

School District of the City of River Rouge

Report to the Board of Education

June 30, 2010



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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") for the year ended June 30, 2010. In addition to our audit report, we are providing the following results of the audit, summary of unrecorded possible adjustments, other recommendations, and informational items which impact the School District:

	<u>Page</u>
Results of the Audit	1-4
Summary of Unrecorded Possible Adjustments	5
Other Recommendations	6-7
Informational Items	8-14

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

October 15, 2010



Results of the Audit

October 15, 2010

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") for the year ended June 30, 2010 and have issued our report thereon dated October 15, 2010. 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 March 1, 2010, 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 October 15, 2010 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. No such disclosures were required.

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 October 1, 2010.

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. No new accounting policies were adopted and one application of existing policies was changed during the year. This change related to the recognition of property taxes under the modified accrual method. Property taxes were received outside of the normal 60 days; however, unavailable amounts were recognized as revenue on the modified accrual basis because payment is normally received within this time frame and an unusual circumstance caused a delay in this receipt.

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.

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. The attached schedule summarizes uncorrected misstatements of the financial statements. Management has determined that their effects are immaterial, both individually and in the aggregate, to the financial statements taken as a whole.

Disagreements with Management

For the purpose 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 October 15, 2010.

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 value set by the City of River Rouge. If successful, the City and, subsequently, the School District, would have refund obligations from the General and Debt Service Funds. As of June 30, 2010, the administration has no ability to estimate the outcome and accordingly no amounts have been accrued on the governmental or fund level. Should amounts become estimable, the School District would be required under generally accepted accounting principles to reflect refundable amounts as fund level liabilities.

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 October 15, 2010.

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

October 15, 2010

In addition to the comments and recommendations in this letter, our observations and comments regarding the School District's internal control, 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". The signature is written in black ink and is positioned above the printed name and title.

Paul D. Bryant
Partner

Client: School District of the City of River Rouge
Opinion Unit: Governmental Activities
Y/E: 6/30/2010

SUMMARY OF UNRECORDED POSSIBLE ADJUSTMENTS

The effect of misstatements and classification errors identified would be to increase (decrease) the reported amounts in the financial statement categories identified below:

Ref. #	Description of Misstatement	Current Assets	Long-term Assets	Current Liabilities	Long-term Liabilities	Net Assets	Revenue	Expenses
KNOWN MISSTATEMENTS:								
A1	To record the known outcome of a lawsuit that the School District is involved in at June 30, 2010			\$ 150,000				\$ 150,000
A2								
ESTIMATE ADJUSTMENTS:								
B1								
B2								
IMPLIED ADJUSTMENTS:								
C1								
C2								
		\$ -	\$ -	-	\$ -	\$ -	\$ -	-
	Total	\$ -	\$ -	\$ 150,000	\$ -	\$ -	\$ -	\$ 150,000

Other Recommendations

School District of the City of River Rouge

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 related to 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.

Bank Reconciliations

During the audit, it was noted that various bank reconciliations did not include a date indicating when they were prepared or reviewed. We recommend that the preparer and reviewer of the bank reconciliations indicate the date in order to ensure timely preparation.

Payroll

During our review of the payroll functions, it was noted on a time card of an hourly employee that no department head approval was included on the time card, as well as a minimal difference in the number of hours worked on the time card and payroll register. The School District does not employ a significant number of hourly employees; however, payroll does have a process in place to review time cards and payroll registers along with performing budget to actual analysis. We continue to recommend that the School District ensure proper controls are being carried out.

Compensated Absences

Currently, the School District pays out its sick and vacation pay at 50 percent. We recommend the School District put a policy in place for employees to cap out at a specific number of days or hours.

Informational

School District of the City of River Rouge

Informational

New Form 1099 Requirements

The recently enacted federal healthcare reform legislation contained certain tax provisions affecting all businesses and public sector entities. Beginning January 1, 2012, public schools will be required to issue Form 1099s to every vendor to which they make payments totaling \$600 or more during the calendar year for the purchase of goods, services, or other items. Vendors include almost everyone other than employees who receive a Form W-2. Increased recordkeeping will be required, and planning for this change will be important. Ignoring the requirements could lead to expensive penalties for failure to comply. We recommend all entities begin obtaining tax information from all vendors, and ensuring that existing software has the necessary tools to start accumulating this data and organizing it in order to generate the 1099 form. It is also possible that some repeal or limitation of these requirements may occur in response to concerns over the administrative burden placed on small businesses and others. We will keep you apprised of any future changes to the requirements.

State Aid Act Changes Impacting 2010/2011

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:

Service Consolidation Plans - Districts are required to report on efforts to consolidate serves by February 1, 2011.

School Bus Inspections - Inspections to be completed by the School District with random audits performed by the Michigan state police.

Distance Learning and Alternative Instruction Delivery - By September 10, 2012, the School District will be required to report on the costs of providing distance learning and other forms of “alternative” instruction delivery.

Certain Reports No Longer Required - The requirement to file the following reports has been eliminated: the annual education report, school improvement plan, core academic curriculum, and accreditation. The elimination of reports does not impact district responsibility if actions are required under No Child Left Behind.

Professional Development - The five hours of online training requirement was removed.

Days of Instruction - The requirement to provide a minimum of 165 days of instruction is retained.

21st Century Schools Intent Language - The “intent to fund” language for the 21st Century Schools initiative was removed from the State Aid Act.

School District of the City of River Rouge

Informational (Continued)

Retirement Rate - The contribution rate for the members who first worked July 1, 2010 or later (Pension Plus members) has been changed for the time period from July 1, 2010 to September 30, 2010. This change will be in your download detail as well as your employer statement. The employer contribution rate charged for Pension Plus members for this time period is 15.44 percent. For all other members, it remains at 16.94 percent through September 30, 2010.

Effective October 1, the employer contribution rate for all employees except Pension Plus members is 19.41 percent as communicated to you in February. For Pension Plus members, the employer contribution rate is 17.91 percent.

Due to the increased number of retirees associated with the early retirement incentive, the revised contribution rate due on members' wages paid between November 1, 2010 and September 30, 2011 will be 20.66 percent for members who first worked prior to July 1, 2010 and 19.16 percent for members who first worked July 1, 2010 or later (Pension Plus plan members). This rate is approximately 3 percent higher than it would be without the preliminary injunction, which prevents the use of employee contributions, ordered by the Court of Claims in the McMillan et al v. MPSERS et al lawsuit. At such time as this injunction may be lifted, the contribution rate will be reduced.

Remember, the Pension Plus rate is based on reportable wages for each newly hired staff member from July 1, 2010 to the present. This does not include the match of up to 1 percent the School District will be responsible for the defined contribution component of the Pension Plus plan. The defined contribution portion of the plan is based on gross compensation and is set up as an IRS Section 457 Retirement Plan, subject to restrictions, limitations, and regulations of that type of plan.

State Aid Planning Considerations for 2010/2011

In the last few months, the Michigan economy has shown mild signs of improvement. While we have seen small reductions in unemployment and some small improvements in home sales, there are no signs of a quick recovery. In addition, the November 2010 state elections will create significant leadership changes in the legislative and executive branches. In the past, similar factors have made for significant uncertainty for school districts when planning district budgets. The current State Aid Act does not make significant changes from 2010. It presumes essentially a flat funding level compared to 2009/2010. However, history suggests that prudence in district budgeting is appropriate. Given the fragile position of the State's revenue picture and the likely changing priorities from new leadership, it is possible that the revenue enacted in July 2010 could be altered as the year progresses. As a result, we encourage the School District to continue to plan carefully and monitor the funding progress throughout the year. As the finding facts change, the School District may be put in a position, once again, where budget modifications may be necessary midyear.

School District of the City of River Rouge

Informational (Continued)

As the State's budget year moves forward, revenue intake will be monitored with periodic revenue-estimating conferences. State law requires that the appropriations cannot exceed revenue estimates. As a result, it is possible there could be further reductions to district funding if the State is not able to generate the funding levels identified in the May 2010 revenue-estimating conference. Past practice has suggested that if future reductions are necessary, they will come in the form of an additional proration. Prudence is appropriate in managing district programs given the instability of state funding over the last several years.

Planning for the "End" of ARRA - In 2010/2011, the School District will continue to receive ARRA funding. As of now, the funding at the federal level is scheduled to end in fall 2011. The potential impacts of this include the following:

- Stabilization funding will end at the end of the 2010/2011 fiscal year. Replacing this revenue will be left to the State.
- Additional ARRA funding coupled with traditional programs such as Title I will be substantial in 2010/2011.
- Additional ARRA funding coupled with traditional programs will likely see reduced funding in 2011/2012. This should be the last fiscal year where the School District receives ARRA funds.
- There is some speculation that some of the education activities funded with ARRA may end up as recurring funding. As of now, there is nothing to validate this.
- If the State of Michigan receives approval for Race to the Top funding, some districts may receive funding for related initiatives.

Clearly, careful planning on the use of current ARRA is critical. If funds are used for recurring activities, the School District will need to consider how it will respond when the funding ends.

Districts have been asked to accomplish much with the infusion of the American Recovery and Reinvestment Act funds and the changes to grants management requirements. Unfortunately, the American Recovery and Reinvestment Act does not provide funds to aid the School District in paying for the increased grants management effort. To aid the School District, we will continue to carefully monitor requirement changes. Our goal is to maximize lead time for the School District to respond to changes and offer suggestions on ways to comply while minimizing overall effort.

Budgeting Strategy in Difficult Financial Times

Over the last several years, Michigan schools have struggled with the reality that the State has not been able to significantly increase school funding. Based on the State's current budgetary outlook, it is apparent that there will not be any additional funds for the foreseeable future. The stabilization funds will essentially run out in 2011. If the State cannot generate other revenue sources to replace it, the School Aid Fund will not be equipped to maintain funding at the current level, creating a significant funding cliff.

School District of the City of River Rouge

Informational (Continued)

For the last several years, financial struggles have been a way of life for Michigan schools. As of today, the outlook continues to be discouraging. However, we do know that the School District's budget plan for 2011 and beyond will require continuing difficult financial decisions of a significant scale. Never before have districts been required to examine how educational programs and services need to be adapted or redefined to cope with the funding issues while meeting educational needs of the students. These tasks are not easy, but in the end the decisions made could become opportunities to redesign how services are provided and educational objectives are met. If the School District can identify opportunities to "do things differently" it may be able to mitigate some of the negative effects of a reduced funding environment.

GASB Statement No. 54 - Time for Implementation

By now, you are likely aware that GASB Statement No. 54, *Fund Balance Reporting and Governmental Fund-type Definitions*, is effective for your 2010-2011 fiscal year. GASB Statement No. 54 clarifies the definition of fund types and requires fund balances to be classified into new categories based on the level of availability for discretionary spending. In order to have a smooth transition to the new standard, you will likely need to modify your budgets, general ledger account structure, and board policies. Also, key stockholders in the School District such as administrators, board members, and bargaining groups may need education to fully understand the new reporting.

Changes to Special Revenue Fund Type

GASB Statement No. 54 provides a new and clearer description of when it is appropriate to account for an activity using a special revenue fund. Special revenue funds are used to report specific revenue sources that are restricted or committed to specified purposes other than debt service and capital projects, whereas the restricted or committed revenue sources comprise a substantial portion of the fund's resources, and are expected to continue to do so in the future. Under this definition, it is clear that most athletics funds no longer qualify for special revenue fund treatment. The Michigan Department of Education has revised the 1022 Manual to now include athletic activities as part of the General Fund coding structure. Districts should review their other special revenue funds to ensure these funds continue to warrant this treatment.

In order to transition the athletics activities to the General Fund, consider the following tasks:

- General ledger coding will need revision to eliminate the Athletics Fund and expand the General Fund codes to capture these activities.
- Program codes and special reports may need to be developed to provide management information on the athletics activities.
- Budgets for the Special Revenue and General Funds may need amendments to reflect this new treatment.

School District of the City of River Rouge

Informational (Continued)

- Opening fund balance in the General Fund at July 1, 2010 may need modification to incorporate any June 30, 2010 fund balance remaining in the old collapsed funds.

Fund Balance Definitions

GASB Statement No. 4 eliminates the current use of the terms “reserved” and “designated” in the reporting of fund balance and replaces those terms with five new categories for segregating fund balance.

The following are the new categories and related definitions to be used for describing the components of your fund balance:

- **Nonspendable** - Includes amounts either not in spendable form or legally or contractually required to be maintained intact. This would include inventory, prepaids, and noncurrent receivables.
- **Restricted** - Reflects the same definition as restricted net assets: constraints placed on the use of amounts 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. This would generally include amounts in bonded capital projects funds, debt service funds, and cafeteria and center program funds funded with federal program dollars.
- **Committed** - Includes amounts that are committed for specific purposes by formal action of the school board. Amounts classified as “committed” are not subject to legal enforceability like restricted fund balance; however, those amounts cannot be used for any other purpose unless the board removes or changes the limitation by taking the same form of action it employed to previously impose the limitation.
- **Assigned** - Amounts that are intended by the School District to be used for specific purposes, but are neither restricted nor limited, should be reported as assigned fund balance. Intent should be expressed by the board itself or a subordinate high-level body or official possessing the authority to assign amounts to be used for specific purposes in accordance with policy established by the board. This would include any activity reported in a fund other than the General Fund that is not otherwise restricted more narrowly by the above definitions.
- **Unassigned** - Includes any remaining amounts after applying the above definitions. Planned spending in the subsequent year’s budget would be included here and can no longer be described as “designated” unless formally committed or assigned.

The Michigan Department of Education has updated the state-mandated chart of accounts for 2011 to reflect the new definitions, and the School District will need to modify its general ledger coding and financial reporting practices accordingly.

School District of the City of River Rouge

Informational (Continued)

You will likely want to consider what formal “commitments” the board wishes to adopt, and adopt formal board policies or budget approvals to document these decisions. Commitments or assignments of fund balance should be made prior to June 30, 2011.

The standard also requires disclosure in the financial statements of any minimum fund balance policies, and the purposes for restrictions, commitments, and assignments of fund balance.

We encourage the School District to become familiar with the new terms and definitions and work with the users of the financial statements to ensure a clear presentation and understanding of the new requirements.