

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

REPORT OF AUDIT
Year Ended June 30, 2014

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Marr, Miller & Myers, PSC

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INDEPENDENT AUDITOR'S REPORT

September 30, 2014

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

Report on the Financial Statements

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 the Middlesboro Independent School District (the "District"), as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements as listed in the table of contents.

Management's Responsibility for the Financial Statements

Management is responsible for the preparation and fair presentation of these financial statements in accordance with U.S. generally accepted accounting principles; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor's Responsibility

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; the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States; the provisions of Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations; Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the Independent Auditor's Contract – State Audit Requirements, Appendix III to the Independent Auditor's Contract – Audit Extension Request and Appendix IV to the Independent Auditor's Contract – Instructions for Submission of the Audit Report. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the District's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

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We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

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 the District as of June 30, 2014, and the respective changes in financial position, and, where applicable, cash flows thereof for the year then ended in accordance with U.S. generally accepted accounting principles.

Other Matters

Required Supplementary Information

U.S. generally accepted accounting principles require that the management's discussion and analysis and budgetary comparison information on pages 4-7 and 14-15 be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board, who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with U.S. generally accepted auditing standards, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

Other Information

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the District's basic financial statements. The introductory section and combining and individual nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. The schedule of expenditures of federal awards is presented for purposes of additional analysis as required by U.S. Office of Management and Budget Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*, and is also not a required part of the basic financial statements.

The combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards are the responsibility of management and were derived from and relate directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with U.S. generally accepted auditing standards. In our opinion, the combining and individual nonmajor fund financial statements and the schedule of expenditures of federal awards are fairly stated in all material respects in relation to the basic financial statements as a whole.

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The introductory section has not been subjected to the auditing procedures applied in the audit of the basic financial statements and, accordingly, we do not express an opinion or provide any assurance on them.

Other Reporting Required by Government Auditing Standards

In accordance with *Government Auditing Standards*, we have also issued our report dated September 30, 2014, on our consideration of the District's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements and other matters. The purpose of that report is to describe the scope of our testing of internal control over financial reporting and compliance and the results of that testing, and not to provide an opinion on internal control over financial reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control over financial reporting and compliance.

Marr, Miller & Myers, PSC

Certified Public Accountants

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2014

The management of the Middlesboro Independent School District (District) offers readers this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2014. We encourage readers to review the information presented here in conjunction with additional information found within the body of the audit.

SUPERINTENDENT'S REVIEW OF THE YEAR

During the year ended June 30, 2014, the Middlesboro Independent School District made several decisions that had a direct impact on the end of the year financial balance. Because of the continued declining enrollment, it was evident that we needed to re-adjust our spending to guarantee an appropriate fiscal balance in succeeding years. Some of the steps initiated by the District were to assess our current level of staffing and evaluate all transportation costs for the District.

Overall, this has been a financially successful year for the District. Although our funding from federal and state sources decreased, and continues to diminish, we have been able to increase our overall fund balance. This is especially critical due to continuing financial shortfalls of federal and state funding.

FINANCIAL HIGHLIGHTS

- The ending cash balance for the District was \$1,419,309 in 2014 and \$130,232 in 2013. The cash balances include \$93,475 for 2014 and 2013, respectively, reserved for debt service payments, and \$280,978 and \$10 for 2014 and 2013, respectively, reserved for future construction projects.
- The General Fund had \$10,109,984 in revenue, excluding interfund transfers and compensation for gain on assets, which primarily consisted of the state program (SEEK) and property, utilities, and motor vehicle taxes. Excluding interfund transfers, there were \$9,446,082 in General Fund expenditures.
- When funds are available, the District may use cash or sell bonds to build or renovate facilities within the school district. The projects must be identified on the District Facility Plan.

OVERVIEW OF FINANCIAL STATEMENTS

This discussion and analysis is intended to serve as an introduction to the District's basic financial statements. The District's basic financial statements comprise three components: 1) government-wide financial statements, 2) fund financial statements, and 3) notes to the basic financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

Government-wide financial statements. The government-wide financial statements are designed to provide readers with a broad overview of the District's finances, in a manner similar to a private-sector business.

The statement of net position presents information on all of the District's assets and liabilities, with the difference between the two reported as net position. Over time, increases or decreases in net position may serve as a useful indicator of whether the financial position of the District is improving or deteriorating.

The statement of activities presents information showing how the District's net position changed during the most recent fiscal year. All changes in net position are reported as soon as the underlying event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in future fiscal periods.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2014

The government-wide financial statements outline functions of the District that are principally supported by property taxes and intergovernmental revenues (governmental activities). The governmental activities of the District include instruction, support services, plant operations and maintenance, student transportation and operation of non-instructional services. Fixed assets and related debt is also supported by taxes and intergovernmental revenues.

The government-wide financial statements can be found on pages 8 and 9 of this report.

Fund financial statements. A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. This is a state mandated uniform system and chart of accounts for all Kentucky public school districts utilizing the MUNIS administrative software. The District uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the District can be divided into three categories: governmental, proprietary and fiduciary. Fiduciary funds are trust funds established by benefactors to aid in student education, welfare and teacher support. The proprietary fund is vending and food service operations. All other activities of the District are included in the governmental funds.

The basic governmental fund financial statements can be found on pages 10 through 13 of this report.

Notes to the basic financial statements. The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The notes to the basic financial statements can be found on pages 20 through 35 of this report.

GOVERNMENT-WIDE FINANCIAL ANALYSIS

The largest portion of the District's net assets reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, vehicles, general equipment and construction in progress); less any related debt used to acquire those assets that are still outstanding. The District uses these capital assets to provide services to its students; consequently, these assets are not available for future spending. Although the District's investment in its capital assets is reported net of related debt, it should be noted that the resources needed to repay this debt must be provided from other sources, since the capital assets themselves cannot be used to liquidate these liabilities.

The District's financial position is the product of several financial transactions including the net results of activities, the acquisition and payment of debt, the acquisition and disposal of capital assets, and the depreciation of capital assets.

Net Position for the period ending June 30, 2014

Fiscal year 2014 government-wide net position compared to 2013 is as follows:

	2014	2013
Current assets	\$ 1,981,598	\$ 943,691
Capital assets	<u>5,753,296</u>	<u>6,256,264</u>
Total Assets	<u>\$ 7,734,894</u>	<u>\$ 7,199,955</u>
Current liabilities	\$ 677,189	\$ 650,815
Noncurrent liabilities	<u>2,702,704</u>	<u>2,816,440</u>
Total Liabilities	<u>\$ 3,379,893</u>	<u>\$ 3,467,255</u>
Net position		
Investment in capital assets, net of related debt	\$ 3,099,421	\$ 3,300,419
Restricted	581,532	213,189
Unrestricted	<u>674,048</u>	<u>219,092</u>
Total Net Position	<u>\$ 4,355,001</u>	<u>\$ 3,732,700</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2014

The District had an overall increase in total net position of \$622,301, comprised of an increase in business-type activities of \$34,554 and in governmental activities of \$587,747.

The following table presents a summary of revenues and expenditures, Governmental Funds only, for the fiscal years ended June 30:

	<u>2014</u>	<u>Percent</u>	<u>2013</u>	<u>Percent</u>
REVENUES				
Local revenue sources	\$ 3,164,069	24.85 %	\$ 3,057,066	22.75 %
State revenue sources	8,087,711	63.51	8,543,742	63.58
Federal sources	<u>1,482,205</u>	<u>11.64</u>	<u>1,836,973</u>	<u>13.67</u>
Total revenues	<u>12,733,985</u>	<u>100.00</u>	<u>13,437,781</u>	<u>100.00</u>
EXPENDITURES				
Instruction	6,997,203	54.95	7,763,721	57.78
Student support services	524,684	4.12	534,508	3.98
Instructional staff	715,654	5.62	844,175	6.28
District administration	654,736	5.14	641,219	4.77
School administration	642,929	5.05	835,367	6.22
Business	150,882	1.18	176,354	1.31
Plant operations and maintenance	1,085,299	8.52	1,223,917	9.11
Student transportation	443,606	3.48	505,770	3.76
Architectural/engineering	-	-	103,553	.77
Building improvements	16,646	.13	-	-
Community services activities	173,875	1.38	186,418	1.39
Debt service/lease obligations	<u>402,363</u>	<u>3.16</u>	<u>688,866</u>	<u>5.13</u>
Total expenditures	<u>11,807,877</u>	<u>92.73</u>	<u>13,503,868</u>	<u>100.50</u>
Excess revenues (expenditures)	<u>\$ 926,108</u>	<u>7.27 %</u>	<u>\$ (66,087)</u>	<u>(.50)%</u>

The majority of the District's revenues were derived from state revenue sources making up 63.51% of total revenues in 2014 as compared to 63.58% in 2013. Local revenue sources comprised 24.85% of total revenues in 2014 as compared to 22.75% in 2013.

Instructional expenditures comprised 54.95% of the District's total expenses for 2014 as compared to 57.78% in 2013. Plant operations and maintenance was the next largest consumption of revenues at 8.52% in 2014 as compared to 9.11% in 2013.

Comments on Budget Comparisons

In Kentucky, the public schools fiscal year is July 1 to June 30. Other programs operate on a different fiscal calendar, but are reflected in the District's overall budget. By law, the budget must have a minimum 2% contingency. The District adopted a 2013-14 budget with \$822,769 in contingency (8.6%).

- The District's total general fund revenues for the fiscal year ended June 30, 2014 were \$10,109,984.
- General fund budgeted revenues compared to actual revenues varied from line item to line item with the ending actual balance being \$2,380,720 more than budget or 30.80%. This is due primarily to recording on-behalf payments made by the State of Kentucky of \$1,803,082 that were not budgeted. When these are eliminated, revenues compared to budget were \$577,638 or 7.47% more than anticipated.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT'S DISCUSSION AND ANALYSIS
June 30, 2014

- The total cost of all general fund programs and services for the fiscal year ended June 30, 2014 were \$9,446,082.
- General fund budgeted expenditures compared to actual expenditures varied from line item to line item with the ending actual balance being \$1,212,376 more than budget or 14.72%. This is due primarily to recording on-behalf payments made by the State of Kentucky of \$1,803,082 that were not budgeted. When these are eliminated, expenditures compared to budget were \$590,706 or 7.17% less than anticipated.

FUTURE BUDGET IMPLICATIONS

In Kentucky, the public schools fiscal year is July 1 to June 30. Other programs operate on a different fiscal calendar, but are reflected in the District's overall budget. By law, the budget must have a minimum 2% contingency. The District has a tentative working budget for FY 2015 with \$902,072 in contingency (7.8%). Board action that impacts the finances includes:

- Expanding technology.
- Board match on Offers of Assistance from SFCC and Technology.
- Maintaining current staff levels.

Contacting the District's Financial Management

This financial report is designed to provide our citizens, taxpayers, customers, investors and creditors with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives.

Questions regarding this report should be directed to the Superintendent or to Ava Wilder, Director of Financial Services (606) 242-8800 or by mail at 220 North Twentieth Street, Middlesboro, KY 40965.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF NET POSITION
June 30, 2014

<u>ASSETS</u>	<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
CURRENT ASSETS			
Cash and cash equivalents	\$ 1,393,827	\$ 25,482	\$ 1,419,309
Accounts receivable:			
Taxes – current	156,670	-	156,670
Accounts receivable	3,581	504	4,085
Intergovernmental – state	23,949	-	23,949
Intergovernmental – federal	346,719	16,073	362,792
Materials and supplies inventory	-	14,793	14,793
Total current assets	<u>1,924,746</u>	<u>56,852</u>	<u>1,981,598</u>
NONCURRENT ASSETS			
Capital assets, net	<u>5,690,020</u>	<u>63,276</u>	<u>5,753,296</u>
Total noncurrent assets	<u>5,690,020</u>	<u>63,276</u>	<u>5,753,296</u>
TOTAL ASSETS	<u>7,614,766</u>	<u>120,128</u>	<u>7,734,894</u>
<u>LIABILITIES AND NET POSITION</u>			
CURRENT LIABILITIES			
Accounts payable	149,069	4,516	153,585
Accrued salaries and benefits payable	17,721	3,485	21,206
Deferred revenue	139,943	-	139,943
Current portion of bond obligations	255,000	-	255,000
Current portion of lease obligations	53,845	-	53,845
Current portion of accumulated sick leave	53,610	-	53,610
Total current liabilities	<u>669,188</u>	<u>8,001</u>	<u>677,189</u>
NONCURRENT LIABILITIES			
Noncurrent portion of bond obligations	2,170,000	-	2,170,000
Noncurrent portion of lease obligations	175,030	-	175,030
Noncurrent portion of accumulated sick leave	165,945	-	165,945
Noncurrent portion of insurance settlement payment	191,729	-	191,729
Total noncurrent liabilities	<u>2,702,704</u>	<u>-</u>	<u>2,702,704</u>
TOTAL LIABILITIES	<u>3,371,892</u>	<u>8,001</u>	<u>3,379,893</u>
NET POSITION			
Investment in capital assets, net of related debt	3,036,145	63,276	3,099,421
Restricted	563,167	18,365	581,532
Unrestricted	643,562	30,486	674,048
TOTAL NET POSITION	<u>\$ 4,242,874</u>	<u>\$ 112,127</u>	<u>\$ 4,355,001</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF ACTIVITIES
Year Ended June 30, 2014

<u>FUNCTIONS/PROGRAMS</u>	<u>Expenses</u>	<u>PROGRAM REVENUES</u>		
		<u>Charges for Services and Sales</u>	<u>Operating Grants and Contributions</u>	<u>Capital Grants and Contributions</u>
GOVERNMENTAL ACTIVITIES:				
Instruction	\$ 7,422,354	\$ 756	\$ 4,164,335	\$ -
Support services:				
Student	538,811	-	-	-
Instructional staff	720,629	-	-	-
District administration	658,342	-	-	-
School administration	647,815	-	-	-
Business	342,611	-	-	-
Plant operations and maintenance	1,092,369	-	-	-
Student transportation	487,307	-	-	-
Building improvements	184	-	-	24,093
Community services activities	175,436	-	-	-
Interest on long-term debt	106,532	-	-	-
TOTAL GOVERNMENTAL ACTIVITIES	<u>\$12,192,390</u>	<u>\$ 756</u>	<u>\$ 4,164,335</u>	<u>\$ 24,093</u>
BUSINESS-TYPE ACTIVITIES:				
Food service	\$ 1,034,878	\$ 120,663	\$ 991,585	\$ -
TOTAL BUSINESS-TYPE ACTIVITIES	<u>\$ 1,034,878</u>	<u>\$ 120,663</u>	<u>\$ 991,585</u>	<u>\$ -</u>
TOTAL PRIMARY GOVERNMENT	<u>\$13,227,268</u>	<u>\$ 121,419</u>	<u>\$ 5,155,920</u>	<u>\$ 24,093</u>

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

**NET (EXPENSES) REVENUES AND
CHANGES IN NET POSITION**

<u>Governmental Activities</u>	<u>Business-Type Activities</u>	<u>Total</u>
\$ (3,257,263)		\$ (3,257,263)
(538,811)		(538,811)
(720,629)		(720,629)
(658,342)		(658,342)
(647,815)		(647,815)
(342,611)		(342,611)
(1,092,369)		(1,092,369)
(487,307)		(487,307)
23,909		23,909
(175,436)		(175,436)
<u>(106,532)</u>		<u>(106,532)</u>
<u>(8,003,206)</u>		<u>(8,003,206)</u>
	<u>\$ 77,370</u>	<u>77,370</u>
	<u>77,370</u>	<u>77,370</u>
		<u>(7,925,836)</u>

GENERAL REVENUES

Taxes			
Property	2,075,421	-	2,075,421
Motor vehicle	246,465	-	246,465
Utilities	694,189	-	694,189
State and formula grants	5,381,488	-	5,381,488
Earnings on investments	24,647	368	25,015
Compensation for gain on assets	2,968	-	2,968
Other local revenues	<u>122,591</u>	-	<u>122,591</u>
Total general revenues	8,547,769	368	8,548,137
Operating transfers (net)	<u>43,184</u>	<u>(43,184)</u>	<u>-</u>
Total general revenues and transfers	<u>8,590,953</u>	<u>(42,816)</u>	<u>8,548,137</u>
Change in net position	587,747	34,554	622,301
Net position, July 1, 2013	<u>3,655,127</u>	<u>77,573</u>	<u>3,732,700</u>
Net position, June 30, 2014	<u>\$ 4,242,874</u>	<u>\$ 112,127</u>	<u>\$ 4,355,001</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

BALANCE SHEET
GOVERNMENTAL FUNDS
June 30, 2014

	General Fund	Special Revenue	Other Governmental Funds	Total Governmental Funds
ASSETS AND RESOURCES				
Cash and cash equivalents	\$ 1,209,088	\$ (189,714)	\$ 374,453	\$ 1,393,827
Accounts receivable:				
Taxes – current	156,670	-	-	156,670
Accounts receivable	3,581	-	-	3,581
Intergovernmental – state	-	23,949	-	23,949
Intergovernmental – federal	-	346,719	-	346,719
TOTAL ASSETS AND RESOURCES	<u>\$ 1,369,339</u>	<u>\$ 180,954</u>	<u>\$ 374,453</u>	<u>\$ 1,924,746</u>
LIABILITIES				
Accounts payable	\$ 124,520	\$ 24,549	\$ -	\$ 149,069
Accrued salaries and benefits payable	1,259	16,462	-	17,721
Deferred revenue	-	139,943	-	139,943
TOTAL LIABILITIES	<u>125,779</u>	<u>180,954</u>	<u>-</u>	<u>306,733</u>
FUND BALANCES				
Restricted				
Sick leave payable	53,610	-	-	53,610
Future construction projects	-	-	280,978	280,978
Debt service	-	-	93,475	93,475
Assigned				
Purchase obligations	85,812	68,886	-	154,698
Site based carryforward	199,961	-	-	199,961
Unassigned	904,177	(68,886)	-	835,291
TOTAL FUND BALANCES	<u>1,243,560</u>	<u>-</u>	<u>374,453</u>	<u>1,618,013</u>
TOTAL LIABILITIES AND FUND BALANCES	<u>\$ 1,369,339</u>	<u>\$ 180,954</u>	<u>\$ 374,453</u>	<u>\$ 1,924,746</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

RECONCILIATION OF THE BALANCE SHEET – GOVERNMENTAL FUNDS TO THE
STATEMENT OF NET POSITION
June 30, 2014

Total Fund Balances per fund financial statements			\$ 1,618,013
Amounts reported for governmental activities in the statement of net position are different because:			
Capital assets used in governmental activities are not financial resources, but they are reported in the statement of net position			5,690,020
Long-term liabilities are not due and payable in the current period and therefore are not reported as liabilities in the governmental funds, but they are presented in the statement of net position. Long-term liabilities at year end consists of:			
Bonds payable	\$	2,425,000	
Lease obligations		228,875	
Insurance settlement payment		191,729	
Accumulated sick leave payable		<u>219,555</u>	<u>(3,065,159)</u>
Total Net Position for Governmental Activities			<u>\$ 4,242,874</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
GOVERNMENTAL FUNDS
Year Ended June 30, 2014

	<u>General Fund</u>	<u>Special Revenue</u>
REVENUES		
From local sources:		
Taxes		
Property	\$ 1,853,791	\$ -
Motor vehicle	246,465	-
Utilities	694,189	-
Tuition and fees	756	-
Earnings on investments	24,647	-
Other local revenues	122,591	-
Intergovernmental – state	7,137,754	539,087
Intergovernmental – indirect federal	-	1,452,414
Intergovernmental – direct federal	29,791	-
TOTAL REVENUES	<u>10,109,984</u>	<u>1,991,501</u>
EXPENDITURES		
Instruction	5,384,511	1,612,692
Support services:		
Student	458,815	65,869
Instructional staff	602,983	112,671
District administration	635,865	18,871
School administration	642,387	542
Business	139,133	11,749
Plant operations and maintenance	1,085,299	-
Student transportation	438,032	5,574
Building improvements	-	-
Community services activities	8,226	165,649
Payment of bonds/debt service	-	-
Payment of lease obligations	50,831	-
Payment of interest	-	-
TOTAL EXPENDITURES	<u>9,446,082</u>	<u>1,993,617</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>663,902</u>	<u>(2,116)</u>
OTHER FINANCING SOURCES (USES)		
Compensation for gain on assets	2,968	-
Operating transfers in	43,184	18,762
Operating transfers out	(18,762)	(16,646)
TOTAL OTHER FINANCING SOURCES (USES)	<u>27,390</u>	<u>2,116</u>
NET CHANGES IN FUND BALANCES	691,292	-
FUND BALANCES, JULY 1, 2013	<u>552,268</u>	<u>-</u>
FUND BALANCES, JUNE 30, 2014	<u>\$ 1,243,560</u>	<u>\$ -</u>

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

Other Governmental Funds	Total Governmental Funds
\$ 221,630	\$ 2,075,421
-	246,465
-	694,189
-	756
-	24,647
-	122,591
410,870	8,087,711
-	1,452,414
-	29,791
<u>632,500</u>	<u>12,733,985</u>
-	6,997,203
-	524,684
-	715,654
-	654,736
-	642,929
-	150,882
-	1,085,299
-	443,606
16,646	16,646
-	173,875
245,000	245,000
-	50,831
<u>106,532</u>	<u>106,532</u>
<u>368,178</u>	<u>11,807,877</u>
<u>264,322</u>	<u>926,108</u>
-	2,968
278,025	339,971
<u>(261,379)</u>	<u>(296,787)</u>
<u>16,646</u>	<u>46,152</u>
280,968	972,260
<u>93,485</u>	<u>645,753</u>
<u>\$ 374,453</u>	<u>\$ 1,618,013</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES
IN FUND BALANCES OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES
Year Ended June 30, 2014

Total Net Change In Fund Balances – per fund financial statements	\$	972,260
Amounts reported for governmental activities in the statement of activities are different because:		
Governmental funds report capital outlays as expenditures. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives as depreciation expense.		
Depreciation	\$ (522,376)	
Capital outlays	<u>30,179</u>	(492,197)
Repayment of bond principal is an expenditure in the governmental funds, but the repayment reduces noncurrent liabilities in the statement of net position and does not result in an expense in the statement of activities.		
		245,000
Payments on lease obligations are an expenditure in the governmental funds, but the payments reduce noncurrent lease obligations in the statement of net position and do not result in an expense in the statement of activities.		
		56,970
Compensated absences (sick leave) are measured by the amounts earned during the year in the statement of activities. In the governmental funds, expenditures for these amounts are measured by the amount of financial resources used (the amount paid). The difference in expenses reported in the statement of activities is a result in the change in accumulated sick leave.		
		(2,557)
The insurance settlement payment was measured by the amounts incurred during the year in the statement of activities. In the governmental funds, expenditures for this payable were measured by the amount of financial resources used (the current payment). The difference in expenses reported in the statement of activities is a result of the noncurrent portion of the payment due on the settlement.		
		<u>(191,729)</u>
Change In Net Position of Governmental Activities	\$	<u>587,747</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE – BUDGET AND ACTUAL
GENERAL FUND
Year Ended June 30, 2014

	Budgeted Amounts		Actual	Variance with Final Budget Favorable or (Unfavorable)
	Original	Final		
REVENUES				
From local sources:				
Taxes				
Property	\$ 1,639,000	\$ 1,639,000	\$ 1,832,775	\$ 193,775
Motor vehicle	230,000	230,000	246,465	16,465
Utilities	590,000	590,000	694,189	104,189
Revenue in lieu of taxes – state and local	22,000	22,000	21,016	(984)
Tuition and fees	2,000	2,000	756	(1,244)
Earnings on investments	17,000	17,000	24,647	7,647
Other local revenues	42,200	42,200	122,591	80,391
Intergovernmental – state	5,155,064	5,155,064	7,137,754	1,982,690
Intergovernmental – direct federal	32,000	32,000	29,791	(2,209)
TOTAL REVENUES	7,729,264	7,729,264	10,109,984	2,380,720
EXPENDITURES				
Instruction	4,170,710	4,170,710	5,384,511	(1,213,801)
Support services:				
Student	361,978	361,978	458,815	(96,837)
Instructional staff	445,170	445,170	602,983	(157,813)
District administration	478,115	478,115	635,865	(157,750)
School administration	521,286	521,286	642,387	(121,101)
Business	100,853	100,853	139,133	(38,280)
Plant operations and maintenance	1,105,890	1,105,890	1,085,299	20,591
Student transportation	446,565	446,565	438,032	8,533
Community services activities	8,173	8,173	8,226	(53)
Payment of lease obligations	50,831	50,831	50,831	-
Contingency	544,135	544,135	-	544,135
TOTAL EXPENDITURES	8,233,706	8,233,706	9,446,082	(1,212,376)
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	(504,442)	(504,442)	663,902	1,168,344
OTHER FINANCING SOURCES (USES)				
Compensation for gain on assets	-	-	2,968	2,968
Operating transfers in	35,000	35,000	43,184	8,184
Operating transfers out	(25,000)	(25,000)	(18,762)	6,238
TOTAL OTHER FINANCING SOURCES (USES)	10,000	10,000	27,390	17,390
NET CHANGE IN FUND BALANCE	(494,442)	(494,442)	691,292	1,185,734
FUND BALANCE, JULY 1, 2013	494,442	494,442	552,268	57,826
FUND BALANCE, JUNE 30, 2014	\$ -	\$ -	\$ 1,243,560	\$ 1,243,560

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCE – BUDGET AND ACTUAL
SPECIAL REVENUE FUND
Year Ended June 30, 2014

	Budgeted Amounts		Actual	Variance with Final Budget Favorable or (Unfavorable)
	Original	Final		
REVENUES				
From local sources:				
Taxes				
Property	\$ -	\$ -	\$ -	\$ -
Motor vehicle	-	-	-	-
Utilities	-	-	-	-
Revenue in lieu of taxes – state and local	-	-	-	-
Tuition and fees	-	-	-	-
Earnings on investments	600	600	-	(600)
Other local revenues	10,000	10,000	-	(10,000)
Intergovernmental – state	168,514	168,514	539,087	370,573
Intergovernmental – indirect federal	<u>2,243,903</u>	<u>2,243,903</u>	<u>1,452,414</u>	<u>(791,489)</u>
TOTAL REVENUES	<u>2,423,017</u>	<u>2,423,017</u>	<u>1,991,501</u>	<u>(431,516)</u>
EXPENDITURES				
Instruction	2,076,646	2,076,646	1,612,692	463,954
Support services:				
Student	3,704	3,704	65,869	(62,165)
Instructional staff	305,561	305,561	112,671	192,890
District administration	-	-	18,871	(18,871)
School administration	-	-	542	(542)
Business	33,106	33,106	11,749	21,357
Plant operations and maintenance	10,000	10,000	-	10,000
Student transportation	-	-	5,574	(5,574)
Community services activities	<u>18,000</u>	<u>18,000</u>	<u>165,649</u>	<u>(147,649)</u>
TOTAL EXPENDITURES	<u>2,447,017</u>	<u>2,447,017</u>	<u>1,993,617</u>	<u>453,400</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>(24,000)</u>	<u>(24,000)</u>	<u>(2,116)</u>	<u>21,884</u>
OTHER FINANCING SOURCES (USES)				
Operating transfers in	39,000	39,000	18,762	(20,238)
Operating transfers out	<u>(15,000)</u>	<u>(15,000)</u>	<u>(16,646)</u>	<u>(1,646)</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>24,000</u>	<u>24,000</u>	<u>2,116</u>	<u>(21,884)</u>
NET CHANGE IN FUND BALANCE	-	-	-	-
FUND BALANCE, JULY 1, 2013	-	-	-	-
FUND BALANCE, JUNE 30, 2014	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF NET POSITION
PROPRIETARY FUND
June 30, 2014

	<u>ASSETS</u>	<u>Food Service</u>
CURRENT ASSETS		
Cash and cash equivalents		\$ 25,482
Accounts receivable:		
Accounts receivable		504
Intergovernmental – federal		16,073
Materials and supplies inventory		<u>14,793</u>
Total current assets		56,852
NONCURRENT ASSETS		
Capital assets, net		<u>63,276</u>
TOTAL ASSETS		<u><u>120,128</u></u>
	<u>LIABILITIES AND NET POSITION</u>	
CURRENT LIABILITIES		
Accounts payable		4,516
Accrued salaries and benefits payable		<u>3,485</u>
TOTAL CURRENT LIABILITIES		<u>8,001</u>
NET POSITION		
Investment in capital assets		63,276
Nonspendable – inventories		14,793
Restricted		
Sick leave payable		17,965
Purchase obligations		400
Unrestricted		<u>15,693</u>
TOTAL NET POSITION		<u><u>\$ 112,127</u></u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET POSITION
PROPRIETARY FUND
Year Ended June 30, 2014

	<u>Food Service</u>
OPERATING REVENUES	
Sales	\$ 120,663
TOTAL OPERATING REVENUES	<u>120,663</u>
OPERATING EXPENSES	
Salaries	326,874
Employee benefits	150,147
Purchased services	10,574
Supplies and materials	536,512
Depreciation	10,771
Operating transfers	43,184
TOTAL OPERATING EXPENSES	<u>1,078,062</u>
OPERATING INCOME (LOSS)	<u>(957,399)</u>
NON-OPERATING REVENUES (EXPENSES)	
Operating grants-federal	863,659
Operating grants-state	74,505
Child nutrition program – donated commodities	53,421
Earnings on investments	368
TOTAL NON-OPERATING REVENUES (EXPENSES)	<u>991,953</u>
CHANGE IN NET POSITION	34,554
NET POSITION, JULY 1, 2013	<u>77,573</u>
NET POSITION, JUNE 30, 2014	<u>\$ 112,127</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF CASH FLOWS
PROPRIETARY FUND
Year Ended June 30, 2014

	<u>Food Service</u>
CASH FLOWS FROM OPERATING ACTIVITIES	
Cash received from sales	\$ 123,076
Cash payments for salaries	(327,638)
Cash payments for employee benefits	(150,147)
Cash payments for purchased services	(10,574)
Cash payments for supplies and materials	(540,065)
Cash payments for other operating expenses	(43,184)
Net cash provided (used) by operating activities	<u>(948,532)</u>
CASH FLOWS FROM INVESTING ACTIVITIES	
Receipt of interest	368
Receipt of grants	1,023,782
Receipt of donated commodities	53,421
Net cash provided (used) by investing activities	<u>1,077,571</u>
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	129,039
CASH AND CASH EQUIVALENTS, JULY 1, 2013	<u>(103,557)</u>
CASH AND CASH EQUIVALENTS, JUNE 30, 2014	<u>\$ 25,482</u>
RECONCILIATION OF OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	
Operating income (loss)	\$ (957,399)
ADJUSTMENTS TO RECONCILE OPERATING INCOME (LOSS) TO NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	
Depreciation	10,771
Changes in assets and liabilities:	
Accounts receivable	2,413
Accounts payable	(3,553)
Accrued salaries and benefits payable	(764)
NET CASH PROVIDED (USED) BY OPERATING ACTIVITIES	<u>\$ (948,532)</u>
SCHEDULE OF NONCASH INVESTING, CAPITAL AND FINANCING ACTIVITIES	
Donated commodities received from federal government	<u>\$ 53,421</u>
On-behalf payments from state government	<u>\$ 66,159</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF NET POSITION
FIDUCIARY FUND
June 30, 2014

	<u>ASSETS</u>	<u>SCHOOL ACTIVITY FUNDS</u>
CURRENT ASSETS		
Cash and cash equivalents		\$ 116,655
TOTAL ASSETS		<u>116,655</u>
	<u>LIABILITIES AND NET POSITION</u>	
CURRENT LIABILITIES		
Due to students		<u>116,655</u>
TOTAL LIABILITIES		<u>116,655</u>
NET POSITION		<u>\$ -</u>

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

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The accounting policies that affect the significant elements of the Middlesboro Independent School District are summarized as follows:

RECLASSIFICATIONS

Certain accounts on the prior-year statement of net position have been reclassified for comparative purposes to reflect the noncurrent portion of accumulated sick leave. Current liabilities increased \$54,250, noncurrent liabilities increased \$162,748 and the restricted net position decreased \$216,998.

REPORTING ENTITY

The Middlesboro Independent Board of Education (Board), a five-member group, is the level of government which has oversight responsibilities over all activities related to public elementary and secondary school education within the jurisdiction of the Middlesboro Independent School District (District). The District receives funding from local, state and federal government sources and must comply with the commitment requirements of these funding source entities. However, the District is not included in any other governmental "reporting entity" as defined by the Governmental Accounting Standards Board (GASB) pronouncement since Board members are elected by the public and have decision making authority, the power to designate management, the responsibility to develop policies which may influence operations and primary accountability for fiscal matters.

The District, for financial purposes, includes all of the funds and account groups relevant to the operation of the Middlesboro Independent School District. The financial statements presented herein do not include funds of groups and organizations, which although associated with the school system, have not originated within the District itself such as certain booster clubs.

The financial statements of the District include those of separately administered organizations that are controlled by or dependent on the District. Control or dependence is determined on the basis of budget adoption, funding and appointment of the respective governing board.

Based on the foregoing criteria, the financial statement of the following organization is included in the accompanying financial statements:

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT FINANCE CORPORATION

The Middlesboro Independent Board of Education resolved to authorize the establishment of the Middlesboro Independent School District Finance Corporation (a non-profit, non-stock, public and charitable corporation organized under the School Board Act and KRS 273 and KRS Section 58.180) as an agency of the District for financing the costs of school building facilities. The Board members of the Middlesboro Independent Board of Education also comprise the corporation's Board of Directors.

BASIS OF PRESENTATION

Government-Wide Financial Statements: The statement of net position and the statement of activities display information about the District as a whole. These statements include the financial activities of the primary government, except for fiduciary funds. The statements distinguish between governmental and business-type activities of the District.

The government-wide financial statements are prepared using the economic resources measurement focus. This is the same approach used in the preparation of proprietary fund financial statements but differs from the manner in which governmental fund financial statements are prepared. Governmental fund financial statements therefore include a reconciliation with brief explanations to better identify the relationship between the government-wide statements and the statements of governmental funds.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

The government-wide statement of activities presents a comparison between direct expenses and program revenues for each segment of the business-type activities of the District and for each function or program of the governmental activities of the District. Direct expenses are those that are specifically associated with a service, program or department and therefore clearly identifiable to a particular function. Program revenues include amounts paid by the recipient of goods or services offered by the program and grants and contributions that are restricted to meeting the operational or capital requirements of a particular program. All taxes and revenues not classified as program revenues are presented as general revenues of the District, with certain limited exceptions. The comparison of direct expenses with program revenues identifies the extent to which each business segment or governmental function is self-financing or draws from the general revenues of the District.

Fund Financial Statements: Fund financial statements report detailed information about the District. Their focus is on major funds rather than reporting funds by type. Each major fund is presented in a separate column, and all nonmajor funds are aggregated into one column. Fiduciary funds are reported by fund type.

The accounting and reporting treatment applied to a fund is determined by its measurement focus. All governmental fund types are accounted for using a flow of current financial resources measurement focus. With this measurement focus, only current assets and current liabilities generally are included on the balance sheet. Operating statements of these funds present increases (i.e., revenues and other financing sources) and decreases (i.e., expenditures and other financing uses) in net current assets.

All proprietary funds are accounted for on a flow of economic resources measurement focus. With this measurement focus, all assets and all liabilities associated with the operations of these funds are included on the balance sheet. Proprietary fund's operating statements present increases (i.e., revenues) and decreases (i.e., expenses) in net total position.

The District has the following funds:

I. Governmental Fund Types

- (A) The General Fund is the main operating fund of the District. It accounts for financial resources used for general types of operations. This is a budgeted fund, and any fund balances are considered as resources available for use. This is a major fund of the District.
- (B) The Special Revenue (Grant) Funds account for proceeds of specific revenue sources (other than expendable trusts or major capital projects) that are legally restricted to disbursements for specified purposes. It includes federal financial programs where unused balances are returned to the grantor at the close of the specified project periods as well as the state grant programs. Project accounting is employed to maintain integrity for the various sources of funds. The separate projects of federally funded grant programs are identified in the Schedule of Expenditures of Federal Awards included in this report on pages 40 through 42. This is a major fund of the District.
- (C) Capital Project Funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities and equipment (other than those financed by the Proprietary Fund):
 - 1. The Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund receives those funds designated by the state as Capital Outlay funds and is restricted primarily for use in financing projects identified in the District's facility plan.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

2. The Facility Support Program of Kentucky (FSPK) accounts for funds generated by the building tax levy required to participate in the School Facilities Construction Commission's construction funding and state matching funds, where applicable. Funds may be used for projects identified in the District's facility plan.
3. The Construction Fund accounts for proceeds from sales of bonds and other revenues to be used for authorized construction.

(D) Debt Service Funds

The Debt Service Funds are used to account for the accumulation of resources for, and the payment of, general long-term debt principal and interest and related costs; and for the payment of interest on general obligation notes payable, as required by Kentucky Law.

II. Proprietary Fund Types (Enterprise Funds)

- (A) The Food Service Fund is used to account for school food service activities, including the National School Lunch Program, which is conducted in cooperation with the U.S. Department of Agriculture (USDA). Amounts have been recorded for in-kind contributions of commodities from the USDA. The Food Service Fund is a major fund.

The District applies all GASB pronouncements to proprietary funds as well as the Financial Accounting Standards Board (FASB) pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

III. Fiduciary Fund Types (Agency Funds)

- (A) The School Activity Funds account for activities of student groups and other types of activities requiring clearing accounts. These funds are accounted for in accordance with the Uniform Program of Accounting for School Activity Funds.

BASIS OF ACCOUNTING

Basis of accounting refers to when revenues and expenditures or expenses are recognized in the accounts and reported in the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. The fund financial statements are prepared using either modified accrual for governmental funds or accrual basis for proprietary and fiduciary funds.

Revenues, Exchange and Nonexchange Transactions: Revenues resulting from exchange transactions, in which each party receives essentially equal value, are recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenues are recognized in the fiscal year when they become both measurable and available. Available means collectible within the current period or soon enough thereafter to be used to pay liabilities of the current fiscal year. The available period of the District is sixty days after year end.

Nonexchange transactions, in which the District receives value without directly giving equal value in return, include property taxes, grants, entitlements and donations. On an accrual basis, revenue from property taxes is recognized in the fiscal year for which the taxes are levied. Revenue from grants, entitlements and donations is recognized in the fiscal year in which all eligibility requirements have been met. Eligibility requirements include timing requirements, which specify the year when the resources are required to be used or the fiscal year when use is first permitted, matching requirements, in which the District must provide local resources to be used for a specified

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

purpose, and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. On the modified accrual basis, revenue from nonexchange transactions must also be available before it can be recognized.

Deferred Revenue: The District reports deferred revenue on its statement of net position and governmental funds balance sheet. In both the government-wide and governmental fund statements, grants that are intended to finance future periods are reported as deferred revenue. In subsequent periods, the liability for deferred revenue is removed from the statement of net position and governmental funds balance sheet and revenue is recognized.

Expenditures/Expenses: On the accrual basis of accounting, expenses are recorded at the time they are incurred. The measurement focus of governmental fund accounting is on the flow of current financial resources. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred except for (1) principal and interest on general long-term debt, which is recorded when due, (2) the costs of accumulated unpaid sick leave, (3) lease obligations, and (4) the insurance settlement payment liability, which are reported as fund liabilities in the period in which they will be liquidated with available financial resources rather than in the period earned by employees.

CASH AND INVESTMENTS

The District maintains a cash and investment pool used by all funds. The cash and investment pool has the same characteristics as demand deposits. Each fund type's portion of this pool is displayed in the financial statements as cash and cash equivalents in that fund. The District utilizes a financial institution to service bonded debt as principal and interest payments come due. The monies are either maintained in a central bank account or used to purchase legal investments.

It is the policy of the District to value investment contracts and money market investments with a maturity of one year or less at the time of purchase at cost or amortized cost. Investment contracts and money market investments that had a remaining maturity of greater than one year at the time of purchase are reported at fair value.

The Kentucky Revised Statutes authorized the District to invest in United States and State of Kentucky bonds, notes and other obligations; bank certificates of deposit; bankers' acceptances; and commercial paper notes rated prime and issued by United States corporations. It is the District's policy to invest in all of the above types of investments. Under existing Kentucky statutes, all investment earnings accrue to the general and food service funds except certain trust funds and those funds individually authorized by Board resolution.

PREPAID ASSETS/EXPENDITURES

Payments made that will benefit periods beyond June 30, 2014 are recorded as prepaid items using the consumption method. A current asset for the prepaid amount is recorded at the time of the purchase and an expenditure/expense is reported in the year in which services are consumed.

INVENTORY

On government-wide financial statements, inventories are presented at cost or using the first in, first out (FIFO) method and are expensed when used.

On fund financial statements, inventories are valued at cost while inventories of proprietary funds are stated at lower of cost or market. For all funds, cost is determined using the FIFO method, and are determined by physical count. Inventory in governmental funds consists of expendable supplies held for consumption. The cost is recorded as an expenditure at the time of purchase. Reported inventories in these funds are equally offset by a fund balance reserve, which indicates they do not represent available spendable resources. Inventories of proprietary funds consist of donated and purchased food.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

CAPITAL ASSETS AND DEPRECIATION

General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets are reported in the government-wide statement of net position but are not reported in the fund financial statements. Capital assets utilized by proprietary funds are reported on both statement types.

All capital assets are capitalized at cost (or estimated historical cost) and updated for additions and retirements during the year. Donated fixed assets are recorded at their fair market values as of the date received. The District follows the policy of not capitalizing assets with a cost of less than \$1,000 with the exception of assets acquired with Technology Funds, which has no threshold, and a useful life of less than 1 year. The District does not possess any infrastructure.

All reported capital assets, with the exception of land, are depreciated. Improvements are depreciated over the remaining useful lives of the related capital assets. Depreciation is computed using the straight-line method over the following useful lives for both governmental fund capital assets and proprietary fund capital assets:

<u>Description</u>	<u>Useful Life</u>
Land improvements	20 years
Buildings and improvements	25-50 years
Technology equipment	5 years
Vehicles	5-10 years
Food service equipment	10-12 years
General equipment	7 years

INTERFUND ACTIVITY

Transfers between governmental and business-type activities on the government-wide statements are reported in the same manner as general revenues. Sales of goods and services between funds are reported as revenues in the seller funds and as expenditures/expenses in the purchaser funds. Flows of cash or goods from one fund to another without a requirement for repayment are reported as interfund transfers. Interfund transfers are reported as other financing sources/uses in governmental funds and as operating expenses in proprietary funds.

On fund financial statements, short-term interfund loans are classified as interfund receivables/payables. These amounts are eliminated in the statement of net position, except for amounts due between governmental and business-type activities, which are presented as internal balances.

ACCUMULATED UNPAID SICK LEAVE BENEFITS

Upon retirement from the school system, an employee will receive from the Board, an amount equal to 30% of the value of accumulated sick leave. Sick leave benefits are accrued as a liability using the termination payment method. An accrual for earned sick leave is made to the extent that it is probable that the benefits will result in termination payments. The liability is based on the Board's past experience of making termination payments. The entire compensated absence liability is reported on the district-wide financial statements.

For Governmental Fund financial statements, the current portion of unpaid accumulated sick leave is the amount expected to be paid using expendable available resources. These amounts are recorded in the account restricted for sick leave payable in the General Fund. The non-current portion of the liability is not reported in the Governmental Fund financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

ACCRUED LIABILITIES AND LONG-TERM DEBT

All accrued liabilities and long-term debt are reported in the government-wide financial statements as well as the proprietary fund financial statements.

For governmental fund financial statements, the accrued liabilities are generally reported as a governmental fund liability if due for payment as of the balance sheet date regardless of whether they will be liquidated with current financial resources. However, claims and judgments and compensated absences paid from governmental funds are reported as a liability in the fund financial statements only for the portion expected to be financed from expendable available financial resources. Long-term debt paid from governmental funds is not recognized as a liability in the fund financial statements until due.

RESTRICTED RESOURCES

The District applies restricted resources when an expense is incurred for purposes for which both restricted and unrestricted assets are available.

NET POSITION

Net position in government-wide and proprietary fund financial statements are classified as investment in capital assets, net of related debt; restricted; and unrestricted. Restricted net assets represent constraints on resources that are either a) externally imposed by creditors, grantors, contributors, or laws or regulations of other governments or b) imposed by law through state statute.

In the governmental fund financial statements, fund balance is composed of five classifications designed to disclose the hierarchy of constraint placed on how fund balance can be spent.

The governmental fund types classify fund balances as follows:

Nonspendable Fund Balance – This classification includes amounts that cannot be spent because they are either (a) not in spendable form or (b) legally or contractually required to be maintained intact.

- *Inventories* – Portion of fund balance that is not an available resource because it represents the year-end balance of ending inventories, which are not spendable resources.

Restricted Fund Balance – This classification includes revenue sources that are restricted to specific purposes externally imposed by creditors, grantors or imposed by law.

Committed Fund Balance – Portion of fund balance that can only be used for specific purposes imposed by a majority vote of the Middlesboro Independent School District's Board members. Any changes or removal of specific purposes also requires majority action by the Board.

Assigned Fund Balance – Portion of fund balance that has been budgeted by the Board.

- *Purchase Obligations* – Portion of fund balance that is appropriated in the subsequent year's budget that is not already classified in restricted or committed.
- *Site Base* – Portion of fund balance that has been budgeted for future site base expenditures.

Unassigned Fund Balance – Portion of fund balance that has not been restricted, committed or assigned for a specific purpose.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 1 – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (CONTINUED)

OPERATING REVENUES AND EXPENSES

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the District, those revenues are primarily charges for meals provided by the various schools.

CONTRIBUTIONS OF CAPITAL

Contributions of capital in proprietary fund financial statements arise from outside contributions of fixed assets, or from grants or outside contributions of resources restricted to capital acquisition and construction.

ESTIMATES

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires the District's management to make estimates and assumptions that affect reported amounts of assets, liabilities, fund balances, and disclosure of contingent assets and liabilities at the date of the basic financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

BUDGETARY PROCESS

Budgetary Basis of Accounting: The District's budgetary process accounts for certain transactions on a basis other than U.S. Generally Accepted Accounting Principles (GAAP). The major differences between the budgetary basis and the GAAP basis are:

Revenues are recorded when received in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

Expenditures are recorded when paid in cash (budgetary) as opposed to when susceptible to accrual (GAAP).

Once the budget is approved, it can be amended. Amendments are presented to the Board at their regular meetings. Per Board policy, only amendments that aggregate greater than \$50,000 require Board approval. Such amendments are made before the fact, are reflected in the official minutes of the Board, and are not after fiscal year end as dictated by law.

Each budget is prepared and controlled by the budget coordinator at the revenue and expenditure function/object level. All unencumbered budget appropriations lapse at year-end.

NOTE 2 – CASH AND CASH EQUIVALENTS

The District's funds are required to be deposited and invested under the terms of a depository contract pursuant to the School Depository Act. The depository bank deposits for safekeeping and trust with the District's third party agent approved pledged securities in an amount sufficient to protect District funds on a day-to-day basis during the period of the contract. The pledge of approved securities is waived only to the extent of the dollar amount of Federal Deposit Insurance Corporation insurance.

Under the depository contract, the District, at its own discretion, invests funds in time deposits and certificates of deposit provided by the depository bank at interest rates approximating United States Treasury Bill rates.

At June 30, 2014, the carrying amount of the District's deposits was \$1,419,309 and the bank balance was \$2,430,699. The entire bank balance throughout the year was covered by federal depository insurance or by collateral held by the District's agent in the District's name.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 2 – CASH AND CASH EQUIVALENTS (CONTINUED)

The deposits were deemed collateralized under Kentucky Law during the year and the District maintains copies of all safekeeping receipts. The following is disclosed:

- a. Name of banks utilized during fiscal year: Community Trust Bank and First State Bank.
- b. Amount of bond and/or security pledged as of the date of the highest combined balance on deposit was \$3,120,546.
- c. Largest cash, savings and time deposit combined account balance amounted to \$3,196,993 and occurred during the month of June.
- d. Total amount of FDIC coverage at the time of largest combined balance was \$250,000 per bank.

The cash deposits held at financial institutions can be categorized according to three levels of risk.

These three levels of risk are as follows:

- | | |
|------------|---|
| Category 1 | Deposits, which are insured or collateralized with securities, held by the District or by its agent in the District's name. |
| Category 2 | Deposits, which are collateralized with securities held by the pledging financial institution's trust department or agent in the District's name. |
| Category 3 | Deposits, which are not collateralized or insured. |

Based on these three levels of risk, all of the District's cash deposits are classified as Category 1 and 2.

NOTE 3 – PROPERTY TAXES

The District's ad valorem property tax is levied each October 1 on the assessed value listed as of the prior January 1 for all real and business personal property located in the District. The assessed value of the certified roll, upon which the levy for the 2014 fiscal year was based, was \$406,883,519. The tax rates assessed for the year ended June 30, 2014 to finance general fund operations were \$.508 per \$100 valuation for real estate, \$.508 for tangible property and \$.56 for motor vehicles. The District committed \$.05 of the levy to the FSPK Fund. Taxes are due on December 31, and become delinquent by February 1 following the October 1 levy date. Current tax collections for the year ended June 30, 2014 were ninety-seven percent of the tax levies. Delinquent taxes are allocated to the general fund. The District records taxes receivable only for the amounts collected during the next sixty days from its fiscal year end.

The District levies a utility gross receipts license tax in the amount of 3% of the gross receipts derived from the furnishings, within the county, of telephonic and telegraphic communications services, cablevision services, electric power, water, and natural, artificial and mixed gas.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 3 – PROPERTY TAXES (CONTINUED)

At June 30, 2014, the components of taxes receivable were as follows:

Motor vehicle tax	\$	14,176
PSC property tax		11,424
Delinquent property tax		13,850
Penalties and interest on taxes		10,718
Utilities tax		<u>106,502</u>
	\$	<u>156,670</u>

NOTE 4 – RECEIVABLES

Receivables at June 30, 2014 consisted of taxes, accounts (rent and student fees), interest and intergovernmental grants and entitlements. All receivables are considered collectible in full due to the ability to foreclose for the nonpayment of taxes, the stable condition of State programs and the current year guarantee of federal funds.

NOTE 5 – CAPITAL ASSETS

A summary of capital assets activity during the fiscal year follows:

	<u>Balance</u> <u>July 1, 2013</u>	<u>Additions</u>	<u>Deletions</u>	<u>Balance</u> <u>June 30, 2014</u>
GOVERNMENTAL ACTIVITIES				
Land	\$ 177,607	\$ -	\$ -	\$ 177,607
Land improvements	655,236	-	-	655,236
Buildings and improvements	12,437,023	16,462	-	12,453,485
Technology equipment	1,685,010	12,217	-	1,697,227
Vehicles	1,286,659	-	65,432	1,221,227
General equipment	<u>702,658</u>	<u>1,500</u>	-	<u>704,158</u>
Totals at cost	<u>16,944,193</u>	<u>30,179</u>	<u>65,432</u>	<u>16,908,940</u>
Less accumulated depreciation:				
Land improvements	558,134	24,171	-	582,305
Buildings and improvements	7,185,081	319,763	-	7,504,844
Technology equipment	1,410,558	86,860	-	1,497,418
Vehicles	1,014,799	59,715	65,432	1,009,082
General equipment	<u>593,404</u>	<u>31,867</u>	-	<u>625,271</u>
Total accumulated depreciation	<u>10,761,976</u>	<u>522,376</u>	<u>65,432</u>	<u>11,218,920</u>
Governmental activities capital assets, net	<u>\$ 6,182,217</u>	<u>\$ (492,197)</u>	<u>\$ -</u>	<u>\$ 5,690,020</u>
BUSINESS-TYPE ACTIVITIES				
Food service equipment	\$ 245,560	\$ -	\$ -	\$ 245,560
Technology equipment	24,613	-	-	24,613
Vehicles	<u>8,650</u>	-	-	<u>8,650</u>
Totals at cost	<u>278,823</u>	<u>-</u>	<u>-</u>	<u>278,823</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 5 – CAPITAL ASSETS (CONTINUED)

	Balance <u>July 1, 2013</u>	<u>Additions</u>	<u>Deletions</u>	Balance <u>June 30, 2014</u>
Less accumulated depreciation:				
Food service equipment	173,061	10,282	-	183,343
Technology equipment	23,065	489	-	23,554
Vehicles	8,650	-	-	8,650
Total accumulated depreciation	<u>204,776</u>	<u>10,771</u>	<u>-</u>	<u>215,547</u>
Business-type activities capital assets, net	<u>\$ 74,047</u>	<u>\$ 10,771</u>	<u>\$ -</u>	<u>\$ 63,276</u>

Depreciation expense was allocated to governmental functions as follows:

Instruction	\$ 433,965
Support services:	
Student	14,127
Instructional staff	4,975
District administration	3,606
School administration	4,886
Plant operations and maintenance	8,570
Student transportation	49,840
Community services activities	2,407
Total governmental activities	<u>\$ 522,376</u>

NOTE 6 – BONDED DEBT AND LEASE OBLIGATIONS

The original amount of each bond issue, the issue date, and interest rates are summarized as follows:

<u>Issue</u>	<u>Original</u>	<u>Interest</u>
2004	<u>Amount</u>	<u>Rates</u>
2004	\$ 475,000	4.75%
2005	765,000	3.25% to 3.6%
2006	1,965,000	3.9% to 4.4%

The District, through the General Fund (including utility taxes and the Support Education Excellence in Kentucky (SEEK) Capital Outlay Fund), is obligated to make lease payments in amounts sufficient to satisfy debt service requirements on bonds issued by the Middlesboro Independent School District and the Middlesboro Independent School District Finance Corporation to construct school facilities. The District has an option to purchase the property under lease at any time by retiring the bonds then outstanding.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 6 – BONDED DEBT AND LEASE OBLIGATIONS (CONTINUED)

The following is a summary of the District's long-term debt transactions for the year ended June 30, 2014:

	Amount of Debt Outstanding <u>July 1, 2013</u>	Additions of <u>New Debt</u>	<u>Repayments</u>	Debt Outstanding <u>June 30, 2014</u>	Amount Expected to be Paid Within <u>One Year</u>
Governmental activities:					
General obligation bonds	<u>\$ 2,670,000</u>	<u>\$ -</u>	<u>\$ 245,000</u>	<u>\$ 2,425,000</u>	<u>\$ 255,000</u>
Capital leases	<u>\$ 285,845</u>	<u>\$ -</u>	<u>\$ 56,970</u>	<u>\$ 228,875</u>	<u>\$ 53,845</u>

In 1990, the District entered into "participation agreements" with the Kentucky School Facility Construction Commission. The Commission was created by the Kentucky Legislature for the purpose of assisting local school districts in meeting school construction needs. The table below sets forth the amount to be paid by the District and the Commission for each year until maturity of all bond issues.

The bonds may be called prior to maturity and redemption premiums are specified in each issue. Assuming no bonds are called prior to scheduled maturity, the minimum obligations of the District, including amounts to be paid by the Commission, at June 30, 2014 for debt service (principal and interest) are as follows:

Year	Middlesboro Independent School District		Kentucky School Facility Construction Commission		Total
	Principal	Interest	Principal	Interest	
2014-15	\$ 192,157	\$ 70,035	\$ 62,843	\$ 27,309	\$ 352,344
2015-16	199,529	62,775	65,471	24,681	352,456
2016-17	204,913	55,136	60,087	22,063	342,199
2017-18	93,859	49,284	46,141	19,760	209,044
2018-19	101,854	45,210	48,146	17,756	212,966
2019-20	104,621	40,874	50,379	15,522	211,396
2020-21	112,287	36,291	52,713	13,186	214,477
2021-22	119,951	31,355	55,049	10,853	217,208
2022-23	122,378	26,175	57,622	8,277	214,452
2023-24	124,684	20,864	60,316	5,584	211,448
2024-25	132,107	15,276	27,893	2,764	178,040
2025-26	137,493	9,345	27,507	1,545	175,890
2026-27	143,646	3,160	21,354	470	168,630
	<u>\$ 1,789,479</u>	<u>\$ 465,780</u>	<u>\$ 635,521</u>	<u>\$ 169,770</u>	<u>\$ 3,060,550</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 6 – BONDED DEBT AND LEASE OBLIGATIONS (CONTINUED)

The District has purchased five buses through KISTA. The original amount of each lease obligation, lease date, and purpose are summarized as follows:

<u>Lease</u>	<u>Original Amount</u>	<u>Purpose</u>
Series 2006 (1)	\$ 80,233	KISTA – Bus purchase
Series 2006 (2)	80,396	KISTA – Bus purchase
Series 2008	72,693	KISTA – Bus purchase
Series 2009	77,265	KISTA – Bus purchase
Series 2013	104,420	KISTA – Bus purchase

Principal payments in the amount of \$43,712 were paid during the fiscal year.

The minimum obligations at June 30, 2014 for these lease obligations are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014-15	\$ 43,485	\$ 5,808	\$ 49,293
2015-16	41,403	4,447	45,850
2016-17	33,282	3,097	36,379
2017-18	24,451	2,040	26,491
2018-19	17,910	1,307	19,217
2019-20	10,742	809	11,551
2020-21	11,001	594	11,595
2021-22	9,260	374	9,634
2022-23	9,446	189	9,635
	<u>\$ 200,980</u>	<u>\$ 18,665</u>	<u>\$ 219,645</u>

The District entered into a lease agreement with Kubota Leasing in the amount of \$18,395 for the purchase of a tractor/loader/backhoe and a 60" mower. Interest is being charged at 8.641%. Principal payments in the amount of \$9,123 were paid during the fiscal year.

The District entered into two different lease agreements with GMAC/ALLY for vehicles. One lease was for \$15,098 for the purchase of a 2011 Chevrolet Impala. Interest on this lease is 7.34%. Principal payments in the amount of \$2,210 were paid during the fiscal year. The second lease was for the purchase of a 2007 Chevrolet Uplander Van. Interest on this lease is 8.94%. Principal payments in the amount of \$1,925 were paid during the fiscal year.

The minimum obligations at June 30, 2014 for these lease obligations are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2014-15	\$ 10,360	\$ 1,800	\$ 12,160
2015-16	5,059	1,241	6,300
2016-17	5,486	814	6,300
2017-18	5,950	350	6,300
2018-19	1,040	10	1,050
	<u>\$ 27,895</u>	<u>\$ 4,215</u>	<u>\$ 32,110</u>

The assets under capital lease are being depreciated. This depreciation is included in total depreciation expense and is allocated to governmental functions.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 7 – ACCUMULATED SICK LEAVE LIABILITY

Changes in the District's accumulated sick leave liability during the fiscal year 2014 were as follows:

	Balance June 30, 2013	Additions	Reductions	Balance June 30, 2014	Amount Expected to be Paid Within One Year
Governmental activities					
Accumulated sick leave	\$ 216,998	\$ 2,557	\$ -	\$ 219,555	\$ 53,610
Business-type activities					
Accumulated sick leave	\$ 22,993	\$ -	\$ 5,028	\$ 17,965	\$ -

NOTE 8 – RISK MANAGEMENT

The District is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; injuries to employees; and natural disasters. To obtain insurance for workers' compensation, errors and omissions and general liability coverage, the District obtained coverage through commercial insurance carriers. The District paid an annual premium to each company for coverage.

The District purchased unemployment insurance through the Kentucky School Boards Insurance Trust Unemployment Compensation Fund, however, risk has not been transferred to such fund. In addition, the District continues to carry commercial insurance for all other risks of loss. Settled claims resulting from these risks have not exceeded commercial insurance coverage in any of the past three fiscal years.

The District participated in the Kentucky School Boards Insurance Trust (KSBIT), a pooled self-insurance fund providing property and casualty insurance coverage and workers compensation insurance for public and private schools in the state. In 2013, KSBIT was ordered into rehabilitation by the state for underfunded claim liabilities, and an assessment plan was finalized on July 17, 2014 by the Franklin, Kentucky Circuit Court (Case No. 13-CI-01282) for schools that had participated in the funds since 2007. The District's final assessment was received and totaled \$275,083. One payment of \$83,354 is due September, 2014 and is reflected in accounts payable on the statement of net position and the balance sheet. The remaining two payments of \$191,729 are reflected as the noncurrent portion of insurance settlement on the statement of net position. One payment of \$95,865 is due September, 2015 and the balance is due September, 2016.

The District is exposed to various forms of loss of assets associated with the risks of fire, personal liability, theft, vehicular accidents, errors and omissions, fiduciary responsibility, etc. Each of these risk areas are covered through the purchase of commercial insurance. The District has purchased certain policies, which are retrospectively rated, which includes workers' compensation insurance.

Under COBRA, employers are mandated to notify terminated employees of available continuing insurance coverage. Failure to comply with this requirement may put the school district at risk for a substantial loss (contingency). There were no instances of noncompliance noted.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 9 – RETIREMENT PLANS

Pension Plan

The Middlesboro Independent School System contributes to the Kentucky Teachers' Retirement System ("KTRS"), a cost-sharing, multiple employer defined benefit pension plan. KTRS administers retirement and disability annuities, and death and survivor benefits to employees and beneficiaries of employees of the public school systems and other public educational agencies in Kentucky. KTRS requires that members of KTRS occupy a position requiring either a four (4) year college degree or certification by KY Department of Education (KDE). Job classifications that permit experience to substitute for either of these requirements do not participate in KTRS.

KTRS was created by the 1938 General Assembly and is governed by Chapter 161 Section 220 through Chapter 161 Section 990 of the Kentucky Revised Statutes (KRS). KTRS issues a publicly available financial report that includes financial statements and required supplementary information for the defined benefit pension plan. That report can be obtained by writing to the Kentucky Teachers' Retirement System, 479 Versailles Road, Frankfort, KY 40601 or from the KTRS web site at <http://www.ktrs.ky.gov/>.

Contribution rates are established by KRS. Members are required to contribute 11.355% of their salaries to KTRS. The Commonwealth of Kentucky is required to contribute 14.105% of members' salaries. The federal program for any salaries paid by that program pays the matching contributions. The Board is required to match 1.0% of salaries for all employees paid by the General fund.

The Middlesboro Independent School System's total payroll for the year was \$7,370,453. The payroll for employees covered under KTRS was \$5,008,187. For the year ended June 30, 2014, the Commonwealth contributed \$654,935 to KTRS for the benefit of participating employees. The School Districts' contribution to KTRS for the year ending June 30, 2014 was \$195,391, which represents those employees covered by federal programs.

Substantially all other employees (classified personnel) are covered under the County Employees Retirement System ("CERS"), a cost sharing, multiple-employer, public employers retirement system. Funding for the Plan is provided through payroll withholdings of 6% for employees hired after September 1, 2008 and 5% for employees hired before this date and a Board contribution of 18.89% of the employee's total compensation subject to contribution. The contribution requirement for CERS for the year ended June 30, 2014 was \$332,591, which consisted of \$261,539 from the Board and \$71,052 from the employees.

The "pension benefit obligation" is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increases and step-rate benefits, estimated to be payable in the future as a result of employee service to date. The measure, which is the actuarial present value of credited projected benefits, is intended to help users assess the pensions' funding status on a going-concern basis, assess progress made in accumulating sufficient assets to pay benefits when due, and make comparisons among the plans and employers.

CERS does not make separate measurements of assets and pension benefit obligation for individual employers. As the District is only one of several employers participating in the Plan, it is not practicable to determine the District's portion of the unfunded past service cost of the vested benefits of the District's portion of the Plan assets.

Medical Insurance Plan

In addition to the pension benefits described above, Kentucky Revised Statute 181.875 requires KTRS to provide post-retirement healthcare benefits to eligible members and dependents. The KTRS Medical Insurance benefit is a cost-sharing multiple employer defined benefit plan. Changes made to the medical plan may be made by the KTRS Board of Trustees, the Kentucky Department of Employee Insurance and the General Assembly.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 9 – RETIREMENT PLANS (CONTINUED)

To be eligible for medical benefits, the member must have retired either for service or disability. The KTRS Medical Insurance Fund offers coverage to members under the age of 65 through the Kentucky Employees Health Plan administered by the Kentucky Department of Employee Insurance. Once retired members and eligible spouses attain age 65 and are Medicare eligible, coverage is obtained through the KTRS Medicare Eligible Health Plan.

The post-retirement healthcare provided by KTRS is financed on a pay-as-you-go basis. In order to fund the post-retirement healthcare benefit, one and five tenths percent (1.5%) of the gross annual payroll of all active members is contributed. One-half (1/2) of this amount is derived from member contributions and one-half (1/2) from state appropriation. Also, the premiums collected from retirees, as described in the plan description, and investment interest help meet the medical expenses of the plan.

NOTE 10 – CONTINGENCIES

The District receives funding from federal, state and local government agencies and private contributions. These funds are to be used for designated purposes only. For government agency grants, if the grantor's review indicates that the funds have not been used for the intended purpose, the grantors may request a refund of monies advanced or refuse to reimburse the District for its disbursements. The amount of such future refunds and unreimbursed disbursements, if any, is not expected to be significant. Continuation of the District's grant programs is predicated upon the grantors' satisfaction that the funds provided are being spent as intended and the grantors' intent to continue their programs.

NOTE 11 – TRANSFER OF FUNDS

The following transfers were made during the year:

<u>Type</u>	<u>From Fund</u>	<u>To Fund</u>	<u>Purpose</u>	<u>Amount</u>
Operating	Capital Outlay	Debt Service	Debt service requirement	\$ 117,264
Operating	General	Special Revenue	Matching, Phase II Technology	18,762
Operating	Building/FSPK	Debt Service	Debt service requirement	144,115
Operating	Food Service	General	Indirect costs	43,184
Operating	Special Revenue	Construction	Press box repairs – Bradner Stadium	16,646

NOTE 12 – INTERFUND RECEIVABLES AND PAYABLES

There were no interfund receivables or payables at June 30, 2014.

NOTE 13 – DEFICIT OPERATING/FUND BALANCES

The District had no current year operating deficits.

NOTE 14 – ON-BEHALF PAYMENTS

As amounts are paid by various State agencies on-behalf of the District, the amounts are recognized as revenues and expenditures by the District. On the statement of revenues, expenditures and changes in fund balance, the on-behalf payments are included with State revenue, and are included in the functional expense classifications. On the statement of activities, the on-behalf payments are included in the functional expense classifications, and are included with program operating grants and contributions for the respective functions. A summary of on-behalf payments during 2014 is as follows:

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

NOTES TO THE BASIC FINANCIAL STATEMENTS
June 30, 2014

NOTE 14 – ON-BEHALF PAYMENTS (CONTINUED)

Payments made by the State for fringe benefits of District employees and technology expenses - included in the following functional expense classification:

Instruction	\$ 1,209,440
Support services:	
Student	105,751
Instructional staff	116,927
District administration	33,531
School administration	125,125
Business	20,545
Plant operations and maintenance	65,926
Student transportation	35,629
Community services activities	473
Network support	23,576
Food service	66,159
Total	<u>\$ 1,803,082</u>

Payments made by the KSFCC for its participation in the board's bonds – included in debt service expenditures \$ 90,153

NOTE 15 – SUBSEQUENT EVENTS

We evaluated events and transactions that occurred after the balance sheet date as potential subsequent events. We performed this evaluation through September 30, 2014, the date on which we issued our financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

COMBINING BALANCE SHEET
NONMAJOR GOVERNMENTAL FUNDS
June 30, 2014

	Seek Capital Outlay Fund	FSPK Fund	Construction Fund	Debt Service Funds	Total Nonmajor Governmental Funds
ASSETS AND RESOURCES					
Cash and cash equivalents	\$ -	\$ 374,443	\$ 10	\$ -	\$ 374,453
TOTAL ASSETS AND RESOURCES	\$ -	\$ 374,443	\$ 10	\$ -	\$ 374,453
LIABILITIES AND FUND BALANCES					
Restricted					
Future construction projects	\$ -	\$ 280,968	\$ 10	\$ -	\$ 280,978
Debt service	-	93,475	-	-	93,475
TOTAL LIABILITIES AND FUND BALANCES	\$ -	\$ 374,443	\$ 10	\$ -	\$ 374,453

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

COMBINING STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES
NONMAJOR GOVERNMENTAL FUNDS
Year Ended June 30, 2014

	<u>Seek Capital Outlay Fund</u>	<u>FSPK Fund</u>	<u>Construction Fund</u>	<u>Debt Service Funds</u>	<u>Total Nonmajor Governmental Funds</u>
REVENUES					
From local sources:					
Taxes					
Property	\$ -	\$ 221,630	\$ -	\$ -	\$ 221,630
Intergovernmental – state	<u>117,264</u>	<u>203,453</u>	<u>-</u>	<u>90,153</u>	<u>410,870</u>
TOTAL REVENUES	<u>117,264</u>	<u>425,083</u>	<u>-</u>	<u>90,153</u>	<u>632,500</u>
EXPENDITURES					
Payment of bonds	-	-	-	245,000	245,000
Payment of interest	-	-	-	106,532	106,532
Building improvements	-	-	<u>16,646</u>	-	<u>16,646</u>
TOTAL EXPENDITURES	<u>-</u>	<u>-</u>	<u>16,646</u>	<u>351,532</u>	<u>368,178</u>
EXCESS (DEFICIENCY) OF REVENUES OVER EXPENDITURES	<u>117,264</u>	<u>425,083</u>	<u>(16,646)</u>	<u>(261,379)</u>	<u>264,322</u>
OTHER FINANCING SOURCES (USES)					
Operating transfers in	-	-	16,646	261,379	278,025
Operating transfers out	<u>(117,264)</u>	<u>(144,115)</u>	<u>-</u>	<u>-</u>	<u>(261,379)</u>
TOTAL OTHER FINANCING SOURCES (USES)	<u>(117,264)</u>	<u>(144,115)</u>	<u>16,646</u>	<u>261,379</u>	<u>16,646</u>
NET CHANGES IN FUND BALANCES	-	280,968	-	-	280,968
FUND BALANCES, JULY 1, 2013	<u>-</u>	<u>93,475</u>	<u>10</u>	<u>-</u>	<u>93,485</u>
FUND BALANCES, JUNE 30, 2014	<u>\$ -</u>	<u>\$ 374,443</u>	<u>\$ 10</u>	<u>\$ -</u>	<u>\$ 374,453</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF RECEIPTS, DISBURSEMENTS AND FUND BALANCES – ACTIVITY FUNDS
MIDDLESBORO HIGH SCHOOL
Year Ended June 30, 2014

ACCOUNTS:	Cash Balances July 1, 2013	Receipts	Disbursements	Interfund Transfers
Activity Allotment	\$ 909	\$ -	\$ -	\$ -
Athletics	20,720	82,747	80,915	477
Attendance	2	-	-	-
Audio Visual Club	100	-	-	-
Band	4	204	-	-
Beta Club	641	412	498	-
Choir	111	4,064	3,268	-
Class of 2014	1,641	19,840	11,946	(9,530)
DECA	3	-	-	-
Drama	58	-	-	-
FBLA	58	257	192	-
FCCLA (FHA)	8	-	-	-
FEA	198	-	-	-
General	10,765	59,711	67,036	11,280
Jacket Patch	29	-	-	-
JROTC	291	1,320	1,446	-
Journalism	1,290	14,595	14,780	(147)
Library	80	50	52	-
NFL	5	-	-	-
Parking	568	5,128	3,089	(2,227)
Prom	1,385	9,795	10,751	147
Student Council	626	14,041	13,778	-
Teachers	595	5,369	4,918	-
Technology	752	18	309	-
Textbooks	795	-	-	-
VICA	19	-	-	-
Year Book	5	-	-	-
Totals	<u>\$ 41,658</u>	<u>\$ 217,551</u>	<u>\$ 212,978</u>	<u>\$ -</u>

Cash Balances June 30, 2014	Accounts Receivable June 30, 2014	Accounts Payable June 30, 2014	Fund Balances June 30, 2014
\$ 909	\$ -	\$ -	\$ 909
23,029	-	-	23,029
2	-	-	2
100	-	-	100
208	-	-	208
555	-	-	555
907	-	-	907
5	-	-	5
3	-	-	3
58	-	-	58
123	-	-	123
8	-	-	8
198	-	-	198
14,720	-	-	14,720
29	-	-	29
165	-	-	165
958	-	-	958
78	-	-	78
5	-	-	5
380	-	-	380
576	-	-	576
889	-	-	889
1,046	-	-	1,046
461	-	-	461
795	-	-	795
19	-	-	19
5	-	-	5
<u>\$ 46,231</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 46,231</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

STATEMENT OF RECEIPTS, DISBURSEMENTS AND FUND BALANCES - ACTIVITY FUNDS
Year Ended June 30, 2014

	<u>Cash Balances</u> <u>July 1, 2013</u>	<u>Receipts</u>	<u>Disbursements</u>	<u>Interfund</u> <u>Transfers</u>
MIDDLESBORO MIDDLE SCHOOL All funds	<u>\$ 9,763</u>	<u>\$ 33,303</u>	<u>\$ 27,213</u>	<u>\$ 12,357</u>
MIDDLESBORO PRIMARY SCHOOL All funds	<u>\$ 24,872</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ (24,872)</u>
MIDDLESBORO INTERMEDIATE SCHOOL All funds	<u>\$ 23,006</u>	<u>\$ 1,708</u>	<u>\$ -</u>	<u>\$ (24,714)</u>
MIDDLESBORO ELEMENTARY SCHOOL All funds	<u>\$ -</u>	<u>\$ 91,986</u>	<u>\$ 87,001</u>	<u>\$ 37,229</u>

<u>Cash Balances</u> <u>June 30, 2014</u>	<u>Accounts</u> <u>Receivable</u> <u>June 30,</u> <u>2014</u>	<u>Accounts</u> <u>Payable</u> <u>June 30,</u> <u>2014</u>	<u>Fund</u> <u>Balances</u> <u>June 30,</u> <u>2014</u>
<u>\$ 28,210</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 28,210</u>
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ -</u>
<u>\$ 42,214</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 42,214</u>

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS
Year Ended June 30, 2014

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Program or Award</u>	<u>Federal Disbursements</u>
<u>U.S. Department of Education</u>				
Passed through State Department of Education:				
SPECIAL EDUCATION CLUSTER (IDEA)				
Special Education – Grants to States (IDEA, Part B)	84.027A	3810002-13	\$ 312,071	\$ 281,404*
Special Education – Grants to States (IDEA, Part B)	84.027	3810002-12	328,493	12,514*
Special Education – Preschool Grants (IDEA, Preschool)	84.173	3800002-13	19,908	18,742*
Special Education – Preschool Grants (IDEA, Preschool)	84.173	3800002-12	20,115	<u>1,765*</u>
Total Special Education Cluster (IDEA)				<u>314,425</u>
TITLE I, PART A CLUSTER				
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100002-13	942,682	776,028*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100002-12	952,335	109,066*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010A	3100202-12	8,243	2,948*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100102-13	6,445	1,871*
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010	3100002-11	961,771	<u>2,248*</u>
Total Title I, Part A Cluster				<u>892,161</u>
SCHOOL IMPROVEMENT GRANTS CLUSTER				
School Improvement Grants	84.377	3100302-09	250,000	<u>21,629</u>
Total School Improvement Grants Cluster				<u>21,629</u>

* Denotes major program

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)
Year Ended June 30, 2014

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Program or Award</u>	<u>Federal Disbursements</u>
<u>U.S. Department of Education</u>				
Vocational Education – Basic Grants to States	84.048	3710002-13	26,900	6,781
Vocational Education – Basic Grants to States	84.048	4621332-13	24,733	540
Improving Teacher Quality State Grants	84.367A	3230002-13	117,422	115,569
Improving Teacher Quality State Grants	84.367A	3230002-12	124,141	6,215
Improving Teacher Quality State Grants	84.367	3230002-11	125,425	1,986
Twenty-First Century Community Learning Centers	84.287	3400002-11	60,000	2,371
Twenty-First Century Community Learning Centers	84.287	3400002-12	5,000	2,372
Twenty-First Century Community Learning Centers	84.287	3400002-10	17,000	1,828
Rural Education	84.358	3140002-12	25,753	13,415
Rural Education	84.358	3140002-11	31,306	5,098
Race To The Top	84.413A	4521	38,784	<u>212</u>
Total U.S. Department of Education				<u>\$ 1,384,602</u>
<u>U.S. Department of Agriculture</u>				
Passed through State Department of Education:				
CHILD NUTRITION CLUSTER				
National School Breakfast Program	10.553	7760005-13	\$204,984	\$ 204,984*
	10.553	7760005-12	60,279	60,279*
National School Lunch Program	10.555	7750002-13	432,771	432,771*
	10.555	7750002-12	113,629	113,629*
Summer Food Service Program for Children	10.559	7740023-13	16,073	16,073*
Total Child Nutrition Cluster				<u>827,736</u>
EMERGENCY FOOD ASSISTANCE CLUSTER				
Emergency Food Assistance Program – Non-cash	10.569	4002827	53,421	53,421
Total Emergency Food Assistance Cluster				<u>53,421</u>
Fresh Fruit and Vegetable Program	10.582	7720012-13	29,226	29,226
	10.582	7720012-12	6,697	6,697
Total U.S. Department of Agriculture				<u>\$ 917,080</u>

* Denotes major program

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS (CONTINUED)
Year Ended June 30, 2014

<u>Federal Grantor/Pass-Through Grantor/Program Title</u>	<u>Federal CFDA Number</u>	<u>Pass-Through Grantor's Number</u>	<u>Program or Award</u>	<u>Federal Disbursements</u>
<u>U.S. Department of Defense</u>				
Junior Reserve Officers' Training Corps	12.000	5044	\$ 66,729	\$ <u>66,729</u>
Total U.S. Department of Defense				\$ <u>66,729</u>
<u>Appalachian Regional Commission</u>				
Appalachian Research, Technical Assistance and Demonstration Project	23.011	6883	\$ 4,124	\$ <u>1,084</u>
Total Appalachian Regional Commission				\$ <u>1,084</u>
Total Expenditures of Federal Awards				\$ <u>2,369,495</u>

NOTE A – BASIS OF PRESENTATION

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Middlesboro Independent School District and is presented on the accrual basis of accounting. The information in this schedule is presented in accordance with the requirements of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations. Therefore, some amounts presented in this schedule may differ from amounts presented in, or used in the preparation of, the basic financial statements.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SCHEDULE OF FINDINGS AND QUESTIONED COSTS
June 30, 2014

SUMMARY OF AUDIT RESULTS

1. We have issued an unmodified opinion on the basic financial statements of the Middlesboro Independent School District.
2. No material weakness(es) were identified in our audit of the financial statements.
3. No significant deficiencies were identified in our audit of the financial statements.
4. No material noncompliance was identified in our audit of the financial statements.
5. No material weakness(es) were identified in our audit of internal control over major programs.
6. No significant deficiencies were noted in our audit of internal control over major programs.
7. We have issued an unmodified opinion on compliance for major programs.
8. The audit did not disclose any audit findings, which we are required to report under Section 510(a) of OMB Circular A-133.
9. The programs tested as major programs included:

	<u>CFDA</u>
TITLE I, PART A CLUSTER	
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010
Title I Grants to Local Educational Agencies (Title I, Part A of the ESEA)	84.010A
CHILD NUTRITION CLUSTER	
National School Lunch Program	10.555
Summer Food Service Program for Children	10.559
National School Breakfast Program	10.553
SPECIAL EDUCATION CLUSTER (IDEA)	
Special Education – Preschool Grants (IDEA, Preschool)	84.173
Special Education – Grants to States (IDEA, Part B)	84.027
Special Education – Grants to States (IDEA, Part B)	84.027A

10. The threshold for distinguishing Types A and B programs was \$300,000.
11. Middlesboro Independent School District was determined to be a low risk auditee.

FINDINGS RELATED TO THE FINANCIAL STATEMENTS

None

FINDINGS AND QUESTIONED COSTS FOR FEDERAL AWARDS

None

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS
June 30, 2014

NONE

Marr, Miller & Myers, PSC

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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

September 30, 2014

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

We have audited, 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; the provisions of *Office of Management and Budget Circular No. A-133, Audits of States, Local Governments, and Non-Profit Organizations; Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the Independent Auditor's Contract – State Audit Requirements, Appendix III to the Independent Auditor's Contract – Audit Extension Request and Appendix IV to the Independent Auditor's Contract – Instructions for Submission of the Audit Report*, the financial statements of the governmental activities, the business-type activities, each major fund, and the aggregate remaining fund information of the Middlesboro Independent School District, as of and for the year ended June 30, 2014, and the related notes to the financial statements, which collectively comprise the District's basic financial statements, and have issued our report thereon dated September 30, 2014.

Internal Control Over Financial Reporting

In planning and performing our audit of the financial statements, we considered the District's internal control over financial reporting (internal control) to determine the audit procedures that are appropriate in the circumstances for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the District's internal control. Accordingly, we do not express an opinion on the effectiveness of the District's internal control.

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

Our consideration of internal control was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control that might be material weaknesses or significant deficiencies. Given these limitations, during our audit we did not identify any deficiencies in internal control that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

Marr, Miller & Myers, PSC

Compliance and Other Matters

As part of obtaining reasonable assurance about whether the District's financial statements are free from material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*. In addition, the results of our tests disclosed no instances of material noncompliance of specific state statutes or regulations identified in Appendix II of the Independent Auditor's Contract – State Audit Requirements.

Purpose of this Report

The purpose of this report is solely to describe the scope of our testing of internal control and compliance and the results of that testing, and not to provide an opinion on the effectiveness of the District's internal control or on compliance. This report is an integral part of an audit performed in accordance with *Government Auditing Standards* in considering the District's internal control and compliance. Accordingly, this communication is not suitable for any other purpose.

Marr, Miller & Myers, PSC

Certified Public Accountants

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INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE FOR EACH MAJOR PROGRAM AND ON INTERNAL CONTROL OVER COMPLIANCE REQUIRED BY OMB CIRCULAR A-133

September 30, 2014

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

Report on Compliance for Each Major Federal Program

We have audited Middlesboro Independent School District's compliance with the types of compliance requirements described in the OMB Circular A-133 Compliance Supplement that could have a direct and material effect on each of the District's major federal programs for the year ended June 30, 2014. The District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs.

Management's Responsibility

Management is responsible for compliance with the requirements of laws, regulations, contracts, and grants applicable to its federal programs.

Auditor's Responsibility

Our responsibility is to express an opinion on compliance for each of the District's major federal programs based on our audit of the types of compliance requirements referred to above. 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; the provisions of OMB Circular A-133, Audits of States, Local Governments, and Non-Profit Organizations; Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the Independent Auditor's Contract – State Audit Requirements, Appendix III to the Independent Auditor's Contract – Audit Extension Request and Appendix IV to the Independent Auditor's Contract – Instructions for Submission of the Audit Report. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances.

We believe that our audit provides a reasonable basis for our opinion on compliance for each major federal program. However, our audit does not provide a legal determination of the District's compliance.

Marr, Miller & Myers, PSC

Opinion on Each Major Federal Program

In our opinion, the District, complied, in all material respects, with the types of compliance requirements referred to above that could have a direct and material effect on each of its major federal programs for the year ended June 30, 2014.

Report on Internal Control Over Compliance

Management of the District is responsible for establishing and maintaining effective internal control over compliance with the types of compliance requirements referred to above. In planning and performing our audit of compliance, we considered the District's internal control over compliance with the types of requirements that could have a direct and material effect on each major federal program to determine the auditing procedures that are appropriate in the circumstances for the purpose of expressing an opinion on compliance for each major federal program and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 the District's internal control over compliance.

A deficiency in internal control over compliance exists when the design or operation of a control over compliance does not allow management or employees, in the normal course of performing their assigned functions, to prevent, or detect and correct, noncompliance with a type of compliance requirement of a federal program on a timely basis. *A material weakness in internal control over compliance* is a deficiency, or combination of deficiencies, in internal control over compliance, such that there is a reasonable possibility that material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis. *A significant deficiency in internal control over compliance* is a deficiency, or a combination of deficiencies, in internal control over compliance with a type of compliance requirement of a federal program that is less severe than a material weakness in internal control over compliance, yet important enough to merit attention by those charged with governance.

Our consideration of internal control over compliance was for the limited purpose described in the first paragraph of this section and was not designed to identify all deficiencies in internal control over compliance that might be material weaknesses or significant deficiencies. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses. However, material weaknesses may exist that have not been identified.

The purpose of this report on internal control over compliance is solely to describe the scope of our testing of internal control over compliance and the results of that testing based on the requirements of OMB Circular A-133. Accordingly, this report is not suitable for any other purpose.

Marr, Miller & Myers, PSC

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September 30, 2014

Members of the Board of Education
Middlesboro Independent School District
Middlesboro, Kentucky

In planning and performing our audit of the financial statements of the Middlesboro Independent School District for the year ended June 30, 2014, we considered the District's internal control structure to determine our auditing procedures that are appropriate for the purpose of expressing an opinion on the effectiveness of the District's internal control structure.

However, during our audit we became aware of some items that go beyond internal control related matters that are being communicated for the benefit of management to improve operational and administrative efficiencies. Our comments and recommendations, as well as the action to be taken by the District, accompanies this letter. We will review the status of these comments during our next audit engagement. We have already discussed these comments and suggestions with various District personnel, and we will be pleased to discuss them in further detail at your convenience, to perform any additional study of the matters, or to assist you in implementing the recommendations. This letter does not affect our report dated September 30, 2014 on the financial statements of the Middlesboro Independent School District.

Marr, Miller & Myers, PSC

Certified Public Accountants

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT LETTER POINTS
June 30, 2014

1. CENTRAL OFFICE STAFF

- During the current year audit, we became aware of several central office staff employees that are intending on retiring within the next five-year period. The continuation of the District's financial affairs will be impacted, and we believe the District should start preparing for the anticipated retirements in hopes of a smooth transitional period. The experience levels of the retirees will be a challenge for the District to replace, and new trainees will be required to familiarize themselves with the accounting processes of the District.

2. SCHOOL ACTIVITY FUNDS

GENERAL COMMENTS

- The Kentucky Department of Education introduced the new Accounting Procedures for Kentucky School Activity Funds (the "Redbook"), effective July 1, 2013, which included significant revisions to previously issued guidance. District compliance with the guidance provided seeks to insure school activity funds are expended as intended. The system of safeguarding and accounting for school activity funds is dependent on the soundness and effectiveness of the District's policies and guidelines. Through student participation in school activities, there may be fees collected and fundraisers held for their group to participate in selected activities, producing a need to track the related disbursements and receipts. Implementation of the new "Redbook" requirements during this past fiscal year has been a challenge for the District, and as auditors, we will continue to assist with the learning process and to identify how to improve practices in order to fully comply in the future.
- During our audit, we inquired of various people involved with the District as to their knowledge of, or suspicions of, fraudulent activity. Of those questioned during the audit, no one noted any material fraudulent activity that they were aware of regarding the school activity funds. During our audit procedures at the individual schools, we continued to have various findings. Thus, we recommend the District review the procedures and policies in place at the school activity fund level, and assist the school principals and bookkeepers with improving those procedures if necessary.

MANAGEMENT'S RESPONSE

- Management will investigate options that will assist principals and bookkeepers in instituting stronger and more effective controls.

MIDDLESBORO ELEMENTARY SCHOOL

- It was noted that purchase orders are not always prepared and approved prior to items being purchased. The Redbook requires purchase orders to be prepared and approved by the sponsor and principal before the payment is obligated. We recommend that purchase orders be prepared and approved prior to purchase for all disbursements.

MANAGEMENT'S RESPONSE

- District policies also require prior approval for purchases. In addition to training, a new monitoring process will be considered.

MIDDLESBORO INDEPENDENT SCHOOL DISTRICT
Middlesboro, Kentucky

MANAGEMENT LETTER POINTS
June 30, 2014

2. SCHOOL ACTIVITY FUNDS (CONTINUED)

- We noted several instances of sales tax being paid on purchases. Schools are exempt from the payment of sales tax in Kentucky, with an exception on sales tax paid on meals and hotel expenses for employees and students during travel for school activity fund purposes. Employees purchasing items for the school cannot be reimbursed for sales tax. A copy of the Tax Exemption Certificate should be provided to any vendor from whom the school makes purchases.

MANAGEMENT'S RESPONSE

- The principal and staff will be provided with the current Redbook requirements regarding expenditures, and the Tax Exemption Certificate will be utilized more effectively.
- We noted instances in which the multiple receipt forms were not filled out in their entirety and, in some cases, not completed at all. We recommend training be provided as it relates to these forms and that when required, this form is completed.

MANAGEMENT'S RESPONSE

- The principal and staff will be provided the guidance, and necessary training, on activity fund accounting standards. Staff receiving funds will be held accountable for the proper completion of the forms.
- The District's policy allows schools to accept donations, whether cash or property. The schools are required to provide an annual listing of donations to District officials at year-end, using the donation acceptance form (F-SA-18). A donation acknowledgement may also be provided to donors, upon request.

MANAGEMENT'S RESPONSE

- The principal and staff will be provided the guidance and necessary training on activity fund accounting standards.

MIDDLESBORO MIDDLE SCHOOL

- We noted that purchase orders are not always prepared and approved prior to items being purchased. The Redbook requires purchase orders to be prepared and approved by the sponsor and principal before the payment is obligated. We recommend that purchase orders be prepared and approved prior to purchase for all disbursements.

MANAGEMENT'S RESPONSE

- District policies also require prior approval for purchases. In addition to training, a new monitoring process will be considered.

MIDDLESBORO HIGH SCHOOL

- There were no specific findings.