

# **School District of the City of River Rouge**

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**Report to the Board of Education**

**June 30, 2011**

To the Board of Education  
School District of the City of River Rouge

We have recently completed our audit of the basic financial statements of the School District of the City of River Rouge (the "School District") as of and for the year ended June 30, 2011. In addition to our audit report, we are providing the following results of the audit, summary of unrecorded possible adjustments, recommendations, and informational comments which impact the School District.

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We are grateful for the opportunity to be of service to the School District of the City of River Rouge. Should you have any questions regarding the comments in this report, please do not hesitate to call.

*Plante & Moran, PLLC*

November 9, 2011

## Results of the Audit

November 9, 2011

To the Board of Education  
School District of the City of River Rouge

We have audited the financial statements of the School District of the City of River Rouge, (the "School District") as of and for the year ended June 30, 2011 and have issued our report thereon dated November 9, 2011. Professional standards require that we provide you with the following information related to our audit.

### **Our Responsibility Under U.S. Generally Accepted Auditing Standards**

As stated in our engagement letter dated April 1, 2011, our responsibility, as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. We are responsible for planning and performing the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement. As part of our audit, we considered the internal control of the School District. Our consideration of internal control was solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

We are responsible for communicating significant matters related to the audit that are, in our professional judgment, relevant to your responsibilities in overseeing the financial reporting process. However, we are not required to design procedures specifically to identify such matters and our audit of the financial statements does not relieve you or management of your responsibilities.

Our audit of the School District's financial statements has also been conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Under *Government Auditing Standards*, we have made some assessments of School District's compliance with certain provisions of laws, regulations, contracts, and grant agreements. While those assessments are not sufficient to identify all noncompliance with applicable laws, regulations, and contract provisions, we are required to communicate all noncompliance conditions that come to our attention. We have communicated those conditions in a separate letter dated November 9, 2011 regarding our consideration of the School District's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements.

We are also obligated to communicate certain matters related to our audit to those responsible for the governance of the School District, including certain instances of error or fraud and significant deficiencies in internal control that we identify during our audit. In certain situations, *Government Auditing Standards* require disclosure of illegal acts to applicable government agencies. If such illegal acts were detected during our audit, we would be required to make disclosures regarding these acts to applicable government agencies. As previously discussed with the administration and finance committee, there is a disclosure related to the SES program which has been disclosed in the A-133 report.

### **Planned Scope and Timing of the Audit**

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters on September 27, 2011.

### **Significant Audit Findings**

#### ***Qualitative Aspects of Accounting Practices***

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the School District are described in Note 1 to the financial statements. During the year, the School District implemented GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund-type Definitions*. As a result of this required implementation, the Athletic Fund, previously classified as a special revenue fund, is now reported as a part of the General Fund. In addition, fund balance classifications in the governmental fund financial statements have been changed to reflect the new classifications under GASB No. 54. As described in Note 14, the financial statements for the year ended June 30, 2010 have been restated in order to record the net OPEB obligation related to other postemployment benefits as defined by GASB pronouncement 45. The School District had previously recorded the entire liability related to the benefits. The effect of this correction was to increase net assets and reduce long-term debt by \$1,294,883.

We noted no transactions entered into by the School District during the year for which there is a lack of authoritative guidance or consensus. There are no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred. The disclosures in the financial statements are neutral, consistent, and clear.

Accounting estimates are an integral part of the financial statements prepared by management and are based on management's knowledge and experience about past and current events and assumptions about future events. Certain accounting estimates are particularly sensitive because of their significance to the financial statements and because of the possibility that future events affecting them may differ significantly from those expected. The most sensitive estimate affecting the financial statements is the calculation of the other postemployment benefits.

#### ***Difficulties Encountered in Performing the Audit***

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

***Corrected and Uncorrected Misstatements***

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management.

***Disagreements with Management***

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

***Management Representations***

We have requested certain representations from management that are included in the management representation letter dated November 9, 2011.

***Management Consultations with Other Independent Accountants***

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the School District's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

***Other Audit Findings or Issues***

In the normal course of our professional association with the School District, we generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the School District, and business plans and strategies that may affect the risks of material misstatement. None of the matters discussed resulted in a condition of our retention as the School District's auditors.

A business issue that may affect future business plans and strategies relates to the School District's largest taxpayer, National Steel - Great Lakes Division. The entity has filed a petition with the tax tribunal requesting a 60 percent reduction in the original property tax values set by the City of River Rouge. If successful, the City and, subsequently, the School District, would have refund obligations from the General Fund and debt service fund. As of June 30, 2011, the administration has no ability to estimate the outcome. However, subsequent to year end, the School District hired legal counsel to keep the School District abreast of the settlement talks between the parties. It is reasonable to assume there will be an approximate settlement of \$4 million. The particulars of the settlement such as the breakdown between the General Fund and debt service fund and the potential for interest due is unknown. The Michigan Department of Education is expected to immediately reimburse the School District for any General Fund obligations resulting from this settlement.

To the Board of Education  
School District of the City of River Rouge

November 9, 2011

As required by OMB Circular A-133, we have also completed an audit of the federal programs administered by the School District. The results of that audit are provided to the Board of Education in our report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with OMB Circular A-133 dated November 9, 2011.

In addition to the comments and recommendations in this letter, our observations and comments regarding the School District's internal controls, including any significant deficiencies or material weaknesses that we identified, have been reported to you in the 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*. This report is included in the supplemental schedule of federal awards (single audit report), and we recommend that the matters we have noted there receive your careful consideration.

This information is intended solely for the use of the Board of Education and management of the School District of the City of River Rouge and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

**Plante & Moran, PLLC**

A handwritten signature in cursive script that reads "Paul D. Bryant".

Paul D. Bryant  
Partner

## **Other Recommendations**

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# **School District of the City of River Rouge**

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## **Other Recommendations**

### **Segregation of Duties**

It was noted during the audit that there are a limited number of individuals in the business office, which causes several duties to overlap such as access to cash receipts, journal entry posting, reconciliation of cash accounts, and preparation, posting, and approval of journal entries.

We understand that the School District has hired an additional accountant which has helped internal control; however, there are areas where cash- and revenue-related functions are still performed by the same individual. We recommend that the School District continue to evaluate the roles and responsibilities of all individuals in the business office to further enhance the School District's internal control. Additionally, we also recommend that the board continue its involvement related to oversight responsibilities which include review of the all cash-related activity.

# **Informational**

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### Written Procedures for Grants

Included in the 2010-2011 *Accounting and Audit Alert* issued by the Michigan Department of Education was a summary of certain requirements pertaining to administrative and financial internal controls for grant recipients. As described in 34 CFR Part 80, 2 CFR Part 215 and OMB Circular A-133 Compliance Supplement Part 6, school districts must have written procedures for the following:

- Financial management systems
- Payments
- Allowable costs
- Period of availability
- Matching or cost sharing (if applicable)
- Program income (if applicable)
- Procurement
- Equipment and real property (if applicable)
- Supplies
- Copyrights (if applicable)
- Subawards to debarred and suspended parties
- Monitoring and reporting program performance (if applicable)
- Financial reporting
- Retention and access requirements for records

In addition, districts should also have written procedures for:

- Cash management
- Conflict of interest
- Payroll
- Federal timekeeping

We encourage the School District to review its procedures and the documentation of such procedures to ensure that the items listed above have been addressed. The procedure itself is not required to be specific to federal grants as long as it has applicability to the grants as well. Many, if not all, of the items may already be addressed in various different forms throughout the School District's policies and procedures. It is important the School District be aware of where the documentation resides to cover the items listed above. The MDE has begun the process of performing Federal Program Fiscal Monitoring and will request these procedures when on site. If any items are not currently addressed, we recommend the School District evaluate putting procedures in place and document them accordingly. The MDE has issued a self-assessment checklist on fiscal management which may be helpful to identify areas the MDE will be looking into and address any items in advance of any fiscal monitoring visit.

# School District of the City of River Rouge

## Informational (Continued)

### GASB Proposes Major Changes

The Governmental Accounting Standards Board has recently implemented a major standards change, *Financial Reporting of Deferred Outflows of Resources, Deferred inflows of Resources, and Net Position*.

This standard focuses on changes to balance sheet classifications. Up to this point, there have been three main components reported on a balance sheet - assets, liabilities, and equity. The GASB is effectively adding two new elements to the balance sheet, along with some name changes.

- Deferred outflows, to be reported in a separate section after assets, would represent a consumption of resources that is applicable to a future reporting period. Although not defined as such by the GASB yet, prepaid expenditures might be the closest example of a deferred outflow that we have today. We have paid the expenditure in one year (consumed resources), but since the expenditure relates to a future year, instead of recognizing the expenditure today, we recognize an asset.
- Deferred inflows, which would be reported in a separate section after liabilities, would represent the acquisition of net assets applicable to a future period. Again, although the GASB has not yet defined this as a deferred inflow specifically, one significant example might be deferred revenue that is created when entities receive cash in one year that is earned when expended in a subsequent year's budget.

Along with these two new balance sheet elements come several terminology changes to accommodate the impact these new components have on the financial statements. The balance sheet, formerly known as the "statement of net assets," would be renamed the "statement of net position." Correspondingly, the GASB wants to rename the equity section "net position." Several other more minor changes will come with this implementation. These changes will be effective with the School District's June 30, 2013 financial statements.

### Planning Considerations for 2011-2012

Michigan's economy continues to show signs of improvement but the rate of improvement is slow. The State's ability to generate revenue, especially in the School Aid Fund, is also improving. The governor's budget theme in 2011 was "shared sacrifice" and the State has redeployed school aid funds as part of that theme. He has also suggested that if everyone shares in the sacrifice that there will not be repeated requests for sacrifice in the future. If this is accurate, the School District's revised funding levels (foundation allowance) will become the new normal and budget decisions would begin with that funding level as a base. However, history suggests that prudence in district budgeting is appropriate. Given the continued fragile position of the State's revenue picture and the newness of the governor's agenda, it is possible that further, unanticipated changes may occur. As a result, we encourage the School District to continue to plan carefully and monitor the funding progress throughout the year.

# School District of the City of River Rouge

## Informational (Continued)

Based on legislative actions to date, it is reasonable to assume that the funding picture for 2011-2012 is stable. However, while not as likely as in years past, as the funding facts change, the School District may be put in a position, once again, where budget modifications may be necessary. As the School District begins to plan for 2012-2013, applying the intent language in the State Aid Act is a good place to start. However, given the current focus on best practice and management of results, it is possible future funding increases may be tied to certain, yet unspecified, outcomes.

### Other State Aid Issues Impacting 2011-2012

The amendments to the State Aid Act made several other changes impacting school districts. Several changes we identified that could impact the School District include the following:

**2011-2012 Intent Language for Funding Levels** - One legislature cannot bind another legislature. However, the State Aid Act includes intent language regarding funding levels for 2012-2013.

**Added Higher Education** - The School Aid Fund was restructured and now includes the funding mechanism for higher education as well as K-12.

**Pupil Count Weighting** - The School District will continue to have two pupil counts per year. However, the weighting of the counts is changed from 25 percent/75 percent to 10 percent/90 percent for the winter and fall counts, respectively. The fall count day is now the first Wednesday in October.

**Funding for Half-day Kindergarten** - Beginning in 2012-2013, intent language is included to reduce per-pupil funding for kindergarten students if the School District does not provide a full-day program.

**Proration Language** - Revised language to address how proration would be applied now that higher education is included in the State Aid Act

**Early Childhood** - Intent language added to consolidate programming, administration, and focus of early childhood and utilize a block grant approach

**Bus Inspections** - Fully funded the state police bus inspection program

# School District of the City of River Rouge

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## Informational (Continued)

**Retirement Rate** - For 2011, once again, the School District will experience a rise in the retirement rate and the need to apply multiple rates depending on employee hire date. Beginning October 1, 2011, for employees hired before July 1, 2010, the rate will be 24.46 percent of compensation, up from 20.66 percent. For employees hired on or after July 1, 2010 the rate will be 23.23 percent, up from 19.16 percent. In 2010, the retirement system began requiring an additional 3 percent employee contribution. Legal challenges have not allowed the employee contribution to be “counted” as part of the School District’s contribution and are currently being held in trust by the retirement system pending the legal outcome. As a result, the School District is both collecting and remitting the 3 percent employee contribution but is unable to use the employee contribution to the retirement system to reduce the district-required contribution rate. Without significant changes to the retirement system, it is estimated that the retirement rate will increase to over 30 percent in the next few years.

### **Federal Grants Management Update**

Funding under the American Recovery and Reinvestment Act (ARRA) continues to create grants management challenges for School Districts. In addition, other changes continue to impact the future of districts. Below we have briefly summarized grants management challenges we have identified that could impact your School District.

**Supplement versus Supplant** - Most federal grant agreements require that the federal funds used add to or supplement current nonfederal programs. It is important for the School District to understand the specific rules for supplement versus supplant for each grant and be able to document how the requirement was met. One program where significant funding increases could create increased risk is Title I. Annually reviewing the spending plan for Title I and similar programs is an important element when meeting supplement requirements.

**MDE ARRA Monitoring** - ARRA funding focused on the importance of “transparency and accountability.” As the Michigan Department of Education (MDE) is a direct recipient of ARRA funds used by school districts, it is required to assess “accountability.” One of the ways it is doing this is via a monitoring process. This involves a risk assessment on its part and then an action plan based on that assessment. While not every district will receive a monitoring visit, it is likely that most will receive a monitoring inquiry of some sort. The monitoring will be specific to accounting treatment of ARRA funds and compliance with certain grant requirements and is expected to continue throughout the closing process of ARRA. It is slightly different from previous monitoring by the MDE which usually includes substantial focus on performance aspects of federal grants.

# School District of the City of River Rouge

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## Informational (Continued)

**Fiscal Monitoring** - Separate from the ARRA monitoring discussed above, the MDE has instituted a grants fiscal monitoring process. The MDE has performed grants performance reviews in the past and will continue to do so. In addition, they are now also looking at the School District's accountability process. This process will focus on the financial aspects of grants management with an emphasis on control procedures assessments in the key compliance areas of the grant. These actions are the result of an increased federal emphasis for pass-through entities (the State of Michigan) to improve their monitoring efforts. To assist districts in their compliance efforts, the State has issued a self-evaluation checklist which will allow districts to identify areas which may require addition attention.

**Documenting Work Performed** - A fundamental requirement for federal grants is to document the work performed to fulfill the grant requirements. The method defined in regulation prescribes the use of a Personnel Activity Report (PAR). Essentially this is a more detailed timesheet. In previous years, the MDE had accepted teacher lesson plans as a substitution for the PAR. For the year ended June 30, 2011, the MDE indicated that lesson plans will not be accepted by the MDE and a PAR will be required. As a result, when performing our audit we requested a PAR to prove effort and allocation of cost for employees charged to your federal grants. School districts retain the ability to use a "certification" in certain situations in lieu of a PAR. In short, certifications are acceptable when allowable. If the criteria for certifications are not met, a PAR must be used.

**Audit Requirements** - ARRA funding has a dramatic effect on audit requirements. Due to the requirements built in the ARRA and the related federal office of management and budget regulations, the number of federal programs we are required to audit and the audit procedures we are required to complete for each program have increased. The changes mean that if the School District received ARRA funding combined with the traditional federal assistance and the resulting programs are larger, as defined by regulation, the auditor must test it. In addition, even if some programs are "smaller," the auditor may have to test them as well. The programs we tested this year are listed as "major programs" in the back of the School District's single audit report.