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HAYS
MAGGARD
& HOOD, P.C.

CERTIFIED PUBLIC ACCOUNTANTS

November 17, 2015

Board of Education
District Administrative Staff
San Juan County (Silverton) School District No. 1
Silverton, Colorado 81433

COMMUNICATIONS WITH THOSE CHARGED WITH GOVERNANCE

We have audited the financial statements of the governmental activities, the business-type activities, each major fund, and each fiduciary fund type, of the San Juan County (Silverton) School District No. 1 as of and for the year ended June 30, 2015 and have issued our report thereon dated November 17, 2015. Professional standards require that we provide you with the following information related to our audit.

Our Responsibility under U.S. Generally Accepted Auditing Standards
As stated in our engagement letter dated July 31, 2015, our responsibility as described by professional standards, is to express an opinion about whether the financial statements prepared by management with your oversight are fairly presented, in all material respects, in conformity with U.S. generally accepted accounting principles. Because an audit is designed to provide reasonable, but not absolute assurance and because we did not perform a detailed examination of all transactions, there is a risk that material misstatements may exist and not be detected by us.

As part of our audit, we considered the internal controls of the District. Such considerations were solely for the purpose of determining our audit procedures and not to provide any assurance concerning such internal control.

Our audit of the financial statements does not relieve you or management of your responsibilities.

Planned Scope and Timing of the Audit
We performed the overall audit fieldwork according to the planned scope and timing previously communicated to you during the planning stages of our audit procedures. The final report was delayed due to delays in receiving CDE data transmittal reports from the District for inclusion in the audit.

Significant Audit Findings:

Qualitative Aspects of Accounting Practices

Significant Accounting Policies
Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application.

The significant accounting policies used are described in Note 1 of the financial statements. No new accounting policies were adopted and the application of the existing policies was not changed during the year under audit. We noted no transactions entered into by the District during the year that were both significant and unusual or transactions 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.

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Qualitative Aspects of Accounting Practices – *continued*

Accounting Estimates
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. We evaluated the key factors and assumptions used to develop the estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

Financial Statement Disclosures
The disclosures in the financial statements are neutral, consistent and clear. Certain financial statement disclosures are particularly sensitive because of their significance to the financial statement users. The most sensitive disclosures affecting the financial statements are:

- The disclosure of the measurement focus and basis of accounting in Note 1 of the financial statements.
- The disclosure of capital assets in Note 4 of the financial statements.
- The disclosure of long-term obligations in Note 5 of the financial statements.
- The disclosure of compliance in Note 14 of the financial statements.

We evaluated the key factors and underlying information used to develop the disclosures above in determining that they are reasonable in relation to the financial statements taken as a whole.

Difficulties Encountered in Performing the Audit
We encountered no difficulties in dealing with management in performing and completing our audit.

Corrected and Uncorrected Misstatements
Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are trivial, and communicate them to the appropriate level of management. Management has corrected all such misstatements. 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). In our judgment, none of the adjustments we proposed, whether recorded or unrecorded by the District, either individually or in the aggregate, indicate matters that could have a significant effect on the District's financial reporting process.

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

Management Representations
We have requested certain representations from management that are included in the management representation letter dated November 17, 2015.

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 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 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.

COMMUNICATIONS WITH MANAGEMENT: INTERNAL CONTROLS COMMUNICATIONS

In planning and performing our audit of the financial statements, we considered internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on internal control. Our consideration of internal control would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses.

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 *material weakness* is a deficiency, or a combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the District's financial statements will not be prevented or detected and corrected on a timely basis. A *significant deficiency* is a deficiency, or a combination of deficiencies, in internal control that is less severe than a material weakness, yet important enough to merit the attention by those charged with governance.

Our consideration of internal control was for the limited purpose described above and would not necessarily identify all deficiencies in internal control that might be significant deficiencies or material weaknesses. We did not identify any deficiencies in the internal control system that we consider to be material weakness as defined above. However, we did note the following items which we believe merit your attention:

1) Due to the limited size of the staff, there is a lack of proper segregation of duties for the accounting and reporting functions (i.e., the functions of initiating, recording and processing payments) which results in an inherent risk that a misstatement that is more than inconsequential *could* occur and not be prevented or detected by the internal control system.

2) Management does not prepare its own year-end financial statements, inclusive of note disclosures. As such, management requested our firm to assist in the preparation of the draft financial statements, including the related footnote disclosures. The outsourcing of this service is not unusual in entities of your size and is a result of management's cost-benefit decision to use our accounting expertise rather than to incur additional costs.

Comments and Recommendations

Our audit provides an opportunity to observe operations and identify potential areas where improvements can be made and also areas that are functioning well. We found the books and records to be in sufficient working order. The balance sheet accounts were reconciled, prior year-end adjustments were properly recorded, and all transactions were adequately explained. We noted good awareness and compliance with sound business practices and controls, and no unusual adjustments to the financial records were necessary.

In the spirit of continually improving the efficiency and cost-effectiveness of the District's operations, we offer the following comments and recommendations.

General Accounting System

The general accounting system's overall reporting capabilities revealed no inherent limitations that would preclude access to specific information in order to fulfill internal and external reporting requirements. We recognize the efforts of the staff to maintain sufficient internal controls and other operating procedures and noted the implementation of prior year recommendations.

Governmental Accounting Standards Board Statement No. 68

Fiscal year 2015 is the implementation year for Governmental Accounting Standards Board Statement No. 68, *Accounting and Financial Reporting for Pensions*. This statement relates to accounting and financial reporting issues and how pension costs and obligations are measured and reported in audited external financial reports. The implementation of this standard is the largest change to governmental reporting since the implementation of GASB Statement No. 34.

While there has been a close relationship between how governments fund pensions and how they account and report information until now, the new guidance establishes a decided shift from a funding-based approach to an accounting-based approach. This shift is designed to improve pension reporting and increase the transparency, consistency and comparability of pension information across governments. Historically, GASB viewed an unfunded pension obligation as a liability to be reported in future financial statements, rather than as an existing liability of the employer or plan, and information about the total liability was disclosed in the required supplemental information of the plan. GASB has adopted a formal definition of a liability for purposes of governmental financial reporting, known as the Net Pension Liability, which now shows on each participating employer's balance sheet as a proportionate share of the total net pension liability (unfunded liability) of the pension trust fund at PERA.

It is important to note that this new reporting requirement does not necessarily reflect the financial condition of a governmental entity because a pension liability cannot be made immediately due and payable. Additionally, the implementation of GASB Statement No. 68 has no impact on the District's fund level financial statements which are used for internal and budgetary use; rather, the change only effects the District's government-wide financial statement reporting in the year-end audited financial statements. The District's government-wide Statement of Net Position now reflects the District's share of the State PERA pension liability in the amount of $2,467,950 which is the District's 0.0182091388% proportionate share of the State PERA overall pension liability of $13,553,359,000 for the School Division Trust Fund. Other pension related amounts considered as deferred inflows and deferred outflows are also now reflected on the government-wide Statement of Net Position. As indicated in Note 17, the implementation of GASB Statement No. 68 also required restatement of prior year Net Position in the net amount of $2,478,677 for the applicable previous year pension liability and related deferred outflows.

Disbursements

During our tests of transactions, we noted two checks (#17973 and #18364) that were missing supporting invoices, two checks (#17784 and #18045) that did not have substantiating receipts, one check (#18343) for which no supporting documentation could be located, and 4 checks that were missing dual signatures. The District has internal controls that have been sufficiently designed, but need to be followed for all transactions in order to ensure that all District disbursements have supporting information in accordance with the internal control process.

Visa Card Disbursements

During our procedures we noted that although a visa charge summary face sheet was included with each statement, there were several transactions for which the supporting visa card charge receipts could not be located. We recommend that updated procedures be put into place to ensure that all visa card charges have supporting documentation before the items are paid by the District, or if the individual initiating the charge cannot produce supporting documentation, that the individual be held responsible for the charge.

We also noted that sales tax is being charged on some District purchases. We recommend that the District remind employees who are making purchases with District credit cards of the District's tax-exempt status.

We also noted that it appears that receipts for purchases are not always being turned in on a timely basis, and that reimbursements are being made in advance of all receipts being turned in. Internal Revenue Service regulations require that to qualify as an accountable plan, all reimbursements must be supported by substantiating documentation within 60 days, otherwise reimbursements could be required to be included in employee wages (and left to be deducted on the employees personal income tax return). We recommend that employees be notified that all substantiating documentation (i.e., receipts) must be turned in within 60 days in order to qualify for reimbursement.

In addition, it appears that on occasion that credit cards have been 'accidentally' used for personal purchases when in the employee's possession. Although we did find that amounts in question had been properly reimbursed to the District, we recommend that a policy be put into place that the District's credit cards never be used for personal items.

Employee Payroll Files

During our tests of transactions we noted several employee files that were either missing required I-9 employee information or the Employer portion of the form had not been completed. We recommend that all employee files be reviewed to ensure that all required I-9 documentation is included and that current period approved salary rates be updated in the employee file on an annual basis. (This can be facilitated through the use of a 'checklist' as a face sheet in each employee file.)

Payroll Benefits

During our procedures on the Food Service Fund, we noted that although food service salaries were a consistent amount from month-to-month, that the payroll allocation for benefits fluctuated (the expectation would be for this amount to be consistent as well). Although immaterial to the financial statements taken as a whole, we recommend that future payroll benefit allocations be reviewed to ensure that proper amounts are being recorded in each applicable fund.

Preschool Fund Budgetary Allocations

Rather than budgeting an exact amount for the District's preschool allocation, we recommend that the allocation be rounded up to the nearest $5,000 increment in order to ensure that errors in the computation do not result in potential budgetary violation.

Budgets

As noted in prior years, the Colorado Department of Education Form CDE-18, *Report of Supplemental Budget*, requires that <u>all</u> fund balances available for appropriation be included in "Beginning Fund Balances" to ensure that any non-appropriated operating reserves do not exceed 15% of Total Expenditures and Reserves. The District, again, did not include all available general fund balances in "Beginning Fund Balance" on the Form CDE-18.

Budgets (continued)

As indicated in Note 15(C) of the financial statements, the District's final budgetary appropriations for three funds were insufficient for current year expenditures and other financing uses which may not be in compliance with Colorado Revised Statutes:

General Fund – The general fund total expenditures exceeded final appropriations by $119,089.

Food Service (Special Revenue) Fund – The new food service special revenue fund 21 total expenditures exceeded final appropriations by $16,097.

Food Service (Enterprise) Fund – The old food service enterprise fund 51 was eliminated during the current year in accordance with recommendations of the Colorado Department of Education; however, no appropriations were made for the transfer of total assets to governmental activities, resulting in total other financing uses in excess of final appropriations.

In addition, the Food Service (Special Revenue) Fund final budgetary appropriations exceeded total available fund balances and budgetary resources by $2,810. This also may not be in compliance with Colorado Revised Statutes

We recommend that annual budgets be reviewed at the time of final appropriation to ensure compliance with required budgetary statutes, as well as requirements of the Colorado Department of Education.

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We have provided these and other general recommendations related to accounting for the District's activity; however, management is ultimately responsible for the selection and use of appropriate accounting policies and for oversight, thereof.

We would again like to congratulate the District on CDEs commendation for the overall quality of presentation of the prior several year's audits and submissions of data through the Automated Data Exchange. It is apparent to us that the District strives for continual improvements in financial recordkeeping and reporting.

We are available at your convenience to clarify or assist you with any items discussed above or other concerns you may have.

This report is intended for the information and use of the Board of Education of the San Juan County (Silverton) School District No. 1, District management and others with the organization. This restriction is not intended to limit distribution of the report, which, upon acceptance by the Board of Directors, is a matter of Public Record.

We wish to thank the Board for engaging us to be your independent auditors and would like to extend a special thank you to the District staff for their assistance and cooperation in completing the audit.

Hays, Maggard & Hood P.C.

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