Management Report

for

Independent School District No. 194
Lakeville, Minnesota
June 30, 2008

MMKR
CERTIFIED PUBLIC ACCOUNTANTS

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To the School Board of
Independent School District No. 194
Lakeville, Minnesota

We have prepared this management report in conjunction with our audit of Independent School District No. 194's (the District) financial records for the year ended June 30, 2008. The purpose of this report is to communicate information relevant to the financing of public education in Minnesota and to provide comments resulting from our audit process. We have organized this report into the following sections:

- Audit Summary
- Funding Public Education in Minnesota
- Financial Trends of Your District
- Accounting and Reporting Updates
- Legislative Summary

We would be pleased to further discuss any of the information contained in this report or any other concerns that you would like us to address. We would also like to express our thanks for the courtesy and assistance extended to us during the course of our audit.

This report is intended solely for the information and use of those charged with governance, the School Board, management, and those who have responsibility for oversight of the financial reporting process and is not intended to be, and should not be, used by anyone other than these specified parties.

Malloy, Montague, Karnowski, Radosevich, & Co., P.A.

October 9, 2008

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AUDIT SUMMARY

We hereby provide you with the following summary of our audit work, key conclusions, and other information that we consider important or that is required to be communicated to the School Board or administration of the District.

Our Responsibility Under Auditing Standards Generally Accepted in the United States of America and OMB Circular A-133

Our responsibility, as stated in our engagement letter and as described by professional standards, is to express opinions about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with accounting principles generally accepted in the United States of America. Our audit of the financial statements does not relieve you or management of your responsibilities.

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the financial statements, and not to provide assurance on the internal control over financial reporting. We also considered internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with the U.S. Office of Management and Budget (OMB) Circular A-133.

As part of obtaining reasonable assurance about whether the District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, 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. Also, in accordance with OMB Circular A-133, we examined, on a test basis, evidence about the District's compliance with the types of compliance requirements described in the OMB Circular A-133 *Compliance Supplement*, applicable to each of its major federal programs for the purpose of expressing an opinion on the District's compliance with those requirements. While our audit provides a reasonable basis for our opinion, it does not provide a legal determination on the District's compliance with those requirements.

New Auditing Standards

As you may be aware through our past management reports, engagement letters, and discussions with administration, the audit process has changed this past year. Because of our extensive experience with Minnesota school districts, we have always taken a customized approach to auditing schools. We found this to be both an efficient and effective method to accomplish a quality audit.

Much of the audit process this year under the new standard is the same as what we have done in the past, with the addition of the risk-based model or approach. This involves a much more thorough review, analysis, and documentation of the District's environment, systems, procedures, and internal controls. This provides for an assessment of risk for material misstatement in the financial statements due to error or fraud, and what additional audit procedures we need to perform to address those risks. Although the intent of the new standards is to increase the quality of audits in our profession, a positive by-product is getting management and governance of the District more involved in reviewing and improving procedures and controls. This is very important, as the School Board and management play critical roles in the District's financial controls.

Planned Scope and Timing of the Audit

We performed the audit according to the planned scope and timing previously discussed and coordinated with you in order to obtain sufficient audit evidence and complete an effective audit.

Audit Opinion and Findings

Based on our audit of the District's financial statements for the year ended June 30, 2008:

- We have issued an unqualified opinion on the District's annual financial statements.
- We have reported three deficiencies involving the District's internal controls over financial reporting, none of which were considered material weaknesses.

    1) The District does not have proper segregation of duties with regard to bank reconciliations. The bank reconciliations are prepared by the bookkeeper who has access to and is an integral part of the controls over the cash receipts of the District.
    2) The District has a lack of documentation with regard to components of its internal controls, including governance-level controls.
    3) The District does not have an adequate system in place to assist management personnel in identifying when and if employees are not adequately recording time worked.

- The results of our testing disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.
- We noted that the Schedule of Expenditures of Federal Awards is fairly stated, in all material respects, in relation to the basic financial statements.
- The results of our tests indicate that the District has complied, in all material respects, with the requirements applicable to each major federal program.
- We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses in our testing of major federal programs.
- There was one Minnesota Legal Compliance Finding in the current year. Minnesota Statute § 118A.03 requires that if a school district's deposits exceed federal insurance coverage, excess deposits must be covered by corporate surety bonds or collateral that has a market value of at least 110 percent of such excess. This requirement was not met for one of the District's accounts at June 30, 2008.

Significant Accounting Policies

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting policies used by the District are described in Note 1 of the notes to basic financial statements. No new accounting policies were adopted and the application of existing policies was not changed during the year. We noted no transactions entered into by the 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.

Accounting Estimates and Management Judgments

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 estimates affecting the financial statements were:

General education revenue and certain other revenues are computed by applying an allowance per student to the number of students served by the District. Student attendance is accumulated in a state-wide database—MARSS. Because of the complexity of student accounting and because of certain enrollment options, student information is input by other school districts and the MARSS data for fiscal year 2008 is not finalized until well into fiscal year 2009. General education revenue and certain other revenues are computed using preliminary information on the number of students served in the resident district and also utilizing some estimates, particularly in the area of enrollment options.

Special education state aid revenue and receivables includes an adjustment related to tuition billings to and from other school districts for special education services which are computed using formulas derived by the Minnesota Department of Education (MDE). Because of the timing of the calculations, this adjustment for fiscal 2008 is not finalized until after the District has closed its financial records for the fiscal period. The impact of this adjustment on the receivable and revenue recorded for state special education aid is calculated using preliminary information available to the District.

The District has recorded a liability in the Statement of Net Assets for severance and health benefits payable for which it is probable employees will be compensated. The "vesting method" used by the District to calculate this liability is based on assumptions involving the probability of employees becoming eligible to receive the benefits (vesting), the potential use of accumulated sick leave prior to termination, and the age at which such employees are likely to retire.

The depreciation of capital assets involves estimates pertaining to useful lives.

Management expects any differences between estimates and actual amounts of these estimates to be insignificant. We reviewed and tested management's procedures and underlying supporting documentation in the areas discussed above. We concluded that the accounting estimates and management judgments appeared to consider all significant factors and resulted in appropriate accounting recognition.

Audit Adjustments

For purposes of this letter, professional standards define an audit adjustment as a proposed correction of the financial statements that, in our judgment, may not have been detected except through our auditing procedures. An audit adjustment may or may not indicate matters that could have a significant effect on the District's financial reporting process (that is, cause future financial statements to be materially misstated).

During our audit we proposed and the District recorded four audit adjustments. We do not believe these adjustments had a significant effect on the financial reporting process. They include increases to salaries payable of $42,966, accounts payable of $25,106, contracts payable of $65,140, and long-term severance and health benefits payable of $375,162.

During the fiscal 2008 audit, we also identified known uncorrected financial statement misstatements (passed adjustments). These passed adjustments included approximately $52,000 of unrecorded arbitrage liabilities.

Difficulties Encountered in Performing the Audit

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

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 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 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

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the District's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

Management Representations

We have requested certain representations from management that are included in the management representation letter dated October 9, 2008.

Extracurricular Student Activity Accounts

In accordance with Minnesota Statutes, the District's School Board has elected not to exercise control over the transactions of the extracurricular student activity accounts maintained at various district sites. Consequently, the cash receipts and disbursements of the District's extracurricular student activity accounts are reported in a separate set of financial statements, rather than being reported within the District's General Fund. We have issued an opinion on these separate financial statements, stating that they fairly present the recorded cash transactions of these accounts for the year ended June 30, 2008.

We also issued a report on compliance with the MDE's *Manual for Activity Fund Accounting,* in which we reported the following findings:

- We noted 17 activities accounted for by the District as student activities that do not meet the definition of an extracurricular activity as defined by standards of the *Manual for Activity Fund Accounting*.
- We noted 11 activities accounted for by the District as student activities which are inactive and need to be closed.
- We noted 3 of the District's student activity accounts that had deficit balances at June 30, 2008.
- We noted 3 out of 50 cash receipt transactions we tested that were either not deposited on a timely basis or were for staff related items which are not allowed in a student activity account.
- We noted 19 out of 50 cash disbursements transactions we tested that were not properly approved by the appropriate building official or designee, lacked original vendor invoices and/or backup documentation, or were for labor payments not allowed to be paid by student activity accounts.

FUNDING PUBLIC EDUCATION IN MINNESOTA

Due to its complexity, it would be impossible to fully explain the funding of public education in Minnesota within this report. The last section of this report, which contains a summary of legislative changes affecting school districts, gives an indication of how complicated the funding system is. The following section provides some state-wide funding and financial trend information.

BASIC GENERAL EDUCATION REVENUE

The largest single funding source for Minnesota school districts is basic general education aid. Each year, the Legislature sets a basic formula allowance. Total basic general education revenue is calculated by multiplying the formula allowance by the number of pupil units for which a district is entitled to aid. Pupil units are calculated using a legislatively determined weighting system applied to average daily membership (ADM). Over the years, various modifications have been made to this calculation, including changes in weighting and special consideration for declining enrollment districts.

The table below presents a summary of the formula allowance for the past few years. We have adjusted the percentage change from year to year for non-comparable changes such as referendum reduction and aids that were previously separately funded and subsequently "rolled-in" or "rolled-out" to general education revenue. We have also included state-wide General Fund revenue per un-weighted ADM as calculated by the MDE.

	Formula Allowance		State Calculated Revenue per ADM (2)	
School Year	Amount	Percent Increase	Amount	Percent Increase
2000–2001	$ 3,964	4.2 % (1)	$ 7,057	6.1 %
2001–2002	$ 4,068	2.6 %	$ 7,247	2.7 %
2002–2003	$ 4,601	2.6 % (1)	$ 7,712	6.4 %
2003–2004	$ 4,601	– %	$ 7,898	2.4 %
2004–2005	$ 4,601	– %	$ 7,996	1.2 %
2005–2006	$ 4,783	4.0 %	$ 8,319	4.0 %
2006–2007	$ 4,974	4.0 %	$ 8,776	5.5 %
2007–2008	$ 5,074	2.0 %	$ 9,342 (3)	6.4 % (3)
2008–2009	$ 5,124 (4)	1.0 % (4)	$ 9,648 (3)	3.3 % (3)

(1) Percentage adjusted to eliminate changes caused by referendum reduction; rolled-in (out) aids which do not affect total district revenue.

(2) Includes General Fund state aids, tax credits, tax levies, and referendums.

(3) Estimated.

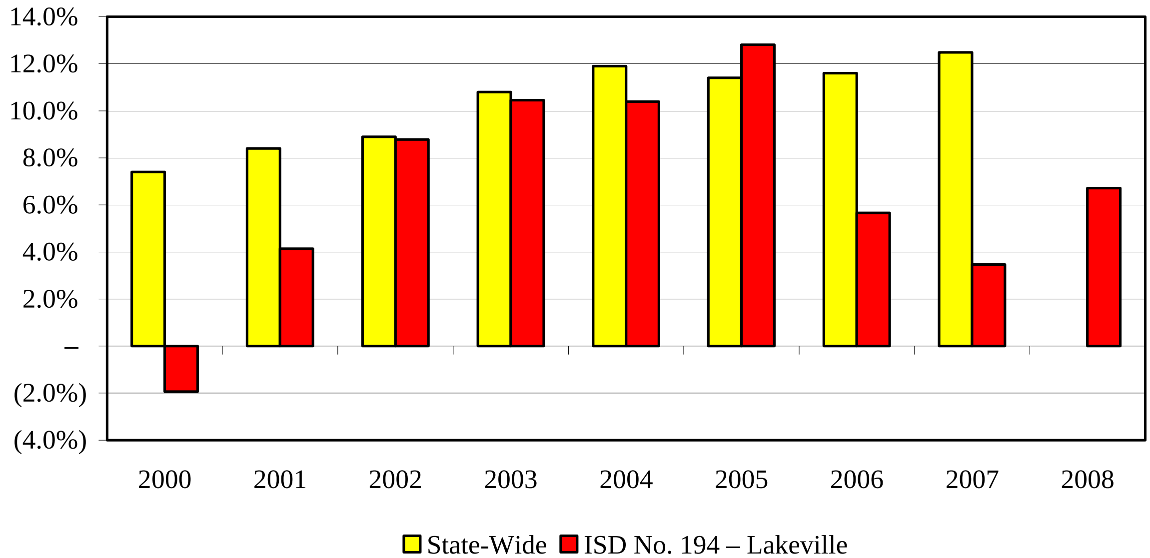
(4) For fiscal 2009 only, all school districts and charter schools will receive an additional $51, which is not included in the table above. This increase is not linked to other formulas that use the general education formula allowance.

The major difference between the basic formula increases and the state calculated increases are operating referendums, including a projection of those that might pass this fall. Excluding operating referenda, the state's projected increases are 6.3 percent for 2007–2008 and 2.5 percent for 2008–2009. In general, the moderate increases in the formula allowance have forced districts to continually cut expenditure budgets or increase referendum revenue in order to maintain programs.

STATE-WIDE SCHOOL DISTRICT FINANCIAL HEALTH

One of the most common and comparable statistics used to evaluate school district financial health is the unreserved operating fund balance as a percentage of operating expenditures.

State-Wide Unreserved Operating Fund Balance
as a Percentage of Operating Expenditures



Note: State-wide information is not available for fiscal 2008.

For years prior to 2001, the percentage calculation includes all of the unreserved operating funds and certain particular reserved fund balances. The more recent years reflect only the unreserved fund balance of the General Fund, and the corresponding expenditures, which is the same method which the state now uses for the calculation of statutory operating debt (SOD). We have also included the comparable percentages for your district.

Even with limited funding increases, school districts have maintained a relatively stable unreserved fund balance on a state-wide basis in recent years. This stability may be the result of districts adapting to funding restrictions, effective cost containment measures, in some cases community support in the way of operating referendums, and other factors.

The graph shows the District's steady decrease in this ratio from fiscal 2005 to fiscal 2007, then the subsequent improvement in the current fiscal year.

The table below shows a comparison of total revenue per ADM received by Minnesota school districts and your district. Revenues for all governmental funds are included, except for the Capital Projects – Building Construction Fund; proceeds from sales of real property and equipment; insurance recoveries; and sales of bonds, loans, and interfund transfers.

Revenue per Student (ADM) Served

	State-Wide		Seven-County Metro Area		ISD No. 194 – Lakeville		
	2006	2007	2006	2007	2006	2007	2008
General Fund							
Property taxes	$ 545	$ 1,020	$ 747	$ 1,365	$ 744	$ 1,112	$ 1,258
Other local sources	520	504	439	414	181	177	190
State	7,545	7,490	7,741	7,613	6,965	6,965	7,211
Federal	464	444	476	464	213	206	201
Special revenue funds							
Food service	398	415	401	418	405	423	434
Community service	421	445	511	538	448	463	510
Debt Service Fund	879	938	946	1,032	957	1,066	1,159
Total revenue	$10,772	$11,256	$11,261	$11,844	$ 9,913	$10,412	$10,963
ADM served and tuition paid					10,930	11,088	11,142

Note: Excludes Capital Projects – Building Construction Fund, refunding bond debt service activity, Internal Service Fund, and fiduciary funds.

Source of state-wide and seven-county metro area data: School District Profiles Report published by the MDE.

The mix of local and state revenues vary from *year to year* primarily based on funding formulas and the state's financial condition. In particular, we saw a significant drop in property tax revenue in 2006 due to the state's buyback of the tax shift. Subsequently, we see an increase in property tax revenue in 2007 as property tax revenue returns to a more normal level. The mix of revenue components from *district to district* varies due to factors such as the strength of property values, mix of property types, operating and bond referendums, enrollment trends, density of population, types of programs offered, and countless other criteria.

The District receives less funding from state sources as compared to the average district. Consequently, the District relies more on property taxes and other funding sources to finance its schools than the average Minnesota school district. The District also receives a considerable amount less in total revenue per student than the average district.

The increase in 2008 of $551 per student is mostly related to increases in state aid, including basic general education aid, school technology and operating capital aid, and special education aid. Increases to property tax revenue include increases for leases and health and safety projects.

The table below reflects comparative data available from the MDE for all expenditures, excluding building construction:

Expenditures per Student (ADM) Served

	State-Wide		Seven-County Metro Area		ISD No. 194 – Lakeville		
	2006	2007	2006	2007	2006	2007	2008
Administration	$ 376	$ 395	$ 366	$ 380	$ 546	$ 538	$ 524
District support services	369	385	378	392	213	222	253
Elementary and secondary regular instruction	4,191	4,362	4,313	4,523	3,785	3,922	3,926
Vocational education instruction	133	131	127	127	53	58	58
Special education instruction	1,632	1,649	1,771	1,815	1,623	1,665	1,683
Instructional support services	405	425	458	481	340	354	330
Pupil support services	741	784	800	857	871	925	813
Sites, buildings, and other	769	782	727	737	781	766	762
Total General Fund operating expenditures	8,616	8,913	8,940	9,312	8,212	8,450	8,349
General Fund capital expenditures	453	451	438	435	189	168	247
Food service	396	415	395	416	428	422	449
Community service	427	446	517	539	459	457	484
Debt service	1,057	1,077	1,125	1,253	1,204	1,399	1,673
Total expenditures	$10,949	$11,302	$11,415	$11,955	$10,492	$10,896	$11,202
ADM served and tuition paid					10,930	11,088	11,142

Note: Excludes Capital Projects – Building Construction Fund, refunding bond debt service activity, Internal Service Fund, and fiduciary funds.

Source of state-wide and seven-county metro area data: School District Profiles Report published by the MDE.

Expenditure patterns also vary from district to district for various reasons. Factors affecting the comparison include the growth cycle or maturity of the district, average employee experience, availability of funding, population density, and even methods of allocating costs.

As the table reflects, the District has traditionally expended less per ADM on general operating costs and total costs than either the state-wide or the seven-county metro area averages. The differences from program to program reflect the District's particular character, such as its community service programs, as well as the fluctuations from year to year for such things as capital expenditures.

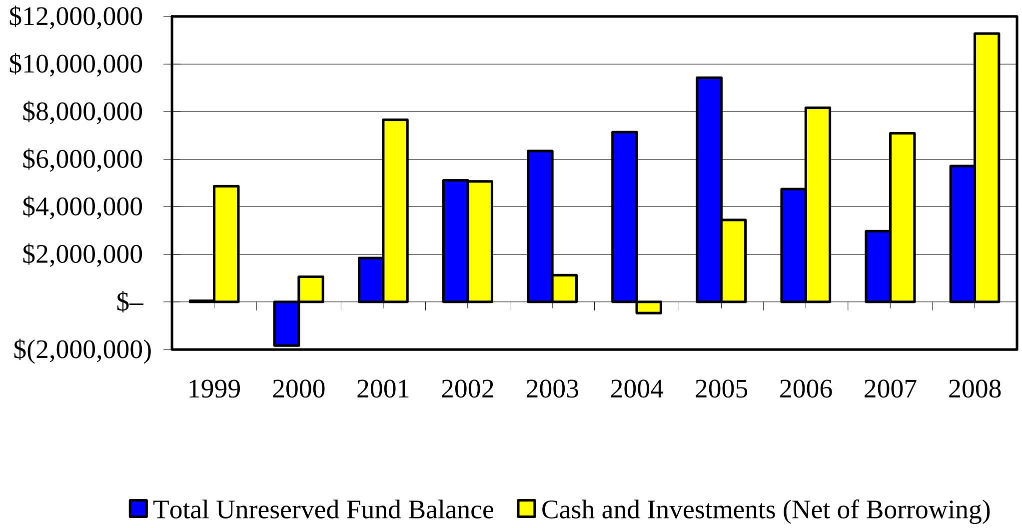
SUMMARY

The funding for and financial position of Minnesota school districts has fluctuated significantly over the past several years due to a number of factors, including those discussed above. This situation has created a challenge for administrators and management of these districts in providing the best education with the limited resources available in a climate of unknown future funding levels.

FINANCIAL TRENDS OF YOUR DISTRICT

GENERAL FUND FINANCIAL POSITION

The following graph displays the District's General Fund trends of financial position. Unreserved fund balance and cash balance are typically used as indicators of financial health or equity.



The District's General Fund ended fiscal year 2008 with unreserved fund balance of $5,715,372, an increase of $2,738,580 from the prior year. The cash and investment balance, net of borrowing at year-end was $11,283,116, up $4,194,238 from the prior year.

The increase in fund balance and cash balance in the General Fund was the result of a planned increase as the District's General Fund budget planned for an increase in total fund balance of about $3,000,000.

The following table presents the components of the General Fund's balance for the past five years:

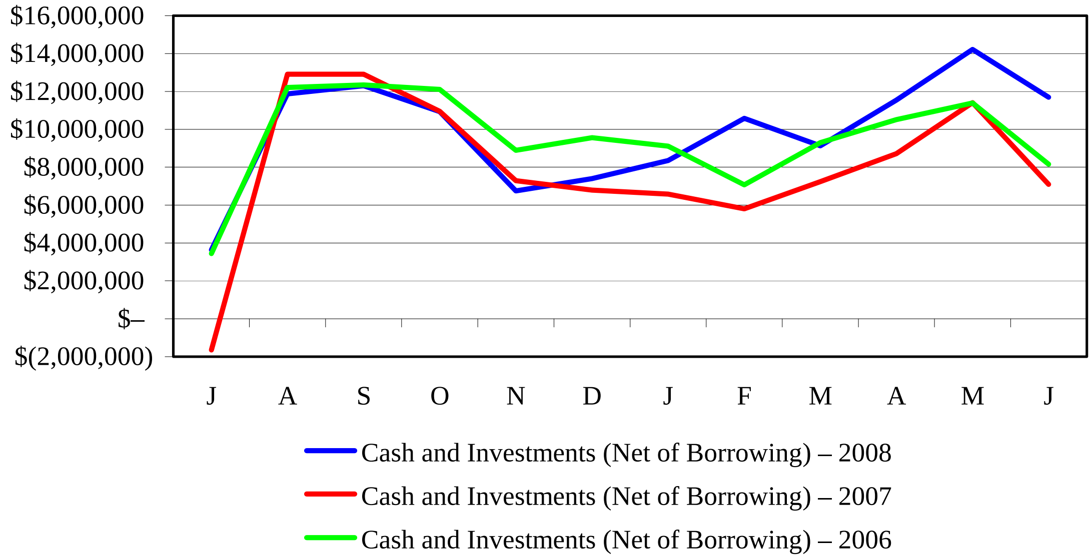
	Year Ended June 30,				
	2004	2005	2006	2007	2008
Reserved fund balance	$ 1,054,281	$ 737,885	$ 1,771,460	$ 1,433,597	$ 1,635,954
Unreserved – designated fund balance	1,866,046	1,913,382	1,849,025	1,804,227	1,893,181
Unreserved – undesignated fund balance	5,272,139	7,511,025	2,890,659	1,172,565	3,822,191
Total fund balance	$ 8,192,466	$ 10,162,292	$ 6,511,144	$ 4,410,389	$ 7,351,326
Unreserved – undesignated fund balance as a percentage of expenditures	6.9%	8.9%	3.1%	1.2%	4.0%
Total unreserved fund balance as a percentage of expenditures	9.4%	11.2%	5.1%	3.1%	6.0%

The table above reflects the total General Fund unreserved fund balance and percentages, which may be different from those used in the previous discussion of state-wide fund balances, which are based on a state formula. The resources represented by this fund balance are critical to a district's ability to maintain adequate cash flow throughout the year, to retain its programs, and to cushion against the impact of unexpected costs or funding shortfalls.

GENERAL FUND CASH FLOW

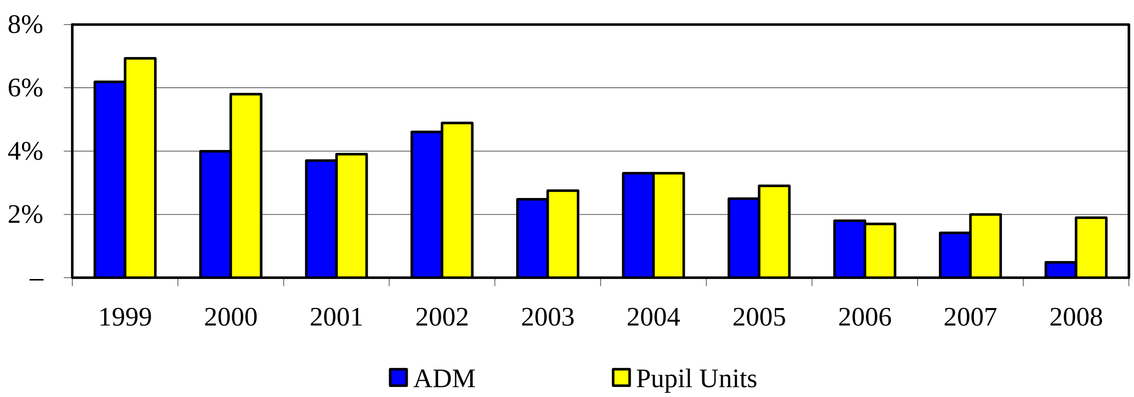
The level of cash and investments varies considerably during the year due to the timing of various revenues and expenditures. The following graph summarizes the level of cash and investments (net of borrowing) over the past three years:

General Fund Cash Flow
Month-End Balances



The graph above shows the peaks and valleys of the General Fund cash and investments balance (net of borrowing) on a monthly basis. The District's cash flow balances during fiscal 2008 were higher than the prior year which was caused by the District having a higher General Fund balance.

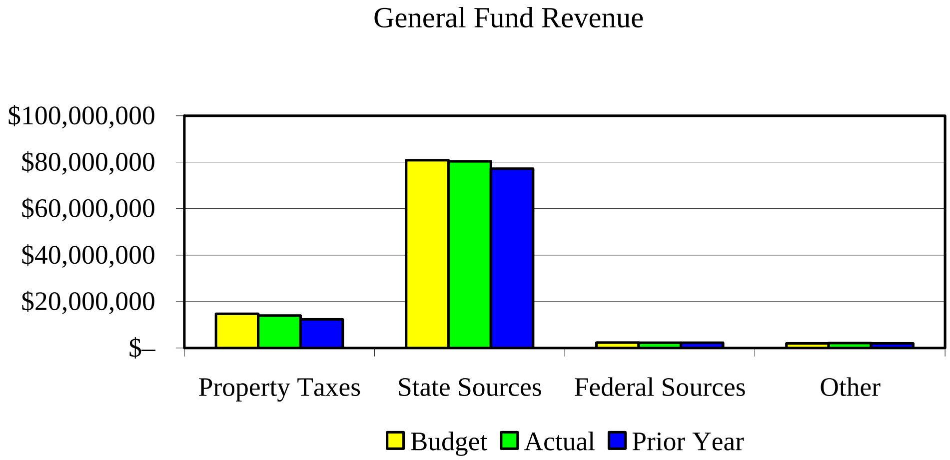
Change in ADM and Pupil Units



ADM is a measure of students attending class, which is then converted to pupil units (the base for determining revenue) using a statutory formula. Not only is the original budget based on ADM estimates, the final audited financial statements are based on updated, but still estimated, ADM since the counts are not finalized until around January of the following year. When viewing revenue budget variances, one needs to consider these ADM changes, the impact of the prior year final adjustments which affect this year's revenue, and also the final adjustments caused by open enrollment gains and losses. The District served an estimated ADM of 11,142 in 2008, an increase of 54 ADM (about 0.5 percent) from the prior year.

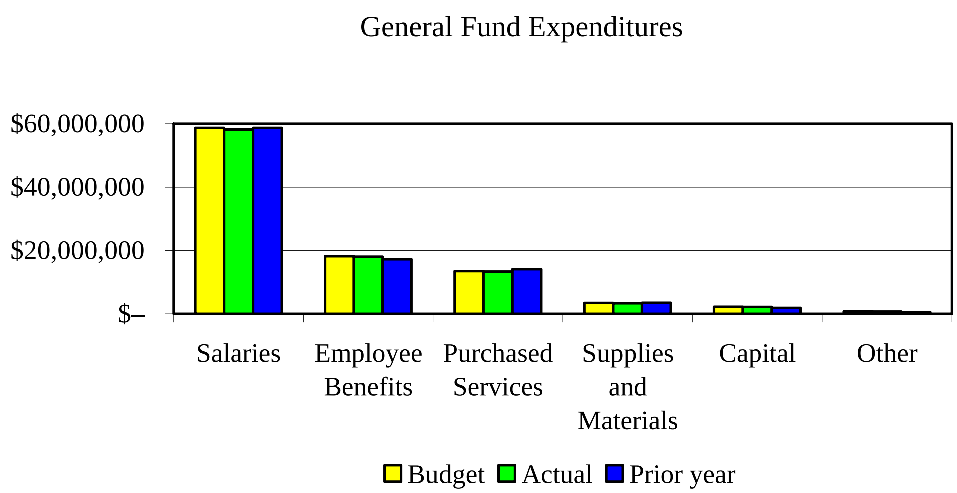
GENERAL FUND REVENUE AND EXPENDITURES

The following graphs summarize the District's General Fund revenue and expenditures for 2007:



Total General Fund revenues for 2008 were $98,718,547, an increase of $4,911,394 from the prior year, and $1,250,566 under budget. A portion of the increase ($1.3 million) in revenues compared to fiscal 2007 is related to an increase in the basic formula allowance in fiscal 2008. Revenues also increased related to increases in general education aid related to the increased student population of about $450,000, increased special education related state aid of about $1,900,000, and increased school technology aid of about $500,000.

Revenues were under budgeted amounts mainly due to special education aid (net of tuition billing costs) being less than budget by nearly $1,000,000.



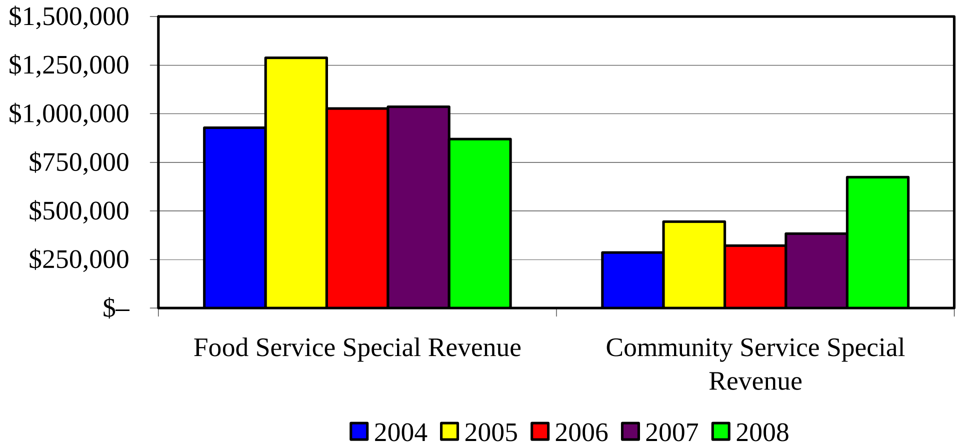
Total General Fund expenditures for 2008 were $95,777,610, a decrease of $131,148 or 0.1 percent from the prior year, and $997,840 or 1.0 percent under budget. The District experienced an expenditure decline due mainly to the decline in transportation costs of nearly $1,000,000 in fiscal 2008.

Expenditures were under budget in most program areas, but most significantly in elementary and secondary regular instruction where expenditures were nearly $500,000 under budgeted amounts.

OTHER GOVERNMENTAL FUNDS

The following graph shows what is referred to as the other operating funds. The remaining non-operating funds are only included in narrative form below, since their level of fund balance can fluctuate significantly due to such things as issuing and spending the proceeds of refunding or building bonds and, therefore, the trend of fund balance levels are not necessarily a key indicator of financial health. It does not mean that these funds cannot experience financial trouble or that their fund balances are unimportant.

Other Governmental Funds
Fund Balances – Last Five Fiscal Years



Food Service Special Revenue Fund

The District's Food Service Special Revenue Fund's financial condition has been stable for the past several years. In 2008, the $166,317 decrease in fund balance was $272,803 better than the planned decrease in fund balance.

Over the years, we have emphasized to our school district clients that food service operations should be self-sustaining, and should not become an additional burden on general education funds. This would include the accumulation of fund balance for future capital improvements to food service facilities and to provide a cushion in the event of a negative trend in operations.

Community Service Special Revenue Fund

The District's Community Service Special Revenue Fund experienced an increase in fund balance of $291,275 for the year ended June 30, 2008, which was $257,303 more than the $33,972 planned increase in fund balance.

The Community Service Special Revenue Fund, like the Food Service Special Revenue Fund, needs to be self-sustaining. In addition to cost controls, financial analysis of the costs of providing programs, including overhead, is important. Fees and tuition charges should be sufficient to cover these costs as well as potential funding shortfalls from state, federal, or property tax sources.

Capital Projects – Building Construction Fund

The District utilized $2,319,809 of capital funds during fiscal 2008 as well as issued $4,000,000 of alternative facility bonds in fiscal 2008. At June 30, 2008, this fund had $3,854,425 of alternative facility funds and $2,115,365 of building bond proceeds available.

Debt Service Fund

The funding of debt service is controlled in accordance with each outstanding debt issue's financing plan.

DISTRICT-WIDE FINANCIAL STATEMENTS

The District's financial statements include fund-based information that focuses on budgetary compliance, and the sufficiency of the District's current assets to finance its current liabilities. The Governmental Accounting Standards Board (GASB) Statement No. 34 reporting model also requires the inclusion of two district-wide financial statements designed to present a clear picture of the District as a single, unified entity. These district-wide statements provide information on the total cost of delivering educational services, including capital assets and long-term liabilities.

Theoretically, net assets represent the resources the District has leftover to use for providing services after its debts are settled. However, those resources are not always in expendable form, or there may be restrictions on how some of those resources can be used. Therefore, the statement divides the net assets into three components: net assets invested in capital assets, net of related debt; restricted net assets; and unrestricted net assets. The following table presents components of the District's net assets at year-end, along with a simplified reconciliation of the difference between the governmental fund balances and total net assets for each of the last three fiscal years:

	June 30,		
	2006	2007	2008
Total fund balances – governmental funds	$ 73,010,906	$ 143,688,596	$ 120,455,651
Net assets – governmental activities			
Capital assets, less accumulated depreciation	151,565,607	145,867,804	140,910,179
Long-term liabilities	(294,965,273)	(363,017,361)	(335,749,955)
Accrued interest payable	(3,650,562)	(5,333,704)	(4,759,308)
Unamortized debt issue discounts	41,323,597	37,081,411	34,985,819
Other	168,882	271,676	399,652
Total net assets – governmental activities	$ (32,546,843)	$ (41,441,578)	$ (43,757,962)
Net assets			
Invested in capital assets, net of related debt	$ (29,181,354)	$ (32,273,825)	$ (35,641,865)
Restricted	2,982,697	2,740,162	3,031,684
Unrestricted	(6,348,186)	(11,907,915)	(11,147,781)
Total net assets	$ (32,546,843)	$ (41,441,578)	$ (43,757,962)

Most of the District's fund balances translate into restricted net assets by virtue of external restrictions (statutory reserves) or by the nature of the fund they are in (e.g. unreserved Food Service Special Revenue Fund balance can only be spent for food service program costs). The unrestricted net assets category consists mainly of the General Fund unreserved fund balances, offset against non-capital long-term obligations such as vacation or severance payable. Consequently, many Minnesota school districts have accumulated deficits in this component of net assets.

Total net assets decreased by $2,316,384. The unrestricted portion increased by $760,134, primarily due to the increase in the General Fund balance which was offset by increases in severance and health benefit obligations. The decline in invested in capital assets, net of related debt is the result of the amortization of large amounts of deep discount debt the District has outstanding.

ACCOUNTING AND REPORTING UPDATES

GASB STATEMENT NO. 45 – ACCOUNTING AND FINANCIAL REPORTING BY EMPLOYERS FOR POST-EMPLOYMENT BENEFITS OTHER THAN PENSIONS

This statement provides new guidance on accounting and reporting for post-employment benefits other than pensions by employers when the plan is not accounted for in their financial statements.

Other post-employment benefits (OPEB) refer to non-pension benefits provided after the termination of employment. One example of this type of benefit is healthcare premiums paid by employers on behalf of former employees. Governmental entities have traditionally accounted for OPEB on a pay-as-you-go basis, with only a few governments funding these benefits in advance of payment. The guidance in this statement rests on the assumption that OPEB liabilities should be accrued as they are earned by employees providing service to the entity.

Under GASB Statement No. 45, governments offering OPEB will recognize the cost of these benefits using a three-step approach. The government will be required to project future benefits, discount those benefits to their present value, then use an acceptable actuarial method to allocate costs to individual accounting periods.

Once calculated, the difference between the present value of OPEB benefits earned by employees as the result of past service and resources set aside to pay those benefits will be considered the "unfunded actuarial liability for OPEB." Every employer will be allowed to start fresh at the time of transition to the new standard. There will be no requirement for an employer to recognize an accounting liability for underfunding prior to the implementation of the new standard. Instead, the unfunded actuarial accrued liability for OPEB at transition would be amortized over 30 years. As long as an employer funds the full amount of the actuarially determined annual required contribution (ARC) for these benefits each year, no asset or liability will be reported on the Statement of Net Assets. However, an employer will need to report a "net pension obligation" on its Statement of Net Assets as an asset or liability if it contributes more or less, respectively, than the ARC each year.

Nothing in the statement is intended to alter the normal application of modified accrual accounting in the governmental funds of the entity. Thus, in governmental funds, OPEB expenditures normally would be recognized when the benefits are due and payable rather than when benefits are earned.

The guidance will require that actuarial valuations for OPEB occur at least every two years for plans with 200 or more members, and every three years for plans with fewer than 200 members. A sole employer plan with fewer than 100 plan members has the option to apply a simplified alternative measurement method rather than obtain actuarial valuations.

The statement will become effective in three phases based on the same criteria as those defined for the implementation of GASB Statement No. 34. GASB Statement No.45 will be phased in for districts over a three-year period, which started with category one districts in the fiscal year ending June 30, 2008.

GASB STATEMENT NO. 47 – ACCOUNTING FOR TERMINATION BENEFITS

GASB Statement No. 47 provides accounting and reporting guidance for state and local governments that offer benefits such as early retirement incentives or severance to employees that are involuntarily terminated. The statement requires that similar forms of termination benefits be accounted for in the same manner and is intended to enhance both the consistency of reporting for termination benefits and the comparability of financial statements.

GASB Statement No. 47 is effective for financial statements for periods beginning after June 15, 2005, or may be implemented simultaneously with GASB Statement No. 45, depending on your circumstances.

GASB STATEMENT NO. 50 – PENSION DISCLOSURES – AN AMENDMENT OF GASB STATEMENT NOS. 25 AND 27

This statement expands the disclosure requirements for pension plans, similar to those requirements in GASB Statement Nos. 43 and 45. This will require additional discussion on funding status, use of assumptions, and the determination of contribution rates. This statement is effective for school districts for the year ended June 30, 2008.

LEGISLATIVE SUMMARY

The following is a brief summary of current legislative changes and issues affecting the funding of Minnesota school districts. More detailed and extensive summaries are available from the MDE.

Basic General Education Revenue – The basic general education formula allowance for fiscal year (FY) 2008 increased by $100 (2 percent) per adjusted marginal cost pupil unit (AMCPU) and will increase $50 (1 percent) in FY 2009.

One-Time General Education Revenue Increase – FY 2009 Only – Provides additional general education aid for FY 2009 only equal to $51 times the school district or charter school's AMCPU. This is equivalent to a 1 percent increase in the general education formula, except that this one-time increase is not linked to other formulas that use the general education formula allowance.

Kindergarten Pupil Unit Weighting – The pupil unit weighting for kindergarten increased from 0.557 to 0.612 in FY 2008.

Gifted and Talented Revenue – The gifted and talented revenue increased from $9 in FY 2007 to $12 in FY 2008 per AMCPU. Districts now must adopt procedures for the academic acceleration of gifted and talented students.

Alternative Teacher Compensation Revenue (Q Comp) – For districts that did not apply for alternative teacher compensation aid by March 20, 2008, the entitlement is limited to $11,397,000 for FY 2009 and for those not qualifying for aid in FY 2009, the limit will be $2,899,000 for FY 2010. Eligibility will be determined on a first-come first-serve basis.

The limit on Basic Q Comp aid returns to the full amount authorized by legislation of $75,636,000 for FY 2011 and later.

Equity Revenue – Beginning in FY 2008, districts with referendum revenue per AMCPU above the regional 95th percentile receive the same equity revenue as other districts, an increase from $23 to $46 per AMCPU.

Alternative Attendance Adjustment – This is a change, beginning in FY 2008, in the calculation of the revenue adjustment for serving districts under open enrollment. This will increase the revenue for certain serving districts meeting various criteria, including cases with open enrollment exceeding 20 percent of resident students.

Tax Base Replacement Aid – Beginning in FY 2008, the tax base replacement aid is rolled into general education aid.

One-Time Transfer From the Operating Capital Reserve Account – Districts were allowed to transfer on June 30, 2008, up to $51 per FY 2007 AMCPU, from the operating capital reserved fund balance to its unreserved General Fund balance.

Repeal of the Endowment Fund Reduction – Beginning in FY 2010, districts will no longer receive a reduction in their general education aid by the amount of endowment payments received. This will have the effect of increasing general education aid by $36 per resident ADM for FY 2010.

School Technology and Operating Capital Aid – Qualifies all school districts for technology and operating capital aid equal to $40 per AMCPU for FY 2008 and $55 per AMCPU for FY 2009. The aid must be used only for the purposes authorized for operating capital revenue.

Repeal of Advance Final Payment for Districts in SOD – Districts in SOD will no longer be able to receive an advance on their final state aid payment beginning in FY 2009.

Safe Schools Levy – Beginning for taxes payable in 2008 (revenue in FY 2009), the safe schools levy is increased from $27 to $30 per AMCPU. Districts that are members of an intermediate district can levy $10 per AMCPU, which is then passed on to the intermediate district. Districts are required to set aside $3 per AMCPU for specific costs and annual certifications on spending are required beginning in FY 2010.

Career and Technical Levy – The funding for career and technical programs is changed beginning with the tax levy payable in 2008. Districts with approved programs may levy the lesser of $80 per ADM in Grades 10 through 12 or 25 percent of approved expenditures.

Referendum Equalization – For FY 2008, the first tier of referendum equalization was increased from $600 to $700 per resident marginal cost pupil unit (RMCPU).

Special Education and Related Aids – Beginning in FY 2008, the special education–regular and transition–disabled aid formulas are based on current year expenditures rather than the second prior year expenditures. The state-wide funding caps for these two programs are now combined and, together with expanded funding for Part C services, the state-wide imputed growth factors are 27.5 percent for FY 2008, 3.8 percent for FY 2009, 1.9 percent for FY 2010, 6.6 percent for FY 2011, and 4.6 percent per year after that. The state-wide proration factor for special education–regular funding is projected to be 89 percent for FY 2008 and 88 percent for FY 2009.

Beginning in FY 2008, transition–disabled is included in the formula, and the state-wide imputed growth factors in funding are 5.2 percent for FY 2008, zero percent for FY 2009 through FY 2011, and capped at 2 percent per year after that.

Deferred Maintenance Revenue – Beginning in FY 2008, an equalized deferred maintenance levy is available for smaller districts that do not qualify for the alternative facilities bonding and levy program.

Building Lease Levy – The maximum building lease levy is increased from $100 to $150 per RMCPU. Also, for districts that are members of intermediate districts, the additional building lease for their programs increases from $25 to $43 per AMCPU.

Ice Arena Levy – The ice arena levy is increased from 90 percent to 100 percent of the operating costs of the arena.

Capital Facilities Bonds – The maximum term of these bonds is extended from 10 years to 15 years and their use now includes modifying buildings and equipment for security.

Kindergarten Milk – Reimbursement for kindergarten milk, not included with school lunch or breakfast programs, increases from 14 cents to 20 cents per half-pint.

Food Service Reimbursements – School lunch reimbursement increased from 10.5 cents to 12 cents for all students in FY 2008.

Development Screening Aid – Screening aid is increased from $50 to $75 per child at age 3, $40 to $50 at age 4, and $30 to $40 at age 5 or pre-kindergarten age 6.

Intermediate School District Borrowing – Intermediate school districts are now allowed to borrow against expected receipts of state aids, federal aids, membership fees, and tuition payments from member districts. This requires a resolution from each member district pledging their full faith, credit, and full taxing powers to repay the borrowing.

Contracting Threshold Limits – Effective August 1, 2008 the requirement to obtain sealed bids on contracts is increased from $50,000 to $100,000. The thresholds for contracts that require a sealed bid or by direct negotiation after receiving two or more quotes is increased from current law on those estimated between $10,000 and $50,000 to $25,000 and $100,000. The current law for a contract to be made either upon quotation or in the open market estimated is increased for contracts of $10,000 or less to $25,000 or less.

OPEB Funding – New legislation approved in 2008 created new opportunities related to school finance. This new legislation has three main components:

- It allows governments, including school districts, to establish trust (either revocable or irrevocable trusts) to fund OPEB costs and liabilities.
- It permits funds in the trusts to be invested in stocks and other investments that are not allowed for other governmental funds, and which present both greater risk and opportunities for higher long-term rates of return.
- It allows local governments to issue bonds, without voter approval, to fund their OPEB liabilities; payments on the bonds would be financed through additional property tax levies.
- Validates existing trusts created prior to June 2006 to pay OPEB benefits.

Employee Benefit Plans – Makes the identity and number of vendors for tax sheltered annuity plans a term and condition of employment and subject to the negotiations process. Each district's exclusive representative must consider all vendors' ability to comply with IRS regulations, experience in providing 403(b) plans, and factors related to rights and benefits offered under the vendor's plan.