	Payable	Transfers In	Transfers Out
General Fund	\$ 457,923	\$	\$ 189,066	\$ 143,238
Special Aid Fund		177,923	25,460	
School Lunch Fund		94,530	117,778	
Capital Projects Fund		151,217		189,066
Fiduciary Funds	5,266	39,519		
Total	\$ 463,189	\$ 463,189	\$ 332,304	\$ 332,304

The District typically transfers from the general fund to the special aid fund in accordance with the general fund budget. The transfer is to provide the District's 20% share of the summer program for students with disabilities. The District transferred from the general fund to the school lunch fund to subsidize the lunch program. The District transferred \$189,066 from the capital projects fund to the general fund, which represents unspent capital reserve funds from the roof project. The unspent funds were returned to the reserve.

10. SHORT-TERM DEBT

Transactions in short-term debt for the year are summarized below:

	Maturity	Interest Rate	Balance June 30, 2011	Issued	Redeemed	Balance June 30, 2012
TAN	6/28/2012	0.57%	<u> </u>	\$ 1,400,000	\$ (1,400,000)	<u> </u>

Interest on short-term debt for the year was \$5,519.

11. LONG-TERM LIABILITIES

Long-term liability balances and activity, excluding other postemployment benefits, for the year are summarized below:

	Balance June 30, 2011	Additions	Reductions	Balance June 30, 2012	Amounts Due Within One Year
Other long-term liabilities					
Compensated absences	\$ 556,589	\$ 71,722	\$ (163,660)	\$ 464,651	\$ 148,155
Workers' compensation	43,043	17,114	(10,636)	49,521	
Termination benefits		309,469		309,469	200,250
	<u>\$ 599,632</u>	<u>\$ 398,305</u>	<u>\$ (174,296)</u>	<u>\$ 823,641</u>	<u>\$ 348,405</u>

The general fund has typically been used to liquidate other long-term liabilities.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

12. PENSION PLANS

A. General Information

The District participates in the New York State Teachers' Retirement System (NYSTRS) and the New York State and Local Employees' Retirement System (NYSERS). These are cost-sharing multiple employer, public employee retirement systems. The Systems offer a wide range of plans and benefits which are related to years of service and final average salary, vesting of retirement benefits, death, and disability.

B. Provisions and Administration

Teachers' Retirement System

The NYSTRS is administered by the New York State Teachers' Retirement Board. The System provides benefits to plan members and beneficiaries as authorized by the Education Law and the Retirement and Social Security Law of the state of New York. The NYSTRS issues a publicly available financial report that contains financial statements and required supplementary information for the System. The report may be obtained by writing to the New York State Teachers' Retirement System, 10 Corporate Woods Drive, Albany, NY 12211-2395.

Employees' Retirement System

The NYSERS provides retirement benefits as well as death and disability benefits. Obligations of employers and employees to contribute and benefits to employees are governed by the New York State Retirement and Social Security Law. The System issues a publicly available financial report that includes financial statements and required supplementary information. That report may be obtained by writing to the New York State and Local Employees' Retirement System, Office of the State Comptroller, 110 State Street, Albany, NY 12244.

C. Funding Policies

The Systems are noncontributory for the employee except for those who joined the Systems after July 27, 1976 with less than ten years of credited service who contribute 3% of their salary, or joined the Systems on or after January 1, 2010 and before April 1, 2012, who contribute 3% of their salary to NYSERS or 3.5% of their salary to NYSTRS throughout active membership. For employees hired on or after April 1, 2012, employee contribution rates are dependent upon salaries and range from 3% to 6% of salary throughout active membership. For the NYSERS, the Comptroller shall certify annually the rates expressed as proportions of members' payroll annually, which shall be used in computing the contributions required to be made by employers to the pension accumulation fund. Pursuant to Article 11 of the Education Law, rates are established annually for NYSTRS by the New York State Teachers' Retirement Board.

The District is required to contribute at an actuarially determined rate. The District contributions made to the Systems were equal to 100% of the contributions required for each year. The required contributions for the current year and two preceding years were:

Year	NYSTRS	NYSERS
2012	\$ 424,613	\$ 150,033
2011	453,158	119,678
2010	248,991	84,950

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

13. POSTEMPLOYMENT BENEFITS

A. Plan Description

The District provides medical, Medicare part B reimbursement, and dental and vision coverage (the healthcare plan) to retired employees in accordance with employment contracts. The plan is a single-employer defined benefit healthcare plan primarily administered through United Healthcare.

B. Funding Policy

The District assumes up to 50% of the premiums and recognizes the cost of the healthcare plan annually as expenditures in the general fund of the fund financial statements as payments are made based on the terms of employment contracts. For the year ended June 30, 2012, the District recognized a general fund expenditure of \$545,033 for insurance premiums for 32 currently enrolled retirees. Currently, there is no provision in the law to permit the District to fund other postemployment benefits by any means other than the "pay as you go" method.

C. Annual OPEB Cost and Net OPEB Obligation

The District's annual other postemployment benefit (OPEB) cost (expense) is calculated based on the annual required contribution of the employer (ARC), an amount actuarially determined in accordance with parameters of GASB Statement No. 45. The ARC represents a level of funding that, if paid on an ongoing basis, is projected to cover normal costs each year and amortize any unfunded actuarial liabilities over a period not to exceed 30 years. The following table shows the components of the District's annual OPEB cost for the year, the amount actually contributed to the plan, and changes in the District's net OPEB obligation.

Annual required contribution (ARC)	\$ 1,457,386
Interest on net OPEB obligation	48,344
Adjustment to ARC	<u>(73,532)</u>
Annual OPEB cost (expense)	1,432,198
Contributions made	<u>(545,033)</u>
Increase in net OPEB obligation	887,165
Net OPEB obligation - beginning of year	<u>1,208,592</u>
Net OPEB obligation - end of year	<u>\$ 2,095,757</u>

The District's annual OPEB cost, the percentage of annual OPEB cost contributed to the plan, and the net OPEB obligation for the year ended June 30, 2012 and the two preceding years are as follows:

<u>Fiscal</u> <u>Year Ended</u>	<u>Annual</u> <u>OPEB Cost</u>	<u>Percentage of</u> <u>Annual OPEB</u> <u>Cost Contributed</u>	<u>Net OPEB</u> <u>Obligation</u>
June 30, 2012	\$ 1,432,198	38.1%	\$ 2,095,757
June 30, 2011	1,451,695	37.0%	1,208,592
June 30, 2010	630,319	54.0%	291,681

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

D. Funded Status and Funding Progress

As of December 31, 2010, the most recent actuarial valuation date, the plan was 0% funded. The actuarial accrued liability for benefits was \$16,319,228 and the actuarial value of assets was \$-0-, resulting in an unfunded actuarial accrued liability (UAAL) of \$16,319,228. The covered payroll (annual payroll of active employees covered by the plan) was \$4,742,584, and the ratio of the UAAL to the covered payroll was 344%.

Actuarial valuations of an ongoing plan involved estimates of the value of reported amounts and assumptions about the probability of occurrence of events far into the future. Examples include assumptions about future employment, mortality, and the healthcare cost trend. Amounts determined regarding the funded status of the plan and the annual required contributions of the employer are subject to continual revision as actual results are compared with past expectations and new estimates are made about the future. The required schedule of funding progress following the notes to the financial statements presents multi-year trend information about whether the actuarial value of plan assets is increasing or decreasing over time relative to the actuarial accrued liability for benefits.

E. Actuarial Methods and Assumptions

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

In the December 31, 2010, actuarial valuation, the projected unit credit actuarial cost method was used. The actuarial assumptions included a 4% discount rate and an annual healthcare cost trend rate of 8% initially, reduced by decrements to an ultimate rate of 5% after 6 years and a 4% inflation rate. The UAAL is being amortized as a level percentage of projected payrolls on an open basis. The remaining amortization period at June 30, 2012, was 25.5 years.

14. RISK MANAGEMENT

A. General Information

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; injuries to employees; errors and omissions; and natural disasters. These risks are covered by a combination of self-insurance reserves, public entity risk pools, and commercial insurance purchased from independent third parties. Settled claims from these risks have not exceeded available reserves and commercial insurance coverage for the past three years.

B. Public Entity Risk Pool – Risk Retained

The District participates in a risk pool, the East End Workers' Compensation Consortium (EEWCC), to insure workers' compensation claims. This public entity risk pool was created under Article 5 of Workers' Compensation Law, to evaluate, process, administer, and pay workers' compensation claims. The District retains the risk of loss.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

The District pays an annual assessment to the pool for its workers' compensation claims coverage and related expenses. The EEWCC has obtained an excess compensation insurance policy to buffer the effect that a single large claim may have on the District's loss experience. The EEWCC established a non-discounted liability for both reported and unreported insured events, which includes estimates of both future payments or losses and related claim adjustment expenses. Claim liabilities are calculated considering the effects of inflation, recent claim settlement trends including frequency and amount of payouts, and other economic and social factors. However, because actual claim costs depend on complex factors, the process used in computing claims liabilities does not necessarily result in an exact amount. Such claims are based on the ultimate cost of claims (including future claim adjustment expenses) that have been reported but not settled, and claims that have been incurred but not reported.

The District's liability for incurred but unpaid claims and incurred but not reported claims at June 30, 2012, as processed by the EEWCC, is \$49,521. Claims activity is summarized as follows:

	2011	2012
Claims at beginning of year	\$ 36,816	\$ 43,043
Incurred claims and claim adjustment expenses	11,026	17,114
Claims payments and expenses	(4,799)	(10,636)
Claims liabilities at end of year	\$ 43,043	\$ 49,521

The EEWCC is holding \$323,403 of cash on account for the District to satisfy these liabilities at June 30, 2012.

The EEWCC has issued financial statements for the year ended June 30, 2012. Copies of these statements can be obtained from the District's administrative office.

C. Public Entity Risk Pool – Risk Sharing

The District participates in a public entity risk sharing pool that provides a health benefit program for its employees through the East End Health Plan, a consortium of school districts from the east end of Long Island. The benefit program's administrator is responsible for the approval, processing and payment of claims. This is billed to the District at an established rate based on the number of participants. The District is responsible for contributions to cover their share of the benefits and administrative costs. The trust for the plan reports on a calendar year end. In the event the plan experiences a shortfall, a special assessment against participating districts may be imposed. The District is not aware of any additional assessments related to claims incurred through June 30, 2012.

15. ASSIGNED FUND BALANCE

A. Assigned: Appropriated

The amount of \$325,000 has been appropriated to reduce taxes for the year ending June 30, 2013.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
NOTES TO FINANCIAL STATEMENTS
(Continued)

16. COMMITMENTS AND CONTINGENCIES

A. Encumbrances

All encumbrances are classified as either restricted or assigned fund balance. At June 30, 2012, the District encumbered the following amounts:

Restricted Fund Balance	
Capital Projects Fund	
Capital projects	<u>\$ 1,910,198</u>
Assigned: Unappropriated Fund Balance:	
General Fund	
General Support	41,006
Instruction	<u>3,618</u>
	<u>44,624</u>
School Lunch Fund	
Food service program	<u>8,211</u>
	<u>\$ 1,963,033</u>

B. Grants

The District has received grants, which are subject to audit by agencies of the state and federal governments. Such audits may result in disallowances and a request for a return of funds. Based on prior audits, the District's administration believes disallowances, if any, will be immaterial.

C. Litigation

The District is involved in lawsuits arising from the normal conduct of its affairs. Management believes that the outcome of any matters will not have a material effect on these financial statements.

17. SUBSEQUENT EVENTS

On July 26, 2012, the District issued serial bonds in the amount of \$2,837,000, which are due June 15, 2029 and bear interest at rates ranging from 2.750% to 3.375%. The bonds were issued to finance various building improvements, installation of a new generator, and related lighting system improvements.

On October 30, 2012, the District issued tax anticipation notes in the amount of \$1,500,000, which are due June 27, 2013 and bear interest at the rate of 0.47%.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Schedule of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund
For The Year Ended June 30, 2012

	Original Budget	Final Budget	Actual	Final Budget Variance with Actual
REVENUES				
Local Sources				
Real property taxes	\$ 8,545,134	\$ 8,545,134	\$ 8,545,400	\$ 266
Other tax items	182,090	182,090	182,992	902
Charges for services			350	350
Use of money and property	10,000	10,000	3,739	(6,261)
Miscellaneous	20,000	42,867	168,424	125,557
Total Local Sources	8,757,224	8,780,091	8,900,905	120,814
State Sources	438,390	438,390	392,389	(46,001)
Total Revenues	9,195,614	9,218,481	9,293,294	74,813
OTHER SOURCES				
Operating transfers in			189,066	189,066
Total Revenues and Other Sources	9,195,614	9,218,481	9,482,360	\$ 263,879

Note to Required Supplementary Information

Budget Basis of Accounting

Budgets are adopted on the modified accrual basis of accounting consistent with accounting principles generally accepted in the United States of America.

See Paragraph on Supplementary Information Included in Auditor's Report

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Schedule of Revenues, Expenditures and Changes in Fund Balance
Budget and Actual - General Fund (Continued)
For The Year Ended June 30, 2012

	Original Budget	Final Budget	Actual	Year End Encumbrances	Final Budget Variance with Actual & Encumbrances
EXPENDITURES					
General Support					
Board of education	\$ 34,640	\$ 38,353	\$ 23,200	\$	\$ 15,153
Central administration	195,319	196,062	202,809		(6,747)
Finance	313,046	303,221	277,284	18,230	7,707
Staff	55,335	56,162	52,953	16,336	(13,127)
Central services	971,909	983,495	810,810	6,440	166,245
Special items	166,495	147,218	140,043		7,175
Total General Support	1,736,744	1,724,511	1,507,099	41,006	176,406
Instruction					
Instruction, administration & improvement	103,643	106,638	138,057		(31,419)
Teaching - regular school Programs for children	2,907,295	3,128,437	3,084,191		44,246
with handicapping conditions	946,897	1,094,817	1,094,708		109
Occupational education	95,440	58,134	35,619		22,515
Teaching - special school	22,927	22,981	6,746		16,235
Instructional media	142,404	189,431	173,488	3,618	12,325
Pupil services	560,326	587,906	525,371		62,535
Total Instruction	4,778,932	5,188,344	5,058,180	3,618	126,546
Pupil Transportation	526,790	441,184	267,307		173,877
Community Services	15,200	15,200	28,120		(12,920)
Employee Benefits	2,474,947	2,492,224	2,223,293		268,931
Debt Service					
Interest	34,000	34,000	5,519		28,481
Total Debt Service	34,000	34,000	5,519	-	28,481
Total Expenditures	9,566,613	9,895,463	9,089,518	44,624	761,321
OTHER USES					
Operating transfers out	118,565	131,009	143,238		(12,229)
Total Expenditures and Other Uses	9,685,178	10,026,472	9,232,756	\$ 44,624	\$ 749,092
Net Change in Fund Balances	(489,564)	(807,991)	249,604		
Fund Balances - Beginning of Year	489,564	807,991	2,424,886		
Fund Balances - End of Year	\$ -	\$ -	\$ 2,674,490		

Note to Required Supplementary Information

Budget Basis of Accounting

Budgets are adopted on the modified accrual basis of accounting consistent with accounting principles generally accepted in the United States of America.

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Schedule of Funding Progress - Other Postemployment Benefits
 June 30, 2012

Valuation Date	Actuarial Value of Assets	Accrued Liability	Unfunded Actuarial Accrued Liability (UAAL)	Funded Ratio	Covered Payroll	UAAL as a Percentage of Covered Payroll
December 31, 2008	\$ -	\$ 7,631,003	\$ 7,631,003	0%	\$ 5,082,679	150.1%
December 31, 2010	-	16,319,228	16,319,228	0%	4,742,584	344.1%

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Schedules of Change from Adopted Budget to Final Budget
and Use of Assigned: Appropriated and Unassigned Fund Balance - General Fund
For The Year Ended June 30, 2012

CHANGE FROM ADOPTED BUDGET TO FINAL BUDGET

Adopted Budget	\$	9,640,614
Additions:		
Prior year's encumbrances		44,564
Original Budget		9,685,178
Budget revision		341,294
Final Budget	\$	10,026,472

Next year's budget is a voter-approved budget of	\$	9,739,303
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USE OF ASSIGNED: APPROPRIATED AND UNASSIGNED FUND BALANCE

Assigned: Appropriated and Unassigned Fund Balance - As of the beginning of the year	\$	1,264,842
Less:		
Appropriated fund balance used for the levy of taxes - Adopted budget		325,000
Unassigned Fund Balance - As of the beginning of the year	\$	939,842

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
 Schedule of Project Expenditures -
 Capital Projects Fund
 For The Year Ended June 30, 2012

PROJECT TITLE	Budget		Expenditures		Unexpended Balance	Methods of Financing			Fund Balance June 30, 2012	
	June 30, 2011	June 30, 2012	Prior Years	Current Year		Total	Proceeds of Obligations	State Aid		Local Sources
2008/09 Project Fit	\$ 515,000	\$ 515,000	\$ 166,669	\$ 348,331	\$ -	\$ -	\$ -	\$ 515,000	\$ 515,000	\$ -
2008/09 Roof Project	925,000	925,000	735,934		189,066			925,000	925,000	189,066
2012 District Renovations		2,237,000		207,465	2,029,535	2,237,000			2,237,000	2,029,535
2012 Generator		600,000			600,000	600,000			600,000	600,000
Totals	\$ 1,440,000	\$ 4,277,000	\$ 902,603	\$ 555,796	\$ 2,818,601	\$ 2,837,000	\$ -	\$ 1,440,000	\$ 4,277,000	2,818,601
									Less: Transfer to general fund	(189,066)
									Less: Unissued debt	(2,837,000)
										\$ (207,465)

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Schedule of Certain Revenues and Expenditures
Compared to ST-3 Data
For The Year Ended June 30, 2012

	<u>Code</u>	<u>ST-3 Amount</u>	<u>Audited Amount</u>
REVENUES			
Real Property Taxes	A -1001	\$ 8,545,400	\$ 8,545,400
Non-Property Taxes	AT-1199	-	-
State Aid	AT-3999	392,389	392,389
Federal Aid - Medicaid Reimbursements	AT-4999	-	-
Total Revenues	AT-5999	9,482,360	9,482,360
EXPENDITURES			
General Support	AT-1999	1,507,099	1,507,099
Pupil Transportation	AT-5599	267,307	267,307
Debt Service - Principal	AT-9798.6	-	-
Debt Service - Interest	AT-9798.7	5,519	5,519
Total Expenditures	AT-9999	9,232,756	9,232,756

SHELTER ISLAND UNION FREE SCHOOL DISTRICT
Investment in Capital Assets, Net of Related Debt
For The Year Ended June 30, 2012

Capital assets, net	<u>\$ 5,840,029</u>
Investment in capital assets, net of related debt	<u><u>\$ 5,840,029</u></u>

**REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING
AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS
PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

To the Board of Education
Shelter Island Union Free School District
Shelter Island, New York

We have audited the financial statements of the governmental activities, each major fund and the fiduciary funds of the Shelter Island Union Free School District, as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements and have issued our report thereon dated November 16, 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

The management of the Shelter Island Union Free School District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered the Shelter Island Union Free 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 Shelter Island Union Free School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Shelter Island Union Free 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 that might be deficiencies, significant deficiencies or material weaknesses, as defined previously. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined previously.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the Shelter Island Union Free 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*.

We noted certain matters that we have reported to the Board of Education, Audit Committee and management of the Shelter Island Union Free School District in a separate letter dated November 16, 2012.

This report is intended solely for the use and information of the Board of Education, Audit Committee, management, others you deem appropriate within the District, and any governmental authorities you need to share this information with and is not intended to be and should not be used by anyone other than these specified parties.

Cullen & Danowski, LLP

November 16, 2012

