

Hermitage School District No. 12

Bradley County, Arkansas

Regulatory Basis Financial Statements and Other Reports

June 30, 2005



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BRADLEY COUNTY, ARKANSAS
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Sen. Henry "Hank" Wilkins, IV
Senate Co-Chair
Rep. Tommy G. Roebuck
House Co-Chair
Sen. Randy Laverty
Senate Co-Vice Chair
Rep. Sandra Prater
House Co-Vice Chair

Arkansas



Charles L. Robinson, CPA, CFE
Legislative Auditor

LEGISLATIVE JOINT AUDITING COMMITTEE DIVISION OF LEGISLATIVE AUDIT INDEPENDENT AUDITOR'S REPORT

Hermitage School District No. 12 and School Board Members
Legislative Joint Auditing Committee

We have audited the accompanying financial statements of each major governmental fund and the aggregate remaining fund information of the Hermitage School District No. 12 (the "District"), as of and for the year ended June 30, 2005, as listed in the table of contents. These financial statements are the responsibility of District 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.

As described more fully in Note 1, the District has prepared the financial statements using accounting practices prescribed or permitted by Arkansas Code, which differ from accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between these regulatory accounting practices and accounting principles generally accepted in the United States of America, although not reasonably determined, are presumed to be material.

In our opinion, because of the effects of the matter discussed in the preceding paragraph, the financial statements referred to above do not present fairly, in conformity with accounting principles generally accepted in the United States of America, the financial position of the District as of June 30, 2005, or the changes in financial position thereof, for the year then ended.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of each major governmental fund and the aggregate remaining fund information of the District as of June 30, 2005, and the respective changes in financial position and budgetary results for the year then ended, on the basis of accounting described in Note 1.

In accordance with *Government Auditing Standards*, we have also issued our report dated April 12, 2006 on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on the internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's regulatory basis financial statements. The Schedule of Capital Assets (Schedule 1), Expenditures of Federal Awards (Schedule 2), as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, Federal Award Programs – Findings and Questioned Costs (Schedule 3) and Federal Award Programs – Summary of Prior Audit Findings (Schedule 4) are presented for purposes of additional analysis and are not a required part of the regulatory basis financial statements. The Expenditures of Federal Awards (Schedule 2), Federal Award Programs – Findings and Questioned Costs (Schedule 3) and Federal Award Programs – Summary of Prior Audit Findings (Schedule 4) have been subjected to the auditing procedures applied in the audit of the regulatory basis financial statements and, in our opinion, are fairly stated in all material respects in relation to the regulatory basis financial statements taken as a whole. The Schedule of Capital Assets (Schedule 1) has not been subjected to the auditing procedures applied in the audit of the regulatory basis financial statements and, accordingly, we express no opinion on it.

DIVISION OF LEGISLATIVE AUDIT

A handwritten signature in cursive script, appearing to read "Charles L. Robinson".

Charles L. Robinson, CPA, CFE
Legislative Auditor

Little Rock, Arkansas
April 12, 2006
EDSD03205

Sen. Henry "Hank" Wilkins, IV
Senate Co-Chair
Rep. Tommy G. Roebuck
House Co-Chair
Sen. Randy Laverty
Senate Co-Vice Chair
Rep. Sandra Prater
House Co-Vice Chair

Arkansas



Charles L. Robinson, CPA, CFE
Legislative Auditor

LEGISLATIVE JOINT AUDITING COMMITTEE DIVISION OF LEGISLATIVE AUDIT

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*

Hermitage School District No. 12 and School Board Members
Legislative Joint Auditing Committee

We have audited the financial statements of each major governmental fund and the aggregate remaining fund information of the Hermitage School District No. 12 (the "District"), as of and for the year ended June 30, 2005, which collectively comprise the District's regulatory basis financial statements, and have issued our report thereon dated April 12, 2006. 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. We issued an adverse opinion because the District prepared the financial statements using accounting practices prescribed or permitted by the Arkansas Code, which differ from accounting principles generally accepted in the United States of America. The effects on the financial statements of the variances between these regulatory accounting practices and accounting principles generally accepted in the United States of America, although not reasonably determined, are presumed to be material. However, the financial statements present fairly, in all material respects, the respective financial position of each major governmental fund and the aggregate remaining fund information of the District as of June 30, 2005, and the respective changes in financial position and budgetary results for the year then ended, on the basis of accounting described in Note 1.

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the District's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinions on the regulatory basis financial statements and not to provide an opinion on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the District's ability to initiate, record, process, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described in the accompanying schedule of Federal Award Programs - Findings and Questioned Costs as items 2005-1 and 2005-2.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the regulatory basis financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider finding numbers 2005-1 and 2005-2 in the accompanying schedule of Federal Award Programs - Findings and Questioned Costs to be material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's regulatory basis financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of the state constitution, state and federal laws and regulations, and contracts and grant agreements, 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 or other matters that are required to be reported under *Government Auditing Standards*.

These reports are intended solely for the information and use of the Legislative Joint Auditing Committee, the local school board and District management, state executive and oversight management, federal regulatory and oversight bodies, the federal awarding agencies and pass-through entities, and other parties as required by Arkansas Code, and are not intended to be and should not be used by anyone other than these specified parties. However, pursuant to Arkansas Code Annotated §10-4-417, all reports presented to the Legislative Joint Auditing Committee are matters of public record and distribution is not limited.

DIVISION OF LEGISLATIVE AUDIT

William R. Baum

William R. Baum, CPA, CFE
Deputy Legislative Auditor

Little Rock, Arkansas
April 12, 2006

Sen. Henry "Hank" Wilkins, IV
Senate Co-Chair
Rep. Tommy G. Roebuck
House Co-Chair
Sen. Randy Laverty
Senate Co-Vice Chair
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House Co-Vice Chair

Arkansas



Charles L. Robinson, CPA, CFE
Legislative Auditor

LEGISLATIVE JOINT AUDITING COMMITTEE DIVISION OF LEGISLATIVE AUDIT

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

Hermitage School District No. 12 and School Board Members
Legislative Joint Auditing Committee

Compliance

We have audited the compliance of the Hermitage School District No. 12 (the "District") 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 each of its major federal programs for the year ended June 30, 2005. The District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of Federal Award Programs - 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 District's management. Our responsibility is to express an opinion on the District'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 District'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 District's compliance with those requirements.

In our opinion, the District 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, 2005.

Internal Control Over Compliance

The management of the District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts and grants applicable to federal programs. In planning and performing our audit, we considered the District's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be material weaknesses. A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with applicable requirements of laws, regulations, contracts and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over compliance and its operation that we consider to be material weaknesses.

These reports are intended solely for the information and use of the Legislative Joint Auditing Committee, the local school board and District management, state executive and oversight management, federal regulatory and oversight bodies, the federal awarding agencies and pass-through entities, and other parties as required by Arkansas Code, and are not intended to be and should not be used by anyone other than these specified parties. However, pursuant to Arkansas Code Annotated §10-4-417, all reports presented to the Legislative Joint Auditing Committee are matters of public record and distribution is not limited.

DIVISION OF LEGISLATIVE AUDIT

William R. Baum

William R. Baum, CPA, CFE
Deputy Legislative Auditor

Little Rock, Arkansas
April 12, 2006

HERMITAGE SCHOOL DISTRICT NO. 12
 BRADLEY COUNTY, ARKANSAS
 BALANCE SHEET - REGULATORY BASIS
 JUNE 30, 2005

Exhibit A

	Governmental Funds			
	Major			Fiduciary Fund Types
	General	Special Revenue	Other Aggregate	
ASSETS				
Cash	\$ 968,127	\$ 29,088	\$ 216,046	\$ 9,030
Deposit with paying agent	26,200			
Investments	123,840		1,803,591	
Accounts receivable	14,670	1,480		
Property taxes receivable	26,321			
Due from other funds			1,271	
TOTAL ASSETS	\$ 1,159,158	\$ 30,568	\$ 2,020,908	\$ 9,030
LIABILITIES AND FUND BALANCES				
Liabilities:				
Accounts payable	\$ 44,367			
Due student groups				\$ 9,030
Due to other funds			\$ 1,271	
Total Liabilities	44,367		1,271	9,030
Fund Balances:				
Reserved:				
Debt service	26,200		1,271	
Capital projects			2,018,366	
Unreserved:				
Undesignated	1,088,591	\$ 30,568		
Total Fund Balances	1,114,791	30,568	2,019,637	
TOTAL LIABILITIES AND FUND BALANCES	\$ 1,159,158	\$ 30,568	\$ 2,020,908	\$ 9,030

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

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
GOVERNMENTAL FUNDS - REGULATORY BASIS
FOR THE YEAR ENDED JUNE 30, 2005

Exhibit B

	Major		Other Aggregate
	General	Special Revenue	
REVENUES			
Property taxes	\$ 775,281		
Property tax relief trust distribution	143,716		
State assistance	3,207,004	\$ 2,417	
Federal assistance	49,724	648,207	
Activity revenues	44,947		
Meal sales		51,280	
Investment income	15,158		\$ 43,435
Other revenues	17,474	15,663	
TOTAL REVENUES	4,253,304	717,567	43,435
EXPENDITURES			
Regular programs	1,902,858	40,756	
Special education	115,754	48,533	
Workforce education	141,603		
Compensatory education		215,336	
Other instructional programs	44,093		
Student support services	146,504	32,129	
Instructional staff support services	92,522	48,061	
General administration support services	253,177	6,580	
School administration support services	203,803		
Business support services	42,403		
Operation and maintenance of plant services	378,177		32,768
Student transportation services	251,566	3,190	
Central support services	95,027		
Other support services	930		
Food services operations		328,735	
Non-programmed costs	59,283	28,517	
Activity expenditures	45,474		
Capital outlay	330,537	21,138	20,050
Debt service:			
Principal retirement	8,349		85,000
Interest and fiscal charges	703		152,871
TOTAL EXPENDITURES	4,112,763	772,975	290,689
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	140,541	(55,408)	(247,254)
OTHER FINANCING SOURCES (USES)			
Transfers in		13,788	242,112
Transfers out	(255,900)		
Proceeds from postdated warrants	199,000		200,000
Proceeds from installment contracts	45,829		
Net postdated warrants issuance cost			(6,660)
AND OTHER USES	129,470	(41,620)	188,198
FUND BALANCES - JULY 1	985,321	72,188	1,831,439
FUND BALANCES - JUNE 30	<u>\$ 1,114,791</u>	<u>\$ 30,568</u>	<u>\$ 2,019,637</u>

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

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
BUDGET AND ACTUAL - GENERAL AND SPECIAL REVENUE FUNDS - REGULATORY BASIS
FOR THE YEAR ENDED JUNE 30, 2005

Exhibit C

	General			Special Revenue		
	Budget	Actual	Variance Favorable (Unfavorable)	Budget	Actual	Variance Favorable (Unfavorable)
REVENUES						
Property taxes	\$ 900,646	\$ 775,281	\$ (125,365)			
Property tax relief trust distribution		143,716	143,716			
State assistance	2,922,058	3,207,004	284,946		\$ 2,417	\$ 2,417
Federal assistance	49,724	49,724		\$ 410,397	648,207	237,810
Activity revenues		44,947	44,947			
Meal sales					51,280	51,280
Investment income	8,000	15,158	7,158			
Other revenues	202,000	17,474	(184,526)		15,663	15,663
TOTAL REVENUES	4,082,428	4,253,304	170,876	410,397	717,567	307,170
EXPENDITURES						
Regular programs	1,711,968	1,902,858	(190,890)	45,849	40,756	5,093
Special education	101,790	115,754	(13,964)	56,000	48,533	7,467
Workforce education	129,275	141,603	(12,328)			
Compensatory education				198,971	215,336	(16,365)
Other instructional programs	42,706	44,093	(1,387)			
Student support services	153,568	146,504	7,064	6,000	32,129	(26,129)
Instructional staff support services	101,709	92,522	9,187	78,479	48,061	30,418
General administration support services	235,251	253,177	(17,926)	6,800	6,580	220
School administration support services	207,100	203,803	3,297			
Business support services	48,397	42,403	5,994			
Operation and maintenance of plant services	327,420	378,177	(50,757)	2,500		2,500
Student transportation services	246,570	251,566	(4,996)	18,580	3,190	15,390
Central support services	94,165	95,027	(862)			
Other support services	6,000	930	5,070			
Food services operations				125,281	328,735	(203,454)
Community services				400		400
Non-programmed costs	86,000	59,283	26,717	25,000	28,517	(3,517)
Activity expenditures		45,474	(45,474)			
Capital outlay	306,200	330,537	(24,337)	4,694	21,138	(16,444)
Debt service:						
Principal retirement	13,037	8,349	4,688			
Interest and fiscal charges		703	(703)			
TOTAL EXPENDITURES	3,811,156	4,112,763	(301,607)	568,554	772,975	(204,421)

HERMITAGE SCHOOL DISTRICT NO. 12
 BRADLEY COUNTY, ARKANSAS
 STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES -
 BUDGET AND ACTUAL - GENERAL AND SPECIAL REVENUE FUNDS - REGULATORY BASIS
 FOR THE YEAR ENDED JUNE 30, 2005

Exhibit C

	General			Special Revenue		
	Budget	Actual	Variance Favorable (Unfavorable)	Budget	Actual	Variance Favorable (Unfavorable)
EXCESS OF REVENUES OVER (UNDER) EXPENDITURES	\$ 271,272	\$ 140,541	\$ (130,731)	\$ (158,157)	\$ (55,408)	\$ 102,749
OTHER FINANCING SOURCES (USES)						
Transfers in					13,788	13,788
Transfers out		(255,900)	(255,900)			
Proceeds from postdated warrants		199,000	199,000			
Proceeds from installment contracts		45,829	45,829			
EXCESS OF REVENUES AND OTHER SOURCES OVER (UNDER) EXPENDITURES AND OTHER USES	271,272	129,470	(141,802)	(158,157)	(41,620)	116,537
FUND BALANCES - JULY 1	964,337	985,321	20,984	78,423	72,188	(6,235)
FUND BALANCES - JUNE 30	\$ 1,235,609	\$ 1,114,791	\$ (120,818)	\$ (79,734)	\$ 30,568	\$ 110,302

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

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Board of Education, a (7) member group, is the level of government, which has responsibilities over all activities related to public elementary and secondary school education within the jurisdiction of the Hermitage School District (District). There are no component units.

B. Description of Funds

Major governmental funds (per the regulatory basis of accounting) are defined as General and Special Revenue.

General Fund - The General Fund is the general operating fund and is used to account for all financial resources, except those required to be reported in another fund.

Special Revenue Fund – The Special Revenue Fund is used to account for the proceeds of specific revenue sources (other than trusts for individuals, private organizations, or other governments or for major capital projects) that are legally restricted to expenditures for specified purposes.

Other governmental funds consist of the following:

Capital Projects Fund – The Capital Projects Fund is used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary funds or in trust funds for individuals, private organizations, or other governments).

Debt Service Fund – The Debt Service Fund is used to account for the accumulation of resources for, and the payment of, general long-term debt principal, interest and related costs.

Fiduciary Fund types include the following:

Agency Funds - Agency Funds are used to report resources held by the reporting government in a purely custodial capacity (assets equal liabilities).

C. Measurement Focus and Basis of Accounting

The financial statements are prepared in accordance with a regulatory basis of accounting (RBA). This basis of accounting is prescribed by Arkansas Code Annotated §10-4-413(c), as provided in Act 2201 of 2005, and requires that financial statements be presented on a fund basis with, as a minimum, the general fund and special revenue fund presented separately and all other funds included in the audit presented in the aggregate. The law also stipulates that the financial statements consist of a balance sheet; a statement of revenues, expenditures, and changes in fund balances; a comparison of the final adopted budget to the actual expenditures for the general fund and special revenue funds of the entity; notes to financial statements; and a supplemental schedule of capital assets, including land, buildings, and equipment. The law further stipulates that the State Board of Education shall promulgate the rules necessary to administer the regulatory basis of presentation.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

C. Measurement Focus and Basis of Accounting (Continued)

The RBA is not in accordance with generally accepted accounting principles (GAAP). GAAP require that basic financial statements present government-wide financial statements. Additionally, GAAP require the following major concepts: Management's Discussion and Analysis, accrual basis of accounting for government-wide financial statements, including depreciation expense, modified accrual basis of accounting for fund financial statements, separate financial statements for fiduciary fund types, separate identification of special and extraordinary items, inclusion of capital assets and debt in the financial statements, specific procedures for the identification of major governmental funds and applicable note disclosures. The RBA does not require government-wide financial statements or the previously identified concepts.

The accompanying financial statements are presented on a fund basis. A fund is defined as a fiscal and accounting entity with a self-balancing set of accounts, which are segregated for purposes of recording specific activities or attaining certain objectives. Revenues are reported by major sources and expenditures are reported by major function. Other transactions, which are not reported as revenues or expenditures, are reported as other financing sources and uses. Transactions related to the recording of installment contracts and capital leases are reported as other financing sources. Changes in private-purpose trust funds will be reflected in the notes to the financial statements.

D. Revenue Recognition Policies

Revenues are recognized when they become susceptible to accrual in accordance with the RBA.

E. Capital Assets

Information on capital assets and related depreciation is reported at Schedule 1. Capital assets are capitalized at historical cost or estimated historical cost, if actual data is not available. Capital assets purchased are recorded as expenditures in the applicable fund at the time of purchase. Donated capital assets are reported at fair value when received. The District maintains a threshold level of \$1,000 for capitalizing equipment. Library holdings are not capitalized.

No salvage value is taken into consideration for depreciation purposes. All capital assets, other than land and construction in progress, are depreciated using the straight-line method over the following useful lives:

Asset Class	Estimated Useful Life in Years
Improvements/infrastructure	7-30
Buildings	20-50
Equipment	5-20

F. Property Taxes

Property taxes are levied in November based on property assessment made between January 1 and May 31 and are an enforceable lien on January 1 for real property and June 1 for personal property. The tax records are opened on the first business day of March of the year following the levy date and are considered delinquent after October 10 of the same calendar year. Property taxes that are due at the end of the fiscal year and collected within 60 days are accrued. Deferred property taxes are not recognized.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

G. Interfund Receivables and Payables

Interfund receivables and payables result from services rendered from one fund to another or from interfund loans.

H. Fund Balance Designations

1. Reserved fund balance represents that portion of the fund balance which is not appropriate for expenditure or is legally segregated for a specific future use.
2. Undesignated fund balance indicates that portion of the fund balance not reserved or designated.

I. Budget and Budgetary Accounting

The District is required by state law to prepare an annual budget. The annual budget is prepared on a fiscal year basis. The District does not prepare and submit amended budgets during the fiscal year. The State Department of Education's regulations allow for the cash basis or the modified accrual basis. However, the majority of the school districts employ the cash basis method.

The District budgets intra-fund transfers. Significant variances may result in the comparison of transfers at the Statement of Revenues, Expenditures and Changes in Fund Balances – Budget and Actual – General and Special Revenue Funds – Regulatory Basis because only interfund transfers are reported at the Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds – Regulatory Basis.

Budgetary perspective differences are not considered to be significant, because the structure of the information utilized in preparing the budget and the applicable fund financial statements is essentially the same.

2: CASH DEPOSITS WITH FINANCIAL INSTITUTIONS

Cash deposits are carried at cost (carrying value). A comparison of the bank balance and carrying value is as follows:

	Carrying Amount	Bank Balance
Insured (FDIC)	\$ 200,000	\$ 200,000
Collateralized:		
Collateral held by the pledging bank or pledging bank's trust department in the District's name	2,949,558	3,082,030
Total Deposits	\$ 3,149,558	\$ 3,282,030

The above total deposits do not include cash on hand in the amount of \$164. The above total deposits include certificates of deposits of \$1,927,431 reported as investments and classified as nonparticipating contracts.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

3: RECEIVABLES

The receivables of \$42,471 at June 30, 2005, are as follows:

Class of Receivable	General Fund	Special Revenue Fund	Total
Taxes:			
Local	\$ 26,321		\$ 26,321
Grants:			
Federal		\$ 1,480	1,480
State assistance	14,670		14,670
Totals	<u>\$ 40,991</u>	<u>\$ 1,480</u>	<u>\$ 42,471</u>

4: COMMITMENTS

The District was contractually obligated for the following at June 30, 2005:

Long-term Debt Issued and Outstanding

The District is presently paying on the following long-term debt:

Date of Issue	Date of Final Maturity	Rate of Interest	Amount Authorized and Issued	Debt Outstanding June 30, 2005	Maturities To June 30, 2005
12/1/2003	12/1/2028	3.60%-4.95%	\$ 3,600,000	\$ 3,515,000	\$ 85,000
6/18/2003	6/18/2013	0.00%	141,175	141,175	
8/3/2004	8/3/2012	5.40%	199,000	199,000	
5/31/2005	5/31/2015	0.00%	200,000	200,000	
9/15/2004	12/5/2007	9.00%	18,628	13,620	5,008
9/20/2004	12/6/2008	5.75%	27,201	23,860	3,341
Totals			<u>\$ 4,186,004</u>	<u>\$ 4,092,655</u>	<u>\$ 93,349</u>

Changes in Long-term Debt

	Balance July 1, 2004	Issued	Retired	Balance June 30, 2005
Bonds payable	\$ 3,600,000		\$ 85,000	\$ 3,515,000
Postdated warrants	141,175	\$ 399,000		540,175
Installment contracts		45,829	8,349	37,480
Totals	<u>\$ 3,741,175</u>	<u>\$ 444,829</u>	<u>\$ 93,349</u>	<u>\$ 4,092,655</u>

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

4: COMMITMENTS (CONTINUED)

Total long-term debt principal and interest payments are as follows:

Year Ended June 30,	Principal	Interest	Total
2006	\$ 116,998	\$ 162,755	\$ 279,753
2007	123,613	157,900	281,513
2008	130,330	152,763	283,093
2009	145,612	146,386	291,998
2010	135,353	750,007	885,360
2011-2015	1,035,749	624,106	1,659,855
2016-2020	760,000	486,941	1,246,941
2021-2025	955,000	306,098	1,261,098
2026-2028	690,000	68,850	758,850
Totals	<u>\$ 4,092,655</u>	<u>\$ 2,855,806</u>	<u>\$ 6,948,461</u>

5: QUALIFIED ZONE ACADEMY BONDS (QZAB)

The District issued Qualified Zone Academy Bonds (QZAB's). This is a new financing vehicle created by the Tax Relief Act of 1997. QZAB's do not generally require interest payments from the borrower. The eligible financial institution holding the bond receives a tax credit in lieu of interest payments. The principal is not due until the end of the term. The borrower makes deposits into a sinking fund account annually and the sinking fund will earn interest.

- A. On June 18, 2003, the District borrowed \$141,175 using this method by issuing a postdate warrant. The District will deposit into a sinking fund at Bank of America \$13,037 for ten years, depositing a total of \$130,370 into the sinking fund. This amount plus interest will be used to retire the debt on June 18, 2013, the maturity date.
- B. On May 31, 2005, the District borrowed \$200,000 using this method by issuing a postdated warrant. The District will deposit into a sinking fund at Bank of America \$19,054 for ten years, depositing a total of \$190,540 into the sinking fund. This amount plus interest will be used to retire the debt on May 31, 2015, the maturity date.

6: ACCOUNTS PAYABLE

The payables of \$44,367 at June 30, 2005, are as follows:

	<u>General Fund</u>
Accounts	<u>\$ 44,367</u>

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

7: INTERFUND TRANSFERS

The Statement of Revenues, Expenditures and Changes in Fund Balances – Governmental Funds – Regulatory Basis (Exhibit B) reflects the following interfund transfers:

- A. A transfer of \$4,241 from the General Fund to the Building Fund for the acquisition or improvement to current capital facilities.
- B. A transfer of \$237,871 from the General Fund to the Debt Service Fund for debt related payments.
- C. A transfer of \$13,788 from the General Fund to the Special Revenue Fund to supplement the District's food service operation.

8: RETIREMENT PLANS

Arkansas Teacher Retirement System

Plan Description. The District contributes to the Arkansas Teacher Retirement System (ATRS), a cost-sharing multiple-employer defined benefit pension plan that covers all Arkansas public school employees, except certain nonteachers hired prior to July 1, 1989. ATRS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit and contribution provisions are established by State law and can be amended only by the Arkansas General Assembly. The Arkansas Teacher Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for ATRS. That report may be obtained by writing to Arkansas Teacher Retirement System, 1400 West Third Street, Little Rock, Arkansas 72201 or by calling 1-800-666-2877.

Funding Policy. ATRS has contributory and non-contributory plans. Contributory members are required by law to contribute 6% of their salary. Each participating employer is required by law to contribute at a rate established by the Arkansas General Assembly. The current employer rate is 14%. The District's contributions to ATRS for the years ended June 30, 2005, 2004 and 2003 were \$327,216, \$214,469 and \$184,848, respectively, equal to the required contributions for each year.

Arkansas Public Employees Retirement System

Plan Description. The District contributes to the Arkansas Public Employees Retirement System (PERS), a cost-sharing multiple-employer defined benefit pension plan that covers certain nonteaching Arkansas public school employees hired before July 1, 1989. PERS provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to plan members and beneficiaries. Benefit and contribution provisions are established by State law and can be amended only by the Arkansas General Assembly. The Arkansas Public Employees Retirement System issues a publicly available financial report that includes financial statements and required supplementary information for PERS. That report may be obtained by writing to Arkansas Public Employees Retirement System, One Union National Plaza, 124 W. Capitol, Little Rock, Arkansas 72201 or by calling 1-800-682-7377.

Funding Policy. PERS has contributory and non-contributory plans. Contributory members are required by law to contribute 6% of their salary. Each participating employer is required by law to contribute at a rate established by the Arkansas General Assembly. The current statutory employer rate is 4% of annual covered payroll. The District's contributions to PERS for the years ended June 30, 2005, 2004, and 2003 were \$942, \$941 and \$869, respectively, equal to the required contributions for each year.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
NOTES TO FINANCIAL STATEMENTS
JUNE 30, 2005

9: PRIOR YEAR ADJUSTMENT (Schedule 1)

A prior year adjustment of \$1,091 was made to adjust for the prior year overstatement of accumulated depreciation for a repair that was improperly capitalized.

10: SUBSEQUENT EVENTS

On November 15, 2005, the District issued \$648,000 in Qualified Zone Academy Bonds.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
SCHEDULE OF CAPITAL ASSETS
FOR THE YEAR ENDED JUNE 30, 2005

Schedule 1

	Balance July 1, 2004	Additions	Deletions	Prior Year Adjustment	Balance June 30, 2005
<i>Nondepreciable capital assets:</i>					
Land	\$ 42,785	\$ 9,612			\$ 52,397
Construction in progress		10,800			10,800
Total nondepreciable capital assets	<u>42,785</u>	<u>20,412</u>			<u>63,197</u>
<i>Depreciable capital assets:</i>					
Buildings	2,707,600	25,089	\$ 64,548		2,668,141
Improvements/infrastructure	73,397	3,315			76,712
Equipment	757,451	328,559	59,106		1,026,904
Total depreciable capital assets	<u>3,538,448</u>	<u>356,963</u>	<u>123,654</u>		<u>3,771,757</u>
Less accumulated depreciation for:					
Buildings	1,438,170	38,418	64,548		1,412,040
Improvements/infrastructure	20,211	2,927			23,138
Equipment	564,706	30,795	58,895	\$ (1,091)	535,515
Total accumulated depreciation	<u>2,023,087</u>	<u>72,140</u>	<u>123,443</u>	<u>(1,091)</u>	<u>1,970,693</u>
Total depreciable capital assets, net	<u>1,515,361</u>	<u>284,823</u>	<u>211</u>	<u>1,091</u>	<u>1,801,064</u>
Capital assets, net	<u>\$ 1,558,146</u>	<u>\$ 305,235</u>	<u>\$ 211</u>	<u>\$ 1,091</u>	<u>\$ 1,864,261</u>

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
EXPENDITURES OF FEDERAL AWARDS
FOR THE YEAR ENDED JUNE 30, 2005

Schedule 2

Federal Grantor/Pass-Through Grantor/Program or Cluster Title	Federal CFDA Number	Agency or Pass-Through Number	Federal Expenditures
CHILD NUTRITION CLUSTER			
<u>U. S. Department of Agriculture</u>			
Passed Through State Department of Education:			
School Breakfast Program	10.553	06-01	\$ 59,414
National School Lunch Program	10.555	06-01	<u>133,931</u>
Total State Department of Education			<u>193,345</u>
Passed Through State Department of Human Services:			
National School Lunch Program (Note 2)	10.555	06-01	<u>14,251</u>
TOTAL CHILD NUTRITION CLUSTER			<u>207,596</u>
OTHER PROGRAMS			
<u>U. S. Department of Education</u>			
Passed Through State Department of Education:			
Title I Grants - Local Educational Agencies	84.010	06-01	217,558
Special Education - Grants to States	84.027	06-01	99,753
Safe and Drug-Free Schools and Communities - State Grants	84.186	06-01	4,323
State Grants For Innovative Programs	84.298	06-01	3,636
Education Technology State Grants	84.318	06-01	3,597
Reading First State Grants	84.357	06-01	73,098
Improving Teacher Quality State Grants	84.367	06-01	<u>37,120</u>
TOTAL OTHER PROGRAMS			<u>439,085</u>
TOTAL EXPENDITURES OF FEDERAL AWARDS			<u><u>\$ 646,681</u></u>

NOTES TO THE SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS

- Note 1: Basis of Presentation - The accompanying schedule of expenditures of federal awards includes the federal grant activity of Hermitage School District No. 12 and is presented on the regulatory basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the presentation of, the basic financial statements.
- Note 2: Nonmonetary assistance is reported at the approximate value as provided by the Arkansas Department of Human Services.

HERMITAGE SCHOOL DISTRICT NO. 12
 BRADLEY COUNTY, ARKANSAS
 FEDERAL AWARD PROGRAMS -
 FINDINGS AND QUESTIONED COSTS
 FOR THE YEAR ENDED JUNE 30, 2005

Schedule 3

SECTION I - SUMMARY OF AUDITOR'S RESULTS

FINANCIAL STATEMENTS

Types of auditor's reports issued: GAAP basis of reporting - adverse
 Regulatory basis opinion units - unqualified

Internal control over financial reporting:

- Material weakness(es) identified? yes no
- Reportable condition(s) identified that are not considered to be material weakness(es)? yes none reported

Noncompliance material to financial statements noted? yes no

FEDERAL AWARDS

Internal control over major programs:

- Material weakness(es) identified? yes no
- Reportable condition(s) identified that are not considered to be material weakness(es)? yes none reported

Type of auditor's report issued on compliance for major programs: Unqualified

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of OMB Circular A-133? yes no

Identification of major programs:

CFDA Numbers	Name of Federal Programs or Cluster
10.553, 10.555 84.010	Child Nutrition Cluster Title I Grants To Local Education Agencies

Dollar threshold used to distinguish between Type A and Type B programs \$300,000

Auditee qualified as low-risk auditee? yes no

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
FEDERAL AWARD PROGRAMS -
FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2005

Schedule 3

SECTION II - FINANCIAL STATEMENT FINDINGS

2005-1. Segregation of Duties

Criteria: Financial accounting duties should be distributed among appropriate employees to ensure the proper safeguarding of assets.

Condition: The District does not have adequate staff to segregate financial accounting duties among appropriate employees.

Context: Completion of internal control questionnaire

Effect: Financial accounting duties are not distributed among the District's employees to sufficiently reduce the risks of fraud or error and to properly safeguard the District's assets.

Cause: Limited financial resources hinder the District's ability to adequately segregate financial accounting duties among employees.

Recommendation: To ensure the proper safeguarding of the District's assets, financial accounting duties should be distributed among appropriate employees.

Views of responsible officials and planned corrective actions: We concur with the recommendation.

2005-2. Internal Controls and Management Oversight

Criteria: Ark. Code Ann. 6-13-701 requires activity funds to be properly receipted and recorded.

Condition: Our examination disclosed the following internal control weaknesses and deficiencies concerning high school activity funds:

- > Policies, procedures, and administrative oversight relating to the collection of high school activity funds were inadequate to ensure proper accountability;
- > Activity fund sponsors were not required to retain documentation of fundraising activities, including original copies of receipts; and
- > Five (5) of thirty-four (34) activity accounts had deficit cash balances totaling \$9,438.

In addition, our review of activity fund receipts and deposits revealed instances where original receipt copies were not retained when receipts were voided; receipts were duplicated; the receipt carbon was not legible; checks were cashed from cash receipts; check/cash composition indicated on the receipt did not agree with bank deposits; receipts were not issued in sequential order; and funds collected were not remitted to the administrative office intact or timely.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
FEDERAL AWARD PROGRAMS -
FINDINGS AND QUESTIONED COSTS
FOR THE YEAR ENDED JUNE 30, 2005

Schedule 3

2005-2. Internal Controls and Management Oversight (Continued)

Context: A review of activity receipts disclosed the lack of internal controls and proper procedures.

Effect: The lack of accountability of cash receipts.

Cause: The lack of internal controls and management oversight resulted in this compliance issue.

Recommendation: To ensure proper accountability of high school activity fund receipts, we recommend that policies and procedures be implemented to accurately record receipts and management exercise adequate fiscal oversight responsibilities.

Views of responsible officials and planned corrective actions: The high school secretary and principal will be informed of all policies and procedures relating to the collection and receipting of activity funds to ensure proper accountability. Activity fund sponsors will be required to retain documentation for funds they are responsible for. Checks will not be issued unless funds have sufficient balances to cover them. Original receipt copies will be kept on any voided receipts. Receipts will not be duplicated. Receipt copies will be legible. No checks will be cashed. Check/cash composition will be the same on receipts and deposits. Receipts will be issued in sequential order. Receipts collected in the school offices will be remitted to the administration office daily.

SECTION III - FEDERAL AWARD FINDINGS AND QUESTIONED COSTS

No findings and questioned costs noted.

HERMITAGE SCHOOL DISTRICT NO. 12
BRADLEY COUNTY, ARKANSAS
FEDERAL AWARD PROGRAMS -
SUMMARY OF PRIOR AUDIT FINDINGS
FOR THE YEAR ENDED JUNE 30, 2005

Schedule 4

There were no findings in the prior audit.