

HILLSDALE COMMUNITY SCHOOLS
FINANCIAL STATEMENTS
AND INDEPENDENT AUDITOR'S REPORT
(with required supplementary information)
YEAR ENDED JUNE 30, 2007

HILLSDALE COMMUNITY SCHOOLS

HILLSDALE, MICHIGAN

BOARD OF EDUCATION

JUNE 30, 2007

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HILLSDALE COMMUNITY SCHOOLS

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Osbourne, March, Condon & Co., P.C.

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INDEPENDENT AUDITOR'S REPORT

Board of Education
Hillsdale Community Schools
Hillsdale, Michigan

We have audited the accompanying financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Hillsdale Community Schools, Hillsdale, Michigan, as of and for the year ended June 30, 2007, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of the School District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, each major fund, and the aggregate remaining fund information of Hillsdale Community Schools, as of June 30, 2007, and the respective changes in financial position for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued our report dated October 11, 2007, on our consideration of the School District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grants. Those reports are an integral part of the audit and of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The management's discussion and analysis and budgetary comparison information on pages iii through ix and page 21 are not a required part of the basic financial statements but are supplementary information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the method of measurement and presentation of the supplementary information. However, we did not audit the information and express no opinion on it.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Hillsdale Community School's basic financial statements. The additional information on pages 22 - 23 is presented for purposes of additional analysis and is not a required part of the basic financial statements. The accompanying schedule of expenditures of federal awards on pages 24 - 26 are presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is not a required part of the basic financial statements of Hillsdale Community Schools. This additional information has been subjected to the auditing procedures applied in the audit of the basic financial statements, and in our opinion, is fairly stated in all material respects in relation to the basic financial statements taken as a whole.

Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

Hillsdale, Michigan
October 11, 2007

Hillsdale Community Schools

Management's Discussion and Analysis Year Ended June 30, 2007

This section of Hillsdale Community School's annual financial report presents our discussion and analysis of the School District's financial performance during the year ended June 30, 2007. Please read it in conjunction with the School District's financial statements, which immediately follow this section.

This annual report consists of a series of financial statements and notes. These statements are organized so the reader can understand Hillsdale Community Schools financially as a whole. The district wide financial statements provide information about the activities of the whole school district presenting both an aggregate view of the School District's finances and a longer-term view of those finances. The fund financial statements look at the School District's operations in more detail than the district wide financial statements by providing information about the district's most significant funds.

DISTRICT WIDE FINANCIAL STATEMENTS

The District wide financial statements are full accrual basis statements, which is similar to the accounting used by most private-sector companies. They report all of the District's assets and liabilities, both short and long-term, regardless if they are "currently available" or not. For example assets that are restricted for use in the Debt Funds solely for the payment of long term principal or interest are grouped with unrestricted assets of the General Fund. Capital assets and long-term obligations of the District are reported in the Statement of Net Assets of the District wide financial statements.

FUND FINANCIAL STATEMENTS

The fund level financial statements are reported on a modified accrual basis. Only those assets that are "measurable" and "currently available" are reported. Liabilities are recognized to the extent that they are normally expected to be paid with current financial resources.

The fund statements are formatted to comply with the legal requirements of the Michigan Department of Education's "Accounting Manual." In the State of Michigan, the District's major instructional and instructional support activities are reported in the General Fund. Additional activities are reported in their relevant funds including: Debt Funds and the School Service Funds which are comprised of: Food Service and Athletic Funds.

In the fund financial statements, purchased capital assets are reported as expenditures in the year of acquisition. No asset is reported. The issuance of debt is recorded as a financial resource. The current year's payments of principal and interest on long-term obligations are recorded as expenditures. Future year's debt obligations are not recorded.

Hillsdale Community Schools

Management's Discussion and Analysis Year Ended June 30, 2007

SUMMARY OF NET ASSETS

The following summarizes the net assets at fiscal years ended June 30, 2007 and 2006.

	2007	2006
Assets		
Current assets	\$ 5,907,226	\$ 5,142,483
Capital assets	\$ 20,776,009	\$ 20,193,478
Less: accumulated depreciation	(11,056,116)	(10,250,491)
Capital assets, net book value	\$ 9,719,893	\$ 9,942,987
Total Assets	<u>\$ 15,627,119</u>	<u>\$ 15,085,470</u>
Liabilities		
Current liabilities	\$ 4,935,830	\$ 4,922,093
Long-term liabilities	\$ 2,970,898	\$ 3,485,572
Total liabilities	<u>\$ 7,906,728</u>	<u>\$ 8,407,665</u>
Net Assets		
Invested in capital assets, net of related debt	\$ 6,648,765	\$ 6,276,285
Restricted for sinking fund expenditures	706,695	606,284
Restricted for debt service	234,151	192,150
Unrestricted (deficit)	130,780	(396,914)
Net Assets	<u>\$ 7,720,391</u>	<u>\$ 6,677,805</u>
Total Liabilities and Net Assets	<u>\$15,627,119</u>	<u>\$ 15,085,470</u>

Hillsdale Community Schools

Management's Discussion and Analysis Year Ended June 30, 2007

RESULTS OF OPERATIONS

The following is the District wide results of operations for the fiscal year ended June 30, 2007 and 2006:

	June 30, 2007	June 30, 2006
REVENUE		
General Revenue:		
Property taxes	\$ 3,611,327	\$ 3,479,248
State foundation allowance	10,105,436	9,980,435
Other	<u>176,451</u>	<u>164,457</u>
Total General Revenue	<u>\$ 13,893,214</u>	<u>\$ 13,624,140</u>
Operating Grants:		
Federal	\$ 794,610	\$ 998,663
State of Michigan	1,304,152	1,150,273
Other operating grants	<u>187,849</u>	<u>38,775</u>
Total Operating Grants	<u>\$ 2,286,611</u>	<u>\$ 2,187,711</u>
Charges for Services:		
Food Service	\$ 281,450	\$ 308,846
Other charges for service	<u>242,718</u>	<u>394,211</u>
Total Charges for Services	<u>\$ 517,718</u>	<u>\$ 703,057</u>
TOTAL REVENUE	<u>\$ 16,697,543</u>	<u>\$ 16,514,908</u>
EXPENSES		
Instruction and instructional support	\$ 10,796,235	\$ 11,502,844
Supporting services	2,778,892	2,842,562
Food Services	750,219	765,977
Athletics	361,345	361,542
Interest on long-term debt	127,597	145,333
Depreciation (unallocated)	<u>805,625</u>	<u>811,004</u>
TOTAL EXPENSES	<u>\$ 15,626,363</u>	<u>\$ 16,429,262</u>
SPECIAL ITEMS		
Proceeds from sale of property	\$	\$ 601,302
Termination benefits expense	<u>(28,594)</u>	<u>(314,534)</u>
TOTAL SPECIAL ITEMS	<u>\$ (28,594)</u>	<u>\$ 286,768</u>
INCREASE IN NET ASSETS	\$ 1,042,586	\$ 372,414
NET ASSETS – BEGINNING	<u>6,677,805</u>	<u>6,305,391</u>
NET ASSETS – ENDING	<u>\$ 7,720,391</u>	<u>\$ 6,677,805</u>

Hillsdale Community Schools

Management's Discussion and Analysis Year Ended June 30, 2007

ANALYSIS OF FINANCIAL POSITION – DISTRICT WIDE

During fiscal year ended June 30, 2007, the District's net assets increased by \$1,042,586 to \$7,720,391. The significant factors affecting net assets during the year are: The financial investments that the General Fund and Building and Site funds were able to maintain through the entire school year. The certificate of deposit interest rates were 5.0% or higher through out the fiscal year. State aid allowance increased for the year. New this year is the equity payment for school districts that showed declining enrollment. Outstanding debt continued to decline with the principal payments and the pay off of two bus loans. On the General Fund expenditures the district kept spending down (3.24%) through the last half of the school year. Other items include improvements at the High School – updated the concession stand and repaired the football field bleachers, landscaping in front of the High School along with Central Office; David Middle School - upgrades in the bathrooms; Gier Elementary – repaired the fascia and soffit on the exterior of the building; Maintenance building built a new structure and renovated the Transportation Center. These projects were down (4.78%) from the previous year. Food service sales were up along with the investment income. Athletic department revenue from tournaments and gate receipts increased due to holding more tournaments and a winning season in football and boys basketball.

Outstanding Long-Term Debt

The District made principal payments on bonded, long-term debt obligations that reduced the amount of the District's long-term liabilities as follows:

	PRINCIPAL BALANCE June 30, 2006	ADDITIONS	PRINCIPAL PAYMENTS/ ADJUSTMENTS	PRINCIPAL BALANCE June 30, 2007
Bonds	\$ 3,445,507	\$	\$ 460,000	\$ 2,985,507
Bus Notes	197,145		118,141	79,004
Capital Leases	24,050		17,433	6,617
Early Retirement Incentive	314,534	28,594	108,840	234,288
	<u>\$ 3,981,236</u>	<u>\$ 28,594</u>	<u>\$ 704,414</u>	<u>\$ 3,305,416</u>

Net Investment in Capital Assets

The District's net investment in capital assets increased during the fiscal year. This can be summarized as follows:

	BALANCE June 30, 2006	ADDITIONS	DELETIONS	BALANCE June 30, 2007
Capital Assets	\$ 20,193,478	\$ 582,531	\$	\$ 20,776,009
Less: Accumulated depreciation	(10,250,491)	(805,625)		(11,056,116)
	<u>\$ 9,942,987</u>	<u>\$ (223,094)</u>	<u>\$</u>	<u>\$ 9,719,893</u>

Hillsdale Community Schools

Management's Discussion and Analysis Year Ended June 30, 2007

MAJOR GOVERNMENTAL FUNDS BUDGETING AND OPERATING HIGHLIGHTS

General Fund

The District's revenues for General Fund operations exceeded expenditures by \$441,465 for fiscal year ended June 30, 2007.

	Original Budget	Final Budget	Actual
Total Revenues and transfers	<u>\$ 14,724,819</u>	<u>\$ 14,626,426</u>	<u>\$ 14,501,119</u>
Total Expenditures and transfers	<u>\$ 14,630,053</u>	<u>\$ 14,531,812</u>	<u>\$ 14,059,655</u>

The final revenue budget reflects the following changes from the original budget:

- Adjustments were made with the decrease of local tax revenue due to reduction in SEV
- The District increased interest earned on investments by \$49,000
- The State revenue decreased due to FTE adjustments with student count
- Increased State revenue to add MS Math/Science funding of \$18,987
- Increased At Risk funding by \$35,006
- Increased Special Education Funding by \$50,947
- Decreased Federal grants by \$43,862
- Reduced HCISD Vocational CTE Programs by \$16,707 due to the less tax collection
- Increased Medbill funding by \$10,123
- Reduced contribution from Food Service

The final expenditure budget reflects the following changes from original budget:

- The District adjusted the following staff:
 - Added a Third and Fifth grade section
 - Moved a Kindergarten teacher to At Risk funding
 - General Education teacher on a long term medical leave and two teachers on maternity leave
 - Resignation of Alternative Education teacher, replaced with teacher called back from lay off
 - Adjusted Principal to Contract Ed (third party contract)
 - Transportation secretary not replaced for the balance of the school year
- The district put a freeze on building supplies due to the talk of a pro-ration at from the State Aid office
- Increased the athletic Transfer for year end expenses
- Increased expenses to HCISD for services
- Accrued unemployment liability for the year
- Adjusted utilities due to the mild weather in November and December

Actual expenditures were less than the final budget resulting from adjustments and less spending made by the School District.

Hillsdale Community Schools

Management's Discussion and Analysis Year Ended June 30, 2007

Building & Site Sinking Fund

	Original Budget	Final Budget	Actual
Total Revenues and transfers	\$ <u>685,463</u>	\$ <u>720,903</u>	\$ <u>725,960</u>
Total Expenditures and transfers	\$ <u>676,218</u>	\$ <u>656,918</u>	\$ <u>625,549</u>

The District's sinking fund levy, which is used towards school buildings and site improvements, is based on the taxable valuation of all properties; homestead and non-homestead. For 2006-2007, the District's sinking fund tax levy was based on 1.9988 mills that generated revenue of \$666,312.

Expenditures are limited to those allowable by the Revised School Code, and vary according to the District's capital plan.

OTHER NONMAJOR FUNDS OPERATING HIGHLIGHTS

Debt Service

The District's debt fund levy, which is used to pay the principal and interest on bond obligations, is based on the taxable valuation of all properties; homestead and non-homestead. For 2006-2007, the District's debt tax levy was based on 1.85 mills that generated revenue of \$613,349. The debt levy of 1.85 mills is .21 mills less than the Board of Education approved levy of 2.06 mills.

Food Service

The District's food and milk sales to students and adults decreased from the prior school year by approximately \$29,034 to \$260,045. In addition, there was a decrease in revenues (21%) from the a-la-carte menu. The total number of meals served per day up 21 meals compared to the 2005-06 school year.

Athletics

Athletic revenue from tournaments and gate receipts increased over the prior year, due to holding more tournaments and a winning season in football and boys basketball.

STUDENT ENROLLMENT

The District's student enrollment for the fall count of 2006-2007 was 1,809.85 students. The District's enrollment decreased from the prior school year's student count. The following summarizes fall student enrollments in the past eight years:

	<u>Student FTE</u>	<u>FTE Change from Prior Year</u>
2006-2007	1809	(52)
2005-2006	1861	(39)
2004-2005	1900	(39)
2003-2004	1939	(29)
2002-2003	1968	6
2001-2002	1962	54
2000-2001	1908	(73)
1999-2000	1981	(49)

FACTORS BEARING ON THE DISTRICT'S FUTURE

- State Aid funding for the 2007-08 school year has not been determined.
- Student enrollment is not known at this time.
- Contracts for teachers and support staff for the 2007-08 year are currently in negotiations

CONTACTING THE SCHOOL DISTRICT'S MANAGEMENT

This financial report is designed to provide the School District's citizens, taxpayers, customers, and investors and creditors with a general overview of the School District's finances and to demonstrate the School District's accountability for the money it receives. If you have questions about this report or need additional financial information, contact the Business Department; 30 South Norwood Avenue; Hillsdale, Michigan 49242.

HILLSDALE COMMUNITY SCHOOLS

STATEMENT OF NET ASSETS

JUNE 30, 2007

	TOTAL GOVERNMENTAL FUNDS
ASSETS	
Current Assets	
Cash and deposits	\$ 3,813,226
Investments	34,565
Accounts receivable	51,233
Prepaid expenses	34,236
Due from Agency funds	5,037
Due from other governmental units	1,955,655
Inventory	<u>13,274</u>
Total Current Assets	<u>\$ 5,907,226</u>
Noncurrent Assets	
Capital assets	\$ 20,776,009
Less: accumulated depreciation	<u>11,056,116</u>
Total Noncurrent Assets	<u>\$ 9,719,893</u>
TOTAL ASSETS	<u><u>\$ 15,627,119</u></u>
LIABILITIES AND NET ASSETS	
Current Liabilities	
Accounts payable	\$ 746,602
Note payable - tax anticipation	2,400,000
Accrued salaries and payroll taxes	1,077,485
Deferred revenue	39,403
Accrued interest	127,211
Long-term debt, current portion	<u>662,273</u>
Total Current Liabilities	<u>\$ 5,052,974</u>
Noncurrent Liabilities	
Long-term debt	\$ 3,305,416
Compensated absences	210,611
Less: current portion of long-term debt	<u>(662,273)</u>
Total Noncurrent Liabilities	<u>\$ 2,853,754</u>
TOTAL LIABILITIES	<u>\$ 7,906,728</u>
Net Assets	
Invested in capital assets, net of related debt	\$ 6,648,765
Restricted	940,846
Unrestricted	<u>130,780</u>
TOTAL NET ASSETS	<u>\$ 7,720,391</u>
TOTAL NET ASSETS AND LIABILITIES	<u><u>\$ 15,627,119</u></u>

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

HILLSDALE COMMUNITY SCHOOLS

STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2007

	<u>PROGRAM REVENUES</u>		<u>GOVERNMENTAL ACTIVITIES</u>
	EXPENSES	CHARGES FOR SERVICES	OPERATING GRANTS
			NET (EXPENSE) REVENUE AND CHANGES IN NET ASSETS
GOVERNMENTAL ACTIVITIES			
Instruction:			
Basic instruction	\$ 7,090,506	\$ 27,096	\$ 404,446
Added needs	2,006,455		1,310,195
Adult education	34,664	95	49,914
Instructional support:			
Pupil support	339,859		
Instructional staff	233,588		37,719
School administration	1,101,994		
Non-instructional support:			
General administration	332,591	3,951	
Business services	326,468	9,927	
Operations and maintenance	1,212,875	9,680	
Transportation	686,410	83,925	
Other non-instructional support	124,674		9,186
Community services	2,069		
Food services	750,219	281,450	466,707
Athletics	361,345	108,044	8,444
Interest on long-term debt	127,597		
Capital outlay	95,874		
Depreciation (unallocated)	805,625		
	<u>\$ 15,632,813</u>	<u>\$ 524,168</u>	<u>\$ 2,286,611</u>
TOTAL GOVERNMENTAL ACTIVITIES			<u>\$ (12,822,034)</u>
 GENERAL REVENUES			
Property taxes, levied for general operations			\$ 2,331,666
Property taxes, levied for debt service			613,349
Property taxes, levied for building and site improvements			666,312
State of Michigan aid, unrestricted			10,105,436
Interest and investment earnings			148,786
Other			27,665
			<u>\$ 13,893,214</u>
 SPECIAL ITEMS:			
Termination benefits expense			\$ (28,594)
 CHANGE IN NET ASSETS			
			1,042,586
 NET ASSETS - BEGINNING OF YEAR			
			<u>\$ 6,677,805</u>
 NET ASSETS - ENDING			
			<u>\$ 7,720,391</u>

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

HILLSDALE COMMUNITY SCHOOLS
GOVERNMENTAL FUNDS BALANCE SHEET

JUNE 30, 2007

	GENERAL	BUILDING AND SITE SINKING FUND	OTHER NONMAJOR FUNDS	TOTAL GOVERNMENTAL FUNDS
ASSETS				
Cash and deposits	\$ 2,787,980	\$ 783,912	\$ 242,712	\$ 3,814,604
Investments	7,225	15,233	10,929	33,387
Accounts receivable	40,818		3,291	44,109
Other deposits			33,000	33,000
Prepaid expenses	1,036			1,036
Due from other funds	17,147		5,037	22,184
Due from other governmental units	1,955,655		7,125	1,962,780
Inventory			13,274	13,274
	<u>\$ 4,809,861</u>	<u>\$ 799,145</u>	<u>\$ 315,368</u>	<u>\$ 5,924,374</u>
LIABILITIES AND FUND BALANCES				
Liabilities				
Accounts payable	\$ 648,468	\$ 92,450	\$ 5,684	\$ 746,602
Accrued payroll	1,044,692		32,793	1,077,485
Accrued interest	88,811			88,811
Deferred revenue	39,403			39,403
Due to other funds			17,147	17,147
Note payable - tax anticipation	2,400,000			2,400,000
	<u>\$ 4,221,374</u>	<u>\$ 92,450</u>	<u>\$ 55,624</u>	<u>\$ 4,369,448</u>
Fund Balances				
Reserved	\$ 588,487	\$ 706,695	\$ 247,425	\$ 954,120
Unreserved, undesignated	588,487		12,319	600,806
	<u>\$ 588,487</u>	<u>\$ 706,695</u>	<u>\$ 259,744</u>	<u>\$ 1,554,926</u>
	<u>\$ 4,809,861</u>	<u>\$ 799,145</u>	<u>\$ 315,368</u>	<u>\$ 5,924,374</u>

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

HILLSDALE COMMUNITY SCHOOLS

RECONCILIATION OF THE GOVERNMENTAL FUNDS BALANCE SHEET
TO THE STATEMENT OF NET ASSETS

YEAR ENDED JUNE 30, 2007

TOTAL GOVERNMENTAL FUND BALANCES		\$	1,554,926
Amounts reported for governmental activities in the statement of net assets are different because:			
Capital assets used in governmental activities are not financial resources, and are not reported in the funds:			
Cost of capital assets	\$	20,776,009	
Accumulated depreciation		<u>(11,056,116)</u>	
			9,719,893
Long-term liabilities are not due and payable in the current period and are not reported in the funds:			
Bonds payable			(2,985,506)
Notes and leases			(85,622)
Compensated absences			(210,611)
Early retirement incentive			(234,288)
Accrued interest on long-term liabilities is not included as a liability in governmental funds, it is recorded when paid			<u>(38,401)</u>
NET ASSETS OF GOVERNMENTAL ACTIVITIES		\$	<u>7,720,391</u>

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

HILLSDALE COMMUNITY SCHOOLS

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
GOVERNMENTAL FUNDS

YEAR ENDED JUNE 30, 2007

	GENERAL	BUILDING AND SITE SINKING FUND	OTHER NON MAJOR FUNDS	TOTAL GOVERNMENTAL FUNDS
REVENUES				
Local sources	\$ 2,731,758	\$ 697,321	\$ 1,004,837	\$ 4,433,916
State sources	11,333,640		46,344	11,379,984
Federal sources	403,850		420,363	824,213
Other sources	31,871	3,639	30,373	65,883
TOTAL REVENUES	\$ 14,501,119	\$ 700,960	\$ 1,501,917	\$ 16,703,996
EXPENDITURES				
Basic Instruction	\$ 7,236,803	\$	\$	\$ 7,236,803
Added needs	2,031,069			2,031,069
Adult education	34,664			34,664
Pupil support	339,859			339,859
Instructional staff support	233,588			233,588
School administration	1,101,994			1,101,994
General administration	332,591			332,591
Business services	326,468	987		327,455
Operations and maintenance	1,208,754			1,208,754
Transportation	686,409			686,409
Other support services	123,687			123,687
Community services	2,068			2,068
Food service			750,220	750,220
Athletics			361,345	361,345
Capital outlay		624,562	4,615	629,177
Debt services				
Principal			460,000	460,000
Interest			128,562	128,562
TOTAL EXPENDITURES	\$ 13,657,954	\$ 625,549	\$ 1,704,742	\$ 15,988,245
REVENUES OVER (UNDER) EXPENDITURES	\$ 843,165	\$ 75,411	\$ (202,825)	\$ 715,751
OTHER FINANCING SOURCES (USES)				
Operating transfers in	\$	\$ 25,000	\$ 252,189	\$ 277,189
Capital lease proceeds				
Loan proceeds				
Proceeds from sale of assets				
Payments on capital leases	(124,511)			(124,511)
Payments on loans				
Operating transfers out	(277,189)			(277,189)
TOTAL OTHER FINANCING SOURCES AND (USES)	\$ (401,700)	\$ 25,000	\$ 252,189	\$ (124,511)
NET CHANGE IN FUND BALANCES	\$ 441,465	\$ 100,411	\$ 49,364	\$ 591,240
FUND BALANCES - BEGINNING	147,022	606,284	210,380	963,686
FUND BALANCES - ENDING	\$ 588,487	\$ 706,695	\$ 259,744	\$ 1,554,926

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

HILLSDALE COMMUNITY SCHOOLS

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES OF GOVERNMENTAL FUNDS
TO THE STATEMENT OF ACTIVITIES

YEAR ENDED JUNE 30, 2007

NET CHANGE IN FUND BALANCES - TOTAL GOVERNMENTAL FUNDS \$ 591,240

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

Capital outlays are reported as expenditures in governmental funds. However, in the statement of activities, the cost of capital assets is allocated over their estimated useful lives as depreciation expense. In the current period, these amounts were:

Depreciation expense	(805,625)
Capital outlay	582,531

Repayment of long-term debt is reported as an expenditure in governmental funds, but it reduces long-term liabilities in the statement of net assets and does not affect the statement of activities. In the current year, these amounts consist of:

Repayment of long-term obligations	704,414
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Proceeds from notes and capital leases are recorded as other financing sources in the governmental funds, but not in the statement of activities

Some items reported in the statement of activities do not require the use of current financial resources, and therefore, are not reported as expenditures in governmental funds. These activities consist of:

Early retirement incentive expense	\$ (28,594)	
Increase in accrued compensated absences	(2,341)	
Decrease in accrued interest payable on long-term debt	<u>961</u>	
		<u>(29,974)</u>

CHANGE IN NET ASSETS OF GOVERNMENTAL ACTIVITIES \$ 1,042,586

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

HILLSDALE COMMUNITY SCHOOLS
STATEMENT OF FIDUCIARY NET ASSETS

JUNE 30, 2007

	AGENCY FUND - STUDENT ACTIVITIES
ASSETS	
Cash	<u>\$ 126,217</u>
LIABILITIES	
Due to other funds	\$ 5,037
Due to student groups	<u>114,581</u>
	<u>\$ 126,217</u>

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

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS

JUNE 30, 2007

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Hillsdale Community Schools is a K-12 public school district with an enrollment of approximately 1,800 students. The School District operates under a locally elected seven-member Board of Education, and a superintendent heads the administrative staff.

The accounting policies of Hillsdale Community Schools (the "School District") conform to accounting principles generally accepted in the United States of America (GAAP) as applicable to governmental units. The Governmental Accounting Standards Board (GASB) is responsible for establishing GAAP for state and local governments through its pronouncements (Statements and Interpretations).

The following is a summary of significant accounting policies used by Hillsdale Community Schools.

REPORTING ENTITY

A reporting entity is comprised of the primary government, component units, and other organizations that are included to ensure the financial statements are not misleading. The primary government of the School District consists of all funds, departments, boards, and agencies that are not legally separate from the School District.

Component units are legally separate organizations for which the School District is financially accountable. Component units may also include organizations that are fiscally dependent on the School District in that the School District approves their budget, the issuance of their debt, or the levying of taxes. The School District has no component units.

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS

Government-Wide Financial Statements

The statement of net assets and the statement of activities (the government-wide statements) display information about the School District as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. Interfund activity has been eliminated in the preparation of the government-wide financial statements.

The government-wide and fiduciary fund financial statements are presented using the economic resources measurement focus, similar to that used by business enterprises or not-for-profit organizations. Because another measurement focus is used in the governmental fund financial statements, reconciliations are provided that explain the differences in detail.

The statement of activities presents the direct functional expenses of the School District and the program revenues that support them. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. Property taxes, State Aid, and other items not properly included among program revenues are reported as general revenues. This includes all taxes, interest, and unrestricted State Aid payments and shows how governmental functions are either self-financing or supported by the general revenues of the School District.

HILLSDALE COMMUNITY SCHOOLS
NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

GOVERNMENT-WIDE AND FUND FINANCIAL STATEMENTS (CONCLUDED)

Fund Financial Statements

The School District uses funds to maintain its financial records during the year. A fund is defined as a fiscal and accounting entity with a self balancing set of accounts. The School District utilized governmental and fiduciary funds.

The governmental fund financial statements present the School District's individual major funds and aggregated nonmajor funds. Separate columns are shown for the major funds on the balance sheet and statement of revenues, expenditures, and changes in fund balances. Nonmajor funds are combined and shown in a single column. The fiduciary funds are reported by type.

The major funds of the School District are:

General Fund - The General Fund is used to account for money or other resources provided to the School District to support the educational programs and general operations of the School District.

Building and Site Sinking Fund - The Building and Site Sinking Fund is used to account for the collection of local property taxes restricted for the use of building and site improvements.

MEASUREMENT FOCUS AND BASIS OF ACCOUNTING

The government-wide statements are prepared using the economic resources measurement focus and the accrual basis of accounting. Revenue is recorded when earned and expenses are recorded when the liability is incurred, regardless of the timing of the related cash flows. Property taxes are recognized as revenue in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met. Fiduciary funds also use the accrual basis of accounting.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenue is recognized as soon as it is both measurable and available. Revenue is considered to be available if it is to be collected within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenue to be available if it is collected within sixty days of the end of the current fiscal period. Expenditures generally are recorded when the liability is incurred, as under accrual accounting. However, debt service expenditures, expenditures relating to compensated absences, and claims and judgments are recorded only when payment is due.

Under the modified accrual basis, property taxes, interest, and grants are considered to be both measurable and available at fiscal year-end. Grants and entitlements received before the eligibility requirements are met are recorded as deferred revenue. The fair value of donated commodities used during the year is reported in the operating statement as an expense with a like amount reported as donated commodities revenue.

HILLSDALE COMMUNITY SCHOOLS
 NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ASSETS, LIABILITIES, AND NET ASSETS

Bank Deposits - Cash and deposits are considered to be cash on hand, demand deposits, and short-term investments with maturity of three months or less.

Inventories - Food service inventories are stated at cost. Federal government food commodity inventories are stated at their assigned U.S.D.A. value. All inventories are charged to expenditures when consumed.

Capital Assets - General Capital Assets result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements.

All Capital Assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. The School District maintains a capitalization threshold of \$5,000. Improvements are capitalized, and the cost of normal maintenance and repairs that do not add to the value of the asset or materially extend an asset's life are not capitalized. The School District has a bus road at one of its elementary schools and reports it as an infrastructure type asset.

All reported capital assets are depreciated. Improvements are depreciated over the remaining useful life of the related assets. Depreciation is computed using the straight-line method over the following useful lives:

<u>Description</u>	<u>Estimated Life</u>
Buildings and improvements	20 - 50 years
Buses and other vehicles	5 - 20 years
Furniture and other equipment	5 - 20 years
Infrastructure	20 years

Compensated Absences (Personal Leave) - It is the School District's policy to permit employees to accumulate earned but unused personal leave benefits. Personal leave is accrued when incurred in the government-wide financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignation, retirement, or death.

Interfund Balances - On fund financial statements, receivables and payables resulting from short-term interfund loans are reported as "due to/from other funds." These amounts are eliminated on the government-wide statement of net assets.

Long-Term Obligations - In the government-wide financial statements, all payables, accrued liabilities and long-term obligations are reported as liabilities in the statement of net assets. Bonds payable are recorded net of the applicable bond premium or discount. Bond premiums and discounts, as well as issuance costs, are deferred and amortized over the term of the related debt. In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources, while discounts are reported as other financing uses. Issuance costs are reported as debt retirement expenditures.

HILLSDALE COMMUNITY SCHOOLS
NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONCLUDED)

ASSETS, LIABILITIES, AND NET ASSETS (CONCLUDED)

Fund Balance - In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

Interfund Activity - Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds. Interfund receivables, payables, and operating transfers of governmental funds have been eliminated in the government-wide financial statement presentation.

Restricted Resources - It is the School District's policy to first apply restricted resources when an expense is incurred for purposes for which both restricted and unrestricted net assets are available.

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

NOTE 2: STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY

Budgetary Information - The budgetary process is prescribed by provisions of the State of Michigan Uniform Budgeting Act and entails the preparation of budgetary documents within an established timetable. The level of budgetary control has been established by the Board of Education at the function level. Any budgetary modifications may only be made by resolution of the Board of Education. All annual appropriations lapse at fiscal year end.

The School District follows these procedures in establishing the budgets for the individual funds as reflected in the financial statements:

- 1) Prior to June 30, the Superintendent submits to the School Board a proposed operating budget for the fiscal year commencing on July 1.
- 2) A public hearing is conducted during June to obtain taxpayer comments.
- 3) Prior to June 30, the budget is legally enacted through passage of a resolution.
- 4) For purposes of meeting emergency needs of the School District, transfer of appropriations may be made by the authorization of the Superintendent. Such transfers must be approved by the Board of Education at its next regularly scheduled meeting.
- 5) The School Superintendent is charged with general supervision of the budget and shall hold the department heads responsible for performance of their responsibilities.
- 6) During the year the budget is monitored, and amendments to the budget resolution are made when deemed necessary.

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 2: STEWARDSHIP, COMPLIANCE, AND ACCOUNTABILITY (CONCLUDED)

During the year, the School District was in violation of the Uniform Budgeting Act. Expenditures were incurred in certain budgeted funds, which were in excess of the amounts appropriated, as follows:

<u>Fund</u>	<u>Description</u>	<u>Budget</u>	<u>Actual</u>	<u>Variance</u>
Food Service Fund	Expenditures	\$ 734,305	\$ 751,932	\$ 17,627

NOTE 3: CASH, DEPOSITS, AND INVESTMENTS

Michigan Compiled Laws, Section 129.91, authorizes the School District to deposit and invest in the accounts of Federally insured banks, credit unions, and savings and loan associations; bonds, securities and other direct obligations of the United States, or any agency or instrumentality of the United States; United States government or Federal agency obligations; repurchase agreements; bankers' acceptance of United States banks; commercial paper rated by two standard rating agencies within the two highest classifications, which mature not more than 270 days after the date of purchase; obligations of the State of Michigan or its political subdivisions which are rated as investment grade; and mutual funds composed of investment vehicles which are legal for direct investment by local units of government in Michigan. Financial institutions eligible for deposit of public funds must maintain an office in Michigan. The School District's deposits and investments are in accordance with statutory authority.

Cash and Deposits

The Federal Deposit Insurance Corporation (FDIC) provides protection of the School District's deposits. At June 30, 2007, the carrying amount of the School District's deposits was \$3,939,443 and the bank balance was \$4,106,037. Of the bank balance, \$206,761 was covered by federal depository insurance and \$3,883,909 was uninsured.

Investments

As of June 30, 2007, the School District had the following investments:

<u>Investment</u>	<u>Fair Value</u>
Michigan Liquid Asset Fund Plus -- MAX Series (MIMAX)	\$ 1,492
Fifth Third Inst'l Gov't PFD	1,178
Federated – Automated Cash Management Trust SS (ACMXX)	<u>31,896</u>
	<u>\$ 34,566</u>

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 3: CASH, DEPOSITS, AND INVESTMENTS (CONCLUDED)

Investment Credit Risk - As noted above, the School District invests its funds as authorized by State law. The School District has no investment policy that would further limit its investment choices. As of June 30, 2007, the School District's investments in MIMAX and ACMXX were rated AAA by Standard & Poor's rating service.

The School District's cash, deposits and investments are recorded in the following areas:

	<u>Cash and Deposits</u>	<u>Investments</u>
Governmental Activities	\$ 3,813,226	\$ 34,565
Fiduciary Fund	<u>126,217</u>	<u> </u>
	<u>\$ 3,939,443</u>	<u>\$ 34,565</u>

NOTE 4: INTERFUND RECEIVABLES AND PAYABLES

The following schedule details interfund receivables and payables related to the School District at June 30, 2007:

Due to General Fund from:	
Food Service	\$ 14,103
Athletics	<u>3,044</u>
	<u>\$ 17,147</u>
Due to Athletic Fund from:	
Student Activity	\$ 5,037
	<u>\$ 5,037</u>

Amounts appearing as interfund payables and receivables arise from two types of transactions. One type of transaction is where a fund will pay for goods or services that at least a portion of the benefit belongs to another fund. The second type of transaction is where one fund provides a good or service, or is otherwise obligated to another fund. Balances at the end of the year are for transfers that have not cleared as of the balance sheet date.

NOTE 5: INTERFUND TRANSFERS

Permanent reallocation of resources between funds of the School District to use for operating are classified as interfund transfers. For the purpose of statement of activities, all interfund transfers between individual governmental funds have been eliminated.

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 5: INTERFUND TRANSFERS (CONCLUDED)

	<u>Transfers in</u>	<u>Transfers out</u>
General Fund	\$	\$ 277,189
Building and Site Fund	25,000	
Athletic Fund	<u>252,189</u>	
	<u>\$ 277,189</u>	<u>\$ 277,189</u>

NOTE 6: CAPITAL ASSETS

Capital asset activity for the fiscal year ended June 30, 2007, was as follows:

	<u>Balance 7/1/06</u>	<u>Additions</u>	<u>Disposals / Adjustments</u>	<u>Balance 6/30/07</u>
Assets not being depreciated:				
Land	\$ 50,740	\$	\$	\$ 50,740
Assets being depreciated:				
Buildings & improvements	13,928,109	523,484		14,451,593
Furniture & equipment	5,241,443	49,228		5,290,671
Vehicles	751,354			751,354
Infrastructure	<u>221,832</u>	<u>9,819</u>		<u>231,651</u>
Total	<u>\$ 20,193,478</u>	<u>\$ 582,531</u>	<u>\$</u>	<u>\$ 20,776,009</u>
Accumulated depreciation for:				
Buildings & improvements	\$ 6,287,765	\$ 375,966	\$	\$ 6,663,731
Furniture & equipment	3,369,681	366,731		3,736,412
Vehicles	537,586	51,592		589,178
Infrastructure	<u>55,459</u>	<u>11,336</u>		<u>66,795</u>
Total	<u>\$ 10,250,491</u>	<u>\$ 805,625</u>	<u>\$</u>	<u>\$ 11,056,116</u>
Net capital assets	<u>\$ 9,942,987</u>	<u>\$ (223,094)</u>	<u>\$</u>	<u>\$ 9,719,893</u>

Depreciation expense was not charged to activities as the School District considers its assets to impact multiple activities and allocation is not practical.

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 7: SHORT-TERM NOTES

In August, 2006, the School District issued a short-term State School Aid Anticipation Note in the amount of \$2,400,000 for the purpose of funding operating expenditures until the 2006 State Aid payments resumed. This short-term note, which has a net outstanding balance of \$2,400,000 at June 30, 2007, is reported in the General Fund under the caption note payable-tax anticipation. The outstanding balance is expected to be refinanced. See Note 18.

NOTE 8: LONG-TERM DEBT

The School District issues bonds, notes, and other contractual commitments to provide for the acquisition and construction of major capital facilities and improvements and the acquisition of certain equipment. Other long-term obligations include retirement buy-outs.

Long-term obligation activity can be summarized as follows:

	Balance <u>7/01/06</u>	<u>Additions</u>	<u>Reductions</u>	Balance <u>6/30/07</u>
Bonds	\$3,445,507	\$	\$ 460,000	\$2,985,507
Capital leases	24,050		17,433	6,617
Notes	197,145		118,141	79,004
Early retirement incentive	314,534	28,594	108,840	234,288
Compensated absences	<u>208,270</u>	<u>2,341</u>	<u> </u>	<u>210,611</u>
	<u>\$4,189,506</u>	<u>\$ 30,935</u>	<u>\$ 704,414</u>	<u>\$3,516,027</u>

At June 30, 2007, long-term debt consisted of the following individual issues:

\$4,750,000 – 2002 School Building and Site Bonds, due in annual installments of \$255,000 to \$630,000, bearing interest at a rate of 3.97%, through May 1, 2012	\$2,870,000
1998 School Improvement Bonds (Durant Non-Plaintiff Resolution), annual installments of \$13,000 to \$20,000 bearing interest at 4.76%, through May 15, 2013	115,507
Note payable, County National Bank, secured by buses, payable beginning with a one time principal and interest payment of \$19,548, due July 15, 2006 and monthly payments thereafter of \$3,910, bearing interest at a rate of 4.15%, through February 9, 2009	79,004
Capital lease obligation, Dell Company, secured by computers, payable in annual installments of \$16,547, bearing interest at a rate of 7.38%, through December 31, 2007	3,286

HILLSDALE COMMUNITY SCHOOLS
 NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 8: LONG-TERM DEBT (CONCLUDED)

Capital lease obligation, Chesterfield Financial Corporation, secured by equipment, payable in monthly installments of \$214, with an imputed interest rate of 7%, through November 10, 2008	3,331
Accrued retirement benefits:	
Compensated absences	210,611
Early retirement	234,288
TOTAL LONG-TERM DEBT	\$ 3,516,027

Annual debt service requirements to maturity for the above debt obligations are as follows:

<u>Year Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2008	\$ 662,273	\$ 113,724	\$ 775,997
2009	754,162	118,430	872,592
2010	591,405	73,632	665,037
2011	641,948	50,614	692,562
2012	642,516	25,632	668,148
2013	13,112	624	13,736
Total	\$ 3,305,416	\$ 382,656	\$ 3,688,072
Compensated absences	210,611		210,611
	\$ 3,516,027	\$ 382,656	\$ 3,898,683

1998 School Improvement Bond Issue

Included in Governmental Activities General Obligation Bonds is the Durant Non-Plaintiff Bond. Annual total payments (principal and interest) of \$13,736 to \$24,476 associated with this Bond are funded by the State of Michigan via specifically appropriated State Aid and will not require any School District debt levy or utilization of any other School District financial resources.

2002 School Building and Site Bonds

The bonds were authorized at an election on March 11, 2002, for the purpose of remodeling and re-equipping the high school and middle school, including boiler replacement and energy conservation improvements. The bonds are direct obligations and pledge the full faith, credit, and resources of the School District for payment of the principal and interest thereon, and will be payable from ad valorem taxes.

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 9: PROPERTY TAXES

The School District levies its property taxes on December 1 on the taxable valuation of property located in the School District as of the preceding December 31. Various municipalities collect the property taxes and remit them to the School District through February. The County purchases the delinquent real property taxes of the School District. The delinquent personal property taxes continue to be collected by the municipalities and recorded as revenue as they are collected. The total levy for 2006 was 18.00 mills on non-homestead valuation for operational purposes and 1.85 mills on total valuation for debt retirement. A building and site sinking fund is also maintained by the School District, which levies 2.00 mills on total valuation. The 2006 taxable valuation of the School District totaled approximately \$324,870,000.

NOTE 10: DEFINED BENEFIT PENSION PLAN

The School District participates in the Michigan Public School Employees' Retirement System (MPSERS), a statewide, cost-sharing, multiple-employer defined benefit public employee retirement system governed by the State of Michigan that covers substantially all employees of the School District. The MPSERS provides retirement, survivor, and disability benefits to plan members and their beneficiaries. The MPSERS issues a publicly available financial report that includes financial statements and requirement supplementary information for the MPSERS. That report may be obtained by writing to the MPSERS at 7150 Harris Drive; P. O. Box 30673; Lansing, MI 48909-8103.

Funding Policy

Employer contributions to the MPSERS result from the implementing effects of the School Finance Reform Act. Under these procedures, each school district is required to contribute the full actuarial funding contribution amount to fund pension benefits, plus an additional amount to fund retiree health care benefit amounts on a cash disbursement basis. The pension benefit rate totals 16.34 percent for the period July 1, 2006 through September 30, 2006, and 17.74 percent for the remainder of the year. Basic plan members make no contributions, but contribute to a member investment plan (MIP) at rates ranging from 3 percent to 4.3 percent of gross wages. The School District's contributions to the MPSERS pension plan for the year ended June 30, 2007 was approximately \$1,361,000. The District received a MPSERS credit of \$228,250 for the year ended June 30, 2007 according to amendment Section 147 in Public Act 6 of 2007 of the State School Aid Act.

Post-Employment Benefits

Under the MPSERS Act, all retirees participating in the MPSERS pension plan have the option of continuing health, dental, and vision coverage. Required contributions for post-employment health care benefits are included as part of the School District's total contribution to the MPSERS pension plan discussed above.

NOTE 11: RISK MANAGEMENT

The School District is exposed to various risks of loss related to property loss, torts, errors and omissions, employee injuries (Workers' Compensation), as well as medical benefits to employees. The School District has purchased commercial insurance for medical benefits and participates in the MASB-SEG Property/Casualty risk pool for claims relating to property loss, torts, errors and omissions, and employee injuries. There has been no significant reduction in coverage, and settled claims have not exceeded the amount of insurance coverage in any of the past three fiscal years.

HILLSDALE COMMUNITY SCHOOLS
 NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 11: RISK MANAGEMENT (CONCLUDED)

The MASB-SEG Property/Casualty Pool, Inc. is a public entity risk pool (self-insurance pool) which provides for reinsurance by various insurance companies at various levels, depending on coverage. Should the pool experience significant losses in the aggregate, the School District may be required to pay additional monies to the pool. At present, the MASB/SET/SEG has not required additional funds, but rather has issued refunds based on experience gains over experience losses over the last few years.

NOTE 12: COMMITMENTS AND CONTINGENCIES

Unemployment Taxes

The School District is a reimbursing employer to the Michigan Unemployment Agency, and as such, is responsible to pay the Agency for those benefits paid and charged to its account. As of June 30, 2007, appropriate liabilities have been recorded for all claims paid by the Agency. However, no provision has been made for future payments that might result from claims in process or not filed.

Grant Programs

The School District participates in numerous State and Federal grant programs, which are governed by various rules and regulations of the grantor agencies. Costs charged to the respective grant programs are subject to audit and adjustments by the grantor agencies; therefore, to the extent that the School District has not complied with the rules and regulations governing the grants, refunds of any money received may be required and the collectibility of any related receivable at June 30, 2007 may be impaired. In the opinion of the School District, there are no significant contingent liabilities relating to compliance with the rules and regulations governing the respective grants.

NOTE 13: SINKING FUNDS

The School District's Building and Site Capital Project Fund records capital project activities funded with Sinking Fund millage. For these funds, the School District has complied with the applicable provisions of §1212(1) of the Revised School Code and the State of Michigan Department of Treasury Letter No. 01-95.

NOTE 14: FIDUCIARY FUND

The following is a summary of cash receipts, disbursements, and adjustments of the School District's student activity accounts for the year ended June 30, 2007:

Beginning balance – July 1, 2006	\$ 119,160
Receipts	255,461
Disbursements	<u>248,404</u>
Ending balance – June 30, 2007	<u>\$ 126,217</u>

HILLSDALE COMMUNITY SCHOOLS
NOTES TO FINANCIAL STATEMENTS (CONTINUED)

JUNE 30, 2007

NOTE 15: FUND FINANCIAL STATEMENTS RESERVED FUND BALANCE

Reserved fund balance is used to earmark a portion of fund balance to indicate that it is not appropriate for expenditures or has been legally identified for specific purposes.

Reserves:

School Services Fund – reserved for inventory	\$ 13,274
Building and Site Sinking Fund – reserves to be used for School improvements	706,695
Debt Retirement Fund – reserve to be used for retiring school debt approved by the voters	<u>234,151</u>
	<u>\$ 954,120</u>

NOTE 16: RESTRICTED NET ASSETS

Restrictions of net assets shown in the government-wide financial statements indicate that restrictions imposed by the funding source or some other outside source, precludes their use for unrestricted purposes.

The following are net asset restrictions as of June 30, 2007:

Governmental Activities

Restricted for debt service	\$ 234,151
Restricted for capital projects	<u>706,695</u>
	<u>\$ 940,846</u>

NOTE 17: SPECIAL ITEM

Statement of Activities

Termination Benefits Expense

The School District entered into an early retirement incentive agreement with one additional teacher during the year. The agreement requires annual payments of \$10,000 for three years. The expense of \$28,594 is reported in the Statement of Activities, and is measured at the discounted present value of future payments using a discount rate of 5%.

NOTE 18: OPERATING LEASE

The School District leases a building for its Adult and Alternative Education activities. The lease agreement is on an annual basis. The total annual lease expense for the year was \$20,000.

HILLSDALE COMMUNITY SCHOOLS

NOTES TO FINANCIAL STATEMENTS (CONCLUDED)

JUNE 30, 2007

NOTE 19: SUBSEQUENT EVENTS

After the year ended June 30, 2007, the following subsequent event occurred:

Additional Borrowing - In August 2007, the School District received funds from the Michigan Municipal Bond Authority short-term cash flow borrowing program. The loan totaled \$2,000,000 and future anticipated State Aid and other local funds are expected to be sufficient to cover this commitment.

REQUIRED SUPPLEMENTAL INFORMATION

HILLSDALE COMMUNITY SCHOOLS

REQUIRED SUPPLEMENTAL INFORMATION
BUDGETARY COMPARISON SCHEDULE - GENERAL FUND

YEAR ENDED JUNE 30, 2007

	ORIGINAL BUDGET	FINAL AMENDED BUDGET	ACTUAL
REVENUES			
Local sources	\$ 2,783,176	\$ 2,740,626	\$ 2,731,758
State sources	11,344,209	11,328,819	11,333,640
Federal sources	565,451	521,590	403,850
Other sources	9,983	35,391	31,871
TOTAL REVENUES	\$ 14,702,819	\$ 14,626,426	\$ 14,501,119
EXPENDITURES			
Instruction:			
Basic programs	\$ 7,401,143	\$ 7,355,223	\$ 7,236,803
Added needs	2,174,387	2,145,109	2,031,069
Adult education	36,785	36,270	34,664
Instructional support:			
Pupil support	361,273	354,283	339,859
Instructional staff	265,523	281,073	233,588
School administration	1,142,905	1,117,330	1,101,994
Non-instructional support:			
General administration	351,845	355,913	332,591
Business services	320,835	334,250	326,468
Operations and maintenance	1,335,509	1,280,649	1,208,754
Transportation	739,932	718,957	686,409
Other non-instructional support	144,521	143,335	123,687
Community services	3,060	6,450	2,068
TOTAL EXPENDITURES	\$ 14,277,718	\$ 14,128,842	\$ 13,657,954
REVENUES OVER (UNDER) EXPENDITURES	\$ 425,101	\$ 497,584	\$ 843,165
OTHER FINANCING SOURCES (USES)			
Operating transfers in	\$ 22,000	\$	\$
Capital lease proceeds			
Loan proceeds			
Proceeds from sale of assets			
Payments on capital leases	(108,020)	(125,216)	(124,511)
Payments on loans			
Operating transfers out	(244,315)	(277,754)	(277,189)
TOTAL OTHER FINANCING SOURCES AND (USES)	\$ (330,335)	\$ (402,970)	\$ (401,700)
NET CHANGE IN FUND BALANCES	\$ 94,766	\$ 94,614	\$ 441,465
FUND BALANCES - BEGINNING	\$ 147,022	\$ 147,022	\$ 147,022
FUND BALANCES - ENDING	\$ 241,788	\$ 241,636	\$ 588,487

ADDITIONAL INFORMATION

HILLSDALE COMMUNITY SCHOOLS

COMBINING BALANCE SHEETS -
NONMAJOR GOVERNMENTAL FUNDS

JUNE 30, 2007

	Debt Service Fund	Food Service Fund	Athletics Fund	Total Nonmajor Governmental Funds
ASSETS				
Cash	\$ 234,151	\$ 552	\$ 8,009	\$ 242,712
Investments		10,929		10,929
Due from other governments		7,125		7,125
Due from other funds			5,037	5,037
Accounts receivable		3,106	185	3,291
Other deposits		33,000		33,000
Inventory		13,274		13,274
TOTAL ASSETS	\$ 234,151	\$ 67,986	\$ 13,231	\$ 315,368
LIABILITIES				
Accounts payable	\$	\$ 5,445	\$ 239	\$ 5,684
Salaries payable		27,699	5,094	32,793
Due to other funds		14,103	3,044	17,147
TOTAL LIABILITIES	\$	\$ 47,247	\$ 8,377	\$ 55,624
FUND BALANCES				
Reserved	\$ 234,151	\$ 13,274	\$	\$ 247,425
Unreserved, undesignated		7,465	4,854	12,319
Total Fund Balances	\$ 234,151	\$ 20,739	\$ 4,854	\$ 259,744
TOTAL LIABILITIES AND FUND BALANCES	\$ 234,151	\$ 67,986	\$ 13,231	\$ 315,368

HILLSDALE COMMUNITY SCHOOLS

COMBINING STATEMENTS OF REVENUE, EXPENDITURES
AND CHANGES IN FUND BALANCES -
NONMAJOR GOVERNMENTAL FUNDS

YEAR ENDED JUNE 30, 2007

	Debt Service Fund	Food Service Fund	Athletics Fund	Total Nonmajor Governmental Funds
REVENUE				
Local sources	\$ 613,349	\$ 275,000	\$ 116,488	\$ 1,004,837
State sources		46,344		46,344
Federal sources		420,363		420,363
Other sources	17,214	13,131	28	30,373
TOTAL REVENUE	<u>\$ 630,563</u>	<u>\$ 754,838</u>	<u>\$ 116,516</u>	<u>\$ 1,501,917</u>
EXPENDITURES				
Salaries and benefits	\$	\$ 339,530	\$ 253,803	\$ 593,333
Supplies & materials		410,690	107,542	518,232
Capital outlay		1,712	2,903	4,615
Debt principal	460,000			460,000
Debt interest and other	128,562			128,562
TOTAL EXPENDITURES	<u>\$ 588,562</u>	<u>\$ 751,932</u>	<u>\$ 364,248</u>	<u>\$ 1,704,742</u>
REVENUES OVER (UNDER) EXPENDITURES	<u>\$ 42,001</u>	<u>\$ 2,906</u>	<u>\$ (247,732)</u>	<u>\$ (202,825)</u>
OTHER FINANCING SOURCES				
Transfers in	\$	\$	\$ 252,189	\$ 252,189
NET CHANGE IN FUND BALANCE	\$ 42,001	\$ 2,906	\$ 4,457	\$ 49,364
FUND BALANCE - BEGINNING	192,150	17,833	397	210,380
FUND BALANCE - ENDING	<u>\$ 234,151</u>	<u>\$ 20,739</u>	<u>\$ 4,854</u>	<u>\$ 259,744</u>

HILLSDALE COMMUNITY SCHOOLS
SINGLE AUDIT OF FEDERAL
FINANCIAL ASSISTANCE PROGRAMS
FINANCIAL REPORT AND
INDEPENDENT AUDITOR'S REPORTS
JUNE 30, 2007

HILLSDALE COMMUNITY SCHOOLS

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Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

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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

Board of Education
Hillsdale Community Schools
Hillsdale, Michigan

We have audited the financial statements of the governmental activities, each major fund, and the aggregate remaining fund information of Hillsdale Community Schools as of and for the year ended June 30, 2007, which collectively comprise the Hillsdale Community School's basic financial statements and have issued our report thereon dated October 11, 2007. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the Hillsdale Community School's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinion on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Hillsdale Community School's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Hillsdale Community School's internal control over financial reporting.

Our consideration of internal control over financial reporting was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in internal control over financial reporting that might be significant deficiencies or material weaknesses. However, as discussed below, we identified certain deficiencies in internal control over financial reporting that we consider to be significant deficiencies.

A control deficiency exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect misstatements on a timely basis. A significant deficiency is a control deficiency, or combination of control deficiencies, that adversely affects Hillsdale Community School's ability to initiate, authorize, record, process, or report financial data reliably in accordance with generally accepted accounting principles such that there is more than a remote likelihood that a misstatement of Hillsdale Community School's financial statements that is more than inconsequential will not be prevented or detected by Hillsdale Community School's internal control. We consider the deficiencies described in the accompanying Schedule of Findings and Questioned Costs as finding 2007-1, 2007-2, and 2007-3 to be significant deficiencies in internal control over financial reporting.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that a material misstatement of the financial statements will not be prevented or detected by Hillsdale Community School's internal control.

Our consideration of the internal control over financial reporting was for the limited purpose described in the first paragraph of this section and would not necessarily identify all deficiencies in the internal control that might be significant deficiencies and, accordingly, would not necessarily disclose all significant deficiencies that are also considered to be material weaknesses. However, we believe that item 2007-2 of the significant deficiencies described above is a material weakness.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Hillsdale Community School'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 and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Hillsdale Community School's response to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit Hillsdale Community School's response, and, accordingly, we express no opinion on it.

This report is intended for the information of the Board of Education, management and federal and state awarding agencies. It should not be used by anyone other than these specified parties.

Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

Hillsdale, Michigan
October 11, 2007



Osbourne, March, Condon & Co., P.C.

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REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE
TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE
IN ACCORDANCE WITH *OMB CIRCULAR A-133*

Board of Education
Hillsdale Community Schools
Hillsdale, Michigan

Compliance

We have audited the compliance of Hillsdale Community Schools with the types of compliance requirements described in the *U.S. Office of Management and Budget (OMB) Circular A-133 Compliance Supplement* that are applicable to its major federal program for the year ended June 30, 2007. Hillsdale Community School's major federal programs are identified in the summary of auditor's results section of the accompanying Schedule of Findings and Questioned costs. Compliance with the requirements of laws, regulations, contracts and grants applicable to each of its major federal programs is the responsibility of the Hillsdale Community School's management. Our responsibility is to express an opinion on the Hillsdale Community School's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the Hillsdale Community School's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the Hillsdale Community School's compliance with those requirements.

In our opinion the School District's complied, in all material respects, with the requirements referred to above that are applicable to each of its major federal programs for the year ended June 30, 2007. However, the results of our auditing procedures disclosed instances of noncompliance with those requirements, which are required to be reported in accordance with OMB Circular A-133 and which are described in the accompanying schedule of findings and questioned costs as items 2007-4.

Internal Control Over Compliance

The management of Hillsdale Community Schools is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the School District's internal control over compliance with the 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, but not for the purpose of expressing an opinion on the effectiveness of internal control over compliance. Accordingly, we do not express an opinion on the effectiveness of Hillsdale Community School's internal control over compliance.

Our consideration of the internal control over compliance was for the limited purpose described in the preceding paragraph and would not necessarily identify all deficiencies in the entity's internal control that might be significant deficiencies or material weaknesses as defined below. However, as discussed below, we identified certain deficiencies in internal control over compliance that we consider to be significant deficiencies.

A *control deficiency* is an entity's internal control over compliance exists when the design or operation of a control does not allow management or employees, in the normal course of performing their assigned functions, to prevent or detect noncompliance with a type of compliance requirement of a federal program on a timely basis. A *significant deficiency* is a control deficiency, or combination of control deficiencies, that adversely affects the entity's ability to administer a federal program such that there is more than a remote likelihood that noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the entity's internal control.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood that material noncompliance with a type of compliance requirement of a federal program will not be prevented or detected by the entity's internal control. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 2007-2 to be a material weakness.

Hillsdale Community School's response to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. We did not audit Hillsdale Community School's response, and, accordingly, we express no opinion on it.

This report is intended for the information of management, the Board of Education, federal and state awarding agencies and pass-through entities. However, this report is a matter of public record and its distribution is not limited.

Osbourne, March, Condon & Co., P.C.

Certified Public Accountants

Hillsdale, Michigan
October 11, 2007

HILLSDALE COMMUNITY SCHOOLS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2007

FEDERAL CFDA NUMBER	APPROVED GRANT AWARD AMOUNT	(ACCRUED) DEFERRED REVENUE 07/01/06	(MEMO ONLY) PRIOR YEAR EXPENDITURES	CURRENT YEAR EXPENDITURES	CURRENT YEAR RECEIPTS- CASH BASIS	ACCRUED (DEFERRED) REVENUE 06/30/07
U.S. DEPARTMENT OF EDUCATION						
<i>Passed through M.D.E.</i>						
* Title I - Educationally Deprived						
84.010	\$ 404,432	\$ (56,297)	\$ 374,283	\$ 4,963	\$ 61,260	\$
84.010	25,186			25,186	25,186	
84.010	<u>355,627</u>			<u>287,192</u>	<u>264,291</u>	<u>22,901</u>
	\$ 785,245	\$ (56,297)	\$ 374,283	\$ 317,341	\$ 350,737	\$ 22,901
Title II-A Improving Teacher Quality						
84.367	\$ 126,151	\$ (13,629)	\$ 113,307	\$	\$ 13,629	\$
84.367	12,844			12,844		
84.367	<u>122,272</u>			<u>62,594</u>	<u>45,542</u>	<u>17,052</u>
	\$ 261,267	\$ (13,629)	\$ 113,307	\$ 75,438	\$ 59,171	\$ 17,052
Title II-D Enhancing Education/Tech						
84.318	\$ 7,545	\$ (640)	\$ 4,603	\$	\$ 640	\$
84.318	2,942			2,942	2,942	
84.318	<u>3,590</u>			<u>3,254</u>	<u>2,935</u>	<u>319</u>
	\$ 14,077	\$ (640)	\$ 4,603	\$ 6,196	\$ 6,517	\$ 319
Title V Innovative Programs						
84.298	\$ 6,552	\$ (186)	\$ 4,579	\$ 19	\$ 205	\$
84.298	1,924			1,924	1,924	
84.298	<u>1,789</u>			<u>1,789</u>	<u>1,789</u>	
	\$ 10,265	\$ (186)	\$ 4,579	\$ 3,732	\$ 3,918	\$

The accompanying notes are an integral part of this schedule.

HILLSDALE COMMUNITY SCHOOLS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2007

FEDERAL CFDA NUMBER	APPROVED GRANT AWARD AMOUNT	(ACCRUED) DEFERRED REVENUE 07/01/06	(MEMO ONLY) PRIOR YEAR EXPENDITURES	CURRENT YEAR EXPENDITURES	CURRENT YEAR RECEIPTS- CASH BASIS	ACCRUED (DEFERRED) REVENUE 06/30/07
U.S. DEPARTMENT OF EDUCATION (continued)						
84.027	\$ 3,115	\$	\$	\$ 98	\$ 98	\$
Handicapped Preschool Program 060440 SPSR Regular						
84.938C	\$ 565	\$	\$ 413	\$ 152	\$ 152	\$
Katrina FY 2006 061420 Regular						
	\$ 1,074,534	\$ (70,752)	\$ 497,185	\$ 402,957	\$ 420,593	\$ 40,272
<i>Total passed through M.D.E.</i>						
<i>Passed through I.S.D.</i>						
84.186	\$ 893	\$	\$	\$ 893	\$ 893	\$
Drug Free Schools Supplement Grant 022860DRUG0607						
	\$ 1,075,427	\$ (70,752)	\$ 497,185	\$ 403,850	\$ 421,486	\$ 40,272
TOTAL U.S. DEPARTMENT OF EDUCATION						
U.S. DEPARTMENT OF AGRICULTURE						
<i>Passed through M.D.E.</i>						
10.553	\$ 81,121	\$	\$	\$ 81,121	\$ 81,121	\$
* National School Lunch - Breakfast Breakfast - 2006-07						
10.555	\$ 4,873	\$	\$	\$ 4,873	\$ 4,873	\$
10.555	25,675			25,675	25,675	
10.555	42,796			42,796	42,796	
10.555	236,295			236,295	236,295	
* National School Lunch 061950 Section 4 lunches 061960 Section 11 free and reduced 071950 Section 4 lunches 071960 Section 11 free and reduced						
	\$ 309,639	\$	\$	\$ 309,639	\$ 309,639	\$

The accompanying notes are an integral part of this schedule.

HILLSDALE COMMUNITY SCHOOLS

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

YEAR ENDED JUNE 30, 2007

FEDERAL CFDA NUMBER	APPROVED GRANT AWARD AMOUNT	(ACCRUED) DEFERRED REVENUE 07/01/06	(MEMO ONLY) PRIOR YEAR EXPENDITURES	CURRENT YEAR EXPENDITURES	CURRENT YEAR RECEIPTS- CASH BASIS	ACCRUED (DEFERRED) REVENUE 06/30/07
U.S. DEPARTMENT OF AGRICULTURE (Continued)						
* Summer Food Service						
10.559	\$ 1,027	\$ (1,027)	\$	\$	\$ 1,027	\$
060900	107	(107)			107	
10.559	<u>1,565</u>			<u>1,565</u>		<u>1,565</u>
070900	<u>\$ 2,699</u>	<u>\$ (1,134)</u>	<u>\$</u>	<u>\$ 1,565</u>	<u>\$ 1,134</u>	<u>\$ 1,565</u>
National School Lunch						
10.550	\$ 27,339	\$	\$	\$ 27,339	\$ 27,339	\$
Entitlements Commodities	699			699	699	
10.550	<u>\$ 28,038</u>	<u>\$</u>	<u>\$</u>	<u>\$ 28,038</u>	<u>\$ 28,038</u>	<u>\$</u>
TOTAL U.S. DEPARTMENT OF AGRICULTURE	<u>\$ 421,497</u>	<u>\$</u>	<u>\$</u>	<u>\$ 420,363</u>	<u>\$ 419,932</u>	<u>\$ 1,565</u>
TOTAL FEDERAL FINANCIAL ASSISTANCE	<u>\$ 1,496,924</u>	<u>\$ (70,752)</u>	<u>\$ 497,185</u>	<u>\$ 824,213</u>	<u>\$ 841,418</u>	<u>\$ 41,837</u>

The accompanying notes are an integral part of this schedule.

HILLSDALE COMMUNITY SCHOOLS
NOTES TO SCHEDULE OF EXPENDITURES
OF FEDERAL AWARDS

JUNE 30, 2007

NOTE 1: *Designates a major program.

NOTE 2: The schedule includes all Federal financial assistance and related expenditures that are reported as passed through the State of Michigan and the local intermediate school district. The schedule was prepared using the same applicable, significant policies as used in the preparation of the general purpose financial statements.

NOTE 3: The School District had two Type A programs; i.e., programs with expenditures equal to or greater than \$300,000. Based on Section .520(c)(1) of the OMB Circular A-133, the two Type A programs were assessed at low risk. There were no high risk Type B programs identified in accordance with Section .520(d)(1) of the OMB Circular A-133.

The federal programs identified as a Type A programs subject to testing as a major program was as follows:

Child Nutrition Cluster
Title I – Part A

The expenditures of the major programs equal \$708,101, which exceeds the fifty percent coverage rule.

NOTE 4: Management has utilized the Grant Auditor Reports from the Michigan Department of Education in preparing the Schedule of Expenditures of Federal Awards. This schedule reconciles with the reports, except for the State School Lunch allocations, which are not federal funds.

NOTE 5: The amounts reported on the Recipient Entitlement Balance Report (PAL Report) agree with this schedule for U.S.D.A. donated food commodities and are reported in the Cash Receipts column.

NOTE 6: Expenditures include spoilage.

HILLSDALE COMMUNITY SCHOOLS
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS
 YEAR ENDED JUNE 30, 2007

Section I - Summary of Auditor's Results

Financial Statements

Type of auditors' report issued:	Unqualified	
Internal control over financial reporting:		
Material weakness(es) identified?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Significant deficiency(s) identified that are Not considered to be material weaknesses?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Noncompliance material to financial statements noted?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

Federal Awards

Internal control over major programs:		
Material weakness(es) identified?	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No
Significant deficiency(s) identified that are Not considered to be material weaknesses?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No
Type of auditors' report issued: Unqualified		
Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133	<input checked="" type="checkbox"/> Yes	<input type="checkbox"/> No

Major Programs

<u>CFDA Number(s)</u>	<u>Name of Federal Program or Cluster</u>
10.553	Child Nutrition Cluster
10.555	
10.559	
84.010	Title I - Part A

Dollar threshold used to distinguish between Type A and Type B programs:	<u>\$300,000</u>	
Auditee qualified as low-risk auditee?	<input type="checkbox"/> Yes	<input checked="" type="checkbox"/> No

HILLSDALE COMMUNITY SCHOOLS
SCHEDULE OF FINDINGS AND QUESTIONED COSTS
YEAR ENDED JUNE 30, 2007

Section II - Financial Statement Findings

Finding 2007-1

Finding considered a significant deficiency

All Michigan School Districts are required to prepare financial statements in accordance with generally accepted accounting principles (GAAP). This is the responsibility of the School District's management. The preparation of financial statements in accordance with GAAP requires internal controls over both (1) recording, processing, and summarizing accounting data, and (2) reporting government-wide and fund financial statements, including the related footnotes.

Condition: The School District has historically relied on its independent external auditors to assist in the preparation of the government-wide financial statements and footnotes as part of its external financial reporting process. Accordingly, the School District's ability to prepare financial statements in accordance with GAAP is based, in part, on its reliance on its external auditors, who cannot by definition be considered part of the District's internal controls.

Cause: This condition was caused by the School District's decision that it is more cost effective to outsource the preparation of its annual financial statements to the auditors than to incur the added time and expense of obtaining the necessary training for its business department to perform this task.

Effect: The result of this condition is that the School District lacks internal controls over the preparation of financial statements in accordance with GAAP, and instead relies, in part, on its external auditors for assistance with this task.

View of responsible officials: The School District's will continue to evaluate the cost vs. benefit of establishing internal controls over the preparation of financial statements in accordance with GAAP. In addition, the School District will carefully review the draft financial statements and notes prior to approving them and accept responsibility for their content and presentation.

Finding 2007-2

Finding considered a material weakness

Condition: The School District does not have a control system in place that would prevent or detect an inappropriate request for Federal Award funds from the Michigan Department of Education.

Effect: Without a control system in place over requesting Federal Award funds, the District could receive funds for program expenditures in excess of the three day cash needs compliance requirement.

View of responsible officials: The School District will construct a control system over the request for Federal Awards.

Finding 2007-3

Finding considered a significant deficiency

Condition: The School District has a control system in place over journal entries recorded into the general ledger. However, during the year, there was a breakdown in the approval process that allowed a journal entry to be recorded in error.

Effect: The approval process, as part of the control system, should be performed by someone who has adequate information surrounding the transaction to appropriately authorize the journal entry.

View of responsible officials: The School District's accounting staff will strive to communicate with the authorizing person, the details of journal entry transactions.

Section III – Federal Award Findings and Questioned Costs

Internal Control Related Matters:

See Finding 2007-2

Compliance Related Matters:

Finding 2007-4: Cash Management

Federal Agency: U.S. Department of Education
CDFA 84.010 Title I – Part A

Criteria: School Districts (grantees) may request program funding for expenditures already made and for amounts estimated for a three day cash needs.

Condition: The School District expended \$287,192 on the Title I – Part A program. Cash receipts for the same period totaled \$298,606.

Effect: The Michigan Department of Education may require the School District to provide documentation regarding the cash needs of the program and refund any over requested amounts, if necessary.

Views of Responsible Officials: See Hillsdale Community School's Corrective Action Plan (attached)

CLIENT DOCUMENTS



Hillsdale Community Schools

30 South Norwood Avenue

Hillsdale, MI 49242

Telephone (517) 437-4401 - Fax (517) 439-4194

"Learning For A Lifetime"

Hillsdale Community Schools respectfully submits the following Corrective Action Plan for the year ended June 30, 2007.

FINDINGS – FINANCIAL STATEMENT AUDIT – INTERNAL CONTROL

Finding 2007-1 – Internal Control over Financial Reporting

Condition: The School District lacks internal controls over the preparation of financial statements in accordance with GAAP.

Action Taken: The district is requesting all work papers that the auditing firm has created for the 2006-2007 fiscal year. These work papers will be used to create an internal template of the district's financials. Also, the local intermediate school district chief financial officer has agreed to work with the business office to help create the financial statements. Other action will also be taken with training through Michigan School Business Officials and other workshops that are available.

Finding 2007-2 – Lack of Internal Controls over Requesting Federal Funds

Condition: The School District does not have a control system in place over cash management over Federal Funds

Action Taken: The school district is implementing an internal control sheet for the Title Director to approve upon any Federal Fund dollar requests. The Title Director works with the budgets for each of the Federal Allocations that are approved by the Michigan Department of Education.

Finding 2007-3 – Internal Controls over Journal Entries are not working effectively.

Condition: The School District's internal control process over journal entries did not detect errors.

Action Taken: The school district is continuing to improve in this area. Journal entries are made by only two staff employees. These two staff employees are the Business Manager and the Financial Secretary. Before journal entries are entered the Business Manager reviews, initials and approves the entries. Once approved, the Financial Secretary enters edits and posts the entries in the computer. Because the auditors felt

that this was not enough of an internal control, the district is going to make sure that the proper documentation (back-up) for the journal entry/entries is attached to all handwritten entries and the computer generated reports.

**FINDINGS AND QUESTIONED COSTS-MAJOR FEDERAL PROGRAMS
AUDIT**

INTERNAL CONTROL – Significant Deficiency – See 2007-2 above.

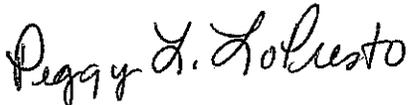
COMPLIANCE:

U.S. Department of Education
Finding 2007-4: Title I, Part A – Cash Management

Condition: Funds received were greater than the 3-day cash needs

Action Taken: The school district was very aware of the over request of funds at the end of June 2007. Upon receipt of the State Aid Financial Status Report and the notice from Treasury of the MPSEERS retirement credit the over request appeared. The retirement credit created confusion on how to record the information. Upon talking and working through the process with the auditors the error was found and corrected. The district corrected the oversight by deducting the over request with the next request of funds. Since this type of accounting occurred with the state, the district now has notes in place on how to record any further credits.

Sincerely,



Peggy L. LoPresto
Business Manager