# The Dearborn Academy

**Report to the Board of Directors**

**June 30, 2019**

plante moran

**Plante & Moran, PLLC**
Suite 100
1111 Michigan Ave.
East Lansing, MI 48823
Tel: 517.332.6200
Fax: 517.332.8502
plantemoran.com

To the Board of Directors
The Dearborn Academy

We have recently completed our audit of the basic financial statements of The Dearborn Academy (the "Academy") as of and for the year ended June 30, 2019. In addition to our audit report, we are providing the following results of the audit and informational items that impact the Academy:



We are grateful for the opportunity to be of service to The Dearborn Academy. We would also like to extend our thanks to Zeina Hamdan for her assistance and preparedness during the audit. We recognize that preparing for the audit is carried out in addition to your staff's normal daily activities. Should you have any questions regarding the comments in this report, please do not hesitate to call.

Plante & Moran, PLLC

October 21, 2019

# Results of the Audit

plante moran

Plante & Moran, PLLC
Suite 100
1111 Michigan Ave.
East Lansing, MI 48823
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October 21, 2019

To the Board of Directors
The Dearborn Academy

We have audited the financial statements of The Dearborn Academy (the "Academy") as of and for the year ended June 30, 2019 and have issued our report thereon dated October 21, 2019. 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 May 29, 2019, 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. Our audit of the financial statements does not relieve you or management of your responsibilities. Our responsibility is to plan and perform the audit to obtain reasonable, but not absolute, assurance that the financial statements are free of material misstatement.

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

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

Our audit of the Academy's financial statements has also been conducted in accordance with *Government Auditing Standards*, issued by the Comptroller General of the United States. Under *Government Auditing Standards*, we are obligated to communicate certain matters that come to our attention related to our audit to those responsible for the governance of the Academy, including compliance with certain provisions of laws, regulations, contracts, grant agreements, certain instances of error or fraud, illegal acts applicable to government agencies, and significant deficiencies in internal control that we identify during our audit. Toward this end, we issued a separate letter dated October 21, 2019 regarding our consideration of the Academy's internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements.

**Planned Scope and Timing of the Audit**

We performed the audit according to the planned scope and timing previously communicated to you in our meeting about planning matters on September 23, 2019.

## Significant Audit Findings

### *Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. In accordance with the terms of our engagement letter, we will advise management about the appropriateness of accounting policies and their application. The significant accounting policies used by the Academy are described in Note 2 to the financial statements.

No new accounting policies were adopted, and the application of existing policies was not changed during 2019.

We noted no transactions entered into by the Academy during the year for which there is a lack of authoritative guidance or consensus.

We noted no significant transactions that have been recognized in the financial statements in a different period than when the transaction occurred.

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

The most sensitive estimates affecting the financial statements were the Academy's share of the MPSERS net liabilities for the pension and other postemployment benefit (OPEB) plans recorded on the government-wide statements related to GASB Statement Nos. 68 and 75, respectively. The Academy's estimates as of June 30, 2019 were $230,718 and $61,148 for the pension and OPEB plans, respectively, based on data received from the Office of Retirement Services. We evaluated the key factors and assumptions used to develop the accounting estimates in determining that they are reasonable in relation to the financial statements taken as a whole.

The disclosures in the financial statements are neutral, consistent, and clear.

### *Difficulties Encountered in Performing the Audit*

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

### *Disagreements with Management*

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

### *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. We did not detect any misstatements as a result of audit procedures.

***Significant Findings or Issues***

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, business conditions affecting the Academy, and business plans and strategies that may affect the risks of material misstatement, with management each year prior to our retention as the Academy's auditors. However, these discussions occurred in the normal course of our professional relationship, and our responses were not a condition of our retention.

As required by 2 CFR Part 200, we have also completed an audit of the federal programs administered by the Academy. The results of that audit are provided to the board of directors in our report on compliance with requirements applicable to each major program and on internal control over compliance in accordance with 2 CFR Part 200 dated October 21, 2019.

***Management Representations***

We have requested certain representations from management that are included in the management representation letter dated October 21, 2019.

***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 Academy's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were no such consultations with other accountants.

This information is intended solely for the use of the board of directors and management of the Academy and is not intended to be and should not be used by anyone other than these specified parties.

Very truly yours,

**Plante & Moran, PLLC**

Michael D. Foster

Michael D. Foster, CPA, CGMA
Partner

# Informational Items

## State Aid Funding

### State Aid and the Foundation Allowance

With a new governor comes new funding priorities. The governor has laid out her executive recommendations, which include a comprehensive plan to fund roads and school funding improvements. These initiatives created significant discussion and encouraged the Legislature to develop its own plans and strategies. This meant that Michigan schools began the July 1, 2019 budget year without knowing what their funding levels would be for the 2019-2020 school year. It also meant a lack of clarity surrounding which initiatives would survive the legislative process and whether any new initiatives would be funded, which limited the ability to plan and staff for these initiatives accordingly. Academies were required to use the best information at hand to estimate what funding levels might be in place in order to develop annual budgets. As a result, academies will be required to revisit budget assumptions once the State of Michigan finalizes its funding plan for public schools. Factors continuing to impact school funding include the level of increase for the foundation allowance; additional funding boosts for academies at the minimum foundation; the student count blending formula; resources dedicated to assisting with funding the Academy's retirement/postretirement healthcare obligation (MPSERS), including implications from changes in plan assumptions and costs incurred from changes to retirement system programs; and what, if any, supplemental funding is provided based on the School Finance Collaborative recommendations.

2018-2019 Foundation: For the 2018-2019 fiscal year, the academy maximum foundation allowance increased by $240, from $7,631 to $7,871. The State continued its use of the "2X formula," providing academies at the minimum foundation with an increase of $240 per pupil to $7,871. The Academy's foundation allowance was increased to $7,871.

2019-2020 Foundation: For the 2019-2020 fiscal year, the public school academy target foundation allowance is yet to be determined, as the governor has vetoed a portion of Section 20 of the State Aid Bill. When signing the bill, the governor exercised several significant line item vetoes. As a result, it is likely that there will be additional changes to funding for public education for 2019-2020. What will ultimately occur is unclear and will require careful monitoring by the Academy. Although the foundation allowance for academies has been finalized, the governor has made multiple line item vetoes to the School Aid bill that impact various funding categoricals. The impact on the Academy will not be determined until the governor signs the final bill.

Pupil Membership Blend for 2018-2019 and 2019-2020: The method for counting students for 2018-2019 used calendar year counts with a weighting of 90 percent of the fall count and 10 percent of the February count. The 2018 calendar year counts were used for the 2018-2019 fiscal year funding. It is expected that this methodology will continue for 2019-2020.

MPSERS Cost Support: Retirement system contributions are a significant part of the Academy's labor costs. During 2018-2019, the contribution rate the Academy is required to pay continued to rise, though the growth rate has slowed. In addition, as a result of PA 92, the program offerings have changed and increased in complexity. The Academy has no ability to influence the rate and no choice regarding its participation in the program. To aid the Academy in meeting its obligation, the 2018-2019 State Aid Act continued to include several funding sources to help pay for some of the increased cost. Each categorical aid section is formula driven using the Academy's MPSERS payroll participation data, and each is designed to support a specific cost factor in the retirement contribution. Funding is provided in three separate sections of the State Aid Act: Sections 147a, 147c, and 147e. The Academy received a total of $912 in 147a1, $721 in 147a2, and $8,448 in 147c1 categorical aid to help offset the impact of its retirement costs. Both governor and legislative proposals included these categoricals for 2019-2020. In general terms, this means that the total cost of the retirement system contributions in 2018-2019, representing approximately 39 percent of covered payroll, is recognized as an expenditure in the Academy's financial statements along with related revenue that was previously considered state support to the system. The net effect is that the Academy is responsible for approximately a 27 percent contribution to the retirement system. The Academy budgeted for additional state revenue and additional retirement expenditures in order to accommodate this funding mechanism, but may encounter some budget variances due to the fact that the state revenue provided is based on prior year academy payroll information, and some amounts were adjusted with the August 2019 state aid payment.

Many factors influence the retirement rate. Two significant factors include rate of return and employee benefit elections. The assumed rate of return within the retirement plan decreased from 7.5 percent to approximately 7.05 percent. When this assumption is reduced, it has the net effect of increasing the value of the retirement obligation for the plan. This then increases the required contributions to fund the plan. For staff hired on or after February 1, 2018, the default employee election is the defined contribution (DC) plan; however, an employee can elect the hybrid plan within a specified time frame. Academy contributions and state support are also modified for employees electing the new DC plan. This benefit election changes the Academy's cost of the benefit for employees new to the retirement system beginning in February 2018. To offset some of the additional cost, funding is provided under Section 147e.

**Other State Aid Act Changes Impacting 2018-2019**

Overall, 2018-2019 State Aid Act amendments did not include significant new program initiatives. Several changes of note impacting the Academy's 2018-2019 revenue include the following:

Student Assessment Changes: The grades that take the summative science test were changed from fourth and seventh grades to fifth and eighth grades. New state funding for a kindergarten entry observation tool was provided that also added requirements for the summative assessments for math and ELA to be aligned to the PSAT. In addition, conditioned reimbursement was set for benchmark assessments on academies choosing one benchmark and using it for at least three years. These provisions were discussed in Sections 102d, 104, and 104c of the 2018-2019 State Aid Act amendments.

Support from the State's General Fund: Since the adoption of Proposal A, the State's General Fund has provided support to the School Aid Fund. For the last several years, the level of General Fund support has continued to fall. For 2018-2019, the trend continued, with a $60 million reduction in support. On a statewide basis, the reduction in support equates to approximately $40 per student.

**State Aid Planning Considerations for 2019-2020 and Beyond**

Michigan's economy is growing steadily, and continued growth is expected, but at a slower pace based on the May 2019 Revenue Estimating Conference predictions. A new governor has brought revised priorities for education and for state operations. The State's budget process demonstrates that state leaders are struggling with how best to address the State's policy needs. This struggle directly impacts the level of school funding, the allocation of school funding resources, and the educational initiatives. Regardless of the results of the 2019-2020 state budget process, it is likely that there will continue to be strains placed on the School Aid Fund resources. How these issues are worked through the legislative process will have a direct impact on the Academy's near-term and long-term funding structures. Careful review of the budget priorities and budget development process will be essential as the Academy continues to craft its plans for delivery of educational services.

Regardless of the results from the 2019-2020 State Aid Act amendments, careful planning will continue to be key for the Academy to create a cost structure that is sustainable. The use of budget modeling is essential, especially as the Academy looks to determine actual state funding available to fund regular education operations, as well as funding for specific initiatives. During the budget planning process, it is important to segregate resources required to fund specific activities, such as federal funding, special education, or At-Risk, when assessing the resources available to fund continuing operations. Especially when facing uncertainty, we recommend the Academy fully analyze the projected revenue assumptions to estimate resources available to fund operations when entering into multiyear expenditure agreements.

**Enrollment Projections**

Academies rely heavily on student enrollment for funding, future academic offerings, and logistical decisions. Detailed projections allow your school board to adequately plan for expansion, contraction, renovation, construction, and academic opportunities, maneuvering them into the best position to fulfill the Academy's mission. Plante Moran Cresa, an affiliate of Plante & Moran, PLLC, is one of the authorized service providers recognized by the Michigan Department of Treasury to provide enrollment projections. Plante Moran Cresa's team has developed a pupil enrollment projection model that has proven to be over 99 percent accurate in helping academies predict enrollment for years into the future. The projections can be conducted for the entire Academy or focused solely on specific buildings or areas.

**Single Audit Update - Changes to Auditor Required Testing and Data Collection Forms**

The 2019 Compliance Supplement has been released. This supplement is issued as one stand-alone document and includes significant and extensive changes this year compared to recent years. The 2019 Compliance Supplement will be effective for audits of fiscal years beginning after June 30, 2018. Appendix V of the 2019 Compliance Supplement identifies all changes at a high level and identifies specific programmatic changes by CFDA number. The most significant change implemented is the six-requirement mandate, in which the Office of Management and Budget (OMB) requires agencies to limit compliance requirements subject to the compliance audit to six per program or cluster included in the 2019 Compliance Supplement. For "counting" purposes, the requirements relating to (a) activities allowed and unallowed, and (b) allowable costs and cost principles are counted as one requirement. In addition at the 11th hour OMB issued a revision to the Supplement issued in July. These changes issued in September did have some impact on grants provided to public education, further complicating the 2019 audit process. It is important to note that auditees are still required to comply with all applicable grant regulations. While auditees may experience some change in audit focus in preparing for the audit, facts and circumstances of each grant will dictate the impact on the audit of federal grants.

The new 2019 data collection form (DCF) has been issued and is effective for period ending dates in 2019 through 2021. This form is very important, as it is the key document reporting federal program grants, auditor opinions, grants tested, and now detailed footnotes and findings to the federal government. A summary of changes to the DCF this year are as follows:

- The collections system now allows all respondents to enter the federal awards and notes to the SEFA prior to the end of their fiscal period and the audit work being conducted. Once this information is entered, users may generate a customizable SEFA and notes to the SEFA from the system to include in their reporting package.
- Part II, Item 2 will be used to provide the notes to the SEFA, including a description of the significant accounting policies used in preparing the SEFA, whether the auditee elected to use the *de minimis* cost rate, and any additional notes included in the reporting package, excluding charts, tables, or footnotes.
- Part III, Item 5 will be used to collect the full, detailed text of any audit findings exactly as it appears in the schedule of findings and questioned costs (2 CFR 200.516(b)), excluding charts, tables, or footnotes. This information is now being collected at the request of federal agencies for audit finding resolution purposes.
- Part IV will be used to collect the full, detailed text of the corrective action plan exactly as it appears in the auditee's corrective action plan (CAP) (2 CFR 200.511(c)), excluding charts, tables, or footnotes. This information is now being collected at the request of federal agencies for audit finding resolution purposes.

## GASB Statement No. 87 - Leases

GASB Statement No. 87, *Leases*, is effective for the first time in the Academy's June 30, 2021 financial statements. The statement requires recognition of certain lease assets and liabilities for leases that previously were classified as operating leases and recognized as inflows or outflows of resources based on payment provisions of the lease. The statement was issued to improve accounting and financial reporting for leases by governments. The statement establishes a single model for lease accounting for both lessees and lessors based on the foundational principle that leases are financings of the right to use an underlying asset. Under this statement, a lessee is required to recognize a lease liability and an intangible right-to-use lease asset on the lessee's government-wide financial statements, and a lessor is required to recognize a lease receivable and a deferred inflow of resources on the lessor's government-wide financial statements. Furthermore, there are additional financial statement disclosures required for the lessee and lessor as a result of the standard. The Academy will have to identify and analyze all significant lease contracts to determine the lease asset and lease liability or deferred inflow or outflow of resources that will be required to be recognized upon implementation of the standard. This review should include all existing lease contracts and contracts that may have embedded lease arrangements that were not previously considered.

### Lessee Accounting Under GASB 87

A lessee should recognize a lease liability and a lease asset at the commencement of the lease term, unless the maximum lease term per the lease contract is 12 months or less or it transfers ownership of the underlying asset. The lease liability is measured at the present value of lease payments expected to be made during the lease term (less any lease incentives). The right-to-use asset is measured at the amount of initial measurement of the lease liability, plus any payments made to the lessor at or before commencement of the lease term and certain direct costs incurred to place the leased asset in service. The lessee should reduce the lease liability as payments are made and recognize an outflow of resources (i.e., expense) for interest on the liability. The lease asset should be amortized in a systematic and rational manner over the shorter of the lease term or the useful life of the underlying asset.