

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

INDEPENDENT AUDITOR'S REPORTS
BASIC FINANCIAL STATEMENTS
AND SUPPLEMENTARY INFORMATION
SCHEDULE OF FINDINGS AND QUESTIONED COSTS

June 30, 2007

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Independent Auditor's Report

To the Board of Education of
Hartley-Melvin-Sanborn Community School District:

We have audited the accompanying financial statements of the governmental activities, the business type activities, each major fund and the aggregate remaining fund information of Hartley-Melvin-Sanborn Community School District, Hartley, Iowa, 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 District officials. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with U.S. generally accepted auditing standards 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 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, the business type activities, each major fund and the aggregate remaining fund information of Hartley-Melvin-Sanborn Community School District at June 30, 2007, and the respective changes in financial position and cash flows, where applicable, for the year then ended in conformity with U.S. generally accepted accounting principles.

In accordance with Government Auditing Standards, we have also issued our report dated February 4, 2008, on our consideration of Hartley-Melvin-Sanborn Community School District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contract 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.

Management's Discussion and Analysis and budgetary comparison information on pages 4 through 14 and 38 through 39 are not required parts of the basic financial statements, but are supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. 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 Hartley-Melvin-Sanborn Community School District's basic financial statements. We previously audited, in accordance with the standards referred to in the second paragraph of this report, the financial statements for the three years ended June 30, 2006, (which are not presented herein) and expressed unqualified opinions on those financial statements. Other supplementary information included in Schedules 1 through 5, including the Schedule of Expenditures of Federal Awards required by U.S. Office of Management and Budget (OMB) Circular A-133, Audits of States, Local Governments and Non-Profit Organizations, is presented for purposes of additional analysis and is not a required part of the basic financial statements. Such information has been subjected to the auditing procedures applied in our 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.

BURTON E. TRACY & CO., P.C.
Certified Public Accountants

February 4, 2008

Hartley-Melvin-Sanborn Community School District

Management Discussion & Analysis

This section of the Hartley-Melvin-Sanborn Community School District's annual financial report presents its discussion and analysis of the District's financial performance during the fiscal year ended June 30, 2007. The analysis focuses on the District's financial performance as a whole. Please read it in conjunction with the District's financial statements, which immediately follow this section.

Overview of the Financial Statements

This report consists of three parts: management's discussion and analysis (this section), the basic financial statements, and required supplementary information. The basic financial statements include two kinds of statements that present different views of the District:

The first two statements are *Government-wide financial statements* that provide both short-term and long-term information about the District's overall financial status.

- The remaining statements are *fund financial statements* that focus on individual parts of the District, reporting the District's operations in more detail than the Government-wide statements.
- The *governmental funds statements* explain how basic services such as regular and special education were financed in the short term as well as what remains for future spending.
- *Proprietary funds statements* offer short-term and long-term financial information about the activities the District operates like businesses, such as food services.
- *Fiduciary funds statements* provide information about the relationships in which the District acts solely as a trustee or agent for the benefit of others.

The financial statements also include notes that explain some of the information in the statements and provide more detailed data. The statements are followed by a section of required supplementary information that further explains and supports the financial statements with a comparison of the District's budget for the year.

Figure A-1 shows how the various parts of this annual report are arranged and relate to one another.

Figure A-1

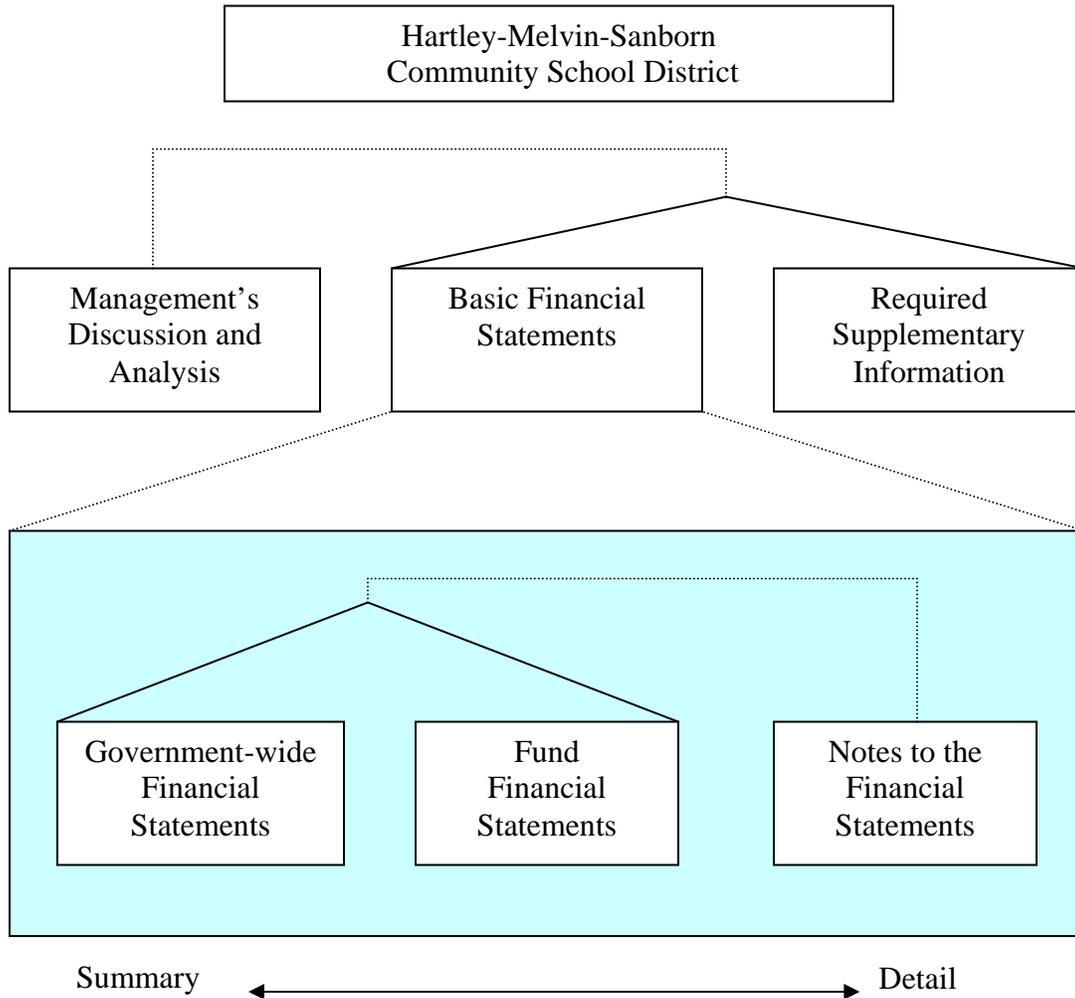


Figure A-2 summarizes the major features of the District’s financial statements, including the portion of the District’s activities they cover and the types of information they contain. The remainder of this overview section of the management’s discussion and analysis highlights the structure and contents of each of the statements.

<i>Figure A-2 Major Features of the Government-wide and Fund Financial Statements</i>				
	Government-wide Statements	Fund Financial Statements		
		Governmental Funds	Proprietary Funds	Fiduciary Funds
Scope	Entire district (except fiduciary funds)	The activities of the district that are not proprietary or fiduciary, such as special education and building maintenance	Activities the district operates similar to private business: food services is included here	Instances in which the district administers resources on behalf of someone else, such as scholarship programs
Required financial statements	<ul style="list-style-type: none"> • Statement of net assets • Statement of activities 	<ul style="list-style-type: none"> • Balance sheet • Statement of revenues, expenditures, and changes in fund balance 	<ul style="list-style-type: none"> • Statement of net assets • Statement of revenues, expenses and changes in net assets • Statement of cash flow 	<ul style="list-style-type: none"> • Statement of fiduciary net assets • Statement of changes in fiduciary net assets
Accounting basis and measurement focus	Accrual accounting and economic resources focus	Modified accrual accounting and current financial resources focus	Accrual accounting and economic resources focus	Accrual accounting and economic resources focus
Type of asset / liability information	All assets and liabilities, both financial and capital, short-term and long-term	Generally assets expected to be used up and liabilities that come due during the year or soon thereafter; no capital assets or long-term liabilities included	All assets and liabilities, both financial and capital, and short-term and long-term	All assets and liabilities, both short-term and long-term; funds do not currently contain capital assets, although they can
Type of inflow / outflow information	All revenues and expenses during year, regardless of when cash is received or paid	Revenues for which cash is received during or soon after the end of the year; expenditures when goods or services have been received and the related liability is due and payable	All revenues and expenses during the year, regardless of when cash is received or paid	All additions and deductions during the year, regardless of when cash is received or paid

Government-wide Statements

The Government-wide statements report information about the District as a whole using accounting methods similar to those used by private-sector companies. The statement of net assets includes all of the District's assets and liabilities. All of the current year's revenues and expenses are accounted for in the statement of activities regardless of when cash is received or paid.

The two Government-wide statements report the District's *net assets* and how they have changed. Net assets – the difference between the District's assets and liabilities – are one way to measure the District's financial health or position.

- Over time, increases or decreases in the District's net assets are an indicator of whether financial position is improving or deteriorating, respectively.
- To assess the District's overall health, you need to consider additional non-financial factors such as changes in the District's property tax base and the condition of school buildings and other facilities.

In the Government-wide financial statements, the District's activities are divided into two categories:

- *Governmental activities*: Most of the District's basic services are included here, such as regular and special education, transportation and administration. Property taxes and state aid finance most of these activities.
- *Business-type activities*: The District charges fees to help cover the costs of certain services it provides. The District's food service program would be included here.

Fund Financial Statements

The fund financial statements provide more detailed information about the District's funds, focusing on its most significant or "major" funds – not the District as a whole. Funds are accounting devices the District uses to keep track of specific sources of funding and spending on particular programs.

- Some funds are required by state law and by bond covenants.
- The District establishes other funds to control and manage money for particular purposes, such as accounting for student activity funds or to show that it is properly using certain revenues such as federal grants.

The District has three kinds of funds:

- *Governmental funds:* Most of the District's basic services are included in governmental funds, which generally focus on (1) how cash and other financial assets that can readily be converted to cash flow in and out and (2) the balances left at year-end that are available for spending. Consequently, the governmental funds statements provide a detailed short-term view that helps you determine whether there are more or fewer financial resources that can be spent in the near future to finance the District's programs. Because this information does not encompass the additional long-term focus of the Government-wide statements, additional information at the bottom of the governmental funds statements explains the relationship or differences between the two statements. The District's governmental funds include the General Fund, Capital Projects Fund, Debt Service Fund, and Special Revenue Funds that consist of Activity, Management, and Physical Plant and Equipment Levy funds.
- *Proprietary funds:* Services for which the District charges a fee are generally reported in proprietary funds. Proprietary funds are reported in the same way as the Government-wide statements. The District's enterprise fund, one type of a proprietary fund, is the same as its business-type activities but provides more detail and additional information, such as cash flows. The District currently has one enterprise fund, the School Nutrition Fund.
- *Fiduciary funds:* The District is the trustee, or fiduciary, for assets that belong to others, such as Scholarship funds. The District accounts for outside donations for specific purposes in this fund. The District is responsible for ensuring that the assets reported in these funds are used only for their intended purposes and by those to whom the assets belong. The District excludes these activities from the Government-wide financial statements because it cannot use these assets to finance its operations.

Financial Analysis of the District as a Whole

Figure A-3 below provides a summary of the District's net assets at June 30, 2007 compared to June 30, 2006.

Figure A-3

Condensed Statement of Net Assets

	Governmental Activities		Business-type Activities		Total School District		Total Percentage Change
	2006	2007	2006	2007	2006	2007	2005-2006
Current and other assets	\$4,959,441	\$5,282,818	\$3,990	\$25,095	\$4,963,431	\$5,307,913	6.94%
Capital assets	\$4,617,936	\$4,568,267	\$14,991	\$13,336	\$4,632,927	\$4,581,603	(1.11%)
Total Assets	\$9,577,377	\$9,851,085	\$18,981	\$38,431	\$9,596,358	\$9,889,516	3.05%
Long-term liabilities	\$2,109,771	\$1,801,959	0	0	\$2,109,771	\$1,801,959	(14.59%)
Other liabilities	\$2,993,737	\$3,154,768	\$3,664	\$27,364	\$2,997,401	\$3,182,132	6.16%
Total liabilities	\$5,103,508	\$4,956,727	\$3,664	\$27,364	\$5,107,172	\$4,984,091	(2.41%)
Net Assets:							
Invested in capital assets, net of related debt	\$2,587,583	\$2,788,267	\$14,991	\$13,336	\$2,602,574	\$2,801,603	7.65%
Restricted	\$1,367,265	\$1,548,805	0	0	\$1,367,265	\$1,548,805	13.28%
Unrestricted	\$519,021	\$557,286	\$326	(\$2,269)	\$519,347	\$555,017	6.87%
TOTAL NET ASSETS	\$4,473,869	\$4,894,358	\$15,317	\$11,067	\$4,489,186	\$4,905,425	9.27%

The District's combined net assets were slightly larger on June 30, 2007, than they were the year before; increasing 9.27% (see Figure A-3). The largest increase is noted in the restricted area where the use of funds are limited by legislation. The large increase in restricted net assets occurred because approximately \$77,000 of fiscal year 2007 local option sales tax revenues and \$80,000 in Physical Plant and Equipment Levy revenue were not spent during fiscal year 2007. The use of the local option sales tax and Physical Plant and Equipment Levy revenues are restricted by the Code of Iowa.

Unrestricted net assets are the part of total net assets that may be used to finance day-to-day operations without constraints established by debt covenants, enabling legislation or other legal requirements.

Figure A-4 shows the change in net assets for the years ended June 30, 2007 and 2006.

Figure A-4

Changes in Net Assets

	Governmental Activities		Business-type Activities		Total School District	
	2006	2007	2006	2007	2005	2006
Revenues						
Program Revenues						
Charges for services	\$435,155	\$422,204	\$144,161	\$158,929	\$579,316	\$581,133
Operating Grants & Contributions	\$995,642	\$1,031,235	\$125,896	\$130,107	\$1,121,538	\$1,161,342
Capital Grants & Contributions	25,000	0	0	0	\$25,000	\$0
General Revenues						
Property taxes & other taxes	\$2,638,961	\$2,885,519	0	0	\$2,638,961	\$2,885,519
Unrestricted State Grants	\$2,748,646	\$2,678,333	0	0	\$2,748,646	\$2,678,333
Unrestricted Investment Earnings	\$57,319	\$127,728	\$868	\$772	\$58,187	\$128,500
Other Revenue	\$73,958	\$12,143	0	0	\$73,958	\$12,143
Total Revenues	\$6,974,681	\$7,157,162	\$270,925	\$289,808	\$7,245,606	\$7,446,970
Expenses						
Instruction	\$4,529,237	\$4,518,650	0	\$0	\$4,529,237	\$4,518,650
Support Services	\$1,697,847	\$1,649,970	0	\$0	\$1,697,847	\$1,649,970
Non-Instructional Programs	\$0	\$0	\$291,360	\$294,058	\$291,360	\$294,058
Other Expenses	\$518,309	\$568,053	-	-	\$518,309	\$568,053
Total Expenses	\$6,745,393	\$6,736,673	\$291,360	\$294,058	\$7,036,753	\$7,030,731
Transfers	0	0	0	0	0	0
Change in Net Assets	\$229,288	\$420,489	(\$20,435)	(\$4,250)	\$208,853	\$416,239

Governmental Activities -

Referring to *Figure A-4*, revenues for the District's governmental activities were \$7,157,162 for fiscal year 2007. Total governmental expenditures were \$6,736,673

Expenses were kept to a minimum to match available revenues in a year when the Board of Directors raised the overall District tax rate from \$11.78 per thousand dollars of taxable valuation to \$12.02.

Figure A-5

Net Cost of Governmental Activities				
	Total Cost of Services 2006	Total Cost of Services 2007	Net Cost of Services 2006	Net Cost of Services 2007
Instruction	\$4,529,237	\$4,518,650	\$3,369,626	\$3,352,766
Support Services	\$1,697,847	\$1,649,970	\$1,687,925	\$1,620,150
Non-instructional Programs	\$0	\$0	\$0	\$0
Other Expenses	\$518,309	\$568,053	\$232,045	\$310,318
TOTAL	\$6,745,393	\$6,736,673	\$5,289,596	\$5,283,234

Figure A-5 presents the cost of the District’s major governmental activities: instruction, support services, non-instruction programs and other expenses. The table shows each activity’s net cost (total cost less fees generated by the activities and intergovernmental aid provided for specific programs). The net cost shows the financial burden placed on the District’s taxpayers by each of these functions.

- The cost of all governmental activities this year was \$6,736,673.
- Some of the cost was financed by the users of the District’s programs (\$422,204).
- The federal and state governments and private contributors subsidized certain programs with grants and contributions (\$1,031,235).
- Most of the District’s costs (\$5,283,234), however, were financed by District and state taxpayers.
- This portion of governmental activities was financed with \$2,885,519 in property and other taxes, and \$2,678,333 in unrestricted state aid (based in large part on the statewide education aid formula), investment earnings and miscellaneous revenues.

Business-Type Activities -

The District’s business-type activities include the School Nutrition Fund. Revenues of these activities were comprised of charges for services, federal and state reimbursements, and investment income. The District’s business-type activities show a decrease in net assets with expenses exceeding revenues \$4,250 (refer to Figure A-4). The Board of Education did increase school meal prices for fiscal year 2007.

Financial Analysis of the District’s Funds

The financial performance of the District as a whole is reflected in its governmental funds. As the District completed the year, its governmental funds reported combined fund balances of \$1,971,970, slightly more than last year’s ending fund balances of \$1,909,193.

Governmental Fund Highlights

The General Fund balance decreased from \$619,281 to \$501,408, due in part to the reduction in student enrollment, increase in negotiated salary and benefit settlement and additional increased operational costs.

The Non-major Governmental Funds balance in 2007 reported the combined fund balance of Capital Projects Sales Tax and Non-major Governmental Funds. The combined Non-major Governmental Funds and Capital Projects Sales Tax increased from \$755,775 to \$855,952. The increase was due in large part to increased revenues in the Capitol Projects Fund from the Local Option Sales Tax. A portion of this fund has been reserved for property tax reduction, and energy cost saving repairs and improvements.

The Physical Plant and Equipment Levy (PPEL) Fund balance increased \$80,473. A portion of this fund has been reserved for the replacement of a bus, small vehicle energy cost saving improvements, tuck pointing and roof repairs.

Business Type Fund Highlights

The School Nutrition Fund net assets decreased from \$15,317 at June 30, 2006 to \$11,067 at June 30, 2007, representing a decrease of 28 %. Overall operating expenses increased by \$2,698.

Budgetary Highlights

In accordance with the Code of Iowa, the Board of Education annually adopts a budget following required public notice and hearing for all funds. Although the budget document presents functional area expenditures or expenses by fund, the legal level of control is at the aggregated functional level, not at the fund or fund type level. The budget may be amended during the year utilizing similar statutorily prescribed procedures. The District's budget is prepared on the GAAP basis. A schedule showing the original and final budget amounts compared to the District's actual financial activity is included in the required supplementary information section of this report.

During FY07, the continued student enrollment decline along with the additional 10% reduction in the budget guarantee contributed to a decrease in revenue to the district while the cost of instruction continues to increase. Additional State and Federal competitive grants were used to fund specific initiatives contributing to an overall increase in revenues, but keeping in mind that these grant funds are designated for specific purposes. When a preliminary budget is set, the District always requests the ability to expend its full budget if necessary, but has the goal of keeping disbursements in line with revenues as actual revenue accumulates. As a result, the District's certified budget should always exceed the actual expenditures during the year. It is apparent that even in such a difficult fiscal year, the District was able to keep total disbursements (\$7,289,786) slightly below total receipts (\$7,343,348).

Capital Asset and Debt Administration

Capital Assets

By the end of 2007, the District had invested \$4,581,603, net of accumulated depreciation, in a broad range of assets, including school buildings, athletic facilities, transportation equipment, and computer and audio-visual equipment (see *Figure A-6*). This amount represents a net decrease of \$51,324 or 1.1% from last year. (More detailed information about capital assets can be found in Note 5 to the financial statements.)

Figure A-6

Capital Assets (net of depreciation)

	Governmental Activities		Business--type Activities		Total School District		Total Percentage Change 2005-06
	2006	2007	2006	2007	2006	2007	
	Land	\$81,804	\$81,804	0	0	\$81,804	
Improvements other than Buildings	\$162,999	\$146,102	0	0	\$162,999	\$146,102	(10.4%)
Buildings	\$4,022,356	\$3,969,029	0	0	\$4,022,356	\$3,969,029	(1.3%)
Equipment & Furniture	\$350,777	\$371,332	\$14,991	\$13,336	\$365,768	\$384,668	5.2%
TOTAL	\$4,617,936	\$4,568,267	\$14,991	\$13,336	\$4,632,927	\$4,581,603	(1.1%)

Long-Term Debt

At June 30, 2007, the District had \$1,801,959 in general obligation and other long-term debt outstanding (Figure A-7). This is a 14.6% reduction from the prior year. Additional information about the District's long-term debt is presented in Note 6 to the financial statements.

Figure A-7

Long-Term Debt

	Balance End of 2007	Due Within One Year
General obligation bonds	\$1,780,000	\$265,000
Early retirement	\$21,959	\$14,733
EPA asbestos removal loan	\$0	\$0
Total	\$1,801,959	\$279,733

Factors Bearing on the District's Future

At the time of the financial statements were prepared and audited, the District was aware of the following existing circumstances that could significantly affect its financial health in the future:

- The condition of the State of Iowa's budget has translated into reduced levels of state aid funding for education. Future increases in state aid to schools (allowable growth), will be predicated upon the condition of the national and state economy. State funding growth for public schools for fiscal year 2008, has been set at 4%.
- District enrollment has suffered substantial decline the last two years. Under Iowa's school funding formula, District funding is highly dependant upon District enrollments. Future projected enrollment declines will make maintaining a sound financial foundation difficult. It will be critical to plan for this decrease in enrollment by decreasing expenditures.
- The budget guarantee will continue to recede at a rate of 10% annually until it is no longer in existence. This, combined with declining enrollment, will translate in a negative new money for the next few years, or until enrollment stabilizes.

Contacting the District's Financial Management

This financial report is designed to provide the District's citizens, taxpayers, customers, and investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability of the money it receives. If you have questions about this report or need additional financial information, contact Lynn Evans, Superintendent, Hartley-Melvin-Sanborn Community School District, 173 S. Central Avenue, Hartley, Iowa 51346.

BASIC FINANCIAL STATEMENTS

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Net Assets

June 30, 2007

	Governmental Activities \$	Business Type Activities \$	Total \$
Assets			
Cash and cash equivalents	2,538,645	21,910	2,560,555
Receivables:			
Property tax:			
Delinquent	38,150	-	38,150
Succeeding year	2,365,097	-	2,365,097
Accounts	454	-	454
Due from other governments	340,472	-	340,472
Inventories	-	3,185	3,185
Capital assets, net of accumulated depreciation	4,568,267	13,336	4,581,603
Total assets	9,851,085	38,431	9,889,516
Liabilities			
Accounts payable	124,636	1,751	126,387
Salaries and benefits payable	614,820	21,800	636,620
Accrued interest payable	6,509	-	6,509
Deferred revenue:			
Succeeding year property tax	2,365,097	-	2,365,097
Other	43,706	3,813	47,519
Long-term liabilities:			
Portion due within one year:			
General obligation bonds payable	265,000	-	265,000
Termination benefits	14,733	-	14,733
Portion due after one year:			
General obligation bonds payable	1,515,000	-	1,515,000
Termination benefits	7,226	-	7,226
Total liabilities	4,956,727	27,364	4,984,091
Net assets			
Invested in capital assets, net of related debt	2,788,267	13,336	2,801,603
Restricted for:			
State categorical aid	32,570	-	32,570
Management levy	19,675	-	19,675
Physical plant and equipment levy	684,291	-	684,291
Other special revenue purposes	132,271	-	132,271
Local option sales tax capital projects	679,998	-	679,998
Unrestricted	557,286	(2,269)	555,017
Total net assets	4,894,358	11,067	4,905,425

See notes to financial statements.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Activities

Year ended June 30, 2007

Functions/Programs	Program Revenues			
	Expenses	Charges for Services	Operating Grants, Contributions and Restricted Interest	Capital Grants, Contributions and Restricted Interest
			\$	\$
Governmental activities:				
Instruction:				
Regular	3,034,135	170,219	591,167	-
Special	781,637	54,802	55,730	-
Other	702,878	196,858	97,108	-
	<u>4,518,650</u>	<u>421,879</u>	<u>744,005</u>	<u>-</u>
Support services:				
Student	83,672	-	-	-
Instructional staff	128,440	-	-	-
Administration	633,302	-	-	-
Operation and maintenance of plant	511,957	325	-	-
Transportation	292,599	-	29,495	-
	<u>1,649,970</u>	<u>325</u>	<u>29,495</u>	<u>-</u>
Other expenditures:				
Facilities acquisition	92,093	-	-	-
Long-term debt interest	88,538	-	-	-
AEA flowthrough	257,735	-	257,735	-
Depreciation (unallocated)*	129,687	-	-	-
	<u>568,053</u>	<u>-</u>	<u>257,735</u>	<u>-</u>
Total governmental activities	6,736,673	422,204	1,031,235	-
Business type activities:				
Non-instructional programs:				
Food service operations	294,058	158,929	130,107	-
Total	<u>7,030,731</u>	<u>581,133</u>	<u>1,161,342</u>	<u>-</u>

General Revenues:

Property taxes levied for:
General purposes
Capital outlay
Income surtax
Local option sales and services tax
Unrestricted state grants
Unrestricted investment earnings
Other
Total general revenues

Change in net assets

Net assets beginning of year
Net assets end of year

*This amount excludes the depreciation that is included in the direct expenses of the various programs.

Net (Expense) Revenue and Changes in Net Assets

Governmental Activities	Business Type Activities	Total
\$	\$	\$
(2,272,749)	-	(2,272,749)
(671,105)	-	(671,105)
(408,912)	-	(408,912)
<u>(3,352,766)</u>	<u>-</u>	<u>(3,352,766)</u>
(83,672)	-	(83,672)
(128,440)	-	(128,440)
(633,302)	-	(633,302)
(511,632)	-	(511,632)
(263,104)	-	(263,104)
<u>(1,620,150)</u>	<u>-</u>	<u>(1,620,150)</u>
(92,093)	-	(92,093)
(88,538)	-	(88,538)
-	-	-
<u>(129,687)</u>	<u>-</u>	<u>(129,687)</u>
<u>(310,318)</u>	<u>-</u>	<u>(310,318)</u>
(5,283,234)	-	(5,283,234)
-	(5,022)	(5,022)
<u>(5,283,234)</u>	<u>(5,022)</u>	<u>(5,288,256)</u>
2,124,162	-	2,124,162
128,038	-	128,038
176,000	-	176,000
457,319	-	457,319
2,678,333	-	2,678,333
127,728	772	128,500
12,143	-	12,143
<u>5,703,723</u>	<u>772</u>	<u>5,704,495</u>
420,489	(4,250)	416,239
<u>4,473,869</u>	<u>15,317</u>	<u>4,489,186</u>
<u>4,894,358</u>	<u>11,067</u>	<u>4,905,425</u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Balance Sheet
Governmental Funds

June 30, 2007

	General Fund	Physical Plant and Equipment Levy	Capital Projects Sales Tax	Nonmajor Governmental Funds	Total
	\$	\$	\$	\$	\$
Assets					
Cash and pooled investments	1,135,021	575,696	650,058	177,870	2,538,645
Receivables:					
Property tax:					
Delinquent	33,529	2,072	-	2,549	38,150
Succeeding year	2,155,735	124,362	-	85,000	2,365,097
Accounts	167	-	-	260	427
Interfund receivable	27	38,817	-	-	38,844
Due from other governments	171,297	69,681	99,494	-	340,472
Total assets	3,495,776	810,628	749,552	265,679	5,321,635
Liabilities and Fund Balances					
Liabilities:					
Accounts payable	48,382	1,975	69,554	4,725	124,636
Salaries and benefits payable	614,820	-	-	-	614,820
Interfund payable	38,817	-	-	-	38,817
Deferred revenue:					
Succeeding year property tax	2,155,735	124,362	-	85,000	2,365,097
Other	136,614	69,681	-	-	206,295
Total liabilities	2,994,368	196,018	69,554	89,725	3,349,665
Fund balances:					
Reserved for:					
State categorical aid	32,570	-	-	-	32,570
Debt service	-	-	-	2,049	2,049
Unreserved reported in:					
General fund	468,838	-	-	-	468,838
Special revenue funds	-	614,610	-	173,905	788,515
Capital projects funds	-	-	679,998	-	679,998
Total fund balances	501,408	614,610	679,998	175,954	1,971,970
Total liabilities and fund balances	3,495,776	810,628	749,552	265,679	5,321,635

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Reconciliation of the Balance Sheet - Governmental Funds
to the Statement of Net Assets

June 30, 2007

	\$
Total fund balances of governmental funds (Exhibit C)	1,971,970
<i>Amounts reported for governmental activities in the Statement of Net Assets are different because:</i>	
Capital assets used in governmental activities are not financial resources and, therefore, are not reported as assets in the governmental funds.	4,568,267
Other long-term assets are not available to pay current period expenditures and, therefore, are deferred in the governmental funds.	162,589
Accrued interest payable on long-term liabilities is not due and payable in the current period and, therefore, is not reported as a liability in the governmental funds.	(6,509)
Long-term liabilities, including bonds payable and termination benefits, are not due and payable in the current period and therefore, are not reported as liabilities in the governmental funds.	<u>(1,801,959)</u>
Net assets of governmental activities (Exhibit A)	<u><u>4,894,358</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT
Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds

Year ended June 30, 2007

	General Fund	Physical Plant and Equipment Levy	Capital Projects Sales Tax	Nonmajor Governmental Funds	Total
	\$	\$	\$	\$	\$
Revenues:					
Local sources:					
Local tax	1,974,095	205,381	457,319	150,067	2,786,862
Tuition	213,057	-	-	-	213,057
Other	70,133	26,996	37,406	209,518	344,053
Intermediate sources	514	-	-	-	514
State sources	3,293,126	120	-	138	3,293,384
Federal sources	415,670	-	-	-	415,670
Total revenues	<u>5,966,595</u>	<u>232,497</u>	<u>494,725</u>	<u>359,723</u>	<u>7,053,540</u>
Expenditures:					
Current:					
Instruction:					
Regular	3,058,337	-	-	46,554	3,104,891
Special	781,369	-	-	-	781,369
Other	485,941	-	-	215,852	701,793
	<u>4,325,647</u>	<u>-</u>	<u>-</u>	<u>262,406</u>	<u>4,588,053</u>
Support services:					
Student	83,672	-	-	-	83,672
Instructional staff	124,973	-	-	-	124,973
Administration	629,847	-	-	-	629,847
Operation and maintenance of plant	422,995	8,221	-	73,269	504,485
Transportation	244,564	71,040	-	-	315,604
	<u>1,506,051</u>	<u>79,261</u>	<u>-</u>	<u>73,269</u>	<u>1,658,581</u>
Other expenditures:					
Facilities acquisition	-	72,410	79,146	-	151,556
Long-term debt:					
Principal	-	-	-	250,353	250,353
Interest and fiscal charges	-	-	-	89,450	89,450
AEA flowthrough	257,735	-	-	-	257,735
	<u>257,735</u>	<u>72,410</u>	<u>79,146</u>	<u>339,803</u>	<u>749,094</u>
Total expenditures	<u>6,089,433</u>	<u>151,671</u>	<u>79,146</u>	<u>675,478</u>	<u>6,995,728</u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Revenues, Expenditures and Changes in Fund Balances
Governmental Funds

Year ended June 30, 2007

	General Fund	Physical Plant and Equipment Levy	Capital Projects Sales Tax	Nonmajor Governmental Funds	Total
	\$	\$	\$	\$	\$
Excess (deficiency) of revenues over (under) expenditures	(122,838)	80,826	415,579	(315,755)	57,812
Other financing sources (uses):					
Sales of equipment	4,965	-	-	-	4,965
Operating transfers in	-	-	-	339,803	339,803
Operating transfers out	-	(353)	(339,450)	-	(339,803)
Total other financing sources (uses)	4,965	(353)	(339,450)	339,803	4,965
Net change in fund balances	(117,873)	80,473	76,129	24,048	62,777
Fund balances beginning of year	619,281	534,137	603,869	151,906	1,909,193
Fund balances end of year	501,408	614,610	679,998	175,954	1,971,970

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Reconciliation of the Statement of Revenues, Expenditures and
Changes in Fund Balances - Governmental Funds to the
Statement of Activities

Year ended June 30, 2007

	\$	\$
Net change in fund balances - total governmental funds (Exhibit E)		62,777
<i>Amounts reported for governmental activities in the Statement of Activities are different because:</i>		
Capital outlays to purchase or build capital assets are reported in governmental funds as expenditures. However, those costs are not reported in the Statement of Activities and are allocated over their estimated useful lives as depreciation expense in the Statement of Activities. Depreciation expense exceeded capital outlay expenditures in the year as follows:		
Expenditures for capital assets	153,404	
Depreciation expense	<u>(203,073)</u>	(49,669)
Income surtaxes not collected for several months after the District's fiscal year ends are not considered "available" revenues in the governmental funds and are included as deferred revenues. They are, however, recorded as revenues in the statement of activities.		
		98,657
Repayment of long-term liability principal is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Assets.		
		250,353
Interest on long-term debt in the Statement of Activities differs from the amount reported in the governmental funds because interest is recorded as an expenditure in the funds when due. In the Statement of Activities interest expense is recognized as the interest accrues, regardless of when it is due.		
		912
Some expenses reported in the Statement of Activities do not require the use of current financial resources and, therefore, are not reported as expenditures in the governmental funds, as follows:		
Termination benefits		<u>57,459</u>
Changes in net assets of governmental activities (Exhibit B)		<u><u>420,489</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Net Assets
Proprietary Fund

June 30, 2007

	Nonmajor School Nutrition
	<u>\$</u>
Assets	
Cash and cash equivalents	21,910
Inventories	3,185
Capital assets, net of accumulated depreciation	<u>13,336</u>
Total assets	<u>38,431</u>
Liabilities	
Accounts payable	1,751
Salaries and benefits payable	21,800
Deferred revenue	<u>3,813</u>
Total liabilities	<u>27,364</u>
Net assets	
Invested in capital assets, net of related debt	13,336
Unrestricted	<u>(2,269)</u>
Total net assets	<u><u>11,067</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT
Statement of Revenues, Expenses, and Changes in Fund Net Assets
Proprietary Fund

Year ended June 30, 2007

	Nonmajor School Nutrition
	\$
Operating revenue:	
Local sources:	
Charges for service	158,929
Operating expenses:	
Non-instructional programs:	
Salaries	100,979
Benefits	36,053
Purchased services	600
Supplies	153,715
Depreciation	2,330
Other	381
	294,058
Operating gain (loss)	(135,129)
Non-operating revenues:	
State sources	3,610
Federal sources	126,497
Interest income	772
Total non-operating revenues	130,879
Change in net assets	(4,250)
Net assets beginning of year	15,317
Net assets end of year	11,067

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Cash Flows
Proprietary Funds

Year ended June 30, 2007

	Nonmajor School Nutrition
	<u>\$</u>
Cash flows from operating activities:	
Cash received from sale of lunches and breakfasts	159,265
Cash payments to employees for services	(133,845)
Cash payments to suppliers for goods or services	(125,068)
Net cash used by operating activities	<u>(99,648)</u>
Cash flows from non-capital financing activities:	
State grants received	3,610
Federal grants received	97,995
Net cash provided by non-capital financing activities	<u>101,605</u>
Cash flows from capital and related financing activities:	
Acquisition of capital assets	<u>(675)</u>
Cash flows from investing activities:	
Interest on investments	<u>772</u>
Net increase (decrease) in cash and cash equivalents	2,054
Cash and cash equivalents at beginning of year	<u>19,856</u>
Cash and cash equivalents at end of year	<u><u>21,910</u></u>
Reconciliation of operating gain (loss) to net cash used by operating activities:	
Operating gain (loss)	(135,129)
Adjustments to reconcile operating gain (loss) to net cash used by operating activities:	
Commodities used	28,502
Depreciation	2,330
Decrease (increase) in inventories	(438)
(Decrease) increase in accounts payable	1,564
(Decrease) increase in salaries and benefits payable	3,187
(Decrease) increase in deferred revenue	336
Net cash used in operating activities	<u><u>(99,648)</u></u>

Non-cash investing, capital and financing activities:

During the year ended June 30, 2007, the District received \$28,502 of federal commodities.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Fiduciary Net Assets
Fiduciary Fund

June 30, 2007

	Private Purpose Trust
	<u>\$</u>
Assets	
Cash and pooled investments	4,609
Liabilities	
Interfund payable	<u>27</u>
Net Assets	
Reserved for scholarships	503
Reserved for student books	<u>4,079</u>
Total net assets	<u><u>4,582</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Statement of Changes in Fiduciary Net Assets
Fiduciary Fund

Year ended June 30, 2007

	Private Purpose Trust
	<u>\$</u>
Additions:	
Local sources:	
Interest	<u>200</u>
Deductions	
Support services:	
Books purchased for individuals	180
Scholarships awarded	<u>60</u>
Total deductions	<u>240</u>
Change in net assets	(40)
Net assets beginning of year	<u>4,622</u>
Net assets end of year	<u><u>4,582</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Notes to Financial Statements

June 30, 2007

1. Summary of Significant Accounting Policies

Hartley-Melvin-Sanborn Community School District is a political subdivision of the State of Iowa and operates public schools for children in grades kindergarten through twelve. The geographic area served includes the Cities of Hartley, Melvin, and Sanborn, Iowa and the predominately agricultural territory in a portion of O'Brien, Osceola, Clay and Dickinson Counties. The District is governed by a Board of Education whose members are elected on a non-partisan basis.

The District's financial statements are prepared in conformity with U.S. generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board.

A. Reporting Entity

For financial reporting purposes, Hartley-Melvin-Sanborn Community School District has included all funds, organizations, agencies, boards, commissions, and authorities. The District has also considered all potential component units for which it is financially accountable and other organizations for which the nature and significance of their relationship with the District are such that exclusion would cause the District's financial statements to be misleading or incomplete. The Governmental Accounting Standards Board has set forth criteria to be considered in determining financial accountability. These criteria include appointing a voting majority of an organization's governing body and (1) the ability of the District to impose its will on that organization or (2) the potential for the organization to provide specific benefits to or impose specific financial burdens on the District. The Hartley-Melvin-Sanborn Community School District has no component units that meet the Governmental Accounting Standards Board criteria.

Jointly Governed Organizations - The District participates in a jointly governed organization that provides services to the District but does not meet the criteria of a joint venture since there is no ongoing financial interest or responsibility by the participating governments. The District is a member of the County Assessor's Conference Board.

B. Basis of Presentation

Government-wide Financial Statements - The Statement of Net Assets and the Statement of Activities report information on all of the nonfiduciary activities of the District. For the most part, the effect of interfund activity has been removed from these statements. Governmental activities, which normally are supported by tax and intergovernmental revenues, are reported separately from business type activities, which rely to a significant extent on fees and charges for service.

The Statement of Net Assets presents the District's nonfiduciary assets and liabilities, with the difference reported as net assets. Net assets are reported in three categories:

Invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation and reduced by outstanding balances for bonds, notes, and other debt that are attributed to the acquisition, construction, or improvement of those assets.

Restricted net assets result when constraints placed on net asset use are either externally imposed or imposed by law through constitutional provisions or enabling legislation.

Unrestricted net assets consist of net assets that do not meet the definition of the two preceding categories. Unrestricted net assets often have constraints on resources imposed by management, which can be removed or modified.

The Statement of Activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those clearly identifiable with a specific function. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function and 2) grants, contributions, and interest restricted to meeting the operational or capital requirements of a particular function. Property tax and other items not properly included among program revenues are reported instead as general revenues.

Fund Financial Statements – Separate financial statements are provided for governmental, proprietary, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds are reported as separate columns in the fund financial statements. All remaining governmental funds are aggregated and reported as nonmajor governmental funds.

The District reports the following major governmental funds:

The General Fund is the general operating fund of the District. All general tax revenues and other revenues not allocated by law or contractual agreement to some other fund are accounted for in this fund. From the fund are paid the general operating expenditures, including instruction, support and other costs.

The Physical Plant and Equipment Levy Fund is a special revenue fund that is established to account for the proceeds and uses of the physical plant and equipment property tax levy.

The Capital Projects Fund is used to account for all resources used in the acquisition and construction of capital facilities.

The District's proprietary fund is the Enterprise, School Nutrition Fund. This fund is used to account for the food service operations of the District.

The District also reports fiduciary funds which focus on net assets and changes in net assets. The District's fiduciary funds include the following:

The Private-Purpose Trust Fund is used to account for assets held by the District under trust agreements, which require income earned to be used to benefit individuals through scholarship awards and the purchase of a book for each kindergarten student.

C. Measurement Focus and Basis of Accounting

The government-wide, proprietary and fiduciary fund financial statements are reported using the economic resources measurement focus and accrual basis of accounting. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property tax is recognized as revenue in the year for which it is levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been satisfied.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days after year end.

Property tax, intergovernmental revenues (shared revenues, grants, and reimbursements from other governments) and interest associated with the current fiscal period are all considered to be susceptible to accrual. All other revenue items are considered to be measurable and available only when cash is received by the District.

Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, principal and interest on long-term debt, claims and judgements, and compensated absences are recognized as expenditures only when payment is due. Capital asset acquisitions are reported as expenditures in governmental funds. Proceeds of general long-term debt and acquisitions under capital leases are reported as other financing sources.

Under the terms of grant agreements, the District funds certain programs by a combination of specific cost-reimbursement grants and general revenues. Thus, when program expenses are incurred, there are both restricted and unrestricted net assets available to finance the program. It is the District's policy to first apply cost-reimbursement grant resources to such programs, and then general revenues.

The proprietary fund of the District applies all applicable GASB pronouncements as well as the following pronouncements issued on or before November 30, 1989, unless these pronouncements conflict with or contradict GASB pronouncements: Financial Accounting Standards Board Statements and Interpretations, Accounting Principles Board Opinions, and Accounting Research Bulletins of the Committee on Accounting Procedure.

Proprietary funds distinguish operating revenues and expenses from non-operating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues of the District's Enterprise Fund is charges to customers for sales and services. Operating expenses for Enterprise Funds include the cost of sales and services, administrative expenses, and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as non-operating revenues and expenses.

The District maintains its financial records on the cash basis. The financial statements of the District are prepared by making memorandum adjusting entries to the cash basis financial records.

D. Assets, Liabilities and Fund Equity

The following accounting policies are followed in preparing the financial statements:

Cash, Pooled Investments and Cash Equivalents - The cash balances of most District funds are pooled and invested. Investments are stated at fair value except for the investment in the Iowa Schools Joint Investment Trust which is valued at amortized cost and non-negotiable certificates of deposit which are stated at cost.

For purposes of the statement of cash flows, all short-term cash investments that are highly liquid are considered to be cash equivalents. Cash equivalents are readily convertible to known amounts of cash, and at the day of purchase, have a maturity date no longer than three months.

Property Tax Receivable – Property tax in governmental funds is accounted for using the modified accrual basis of accounting.

Property tax receivable is recognized in these funds on the levy or lien date, which is the date the tax asking is certified by the Board of Education. Delinquent property tax receivable represents unpaid taxes for the current and prior years. The succeeding year property tax receivable represents taxes certified by the Board of Education to be collected in the next fiscal year for the purposes set out in the budget for the next fiscal year. By statute, the

District is required to certify its budget in April of each year for the subsequent fiscal year. However, by statute, the tax asking and budget certification for the following fiscal year becomes effective on the first day of that year. Although the succeeding year property tax receivable has been recorded, the related revenue is deferred in both the government-wide and fund financial statements and will not be recognized as revenue until the year for which it is levied.

Property tax revenue recognized in these funds became due and collectible in September and March of the fiscal year with a 1 ½% per month penalty for delinquent payments; is based on January 1, 2005 assessed property valuations; is for the tax accrual period July 1, 2006, through June 30, 2007, and reflects the tax asking contained in the budget certified to the County Board of Supervisors in April, 2006.

Due from Other Governments - Due from other governments represents amounts due from the State of Iowa, various shared revenues, grants, and reimbursements from other governments.

Inventories - Inventories are valued at cost using the first-in, first-out method for purchased items and government commodities. Inventories of proprietary funds are recorded as expenses when consumed rather than when purchased or received.

Capital Assets – Capital assets, which include property, furniture and equipment are reported in the applicable governmental or business type activities columns in the government-wide Statement of Net Assets. Capital assets are recorded at historical cost. Donated capital assets are recorded at estimated fair market value at the date of donation. The costs of normal maintenance and repair that do not add to the value of the asset or materially extend asset lives are not capitalized. Capital assets are defined by the District as assets with an initial, individual cost in excess of the following thresholds and estimated useful lives in excess of two years.

<u>Asset Class</u>	<u>Amount</u>
	\$
Land	-
Buildings	5,000
Improvements other than buildings	5,000
Furniture and equipment:	
School Nutrition Fund equipment	500
Other furniture and equipment	5,000

Capital assets are depreciated using the straight line method over the following estimated useful lives:

<u>Asset Class</u>	<u>Estimated Useful Lives</u>
Buildings	50 years
Improvements other than buildings	20 years
Furniture and equipment	5-20 years

The District's collection of library books and other similar materials are not capitalized. These collections are unencumbered, held for public exhibition and education, protected, cared for and preserved and subject to District policy that requires proceeds from the sale of these items, if any, to be used to acquire other collection items.

Salaries and Benefits Payable – Payroll and related expenditures for teachers with annual contracts corresponding to the current school year, which are payable in July and August, have been accrued as liabilities.

Deferred Revenue – Although certain revenues are measurable, they are not available. Available means collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Deferred revenue in the governmental fund financial statements represent the amount of assets that have been recognized, but the related revenue has not been recognized since the assets are not collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period. Deferred revenue consists of unspent grant proceeds as well as property tax receivable and other receivables not collected within sixty days after year end.

Deferred revenue in the Statement of Net Assets consists of unspent grant proceeds, amounts received in advance for meal sales and succeeding year property tax receivable that will not be recognized as revenue until the year for which it is levied.

Compensated Absences - District employees accumulate a limited amount of earned but unused vacation and sick leave hours for subsequent use. Employees are not paid for unused vacation and sick leave benefits when employment with the District ends.

Long-term Liabilities – In the government-wide financial statements, long-term debt and other long-term obligations are reported as liabilities in the governmental activities column in the Statement of Net Assets.

Fund Equity – In the governmental fund financial statements, reservations of fund balance are reported for amounts not available for appropriation or legally restricted by outside parties for use for a specific purpose.

Restricted Net Assets – In the government-wide Statement of Net Assets, net assets are reported as restricted when constraints placed on net asset use are either externally imposed by creditors, grantors, contributors, or laws and regulations of other governments or are imposed by law through constitutional provisions or enabling legislation.

E. Budgeting and Budgetary Control

The budgetary comparison and related disclosures are reported as Required Supplementary Information.

2. **Cash and Pooled Investments**

The District's deposits in banks at June 30, 2007 were entirely covered by federal depository insurance, or by the State Sinking Fund in accordance with Chapter 12C of the Code of Iowa. This chapter provides for additional assessments against the depositories to insure there will be no loss of public funds.

The District is authorized by statute to invest public funds in obligations of the United States government, its agencies and instrumentalities; certificates of deposit or other evidences of deposit at federally insured depository institutions approved by the Board of Education; prime eligible bankers acceptances; certain high rated commercial paper; perfected repurchase agreements; certain registered open-end management investment companies; certain joint investment trusts; and warrants or improvement certificates of a drainage district.

The District had no investments meeting the disclosure requirements of Governmental Accounting Standards Board Statement No. 3 as amended by Statement No. 40.

3. Interfund Receivables and Payables

The detail of interfund receivables and payables at June 30, 2007 is as follows:

Receivable Fund	Payable Fund	Amount
		\$
Physical Plant and Equipment Levy Fund	General Fund	38,817
General Fund	Private Purpose Trust Fund	27

These interfund transactions represent reimbursements due for expenditures paid from the wrong fund.

4. Interfund Transfers

The detail of interfund transfers for the year ended June 30, 2007 is as follows:

Transfer To	Transfer From	Amount
		\$
Debt Service Fund	Physical Plant and Equipment Levy Fund	353
Debt Service Fund	Capital Projects Sales Tax Fund	339,450

Transfers generally move revenues from the fund statutorily required to collect the resources to the fund statutorily required to expend the resources.

5. Capital Assets

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

	Balance Beginning of Year	Increases	Decreases	Balance End of Year
	\$	\$	\$	\$
Governmental activities:				
Capital assets not being depreciated:				
Land	81,804	-	-	81,804
Capital assets being depreciated:				
Buildings	6,089,744	59,463	-	6,149,207
Improvements other than buildings	507,218	-	-	507,218
Furniture and equipment	1,217,515	93,941	85,527	1,225,929
Total capital assets being deprec.	<u>7,814,477</u>	<u>153,404</u>	<u>85,527</u>	<u>7,882,354</u>
Less accumulated depreciation for:				
Buildings	2,067,388	112,790	-	2,180,178
Improvements other than buildings	344,219	16,897	-	361,116
Furniture and equipment	866,738	73,386	85,527	854,597
Total accumulated depreciation	<u>3,278,345</u>	<u>203,073</u>	<u>85,527</u>	<u>3,395,891</u>
Total capital assets being depreciated, net	<u>4,536,132</u>	<u>(49,669)</u>	-	<u>4,486,463</u>
Governmental activities capital assets, net	<u>4,617,936</u>	<u>(49,669)</u>	-	<u>4,568,267</u>

	Balance Beginning of Year	Increases	Decreases	Balance End of Year
	\$	\$	\$	\$
Business type activities:				
Furniture and equipment	99,928	675	-	100,603
Less accumulated depreciation	<u>84,937</u>	<u>2,330</u>	-	<u>87,267</u>
Business type activities capital assets, net	<u>14,991</u>	<u>(1,655)</u>	-	<u>13,336</u>

Depreciation expense was charged to the following functions:

	\$
Governmental activities:	
Instruction:	
Regular	5,103
Special	268
Other	1,085
Support services:	
Instructional staff services	3,467
Administration services	7,956
Operation and maintenance of plant services	7,472
Transportation	<u>48,035</u>
	73,386
Unallocated depreciation	129,687
Total depreciation expense – governmental activities	<u>203,073</u>
Business type activities:	
Food services	<u>2,330</u>

6. Long-Term Liabilities

Changes in long-term liabilities for the year ended June 30, 2007 are summarized as follows:

	Balance Beginning of Year	Additions	Reductions	Balance End of Year	Due Within One Year
	\$	\$	\$	\$	\$
General obligation bonds	2,030,000	-	250,000	1,780,000	265,000
EPA asbestos removal loan	353	-	353	-	-
Termination benefits	<u>79,418</u>	-	<u>57,459</u>	<u>21,959</u>	<u>14,733</u>
Total	<u>2,109,771</u>	-	<u>307,812</u>	<u>1,801,959</u>	<u>279,733</u>

Termination Benefits

The District offers a voluntary early retirement plan to its employees. The current policy expired on January 15, 2007. Eligible employees must have completed at least fifteen years of full-time service to the District and must have reached the age of fifty-five on or before June 30 in the calendar year in which early retirement commences. The application for early retirement is subject to approval by the Board of Education.

Early retirement benefits are equal to 85% of difference between the applicant's current salary schedule amount and that year's base pay.

Early retirement benefits will be paid in two equal installments beginning in July following the start of retirement. The second payment will be paid the following January.

At June 30, 2007, the District has obligations to three participants with a total liability of \$21,859. Actual early retirement expenditures for the year ended June 30, 2007 totaled \$57,459.

General Obligation Bonds Payable

Details of the District's June 30, 2007 general obligation bonded indebtedness are as follows:

Year Ending June 30,	Bond Issue of August 1998			
	Interest Rates	Principal	Interest	Total
	%	\$	\$	\$
2008	4.375	265,000	78,113	343,113
2009	4.375	275,000	66,519	341,519
2010	4.375	290,000	54,488	344,488
2011	4.400	300,000	41,800	341,800
2012	4.400	315,000	28,600	343,600
2013	4.400	335,000	14,740	349,740
		<u>1,780,000</u>	<u>284,260</u>	<u>2,064,260</u>

7. Pension and Retirement Benefits

The District contributes to the Iowa Public Employees Retirement System (IPERS) which is a cost-sharing multiple-employer defined benefit pension plan administered by the State of Iowa. IPERS provides retirement and death benefits which are established by state statute to plan members and beneficiaries. IPERS issues a publicly available financial report that includes financial statements and required supplementary information. The report may be obtained by writing to IPERS, P.O. Box 9117, Des Moines, Iowa, 50306-9117.

Plan members are required to contribute 3.70% of their annual covered salary and the District is required to contribute 5.75% of annual covered payroll for the years ended June 30, 2007, 2006 and 2005. Contribution requirements are established by state statute. The District's contributions to IPERS for the years ended June 30, 2007, 2006, and 2005 were \$208,141, \$212,882 and \$182,859 respectively, equal to the required contributions for each year.

8. Risk Management

The District is exposed to various risks of loss related to torts; theft; damage to and destruction of assets; errors and omissions; injuries to employees; and natural disasters. These risks are covered by the purchase of commercial insurance. The District assumes liability for any deductibles and claims in excess of coverage limitations. Settled claims from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

9. Area Education Agency

The District is required by the Code of Iowa to budget for its share of special education support, media and educational services provided through the area education agency. The District's actual amount for this purpose totaled \$257,735 for the year ended June 30, 2007 and is recorded in the General Fund by making a memorandum adjusting entry to the cash basis financial statements.

10. Related Party Transaction

A District board member owns a portion of the insurance agency from which the District purchases its property, liability and workmen's compensation insurance. The District paid \$73,186 in premiums to this agency during the year ended June 30, 2007.

REQUIRED SUPPLEMENTARY INFORMATION

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Budgetary Comparison Schedule of Revenues, Expenditures and Changes in Balances -
Budget and Actual - All Governmental Funds and Proprietary Fund

Required Supplementary Information

Year ended June 30, 2007

	Governmental Fund Actual	Proprietary Fund Actual	Total Actual	Budgeted Amounts		Final to Actual Variance - Positive (Negative)
				Original	Final	
	\$	\$	\$	\$	\$	\$
Revenues:						
Local sources	3,343,972	159,701	3,503,673	3,346,067	3,346,067	157,606
Intermediate sources	514	-	514	500	500	14
State sources	3,293,384	3,610	3,296,994	3,432,045	3,432,045	(135,051)
Federal sources	415,670	126,497	542,167	578,000	578,000	(35,833)
Total revenues	<u>7,053,540</u>	<u>289,808</u>	<u>7,343,348</u>	<u>7,356,612</u>	<u>7,356,612</u>	<u>(13,264)</u>
Expenditures:						
Instruction	4,588,053	-	4,588,053	4,663,000	4,663,000	74,947
Support services	1,658,581	-	1,658,581	2,039,542	2,039,542	380,961
Non-instructional programs	-	294,058	294,058	386,252	386,252	92,194
Other expenditures	749,094	-	749,094	961,915	961,915	212,821
Total expenditures	<u>6,995,728</u>	<u>294,058</u>	<u>7,289,786</u>	<u>8,050,709</u>	<u>8,050,709</u>	<u>760,923</u>
Excess (deficiency) of revenues over (under) expenditures	57,812	(4,250)	53,562	(694,097)	(694,097)	747,659
Other financing sources (uses) net	<u>4,965</u>	<u>-</u>	<u>4,965</u>	<u>-</u>	<u>-</u>	<u>4,965</u>
Excess (deficiency) of revenues and other financing sources (uses) over (under) expenditures	62,777	(4,250)	58,527	(694,097)	(694,097)	752,624
Balance beginning of year	<u>1,909,193</u>	<u>15,317</u>	<u>1,924,510</u>	<u>1,950,986</u>	<u>1,950,986</u>	<u>(26,476)</u>
Balance end of year	<u><u>1,971,970</u></u>	<u><u>11,067</u></u>	<u><u>1,983,037</u></u>	<u><u>1,256,889</u></u>	<u><u>1,256,889</u></u>	<u><u>726,148</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Notes to Required Supplementary Information - Budgetary Reporting

Year ended June 30, 2007

This budgetary comparison is presented as Required Supplementary Information in accordance with Governmental Accounting Standard Board Statement No. 41 for governments with significant budgetary perspective differences resulting from not being able to present budgetary comparisons for the General Fund and each major Special Revenue Fund.

In accordance with the Code of Iowa, the Board of Education annually adopts a budget following required public notice and hearing for all funds except Internal Service, Private Purpose Trust and Agency Funds. The budget may be amended during the year utilizing similar statutorily prescribed procedures. The District's budget is prepared on a GAAP basis.

Formal and legal budgetary control for the certified budget is based upon four major classes of expenditures known as functions, not by fund. These four functions are instruction, support services, non-instructional programs and other expenditures. Although the budget document presents function expenditures or expenses by fund, the legal level of control is at the aggregated function level, not by fund. The Code of Iowa also provides that District expenditures in the General Fund may not exceed the amount authorized by the school finance formula. The District did not amend its budget during the year.

OTHER SUPPLEMENTARY INFORMATION

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Combining Balance Sheet
Nonmajor Governmental Funds

June 30, 2007

Assets	Special Revenue Funds			Total
	Management	Student	Debt	
	Levy	Activity	Service	
	\$	\$	\$	\$
Cash and pooled investments	40,032	135,789	2,049	177,870
Receivables:				
Property tax:				
Delinquent	2,549	-	-	2,549
Succeeding year	85,000	-	-	85,000
Accounts	-	260	-	260
Total assets	127,581	136,049	2,049	265,679
Liabilities & Fund Balances				
Liabilities:				
Accounts payable	947	3,778	-	4,725
Deferred revenue:				
Succeeding year property tax	85,000	-	-	85,000
Total liabilities	85,947	3,778	-	89,725
Fund balances:				
Reserved for debt service	-	-	2,049	2,049
Unreserved reported in:				
Special revenue funds	41,634	132,271	-	173,905
Total fund balances	41,634	132,271	2,049	175,954
Total liabilities and fund balances	127,581	136,049	2,049	265,679

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Combining Schedule of Revenues, Expenditures and Changes in Fund Balances
Nonmajor Governmental Funds

Year ended June 30, 2007

	Special Revenue Funds			Total
	Management Levy	Student Activity Fund	Debt Service	
	\$	\$	\$	\$
Revenues:				
Local sources:				
Local tax	150,067	-	-	150,067
Other	7,709	201,809	-	209,518
State sources	138	-	-	138
Total revenues	<u>157,914</u>	<u>201,809</u>	<u>-</u>	<u>359,723</u>
Expenditures:				
Current:				
Instruction:				
Regular	46,554	-	-	46,554
Other	-	215,852	-	215,852
Support services:				
Operation and maintenance of plant	73,269	-	-	73,269
Other expenditures:				
Long-term debt:				
Principal	-	-	250,353	250,353
Interest and fiscal charges	-	-	89,450	89,450
Total expenditures	<u>119,823</u>	<u>215,852</u>	<u>339,803</u>	<u>675,478</u>
Excess (deficiency) of revenues over (under) expenditures	38,091	(14,043)	(339,803)	(315,755)
Other financing sources (uses):				
Operating transfers in	-	-	339,803	339,803
Net change in fund balances	38,091	(14,043)	-	24,048
Fund balances beginning of year	<u>3,543</u>	<u>146,314</u>	<u>2,049</u>	<u>151,906</u>
Fund balances end of year	<u><u>41,634</u></u>	<u><u>132,271</u></u>	<u><u>2,049</u></u>	<u><u>175,954</u></u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Changes in Special Revenue Fund, Student Activity Accounts

Year ended June 30, 2007

<u>Account</u>	Balance Beginning of Year	Revenues	Expenditures	Intra-fund Transfers	Balance End of Year
	\$	\$	\$	\$	\$
All athletics	(9,169)	14,250	4,886	(132)	63
Cross country	87	185	770	700	202
Football	16,849	15,773	24,435	(1,500)	6,687
Volleyball	4,803	5,861	7,795	984	3,853
Boys basketball	3,159	13,961	10,226	(1,000)	5,894
Girls basketball	5,945	7,091	4,080	(4,870)	4,086
Boys track	842	3,074	2,411	500	2,005
Girls track	1,211	1,751	2,685	400	677
Boys golf	360	11	312	500	559
Girls golf	152	110	281	700	681
Baseball	819	5,487	12,318	6,200	188
Softball	699	7,152	11,097	3,500	254
Wrestling	1,886	5,984	11,166	3,370	74
Band	1,241	2,248	5,864	4,200	1,825
Chorus	1,246	1,923	6,266	4,700	1,603
Clubs	652	-	652	-	-
Senior class	-	-	645	982	337
Junior class	982	3,414	3,100	765	2,061
Sophomore class	1,747	4,067	2,186	(1,719)	1,909
Freshman class	28	-	-	(28)	-
Class special	3,593	-	47	(2,273)	1,273
HS activities	4,521	28,108	11,180	(19,848)	1,601
Art club	616	2,213	2,101	-	728
Cheerleaders	2,458	11,034	11,518	-	1,974
Computer club	1,270	-	-	-	1,270
Drama club	2,507	2,536	2,053	710	3,700
FCA	4,702	-	100	-	4,602
FFA	3,494	10,972	12,625	(16)	1,825
Industrial tech. club	26	-	4	-	22
Library reading club	1,196	196	666	-	726
Marketing club	746	4,455	3,070	-	2,131
Oracle yearbook organization	11,622	7,327	6,043	-	12,906
Science club	945	500	521	-	924
Spanish club	6,407	7,365	11,513	-	2,259
Student council-HS	8,452	4,944	7,296	-	6,100
Speech club	3,842	-	902	2,201	5,141
Student council K-4	8,699	5,943	4,906	1,106	10,842
Unallocated interest	6,833	3,474	3,618	(132)	6,557
MS all athletics	-	11	326	315	-
MS football	-	-	969	969	-

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT
 Schedule of Changes in Special Revenue Fund, Student Activity Accounts

Year ended June 30, 2007

<u>Account</u>	Balance Beginning of Year	Revenues	Expenditures	Intra-fund Transfers	Balance End of Year
	\$	\$	\$	\$	\$
MS volleyball	-	-	1,047	1,047	-
MS basketball	-	-	2,272	2,272	-
MS wrestling	435	-	354	-	81
MS track	-	143	1,149	1,006	-
MS golf	113	-	-	-	113
MS baseball	-	200	1,013	813	-
Bowling	(1,637)	3,360	1,544	-	179
MS softball	-	220	1,243	1,023	-
MS vocal music	-	-	798	798	-
MS band	816	1,056	1,818	889	943
Middle school activities	9,600	22,747	14,638	(9,132)	8,577
MS student council	7,011	2,301	1,437	-	7,875
Sixth grade	1,092	1,200	311	-	1,981
Seventh grade	288	-	-	-	288
Eighth grade	528	1,082	1,192	-	418
Checking interest	14,722	1,543	-	-	16,265
Concessions	1,530	-	-	-	1,530
June 30, 2007 accrual entries	-	260	3,778	-	(3,518)
June 30, 2006 accrual entries	6,348	(13,723)	(7,375)	-	-
Totals	146,314	201,809	215,852	-	132,271

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Revenues by Source and Expenditures by Function
All Governmental Funds

For the Last Four Years

	Modified Accrual Basis			
	2007	2006	2005	2004
	\$	\$	\$	\$
Revenues:				
Local sources:				
Local tax	2,786,862	2,637,393	2,735,365	2,729,570
Tuition	213,057	204,989	198,123	207,060
Other	344,053	369,380	295,101	286,971
Intermediate sources	514	378	486	-
State sources	3,293,384	3,300,505	3,302,417	3,148,868
Federal sources	415,670	459,728	281,937	220,990
Total revenues	<u>7,053,540</u>	<u>6,972,373</u>	<u>6,813,429</u>	<u>6,593,459</u>
Expenditures:				
Instruction:				
Regular instruction	3,104,891	2,955,437	3,069,291	2,846,476
Special instruction	781,369	809,660	742,105	691,506
Other instruction	701,793	711,725	649,366	662,830
Support services:				
Student services	83,672	99,065	137,792	138,479
Instructional staff services	124,973	202,088	175,448	152,242
Administration services	629,847	607,126	606,568	564,238
Operation and maintenance of plant services	504,485	489,417	457,928	436,054
Transportation services	315,604	318,798	277,414	223,471
Central support services				
Non-instructional programs	-	-	4,337	-
Other expenditures:				
Facilities acquisition	151,556	137,350	55,676	66,050
Long-term debt:				
Principal	250,353	243,489	236,000	346,000
Interest and other charges	89,450	99,950	111,101	126,519
AEA flowthrough	257,735	252,209	252,328	255,572
Total expenditures	<u>6,995,728</u>	<u>6,926,314</u>	<u>6,775,354</u>	<u>6,509,437</u>

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Expenditures of Federal Awards

Year ended June 30, 2007

<u>Grantor/Program</u>	<u>CFDA Number</u>	<u>Grant Number</u>	<u>Expenditures \$</u>
Indirect:			
U.S. Department of Agriculture:			
Iowa Department of Education:			
School Nutrition Cluster Programs:			
National School Lunch Program	10.555	FY07	86,833
School Breakfast Program	10.553	FY07	11,162
			<u>97,995</u>
Food Donation (Non-cash)	10.550	FY07	28,502
U.S. Department of Education:			
Iowa Department of Education:			
Title I Grants to Local Education Agencies	84.010	2862-G-07	84,888
Improving Teacher Quality State Grants	84.367	FY07	30,213
Grants for State Assessments and Related Activities	84.369	FY07	5,180
State Grants for Innovative Programs	84.298	FY07	945
Safe & Drug Free Schools and Communities - State Grants	84.186	FY07	2,752
Comprehensive School Reform Demonstration	84.332	FY07	24,920
Charter Schools	84.282	FY07	131,294
Charter Schools	84.282	FY06	72,323
			<u>203,617</u>
Area Education Agency 4:			
Special Education Grants to States	84.027	FY07	43,756
Vocational Education - Basic Grants to States	84.048	FY07	7,425
			<u>50,181</u>
Total			<u><u>530,193</u></u>

Basis of Presentation - The Schedule of Expenditures of Federal Awards includes the federal grant activity of Hartley-Melvin-Sanborn Community School District and is presented on the accrual or modified accrual basis of accounting. The information on this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Nonprofit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

Independent Auditor's 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

To the Board of Education of
Hartley-Melvin-Sanborn Community School District:

We have audited the accompanying financial statements of the governmental activities, the business-type activities, each major fund and the aggregate remaining fund information of Hartley-Melvin-Sanborn Community School District as of and for the year ended June 30, 2007, which collectively comprise the District's basic financial statements listed in the table of contents, and have issued our report thereon dated February 4, 2008. We conducted our audit in accordance with U.S. generally accepted auditing standards 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 Hartley-Melvin-Sanborn Community School District's 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 our opinion on the effectiveness of Hartley-Melvin-Sanborn Community School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of Hartley-Melvin-Sanborn Community School District'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 and other deficiencies we consider to be material weaknesses.

A control deficiency exists when the design or operation of the 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 Hartley-Melvin-Sanborn Community School District's ability to initiate, authorize, record, process, or report financial data reliably in accordance with U.S. generally accepted accounting principles such that there is more than a remote likelihood a misstatement of Hartley-Melvin-Sanborn Community School District's financial statements that is more than inconsequential will not be prevented or detected by Hartley-Melvin-Sanborn Community School District's internal control. We consider the deficiencies in internal control described in Part II of the accompanying Schedule of Findings and Questioned Costs 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 a material misstatement of the financial statements will not be prevented or detected by Hartley-Melvin-Sanborn Community School District'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, of the significant deficiencies described above, we believe items 07-II-A, 07-II-B, and 07-II-C are material weaknesses.

Compliance and Other Matters

As part of obtaining reasonable assurance about whether Hartley-Melvin-Sanborn Community School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grant agreements, non-compliance 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 non-compliance or other matters that are required to be reported under Government Auditing Standards. However, we noted certain immaterial instances of non-compliance or other matters that are described in Part IV of the accompanying Schedule of Findings and Questioned Costs.

Comments involving statutory and other legal matters about the District's operations for the year ended June 30, 2007 are based exclusively on knowledge obtained from procedures performed during our audit of the financial statements of the District. Since our audit was based on tests and samples, not all transactions that might have had an impact on the comments were necessarily audited. The comments involving statutory and other legal matters are not intended to constitute legal interpretations of those statutes.

Hartley-Melvin-Sanborn Community School District's responses to findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we have expressed our conclusions on the District's responses, we did not audit Hartley-Melvin-Sanborn Community School District's responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Hartley-Melvin-Sanborn Community School District and other parties to whom Hartley-Melvin-Sanborn Community School District may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

We would like to acknowledge the many courtesies and assistance extended to us by personnel of Hartley-Melvin-Sanborn Community School District during the course of our audit. Should you have any questions concerning any of the above matters, we shall be pleased to discuss them with you at your convenience.

BURTON E. TRACY & CO., P.C.
Certified Public Accountants

February 4, 2008

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Independent Auditor's Report on Compliance with Requirements Applicable
to Each Major Program and on Internal Control over Compliance
in Accordance with OMB Circular A-133

To the Board of Education of
Hartley-Melvin-Sanborn Community School District:

Compliance

We have audited the compliance of Hartley-Melvin-Sanborn Community School District with the types of compliance requirements described in 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, 2007. Hartley-Melvin-Sanborn Community School District's major federal programs are identified in Part I of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts and grant agreements applicable to each of its major federal programs is the responsibility of Hartley-Melvin-Sanborn Community School District's management. Our responsibility is to express an opinion on Hartley-Melvin-Sanborn Community School District's compliance based on our audit.

We conducted our audit of compliance in accordance with U.S. generally accepted auditing standards, 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 non-compliance 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 Hartley-Melvin-Sanborn Community School District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on Hartley-Melvin-Sanborn Community School District's compliance with those requirements.

In our opinion, Hartley-Melvin-Sanborn Community School 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, 2007.

Internal Control Over Compliance

The management of Hartley-Melvin-Sanborn Community School District is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts and grant agreements applicable to federal programs. In planning and performing our audit, we considered Hartley-Melvin-Sanborn Community School 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, 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 Hartley-Melvin-Sanborn Community School District's internal control over compliance.

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

A control deficiency in the District'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 District's ability to administer a federal program such that there is more than a remote likelihood noncompliance with a type of compliance requirement of a federal program that is more than inconsequential will not be prevented or detected by the District's internal control. We consider the deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 07-III-A and 07-III-B to be significant deficiencies.

A material weakness is a significant deficiency, or combination of significant deficiencies, that results in more than a remote likelihood material noncompliance with a type of compliance requirement of a federal program, will not be prevented or detected by the District's internal control. We consider the significant deficiency in internal control over compliance described in the accompanying Schedule of Findings and Questioned Costs as items 07-III-A and 07-III-B to be material weaknesses.

Hartley-Melvin-Sanborn Community School District's responses to the findings identified in our audit are described in the accompanying Schedule of Findings and Questioned Costs. While we expressed our conclusions on the District's responses, we did not audit Hartley-Melvin-Sanborn Community School District's responses and, accordingly, we express no opinion on them.

This report, a public record by law, is intended solely for the information and use of the officials, employees and citizens of Hartley-Melvin-Sanborn Community School District and other parties to whom Hartley-Melvin-Sanborn Community School District may report, including federal awarding agencies and pass-through entities. This report is not intended to be and should not be used by anyone other than these specified parties.

BURTON E. TRACY & CO., P.C.
Certified Public Accountants

February 4, 2008

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part I: Summary of the Independent Auditor's Results:

- (a) An unqualified opinion was issued on the governmental activities, the business type activities, each major fund and the aggregate remaining fund information.
- (b) Significant deficiencies in internal control over financial reporting were disclosed by the audit of the financial statements, including material weaknesses.
- (c) The audit did not disclose any noncompliance which is material to the financial statements.
- (d) Significant deficiencies in internal control over major programs were disclosed by the audit of the financial statements, including material weaknesses.
- (e) An unqualified opinion was issued on compliance with requirements applicable to each major program.
- (f) The audit disclosed audit findings which were required to be reported in accordance with Office of Management and Budget Circular A-133, Section .510(a).
- (g) Major programs were as follows:
 - CFDA Number 84.282 Charter Schools
 - CFDA Number 84.010 Title I Grants to Local Education Agencies
- (h) The dollar threshold used to distinguish between Type A and Type B programs was \$300,000.
- (i) Hartley-Melvin-Sanborn School did not qualify as a low-risk auditee.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part II: Findings Related to the Financial Statements:

Significant deficiencies:

07-II-A Segregation of Duties: The limited number of personnel makes it difficult to achieve adequate internal accounting control through the segregation of duties and responsibilities, such as recording and processing cash receipts, preparing checks and bank reconciliations, preparing and posting general journal entries, preparation of journals and general financial information for ledger posting, and the analysis of financial information. A small staff makes it difficult to establish an ideal system of automatic internal checks on accounting record accuracy and reliability, although we noted the District had taken steps to segregate duties between the present personnel. This is not an unusual condition but it is important the District officials are aware that the condition exists.

Recommendation: We realize that with a limited number of office employees, segregation of duties is difficult. However, the District should review its control procedures and investigate methods to increase monitoring activities to obtain the maximum internal control possible under the circumstances.

District Response: The District is aware of the lack of complete segregation of duties and will make changes as the opportunity arises.

Conclusion: Response accepted.

07-II-B Financial Reporting: During the audit, we identified material amounts of receivables, payables and deferred revenue that were not correctly recorded in the District's financial records. Adjustments were subsequently made by the District to correct these amounts in the financial statements.

Recommendation: The District should implement procedures to ensure all receivables, payables and deferred revenues are identified and included in the District's financial statements.

District Response: We will double check these in the future to avoid missing any receivables, payables or deferred revenues.

Conclusion: Response accepted.

07-II-C Financial Statement Preparation: Financial statement preparation is the responsibility of the District. At the present time District personnel do not have the skills necessary to be able to write the District's financial statements and the related note disclosures. This is not an unusual situation for small governmental entities.

Recommendation: District personnel should attend any governmental accounting and reporting training sessions that may be offered by the Iowa Department of Education, State Auditor's Office or Iowa Association of School Business Officials. The school business office should also have governmental accounting and reporting reference materials.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part II: Findings Related to the Financial Statements (continued):

District Response: As a school we certainly understand the need for continuing education classes for all of our staff. However, we have a limited budget and must continually prioritize needs. At this point in time it is not cost effective to train our staff to the level necessary that would enable them to write the financial statements, nor is it feasible to hire additional employees that already possess the skills.

Conclusion: Response accepted.

07-II-D Expenditures for Student Trips: We noted a \$120 check for cash, for student meals on student activity trip, that did not have supporting documentation.

Recommendation: All District expenditures should be documented with invoices, receipts, contracts or other written documentation. If meal money is a part of a student trip, each student receiving the money should sign a receipt when given the money. If activity sponsors purchase meals for students on trips, they should turn in receipts for reimbursement after the trip or use a district credit card for the purchases.

District Response: We will investigate methods to improve our controls over meal money for student trips.

Conclusion: Response accepted.

Instances of Noncompliance:

No matters were reported.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part III: Findings and Questioned Costs for Federal Awards:

Instances of Noncompliance:

No matters were reported.

Significant deficiencies:

CFDA Number 84.282: Charter Schools
Federal Award Years: 2006 and 2007
U.S. Department of Education
Passed through the Iowa Department of Education

CFDA Number 84.010: Title I Grants to Local Education Agencies
Federal Award Year: 2007
U.S. Department of Education
Passed through the Iowa Department of Education

07-III-A Segregation of Duties: The limited number of personnel makes it difficult to achieve adequate internal accounting control through the segregation of duties and responsibilities, such as recording and processing cash receipts, preparing checks and bank reconciliations, preparing and posting general journal entries, preparation of journals and general financial information for ledger posting, and the analysis of financial information. A small staff makes it difficult to establish an ideal system of automatic internal checks on accounting record accuracy and reliability, although we noted the District had taken steps to segregate duties between the present personnel. This is not an unusual condition but it is important the District officials are aware that the condition exists.

Recommendation: We realize that with a limited number of office employees, segregation of duties is difficult. However, the District should review its control procedures to obtain the maximum internal control possible under the circumstances.

District Response: The District is aware of the lack of complete segregation of duties and will make changes as the opportunity arises.

Conclusion: Response accepted.

CFDA Number 84.010: Title I Grants to Local Education Agencies
Federal Award Year: 2007
U.S. Department of Education
Passed through the Iowa Department of Education

07-III-B Title I Salary Expenditures: Office of Management and Budget Circular A-87 requires that employees working on a single Federal award semi-annually certify that 100% of their time is spent on that federal program. The District did not have controls in place to obtain the required certifications.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part III: Findings and Questioned Costs for Federal Awards (continued):

Recommendation: The District should adopt a standard time certification form and a timeline for completing the form twice a year.

District Response: We have created a form and will have it completed twice a year.

Conclusion: Response accepted.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part IV: Other Findings Related to Statutory Reporting:

07-IV-A Certified Budget: Expenditures for the year ended June 30, 2007, did not exceed the amounts budgeted.

07-IV-B Questionable Expenditures: We noted no expenditures that may not meet the requirements of public purpose as defined in an Attorney General's opinion dated April 25, 1979.

07-IV-C Travel Expenses: No expenditures of District money for travel expenses of spouses of District officials or employees were noted. No travel advances to District officials or employees were noted.

07-IV-D Business Transactions: Business transactions between the District and District officials or employees are detailed as follows:

<u>Name, Title and Business Connection</u>	<u>Transaction Description</u>	<u>Amount</u> \$
Bill Treimer, Board Member, Co-owner of local insurance agency	School insurance policy	73,186

This transaction appears to represent a conflict of interest since the dollar amount was more than \$2,500 and the insurance contract was not bid.

Recommendation: Business with district officials is not a conflict of interest if bids are taken or if the total amount is less than \$2,500. The District should consult legal council regarding this matter.

District Response: We have consulted with our attorney and received an opinion that this is not a conflict of interest. Bill Treimer does not handle the commercial insurance for the business, but does receive a benefit of less than \$2,500 from the insurance contract with the school. Bill Treimer will recuse himself in all votes where the Board is considering commercial insurance policies.

Conclusion: Response accepted.

07-IV-E Bond Coverage: Surety bond coverage of District officials and employees is in accordance with statutory provisions. The amount of bond coverage should be reviewed annually to insure that the coverage is adequate for current operations.

07-IV-F Board Minutes: We noted no transactions requiring Board approval that had not been approved by the Board.

07-IV-G Certified Enrollment: No variances in the basic enrollment data certified to the Department of Education were noted.

HARTLEY-MELVIN-SANBORN COMMUNITY SCHOOL DISTRICT

Schedule of Findings and Questioned Costs

Year ended June 30, 2007

Part IV: Other Findings Related to Statutory Reporting (continued):

07-IV-H Deposits and Investments: We noted no instances of noncompliance with the deposit and investment provisions of Chapter 12B and Chapter 12C of the Code of Iowa and the District's investment policy.

07-IV-I Certified Annual Report: The Certified Annual Report was not properly certified to the Iowa Department of Education by September 28, 2007. We noted no significant deficiencies in the amounts reported.

Recommendation: In the future, the District should ensure the Certified Annual Report is timely certified to the Iowa Department of Education.

District Response: We will do so in the future.

Conclusion: Response accepted.

07-IV-J Physical Plant and Equipment Levy Fund Expenditures (PPEL): The PPEL property tax levy may be used to purchase and improve grounds; to construct buildings; to purchase or lease a single unit of equipment or technology exceeding \$500 in value per unit; to repair, remodel improve, or expand buildings; for energy conservation; and to purchase transportation equipment.

We noted that the District used the PPEL Fund to pay \$2,348 for office equipment with per unit costs of less than \$500, \$925 for toner cartridges and \$1,140 for van repairs. These items do not appear to be allowable from the PPEL Fund.

Recommendation: The District should be aware of the limitation on types of expenditures allowed from this fund. And the General Fund should reimburse the PPEL Fund for these expenditures.

District Response: We will monitor expenditures from the PPEL Fund and make the reimbursement.

Conclusion: Response accepted.