

**MERCER COUNTY SCHOOL DISTRICT  
AUDIT REPORT  
YEAR ENDED JUNE 30, 2012**

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October 29, 2012

**INDEPENDENT AUDITOR'S REPORT**

Members of the Board of Education  
Mercer County School District  
Harrodsburg, Kentucky

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Mercer County School District as of and for the year ended June 30, 2012, which collectively comprise the District's basic financial statements as listed in the table of contents. These financial statements are the responsibility of Mercer County School District's management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States and 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 Auditors 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 of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of the Mercer County School District as of June 30, 2012, and the respective changes in financial position, and, where applicable, cash flows thereof and the respective budgetary comparison for the General Fund and the Special Revenue Fund for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards*, we have also issued a report dated October 29, 2012, on our consideration of Mercer County School District's internal control over financial reporting and on 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 reporting or on compliance. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be considered in assessing the results of our audit.

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis and budgetary comparison information on Pages 3 through 9 and 16 and 17 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 auditing standards generally accepted in the United States of America, 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.

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the Mercer County School District's financial statements taken as a whole. The combining and individual nonmajor fund financial statements, and the statement of receipts, disbursements and fund balance – High School Activity Fund are presented for the purpose of additional analysis and is not a required part of the financial statements. The accompanying 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, statement of receipts, disbursements and fund balance – High School Activity Fund and the schedule 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 financial statements. The information has been subjected to the auditing procedures applied in the audit of the financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the financial statements or to the financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the information is fairly stated in all material respects in relation to the financial statements taken as a whole.

Sincerely,

*White and Company, P.S.C.*

Certified Public Accountants

**MERCER COUNTY SCHOOL DISTRICT**  
**Management's Discussion and Analysis (MD&A)**  
**Year Ended June 30, 2012**

As management of the Mercer County School District (District), we offer readers of the District's financial statements this narrative overview and analysis of the financial activities of the District for the fiscal year ended June 30, 2012. We encourage readers to consider the information presented here in conjunction with additional information found within the body of the financial statements.

**FINANCIAL HIGHLIGHTS**

- The beginning General Fund's fund balance was \$1.6 million. The ending fund balance was \$2.5 million. General fund revenues showed an increase of \$963 thousand and expenditures showed a decrease of \$798 thousand as compared with the prior year. The General Fund transferred \$56 thousand to the Special Revenue Fund for the technology grant match and \$151 thousand to the Debt Service Fund for debt service payments.
- The District had \$30.5 million in revenue and \$30.4 million in expenses.
- The District, through routine debt service, reduced bond debt through the Debt Service Fund. Total debt service payments for fiscal year 2012 were \$5.1 million.
- The District's total net assets increased \$85,700 to \$19,280,509. Current assets increased \$875,619, non-current assets decreased \$2,162,910 and total liabilities decreased \$1,372,991.

## 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) district-wide financial statements, 2) fund financial statements, and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

**District-wide financial statements** - The district-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 assets presents information on all of the District's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets 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 assets changed during the most recent fiscal year. All changes in net assets 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.

The district-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, operation and maintenance of plant, student transportation and operation of non-instructional services. Fixed assets and related debt are also supported by taxes and intergovernmental revenues.

The district-wide financial statements can be found on pages 10 - 11 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 funds and fiduciary funds. Fiduciary funds are trust funds established by benefactors to aid in student education, welfare and teacher support. The only proprietary funds are our adult education 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 12 - 21 of this report.

**Notes to the financial statements.** The notes provide additional information that is essential to a full understanding of the data provided in the district-wide and fund financial statements. The notes to the financial statements can be found on pages 22 - 37 of this report.

## DISTRICT-WIDE FINANCIAL ANALYSIS

Net assets may serve over time as a useful indicator of a government's financial position. In the case of the District, assets exceeded liabilities by \$19,280,509 as of June 30, 2012.

The largest portion of the District's net assets reflects its investment in capital assets (e.g., land and improvements, buildings and improvements, vehicles, furniture and equipment), 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 Assets for the period ending June 30, 2012 and June 30, 2011

A comparison of June 30, 2012 and June 30, 2011 government wide net assets is as follows:

	Governmental		Business - Type		Total	
	Activities		Activities		Primary Government	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Current and Other Assets	\$ 4,161,899	\$ 3,252,835	\$ 309,351	\$ 342,796	\$ 4,471,250	\$ 3,595,631
Capital Assets	<u>51,661,821</u>	<u>53,818,658</u>	<u>134,534</u>	<u>140,607</u>	<u>51,796,355</u>	<u>53,959,265</u>
<b>Total Assets</b>	<u>55,823,720</u>	<u>57,071,493</u>	<u>443,885</u>	<u>483,403</u>	<u>56,267,605</u>	<u>57,554,896</u>
Current Liabilities	2,941,761	2,816,060	-	19,030	2,941,761	2,835,090
Non-Current Liabilities	<u>34,045,335</u>	<u>35,524,997</u>	<u>-</u>	<u>-</u>	<u>34,045,335</u>	<u>35,524,997</u>
<b>Total Liabilities</b>	<u>36,987,096</u>	<u>38,341,057</u>	<u>-</u>	<u>19,030</u>	<u>36,987,096</u>	<u>38,360,087</u>
<b>Net Assets</b>						
Investment in capital assets (net of related debt)	16,896,028	17,466,473	134,534	140,607	17,030,562	17,607,080
Restricted	152,660	152,282	309,351	323,766	462,011	476,048
Unrestricted	<u>1,787,936</u>	<u>1,111,681</u>	<u>-</u>	<u>-</u>	<u>1,787,936</u>	<u>1,111,681</u>
<b>Total Net Assets</b>	<u>\$ 18,836,624</u>	<u>\$ 18,730,436</u>	<u>\$ 443,885</u>	<u>\$ 464,373</u>	<u>\$ 19,280,509</u>	<u>\$ 19,194,809</u>

The District's total net assets increased \$85,700. Current assets increased \$875,619, non-current assets decreased \$2,162,910 and total liabilities decreased \$1,372,991.

The following table presents a comparison of revenues, expenses and changes in net assets for the fiscal years ended June 30, 2012 and June 30, 2011.

	Governmental		Business - Type		Total	
	Activities		Activities		Primary Government	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
<b>REVENUES</b>						
Program revenues						
Charges for services	\$ 11,709	\$ 238	\$ 642,975	\$ 645,453	\$ 654,684	\$ 645,691
Operating grants and contributions	2,870,915	4,618,537	990,282	919,138	3,861,197	5,537,675
Capital grants	1,002,148	1,068,717			1,002,148	1,068,717
General revenues						
Property taxes	6,588,001	6,371,147			6,588,001	6,371,147
Motor vehicle taxes	607,163	595,272			607,163	595,272
Utility Taxes	1,367,450	1,257,489			1,367,450	1,257,489
Other taxes	80,857	35,298			80,857	35,298
Investment earnings	66,050	68,737	6,593	5,842	72,643	74,579
State and formula grants	16,226,381	15,665,425			16,226,381	15,665,425
Miscellaneous	88,151	116,740		1,798	88,151	118,538
<b>Total revenues</b>	<u>28,908,825</u>	<u>29,797,600</u>	<u>1,639,850</u>	<u>1,572,231</u>	<u>30,548,675</u>	<u>31,369,831</u>
<b>EXPENSES</b>						
Program Activities						
Instructional	17,510,216	18,346,173			17,510,216	18,346,173
Student support	1,000,295	1,037,267			1,000,295	1,037,267
Instructional staff Support	923,062	1,454,190			923,062	1,454,190
District administrative support	886,958	1,048,798			886,958	1,048,798
School administrative support	1,528,567	1,505,751			1,528,567	1,505,751
Business support	471,005	494,776			471,005	494,776
Plant operations and maintenance	2,274,885	2,421,865			2,274,885	2,421,865
Student transportation	2,127,301	2,178,132			2,127,301	2,178,132
Community service activities	240,800	260,852			240,800	260,852
Other	56,520	71,817			56,520	71,817
Interest costs	1,783,028	1,608,031			1,783,028	1,608,031
Business-type Activities						
Food service			1,660,338	1,637,831	1,660,338	1,637,831
<b>Total expenses</b>	<u>28,802,637</u>	<u>30,427,652</u>	<u>1,660,338</u>	<u>1,637,831</u>	<u>30,462,975</u>	<u>32,065,483</u>
<b>Increase in net assets</b>	<u>\$ 106,188</u>	<u>\$ ( 630,052)</u>	<u>\$ (20,488)</u>	<u>\$ (65,600)</u>	<u>\$ 85,700</u>	<u>\$ (695,652)</u>

On-behalf amounts are included in the above figures. On-behalf payments are payments the state makes on behalf of employees to the various agencies for health and life insurance, benefits, administration fees, technology and debt service. The total on-behalf payments for 2012 and 2011 were \$4,678,810 and \$4,620,031 respectively.

**Governmental Activities**

For the governmental program expenses, instructional expenses comprise 61% of total expenses, support services equate to 32%, and interest and other expenses make up the remaining 7% of the total.

The cost of program services and the charges for services and grants offsetting those services are shown on the Statement of Activities. The Statement of activities identifies the net cost of services supported by tax revenue and unrestricted intergovernmental revenues (State entitlements).

	Governmental Activities Total		Governmental Activities Net	
	Cost of Services		Cost of Services	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Instructional	\$ 17,510,216	\$ 18,346,173	15,211,171	14,862,895
Support Services	9,268,593	10,212,596	8,925,973	9,336,451
Other	240,800	260,852	(159)	1,500
Interest Costs	<u>1,783,028</u>	<u>1,608,031</u>	<u>1,783,028</u>	<u>1,608,031</u>
Total Expenses	<u>\$ 28,802,637</u>	<u>\$ 30,427,652</u>	<u>\$ 25,920,013</u>	<u>\$ 25,808,877</u>

**Business-Type Activities**

The business type activities consists of the food service program. This program had total revenues of \$1,639,850 and expenses of \$1,660,338 for fiscal year 2012. These revenues were made up of \$642,975 charges for services \$990,282 federal and state operating grants and \$6,593 earnings on investments. These business-type activities receive no support from tax revenues, and, as such, the District will continue to monitor these activities and make the necessary adjustments to the operations of these activities.

**The School District's Funds**

The information relative to the School District's Funds starts on page 12. These funds use the modified accrual basis of accounting to account for each fund's revenues and expenses. The combined revenue for all governmental funds for 2012 was \$28,880,262 and expenditures were \$29,788,447. The most significant net change in fund balance was the General Fund with an increase of \$886,686 which is primarily due to decrease in spending, increase in tax revenues along with an increase in the intergovernmental state revenue.

## **General Fund Budgetary Highlights**

The District's budget is based on accounting for certain transactions on the cash basis for receipts and expenditures and encumbrances and is prepared according to Kentucky law. The Kentucky Department of Education requires a zero-based budget with any remaining fund balance to be shown as a contingency expense in the budgeting process.

The most significant budgeted fund is the General Fund. The general fund had budgeted revenues of \$17,843,230 with actual results being \$22,853,835. Budgeted expenditures were \$19,343,230 compared to actual expenditures of \$21,967,149. The most significant cause of the variance between budget and actual was the state on-behalf payments in the amount of \$4,343,785 which are not budgeted.

## **Future Budgetary Implications**

In Kentucky, the public schools fiscal year is July 1 – June 30; other programs, i.e. some federal programs operate on a different fiscal calendar, but are reflected in the District overall budget. By law, the budget must have a minimum 2% contingency. The District adopted a budget for 2011-2012 with a 2% contingency. The District has adopted a budget for 2012-2013 with a 2% contingency.

The Board's obligation for contribution to the Kentucky Retirement System for classified employees increased for FY 2012 from 16.93% to 18.96%. The Kentucky Teachers Retirement mandated an increase contribution from .25% to .50% on all employees and increased the federal grants matching from 13.355% to 14.105%.

The SEEK base funding has decreased from \$3,903 in FY 2011-2012 to \$3,833 per pupil in FY 2012-2013. The reduction of these funds and the decline in enrollment has put a financial strain on the General Fund and other funding sources to continue existing programs. The Kentucky Department of Education has notified the school districts there will be additional funding cuts for the FY 2012 -2013 school year which will put additional strain on the General Fund. In addition, ARRA funding from the federal government has come to an end, and, as such, the General Fund will be closely monitored to support District staffing. The Local Planning Committee is in the process of downsizing the District's buildings from six to five beginning in 2013-14 in order to cover rising costs.

## **CAPITAL ASSET AND DEBT ADMINISTRATION**

### **Capital Assets**

At the end of the 2012 fiscal year, the District had invested \$51,796,357 in a broad range of capital assets, including equipment, buses, buildings, and land net of accumulated depreciation. This amount represents a net decrease of \$2,162,910. Depreciation expense for the year was \$2,339,773 and capital additions were \$177,501.

The table on the following page shows capital assets net of depreciation for the governmental activities, business-type activities and total primary government for fiscal years ended June 30, 2012 and 2011.

	Governmental Activities (Net of Depreciation)		Business - Type Activities (Net of Depreciation)		Total Primary Government (Net of Depreciation)	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Land	\$ 1,622,246	\$ 1,622,246	\$ -	\$ -	\$ 1,622,246	\$ 1,622,246
Construction In Progress	188,549	318,896	-	-	188,549	318,896
Buildings and Improvements	46,751,162	48,132,150	-	-	46,751,162	48,132,150
Technology	1,018,805	1,377,173	3,017	3,697	1,021,822	1,380,870
Vehicles	1,059,211	1,293,699	-	-	1,059,211	1,293,699
General Equipment	1,021,848	1,074,494	131,517	136,910	1,153,365	1,211,404
<b>Total</b>	<b>\$ 51,661,821</b>	<b>\$ 53,818,658</b>	<b>\$134,534</b>	<b>\$ 140,607</b>	<b>\$ 51,796,355</b>	<b>\$ 53,959,265</b>

The table below shows the changes in capital assets for fiscal years ended June 30, 2012 and 2011.

	Governmental Activities		Business - Type Activities		Total Primary Government	
	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>	<u>2012</u>	<u>2011</u>
Beginning Balance	\$ 53,818,658	\$ 52,301,662	\$ 140,607	\$ 154,223	\$ 53,959,265	\$ 52,455,885
Additions	165,621	3,775,428	11,879	4,196	177,500	3,779,624
Retirements	(636)	(6,776)	-	-	(636)	(6,776)
Depreciation	(2,321,822)	(2,251,656)	(17,952)	(17,812)	(2,339,774)	(2,269,468)
Ending Balance	<u>\$ 51,661,821</u>	<u>\$ 53,818,658</u>	<u>\$134,534</u>	<u>\$ 140,607</u>	<u>\$ 51,796,355</u>	<u>\$ 53,959,265</u>

### Long-Term Debt

At year-end the District had \$34,393,747 in bonds outstanding and \$372,046 in capital lease obligations. Bonded debt principal paid for the year ended June 30, 2012 was \$3,377,816 and capital lease obligation principal paid was \$93,576. A total of \$1,800,702 is due within one year.

### Contacting the District's Financial Management

This financial report is designed to provide our citizens, taxpayers and other interested readers with a general overview of the District's finances and to demonstrate the District's accountability for the money it receives. If you have questions about this report or need additional financial information contact the District's Superintendent or Finance Director.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF NET ASSETS  
JUNE 30, 2012

	<u>GOVERNMENTAL ACTIVITIES</u>	<u>BUSINESS-TYPE ACTIVITIES</u>	<u>TOTAL</u>
<b>ASSETS:</b>			
Cash & Cash Equivalents - Note C	3,043,239	277,980	3,321,219
Accounts Receivable:			
Taxes - Current	242,070		242,070
Taxes - Delinquent	10,192		10,192
Accounts	14,995		14,995
Intergovernmental - State	17,994		17,994
Intergovernmental - Federal	121,314		121,314
Bond Issue Costs	712,095		712,095
Inventories for Consumption		31,371	31,371
<b>Total Current Assets</b>	<b>4,161,899</b>	<b>309,351</b>	<b>4,471,250</b>
<b>Noncurrent Assets - Note F</b>			
Land	1,622,246		1,622,246
Construction In Progress	188,549		188,549
Buildings & Improvements	64,383,098		64,383,098
Furniture & Equipment	10,305,959	708,980	11,014,939
Less: Accumulated Depreciation	(24,838,031)	(574,446)	(25,412,477)
<b>Total Noncurrent Assets</b>	<b>51,661,821</b>	<b>134,534</b>	<b>51,796,355</b>
<b>TOTAL ASSETS</b>	<b>55,823,720</b>	<b>443,885</b>	<b>56,267,605</b>
<b>LIABILITIES:</b>			
<b>Current Liabilities:</b>			
Accounts Payable	66,825		66,825
Accrued Salaries & Sick Leave - Note A	406,250		406,250
Deferred Revenues	345,648		345,648
Bond Obligations - Note D	1,707,840		1,707,840
Capital Lease Obligation - Note E	92,862		92,862
Accrued Interest Payable	322,336		322,336
<b>Total Current Liabilities</b>	<b>2,941,761</b>	<b>0</b>	<b>2,941,761</b>
<b>Noncurrent Liabilities:</b>			
Bond Obligations - Note D	32,685,907		32,685,907
Capital Lease Obligation - Note E	279,184		279,184
Accrued Sick Leave - Note A	1,080,244		1,080,244
<b>Total Noncurrent Liabilities</b>	<b>34,045,335</b>		<b>34,045,335</b>
<b>TOTAL LIABILITIES</b>	<b>36,987,096</b>	<b>0</b>	<b>36,987,096</b>
<b>NET ASSETS:</b>			
Invested in Net Assets, Net of Related Debt	16,896,028	134,534	17,030,562
Restricted for:			
Capital Projects	132,727		132,727
Debt Service	1,814		1,814
Other Purposes	18,119	309,351	327,470
Unrestricted	1,787,936		1,787,936
<b>TOTAL NET ASSETS</b>	<b>18,836,624</b>	<b>443,885</b>	<b>19,280,509</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>55,823,720</b>	<b>443,885</b>	<b>56,267,605</b>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2012

FUNCTION/PROGRAMS	EXPENSES	PROGRAM REVENUES			NET(EXPENSE) REVENUE AND CHANGES IN NET ASSETS		
		CHARGES FOR SERVICES	OPERATING GRANTS AND CONTRIBUTIONS	CAPITAL GRANTS AND CONTRIBUTIONS	GOVERNMENTAL ACTIVITIES	BUSINESS-TYPE ACTIVITIES	TOTAL
<b>GOVERNMENTAL ACTIVITIES:</b>							
Instructional	17,510,216	11,709	2,287,336		(15,211,171)		(15,211,171)
Support Services:							
Student Support Services	1,000,295		16,946		(983,349)		(983,349)
Staff Support Services	923,062		264,064		(658,998)		(658,998)
District Administration	886,958				(886,958)		(886,958)
School Administration	1,528,567				(1,528,567)		(1,528,567)
Business Support Services	471,005		2,080		(468,925)		(468,925)
Plant Operation & Maintenance	2,274,885		57,508		(2,217,377)		(2,217,377)
Student Transportation	2,127,301		2,022		(2,125,279)		(2,125,279)
Food Service Operations	56,520				(56,520)		(56,520)
Community Service Operations	240,800		240,959		159		159
Facilities Acquisition & Construction				1,002,148	1,002,148		1,002,148
Interest on Long-Term Debt - Note P	1,783,028				(1,783,028)		(1,783,028)
<b>TOTAL GOVERNMENTAL ACTIVITIES</b>	<b>28,802,637</b>	<b>11,709</b>	<b>2,870,915</b>	<b>1,002,148</b>	<b>(24,917,865)</b>		<b>(24,917,865)</b>
<b>BUSINESS-TYPE ACTIVITIES:</b>							
Food Service	1,660,338	642,975	990,282			(27,081)	(27,081)
<b>TOTAL BUSINESS-TYPE ACTIVITIES</b>	<b>1,660,338</b>	<b>642,975</b>	<b>990,282</b>	<b>0</b>	<b>0</b>	<b>(27,081)</b>	<b>(27,081)</b>
<b>TOTAL SCHOOL DISTRICT</b>	<b>30,462,975</b>	<b>654,684</b>	<b>3,861,197</b>	<b>1,002,148</b>	<b>(24,917,865)</b>	<b>(27,081)</b>	<b>(24,944,946)</b>
<b>GENERAL REVENUES:</b>							
Taxes					8,643,471		8,643,471
State Aid - Formula Grants					16,226,381		16,226,381
Investment Earnings					66,050	6,593	72,643
Miscellaneous					59,586		59,586
<b>SPECIAL ITEMS:</b>							
Gain(Loss) Sale of Assets					4,952		4,952
Loss Compensation					23,613		23,613
<b>TOTAL GENERAL &amp; SPECIAL</b>					<b>25,024,053</b>	<b>6,593</b>	<b>25,030,646</b>
<b>CHANGE IN NET ASSETS</b>					<b>106,188</b>	<b>(20,488)</b>	<b>85,700</b>
<b>NET ASSETS - BEGINNING</b>					<b>18,730,436</b>	<b>464,373</b>	<b>19,194,809</b>
<b>NET ASSETS - ENDING</b>					<b>18,836,624</b>	<b>443,885</b>	<b>19,280,509</b>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
BALANCE SHEET  
GOVERNMENTAL FUNDS  
JUNE 30, 2012

	GENERAL FUND	SPECIAL REVENUE	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
<b>ASSETS:</b>					
Cash & Cash Equivalents	2,696,467	206,340	7,705	132,727	3,043,239
Accounts Receivable:					
Taxes - Current	242,070				242,070
Taxes - Delinquent	10,192				10,192
Accounts	14,995				14,995
Intergovernmental - State		17,994			17,994
Intergovernmental - Federal		121,314			121,314
<b>TOTAL ASSETS</b>	<u>2,963,724</u>	<u>345,648</u>	<u>7,705</u>	<u>132,727</u>	<u>3,449,804</u>
<b>LIABILITIES AND FUND BALANCE:</b>					
Liabilities:					
Accounts Payable	66,825				66,825
Accrued Salaries & Sick Leave	406,250				406,250
Deferred Revenues		345,648			345,648
<b>Total Liabilities</b>	<u>473,075</u>	<u>345,648</u>	<u>0</u>	<u>0</u>	<u>818,723</u>
Fund Balance:					
Restricted for:					
Capital Projects				132,727	132,727
Debt Service			7,705		7,705
Committed For:					
Accrued Sick Leave	1,080,244				1,080,244
Site Based Carryforward	18,119				18,119
Unassigned	1,392,286				1,392,286
<b>Total Fund Balance</b>	<u>2,490,649</u>	<u>0</u>	<u>7,705</u>	<u>132,727</u>	<u>2,631,081</u>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<u>2,963,724</u>	<u>345,648</u>	<u>7,705</u>	<u>132,727</u>	<u>3,449,804</u>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
RECONCILIATION OF THE BALANCE SHEET - GOVERNMENTAL FUNDS  
TO THE STATEMENT OF NET ASSETS  
FOR THE YEAR ENDED JUNE 30, 2012

Amounts reported for governmental activities in the statement of net assets are different because:

TOTAL GOVERNMENTAL FUND BALANCE		2,631,081
Capital assets used in governmental activities are not financial resources and therefore are not reported as assets in governmental funds.		
Cost of Capital Assets	76,499,852	
Accumulated Depreciation	<u>(24,838,031)</u>	51,661,821
Bond Issuance Costs		712,095
Long-term liabilities (including bonds payable) are not due and payable in the current period and therefore are not reported as liabilities in the funds.		
Long-term liabilities at year end consist of:		
Bonds Payable	(34,393,747)	
Capital Lease Obligation	(372,046)	
Accrued Interest on Bonds	(322,336)	
Accrued Sick Leave	<u>(1,080,244)</u>	<u>(36,168,373)</u>
TOTAL NET ASSETS - GOVERNMENTAL ACTIVITIES		<u><u>18,836,624</u></u>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES  
GOVERNMENTAL FUNDS  
FOR THE YEAR ENDED JUNE 30, 2012

	GENERAL	SPECIAL REVENUE	DEBT SERVICE FUND	OTHER GOVERNMENTAL FUNDS	TOTAL GOVERNMENTAL FUNDS
<b>REVENUES:</b>					
Taxes	6,767,432			1,876,039	8,643,471
Earnings on Investments	63,433	2,617			66,050
Intergovernmental - State	15,971,442	884,995	222,368	1,002,149	18,080,954
Intergovernmental - Federal		1,934,334	84,157		2,018,491
Other Sources	22,328	48,968			71,296
<b>TOTAL REVENUES</b>	<b>22,824,635</b>	<b>2,870,914</b>	<b>306,525</b>	<b>2,878,188</b>	<b>28,880,262</b>
<b>EXPENDITURES:</b>					
Instructional	13,334,687	2,362,205			15,696,892
Support Services:					
Student Support Services	892,790	16,946			909,736
Staff Support Services	654,907	264,064			918,971
District Administration	842,538				842,538
School Administration	1,485,684				1,485,684
Business Support Services	463,426	2,080	43,361		508,867
Plant Operation & Maintenance	2,122,888	57,508			2,180,396
Student Transportation	1,888,144	2,022			1,890,166
Food Service Operation	56,520				56,520
Community Service Operations		240,959			240,959
Debt Service:					
Principal			3,471,392		3,471,392
Interest			1,586,326		1,586,326
<b>TOTAL EXPENDITURES</b>	<b>21,741,584</b>	<b>2,945,784</b>	<b>5,101,079</b>	<b>0</b>	<b>29,788,447</b>
<b>EXCESS(DEFICIT) REVENUES OVER EXPENDITURES</b>	<b>1,083,051</b>	<b>(74,870)</b>	<b>(4,794,554)</b>	<b>2,878,188</b>	<b>(908,185)</b>
<b>OTHER FINANCING SOURCES(USES):</b>					
Proceeds from Sale of Bonds			1,885,000		1,885,000
Proceeds from Sale of Assets	29,200				29,200
Operating Transfers In - Note O		74,870	2,917,124	176,440	3,168,434
Operating Transfers Out - Note O	(225,565)			(2,942,869)	(3,168,434)
<b>TOTAL OTHER FINANCING SOURCES</b>	<b>(196,365)</b>	<b>74,870</b>	<b>4,802,124</b>	<b>(2,766,429)</b>	<b>1,914,200</b>
<b>NET CHANGE IN FUND BALANCES</b>	<b>886,686</b>	<b>0</b>	<b>7,570</b>	<b>111,759</b>	<b>1,006,015</b>
<b>FUND BALANCES - BEGINNING</b>	<b>1,603,963</b>	<b>0</b>	<b>135</b>	<b>20,968</b>	<b>1,625,066</b>
<b>FUND BALANCES - ENDING</b>	<b>2,490,649</b>	<b>0</b>	<b>7,705</b>	<b>132,727</b>	<b>2,631,081</b>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
RECONCILIATION OF THE STATEMENT OF REVENUES,  
EXPENDITURES AND CHANGES IN FUND BALANCES OF GOVERNMENTAL FUNDS  
TO THE STATEMENT OF ACTIVITIES  
FOR THE YEAR ENDED JUNE 30, 2012

Amounts reported for governmental activities in the statement of net assets are different because:

NET CHANGES - GOVERNMENTAL FUNDS		1,006,015
<p>Governmental funds report capital outlays as expenditures because they use current financial resources. However, in the statement of activities, the cost of those assets is allocated over their estimated useful lives and reported as depreciation expense. This is the amount by which capital exceeds depreciation expense for the year.</p>		
Depreciation Expense	(2,321,822)	
Capital Outlays	<u>165,621</u>	(2,156,201)
<p>Bond proceeds are reported as financing sources in governmental funds and thus contribute to the change in fund balance. In the statement of net assets, however, issuing debt increases long-term liabilities and does not affect the statement of activities. Similarly, repayment of principal is an expenditure in the governmental funds but reduces the liability in the statement of net assets.</p>		
Principal Paid	3,471,392	
Bond Proceeds	<u>(1,885,000)</u>	1,586,392
<p>Generally, expenditures recognized in this fund financial statement are limited to only those that use current financial resources, but expenses are recognized in the statement of activities when they are incurred.</p>		
Amortization - Bond Issuance Costs	(104,984)	
Bond Issuance Cost	43,361	
Accrued Interest Payable	(91,720)	
Accrued Sick Leave	<u>(176,040)</u>	(329,383)
<p>In the statement of activities the net gain on the sale/disposal of assets is reported in whereas in the governmental funds the proceeds from the sale increases financial resources. Thus the change in net assets differs from change in fund balances by the cost of the asset sold.</p>		
Loss - Sale of Assets		<u>(635)</u>
CHANGES - NET ASSETS GOVERNMENTAL FUNDS		<u><u>106,188</u></u>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN  
FUND BALANCE - BUDGET AND ACTUAL - GENERAL FUND  
FOR THE YEAR ENDED JUNE 30, 2012

	ORIGINAL BUDGET	FINAL BUDGET	ACTUAL	VARIANCE WITH FINAL BUDGET POSITIVE (NEGATIVE)
<b>REVENUES:</b>				
Taxes	6,250,000	6,250,000	6,767,432	517,432
Other Local Sources	70,000	70,000	63,433	(6,567)
State Sources	11,523,230	11,523,230	15,971,442	4,448,212
Federal Sources				
Other Sources			51,528	51,528
<b>TOTAL REVENUES</b>	<u>17,843,230</u>	<u>17,843,230</u>	<u>22,853,835</u>	<u>5,010,605</u>
<b>EXPENDITURES:</b>				
Instructional	10,916,095	10,916,095	13,334,687	(2,418,592)
Student Support Services	684,365	684,365	892,790	(208,425)
Staff Support Services	502,594	502,594	654,907	(152,313)
District Administration	529,454	529,454	842,538	(313,084)
School Administration	1,198,763	1,198,763	1,485,684	(286,921)
Business Support Services	325,838	325,838	463,426	(137,588)
Plant Operation & Maintenance	2,306,781	2,306,781	2,122,888	183,893
Student Transportation	1,736,361	1,736,361	1,888,144	(151,783)
Central Office				
Food Service Operations	74,509	74,509	56,520	17,989
Community Service Operations				
Facility Acquisition & Construction				
Other	1,068,470	1,068,470	225,565	842,905
<b>TOTAL EXPENDITURES</b>	<u>19,343,230</u>	<u>19,343,230</u>	<u>21,967,149</u>	<u>(2,623,919)</u>
<b>NET CHANGE IN FUND BALANCE</b>	(1,500,000)	(1,500,000)	886,686	2,386,686
<b>FUND BALANCES - BEGINNING</b>	<u>1,500,000</u>	<u>1,500,000</u>	<u>1,603,963</u>	<u>0</u>
<b>FUND BALANCES - ENDING</b>	<u><u>0</u></u>	<u><u>0</u></u>	<u><u>2,490,649</u></u>	<u><u>2,386,686</u></u>

On-behalf payments totaling \$4,343,785 are not budgeted by the Mercer County School District.

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN  
FUND BALANCE - BUDGET AND ACTUAL - SPECIAL REVENUE FUND  
FOR THE YEAR ENDED JUNE 30, 2012

	ORIGINAL BUDGET	FINAL BUDGET	ACTUAL	VARIANCE WITH FINAL BUDGET POSITIVE (NEGATIVE)
<b>REVENUES:</b>				
Taxes				
Other Local Sources	17,300	17,300	51,585	(34,285)
State Sources	889,384	889,384	884,995	4,389
Federal Sources	1,726,235	1,726,235	1,934,334	(208,099)
Other Sources	117,381	118,300	74,870	43,430
<b>TOTAL REVENUES</b>	<b>2,750,300</b>	<b>2,751,219</b>	<b>2,945,784</b>	<b>(194,565)</b>
<b>EXPENDITURES:</b>				
Instructional	2,369,227	2,369,227	2,362,205	7,022
Student Support Services	7,198	7,198	16,946	(9,748)
Staff Support Services	120,101	121,010	264,064	(143,054)
District Administration				
School Administration				
Business Support Services			2,080	(2,080)
Plant Operation & Maintenance	29,329	29,329	57,508	(28,179)
Student Transportation			2,022	(2,022)
Central Office				
Community Service Operations	224,445	224,455	240,959	(16,504)
Facility Acquisition & Construction				
Other				
<b>TOTAL EXPENDITURES</b>	<b>2,750,300</b>	<b>2,751,219</b>	<b>2,945,784</b>	<b>(194,565)</b>
<b>NET CHANGE IN FUND BALANCE</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>FUND BALANCES - BEGINNING</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
<b>FUND BALANCES - ENDING</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>

See accompanying auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF NET ASSETS  
PROPRIETARY FUNDS  
JUNE 30, 2012

	ENTERPRISE FUNDS		
	FOOD SERVICE	OTHER ENTERPRISE FUNDS	TOTAL
<b>ASSETS:</b>			
Current Assets:			
Cash & Cash Equivalents	277,980		277,980
Investments			
Accounts Receivable			
Inventories for Consumption	31,371		31,371
Total Current Assets	309,351	0	309,351
Noncurrent Assets:			
Furniture & Equipment	708,980		708,980
Less: Accumulated Depreciation	(574,446)		(574,446)
Total Noncurrent Assets	134,534	0	134,534
<b>TOTAL ASSETS</b>	<b>443,885</b>	<b>0</b>	<b>443,885</b>
<b>LIABILITIES:</b>			
Current Liabilities:			
Account Payable			
Accrued Sick Leave			
Total Current Liabilities	0	0	0
Net Assets:			
Invested in Assets, Net of Debt	134,534		134,534
Restricted	309,351		309,351
Total Net Assets	443,885	0	443,885
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>443,885</b>	<b>0</b>	<b>443,885</b>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS  
PROPRIETARY FUNDS  
FOR THE YEAR ENDED JUNE 30, 2012

	ENTERPRISE FUNDS		
	FOOD SERVICE	OTHER ENTERPRISE FUNDS	TOTAL
OPERATING REVENUES:			
Lunchroom Sales	601,062		601,062
Other Operating Revenues	41,913		41,913
TOTAL OPERATING REVENUES	642,975	0	642,975
OPERATING EXPENSES:			
Salaries & Benefits	797,777		797,777
Contract Services	79,348		79,348
Materials & Supplies	746,994		746,994
Depreciation - Note F	17,951		17,951
Other Operating Expenses	18,268		18,268
TOTAL OPERATING EXPENSES	1,660,338	0	1,660,338
OPERATING INCOME(LOSS)	(1,017,363)	0	(1,017,363)
NONOPERATING REVENUES(EXPENSES):			
Federal Grants	769,696		769,696
State Grants	127,024		127,024
Donated Commodities	93,562		93,562
Interest Income	6,593		6,593
Gain (Loss) Sale of Assets			
Miscellaneous Income			
TOTAL NONOPERATING REVENUE	996,875	0	996,875
INCOME(LOSS) BEFORE CAPITAL CONTRIBUTIONS	(20,488)	0	(20,488)
CAPITAL CONTRIBUTIONS	0	0	0
CHANGE IN NET ASSETS	(20,488)	0	(20,488)
TOTAL NET ASSETS - BEGINNING	464,373	0	464,373
TOTAL NET ASSETS - ENDING	443,885	0	443,885

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF CASH FLOWS  
PROPRIETARY FUNDS  
FOR THE YEAR ENDED JUNE 30, 2012

CASH FLOWS FROM OPERATING ACTIVITIES:

Cash Received from:	
Lunchroom Sales	642,975
Cash Paid to/for:	
Employees	(685,121)
Supplies	(671,073)
Other Activities	(97,616)
	(97,616)

Net Cash Used in Operating Activities (810,835)

CASH FLOWS FROM NON-CAPITAL AND RELATED  
FINANCING ACTIVITIES:

Miscellaneous Receipts	
Federal Grants	769,696
State Grants	14,368
	14,368

Net Cash Provided by Non-Capital and Related Financing Activities 784,064

CASH FLOWS FROM CAPITAL AND RELATED  
FINANCING ACTIVITIES:

Purchases of Capital Assets	(11,879)
-----------------------------	----------

CASH FLOWS FROM INVESTING ACTIVITIES

Receipt of Interest Income	6,593
	6,593

Net Decrease in Cash and Cash Equivalents (32,057)

Balances, Beginning of Year 310,037

Balances, End of Year 277,980

RECONCILIATION OF OPERATING LOSS TO NET CASH  
USED IN OPERATING ACTIVITIES:

Operating Loss (1,017,363)

Adjustments to Reconcile Operating Loss to Net Cash (Used)  
by Operating Activities

Depreciation	17,951
State On-Behalf Payments	112,657
Donated Commodities	93,562
Change in Assets and Liabilities:	
Accounts Receivable	
Inventory	1,388
Accounts Payable	(19,030)
	(19,030)

Net Cash Used in Operating Activities (810,835)

Schedule of Non-Cash Transactions:

Donated Commodities	93,562
State On-Behalf Payments	112,657

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF FIDUCIARY NET ASSETS  
FIDUCIARY FUNDS  
JUNE 30, 2012

	<u>AGENCY FUND</u>
ASSETS:	
Cash and Cash Equivalents	327,444
Accounts Receivable	
Investment Income Receivable	
Loans Receivable	
Investments - Note D	
TOTAL ASSETS	<u>327,444</u>
LIABILITIES:	
Accounts Payable	
Due to Student Groups	<u>327,444</u>
TOTAL LIABILITIES	<u>327,444</u>
NET ASSETS HELD IN TRUST	<u><u>0</u></u>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
NOTES TO FINANCIAL STATEMENTS  
YEAR ENDED JUNE 30, 2012

**NOTE A – SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

Reporting Entity

The Mercer County 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 Mercer County Board of Education (“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 in Section 2100, Codification of Governmental Accounting and Financial Reporting Standards. 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 Mercer County Board of Education. 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 Board itself such as Band Boosters, Parent-Teacher Associations, etc.

The financial statements of the District include those of separately administered organizations that are controlled by or dependent on the Board. 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 statements of the following organizations are included in the accompanying financial statements:

Mercer County Board of Education Finance Corporation – In a prior year, the Board of Education resolved to authorize the establishment of the Mercer County School District Finance Corporation (a non-profit, non-stock, public and charitable corporation organized under the School Bond Act and KRS 273 and KRS Section 58.180) (the “Corporation”) as an agency for the District for financing the costs of school building facilities. The members of the Board also comprise the Corporation’s Board of Directors.

Basis of Presentation

Government-Wide Financial Statements – The statement of net assets 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 those activities of the District that are governmental and those that are considered business-type activities.

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

## NOTES TO FINANCIAL STATEMENTS (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 District's governmental activities. Direct expenses are those that are specifically associated with a service, program or department and are therefore clearly identifiable to a particular function. Program revenues include charges paid by the recipient of the 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. Revenues that are 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. The focus of governmental and enterprise fund financial statements is on major funds rather than reporting funds by type. Each major fund is presented in a separate column. Nonmajor funds are aggregated and presented in a single 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. The financial statements for governmental funds are a balance sheet, which generally includes only current assets and current liabilities, and a statement of revenues, expenditures, and changes in fund balances, which reports on the changes in net total assets. Proprietary funds and fiduciary funds are reported using the economic resources measurement focus. The statement of cash flows provides information about how the District finances and meets the cash flow needs of its proprietary activities.

The District has the following funds:

### I. Governmental Fund Types

- A. The General Fund is the main operating fund of the Board. 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 trust 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 on Pages 42 and 23 in the Schedule of Expenditures of Federal Awards and related notes. 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 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 for use in financing projects identified in the District's facility plan.

## NOTES TO FINANCIAL STATEMENTS (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. This is a major fund of the District.

D. 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 cost; and for the payment of interest on generally obligation notes payable, as required by Kentucky law.

### II. Proprietary Fund Types (Enterprise Fund)

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 contribution 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 pronouncements issued on or before November 30, 1989, unless those pronouncements conflict with or contradict GASB pronouncements.

### III. Fiduciary Fund Type (Agency and Private Purpose Trust Funds)

- A. The Agency Fund accounts for activities of student groups and other types of activities requiring clearing accounts. The funds are accounted for in accordance with the Uniform Program of Accounting for School Activity Funds.
- B. The Private Purpose Trust funds are used to report trust arrangements under which principal and income benefit individuals, private organization, or other governments.

### Basis of Accounting

Basis of accounting determines when transactions are recorded in the financial records and reported on the financial statements. Government-wide financial statements are prepared using the accrual basis of accounting. Governmental funds use the modified accrual basis of accounting. Proprietary and fiduciary funds also use the accrual basis of accounting.

Revenues – Exchange and Nonexchange Transactions – Revenues resulting from exchange transactions, in which each party receives essentially equal value, is recorded on the accrual basis when the exchange takes place. On a modified accrual basis, revenues are recorded in the fiscal year in which the resources are measurable and available. Available means that the resources will be collected within the current fiscal year or are expected to be collected soon enough thereafter to be used to pay liabilities of the current fiscal year. For the District, available means expected to be received within 60 days of the fiscal year-end.

## NOTES TO FINANCIAL STATEMENTS (CONTINUED)

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 satisfied. Eligibility requirements include timing requirements, which specify the year when the resource 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 purpose, and expenditure requirements, in which the resources are provided to the District on a reimbursement basis. On a modified accrual basis, revenues from nonexchange transactions must also be available before it can be recognized.

Deferred Revenue – Deferred revenue arises when assets are recognized before revenue recognition criteria have been satisfied.

Grants and entitlements received before the eligibility requirements are met are recorded as deferred revenue.

Expenses/Expenditures – On the accrual basis of accounting, expenses are recognized at the time they are incurred. The fair value of donated commodities used during the year is reported in the statement of revenues, expenses, and changes in net assets as an expense with a like amount reported as donated commodities revenue. Unused donated commodities are reported as deferred revenue.

The measurement focus of governmental fund accounting is on decreases in net financial resources (expenditures) rather than expenses. Expenditures are generally recognized in the accounting period in which the related fund liability is incurred, if measurable. Allocations of costs, such as depreciation, are not recognized in governmental funds.

### Property Taxes

Property Tax Revenues – Property taxes are levied each September on the assessed value listed as of the prior January 1, for all real and personal property in the county. The billings are considered due upon receipt by the taxpayer; however, the actual date is based on a period ending 30 days after the tax bill mailing. Property taxes collected are recorded as revenues in the fiscal year for which they were levied. All taxes collected are initially deposited into the General fund and then transferred to the appropriate fund.

The property tax rates assessed for the year ended June 30, 2012, to finance the General Fund operations were \$0.596 per \$100 valuation for real property, \$0.596 per \$100 valuation for business personal property, and \$0.491 per \$100 valuation for motor vehicles.

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 gases.

### Capital Assets

General capital assets are those assets not specifically related to activities reported in the proprietary funds. These assets generally result from expenditures in the governmental funds. These assets are reported in the governmental activities column of the government-wide statement of net assets but are not reported in the fund financial statements. Capital assets utilized by the proprietary funds are reported both in the business-type activities column of the government-wide statement of net assets and in the respective funds.

## NOTES TO FINANCIAL STATEMENTS (CONTINUED)

All reported capital assets 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 general capital assets and proprietary fund assets:

<b>Description</b>	<b>Governmental Activities Estimated Lives</b>
Buildings and improvements	25-50 years
Land improvements	20 years
Technology equipment	5 years
Vehicles	5-10 years
Audio-visual equipment	15 years
Food service equipment	10-12 years
Furniture and fixtures	7 years
Rolling stock	15 years
Other	10 years

### Interfund Balances

On fund financial statements, receivables and payable resulting from short-term interfund loans are classified as “interfund receivables/payables.” These amounts are eliminated in the governmental and business-type activities columns of the statements of net assets, except for the net residual 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 received from the District 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 School District’s past experience of making termination payments.

The entire compensated absence liability is reported on the government-wide financial statements.

For governmental fund financial statements the current portion of unpaid accrued sick leave is the amount expected to be paid using expendable available resources. These amounts are recorded in the amount “accumulated sick leave payable” in the general fund. The noncurrent portion of the liability is reported as a reserve of fund balance.

### Budgetary Process

**Budgetary Basis of Accounting:** The District’s budgetary process accounts for certain transactions on a basis other than 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).

## NOTES TO FINANCIAL STATEMENTS (CONTINUED)

Once the budget is approved, it can be amended. Amendments are presented to the Board at their regular meetings. Such amendments are made before the fact, are reflected in the official minutes of the Board, and are not made 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 budget appropriations lapse at year-end.

### Cash and Cash Equivalents

The District considers demand deposits, money market funds, and other investments with an original maturity of 90 days or less, to be cash equivalents.

### Inventories

On government-wide financial statements, inventories are stated at cost and are expensed when used.

On fund financial statements inventories are stated at cost. The cost of inventory items is recorded as an expenditure in the governmental fund types when purchased.

The food service fund uses the specific identification method.

### Investments

The private purpose trust funds record investments at their quoted market prices. All realized gains and losses and changes in fair value are recorded in the Statement of Changes in Fiduciary Net Assets.

### Accrued Liabilities and Long-Term Obligations

All payables, accrued liabilities, and long-term obligations are reported in the government-wide financial statements, and all payables, accrued liabilities, and long-term obligations payable from proprietary funds are reported on the proprietary fund financial statements.

In general, payables and accrued liabilities that will be paid from governmental funds are reported on the governmental fund financial statements regardless of whether they will be liquidated with current resources. However, claims and judgments, the noncurrent portion of capital leases, accumulated sick leave, contractually required pension contributions and special termination benefits that will be paid from governmental funds are reported as a liability in the fund financial statements only to the extent that they will be paid with current, expendable, available financial resources. In general, payments made within sixty days after year-end are considered to have been made with current available financial resources. Bonds and other long-term obligations that will be paid from governmental funds are not recognized as a liability in the fund financial statements until due.

### Fund Balance

In accordance with Government Accounting Standards Board 54, Fund Balance Reporting and Governmental Fund Type Definitions, the District classifies governmental fund balances as follows:

Non-spendable – includes fund balance amounts that cannot be spent either because it is not in spendable form or because of legal or contractual constraints.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

Restricted – includes fund balance amounts that are constrained for specific purposes which are externally imposed by providers, such as creditors or amounts constrained due to constitutional provisions or enabling legislation.

Committed – includes fund balance amounts that are constrained for specific purposes that are internally imposed by the government through formal action of the highest level of decision making authority and does not lapse at year-end.

Assigned – includes fund balance amounts that are intended to be used for specific purposes that are neither considered restricted or committed. Fund Balance may be assigned by the Superintendent.

Unassigned – includes positive fund balance within the General Fund which has not been classified within the above mentioned categories and negative fund balances in other governmental funds.

The District committed the following fund balance type by taking the following action:

<u>Fund Balance Type</u>	<u>Amount</u>	<u>Action</u>
General Fund	1,080,244	Long-Term Sick Leave Commitment
General Fund	18,119	Site Based Carry-forward

The District uses *restricted/committed* amounts to be spent first when both restricted and unrestricted fund balance is available unless there are legal documents/contracts that prohibit doing this, such as grant agreements requiring dollar for dollar spending. Additionally, the District would first use *committed*, then *assigned*, and lastly *unassigned* amounts for unrestricted fund balance when expenditures are made.

The District does not have a formal minimum fund balance policy.

<u>Major Special Revenue Fund</u>	<u>Revenue Source</u>
Special Revenue	State, Local and Federal Grants

Net Assets

Net assets represent the difference between assets and liabilities. Net assets invested in capital assets, net of related debt consists of capital assets, net of accumulated depreciation, reduced by the outstanding balances of any borrowings used for the acquisition, construction, or improvement of those assets. Net assets are reported as restricted when there are limitations imposed on their use either through the enabling legislation adopted by the School District or through external restrictions imposed by creditors, grantors, or laws or regulations of other governments.

Operating Revenues and Expenses

Operating revenues are those revenues that are generated directly from the primary activity of the proprietary funds. For the School 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.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

Interfund Activity

Exchange transactions 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 after nonoperating revenues/expenses in proprietary funds. Repayments from funds responsible for particular expenditures/expenses to the funds that initially paid for them are not presented on the financial statements.

**NOTE B – ESTIMATES**

The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America 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 general purpose financial statements, and the reported amounts of revenues and expenditures during the reporting period. Actual results could differ from those estimates.

**NOTE C – CASH AND CASH EQUIVALENTS**

Custodial Credit Risk - Deposits. Custodial Credit is the risk that in the event of a bank failure, the District's deposits may not be returned to it. The District's policy is to have all deposits secured by pledged securities.

At year-end, the carrying amount of the District's total cash and cash equivalents was \$3,648,663. Of the total cash balance, \$250,000 was covered by Federal Depository Insurance, with the remainder covered by collateral agreements and collateral held by the pledging banks' trust departments in the District's name. Cash equivalents are funds temporarily invested in securities with maturity of 90 days or less.

Cash and cash equivalents at June 30, 2012, consisted of the following:

	<b>Bank Balance</b>	<b>Book Balance</b>
Whitaker Bank	4,842,046	3,569,975
Farmers Bank	<u>78,688</u>	<u>78,688</u>
	<u>4,920,734</u>	<u>3,648,663</u>

Breakdown per financial statements:

Governmental Funds	3,043,239
Proprietary Funds	277,980
Agency Funds	<u>327,444</u>
	<u>3,648,663</u>

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

**NOTE D – LONG TERM OBLIGATIONS**

The amount shown in the accompanying financial statements as bond obligations represents the District's future obligations to make payments relating to the bonds issued by the Mercer County School District Finance Corporation aggregating \$34,393,747.

The original amount of each issue and interest rates are summarized below:

2002	1,670,000	1.40% - 3.80%
2003	235,000	3.75%
2004	2,165,000	2.00% - 3.60%
2004 B	230,000	2.00% - 4.25%
2005	1,945,000	3.20% - 4.20%
2007	25,305,000	4.00% - 4.25%
2008	1,395,000	2.40% - 3.30%
2009	275,496	2.00% - 3.60%
2010	4,185,000	2.50% - 6.25%
2010Refunding	1,785,000	0.50% - 2.60%
2012Refunding	1,885,000	0.75% - 2.125%

The District, through the General Fund (including utility taxes and the SEEK Capital Outlay Fund) is obligated to make bond payments in amounts sufficient to satisfy debt service requirements on bonds issued by Mercer County 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.

In 1995 the Board 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 schools districts in meeting school construction needs. The table sets forth the amount to be paid by the Board and the Commission for each year until maturity of all bonds issued. The Kentucky School Construction Commission's participation is limited to the biennial budget period of the Commonwealth of Kentucky with the right reserved by the Kentucky School Construction Commission to terminate the commitment to pay the agreed participation every two years. The obligation of the Kentucky School Construction Commission to make the agreed payments automatically renews each two years for a period of two years unless the Kentucky School Construction Commission gives notice of its intention not to participate not less than sixty days prior to the end of its biennium.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

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 maturity, the minimum obligations of the District, including amounts to be paid by the Commission at June 30, 2012, for debt service (principal and interest) are as follows:

<u>Year</u>	<u>Principal</u>	<u>Interest</u>	<u>Participation</u>	<u>District's Portion</u>
2012-13	1,707,840	1,378,677	221,646	2,864,872
2013-14	1,778,512	1,317,854	227,025	2,869,341
2014-15	1,744,185	1,257,460	131,237	2,870,408
2015-16	1,794,857	1,200,701	127,190	2,868,368
2016-17	1,850,664	1,139,114	125,321	2,864,457
2017-18	1,901,606	1,074,998	116,600	2,860,004
2018-19	1,942,571	1,008,122	91,703	2,858,990
2019-20	2,003,512	935,520	77,920	2,861,112
2020-21	2,045,000	859,149	77,921	2,826,228
2021-22	2,130,000	780,643	77,921	2,832,722
2022-23	2,220,000	698,779	77,921	2,840,858
2023-24	2,300,000	609,872	77,207	2,832,665
2024-25	2,405,000	519,241	75,318	2,848,923
2025-26	2,500,000	418,878	75,320	2,843,557
2026-27	2,600,000	318,188	75,320	2,842,868
2027-28	825,000	184,694	11,012	998,682
2028-29	850,000	135,475	11,012	974,463
2029-30	885,000	83,425	11,013	957,412
2030-31	<u>910,000</u>	<u>28,438</u>	<u>7,121</u>	<u>931,317</u>
	<u>34,393,747</u>	<u>13,949,227</u>	<u>1,695,727</u>	<u>46,647,247</u>

Long-term liability activity for the year ended June 30, 2012, was as follows:

	<u>Beginning Balance</u>	<u>Additions</u>	<u>Reductions</u>	<u>Ending Balance</u>	<u>Due Within One Year</u>
<b>Primary Government</b>					
Governmental Activities:					
Revenue Bond Payable	35,886,563	1,885,000	3,377,816	34,393,747	1,707,840
Capital Lease Obligations	465,622	0	93,576	372,046	92,862
Accrued Sick Leave	<u>1,330,496</u>	<u>232,202</u>	<u>90,174</u>	<u>1,472,524</u>	<u>392,280</u>
Governmental Activities Long-Term Liabilities	<u>37,682,681</u>	<u>2,117,202</u>	<u>3,561,566</u>	<u>36,238,317</u>	<u>2,192,982</u>

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

**NOTE E - CAPITAL LEASE PAYABLE**

The District is the lessee of buses under capital leases expiring in various years through 2017. The assets and liabilities under capital leases are recorded at the present value of the minimum lease payments or the fair value of the asset. The assets are amortized over their estimated productive lives. Amortization of assets under capital leases is included in depreciation expense for fiscal year 2012.

The following is a summary of property held under capital leases:

<u>Classes of Property</u>	<u>Book Value as of June 30, 2012</u>
Buses	1,086,180
Accumulated Amortization	<u>(898,080)</u>
	<u>188,100</u>

The following is a schedule by years of the future principal payments under capital leases as of June 30, 2012:

<u>Year Ending June 30,</u>	<u>Capital Lease Payable</u>
2013	106,526
2014	103,877
2015	83,300
2016	57,856
2017	<u>57,856</u>
Net minimum lease payments	409,415
Amount representing interest	<u>(37,370)</u>
Present value of net minimum lease payments	<u>372,045</u>

Interest rates on capitalized leases vary from 1.00% to 5.30%. The capital leases provide for the buses to revert to the District at the end of the respective lease with no further payment for purchase.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

**NOTE F - CAPITAL ASSETS**

Capital asset activity for the fiscal year ended June 30, 2012, was as follows:

	BEGINNING BALANCE	ADDITIONS	RETIREMENTS	ENDING BALANCE
<b>GOVERNMENTAL ACTIVITIES:</b>				
Non-Depreciable Assets:				
Land	1,622,246			1,622,246
Construction	318,896	(130,347)		188,549
Depreciable Assets:				
Buildings & Building Improvements	64,252,751	130,347		64,383,098
Technology Equipment	3,157,442	92,142	22,137	3,227,447
Vehicles	4,776,273			4,776,273
General Equipment	2,230,100	73,479	1,339	2,302,240
<b>TOTAL AT HISTORICAL COST</b>	<u>76,357,708</u>	<u>165,621</u>	<u>23,476</u>	<u>76,499,853</u>
<b>LESS ACCUMULATED DEPRECIATION FOR:</b>				
Buildings & Building Improvements	16,120,601	1,511,335		17,631,936
Technology Equipment	1,780,269	450,395	22,022	2,208,642
Vehicles	3,482,574	234,488		3,717,062
General Equipment	1,155,606	125,604	818	1,280,392
<b>TOTAL ACCUMULATED DEPRECIATION</b>	<u>22,539,050</u>	<u>2,321,822</u>	<u>22,840</u>	<u>24,838,032</u>
<b>GOVERNMENTAL ACTIVITIES CAPITAL NET</b>	<u>53,818,658</u>	<u>(2,156,201)</u>	<u>636</u>	<u>51,661,821</u>
<b>PROPRIETARY ACTIVITIES:</b>				
Depreciable Assets:				
Technology Equipment	11,277	699		11,976
General Equipment	685,824	11,180		697,004
<b>TOTALS AT HISTORICAL COST</b>	<u>697,101</u>	<u>11,879</u>	<u>0</u>	<u>708,980</u>
<b>LESS ACCUMULATED DEPRECIATION FOR:</b>				
Technology Equipment	7,580	1,379		8,959
General Equipment	548,914	16,573		565,487
<b>TOTAL ACCUMULATED DEPRECIATION</b>	<u>556,494</u>	<u>17,952</u>	<u>0</u>	<u>574,446</u>
<b>PROPRIETARY ACTIVITIES CAPITAL NET</b>	<u>140,607</u>	<u>(6,073)</u>	<u>0</u>	<u>134,534</u>
<b>DEPRECIATION EXPENSE CHARGED TO GOVERNMENTAL FUNCTIONS AS FOLLOWS:</b>				
Instructional				1,747,703
Student Support Services				90,559
Staff Support Services				4,091
District Administration				49,003
School Administration				44,029
Business Support Services				5,499
Plant Operation & Maintenance				141,971
Student Transportation				237,135
Community Service Operations				1,832
<b>TOTAL</b>				<u>2,321,822</u>

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

**NOTE G – COMMITMENTS UNDER NONCAPITALIZED LEASES**

Commitments under operating lease agreements for office equipment provide the minimum future rental payments as of June 30, 2012, as follows:

<u>Year Ending June 30,</u>	
2013	<u>66,158</u>
Total minimum payments	<u>66,158</u>

**NOTE H – RETIREMENT PLANS**

Certified employees are covered under the Teachers' Retirement System of Kentucky ("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 public educational agencies in Kentucky.

KTRS was created by the 1938 General Assembly and is governed by Chapter 161 Section 220 through 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 Kentucky Teachers' Retirement System, 479 Versailles Road, Frankfort, KY 40601.

Contribution rates are established by KRS. Members hired before July 1, 2008, are required to contribute 10.355% of their salaries and for members hired after July 1, 2008, to contribute 10.855% to KTRS. The Commonwealth of Kentucky is required to contribute 13.605% and 14.105% of salaries respectively. The federal program for any salaries paid by that program pays the matching contributions. 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)

Substantially all other employees (classified personnel) are covered under the County Employee's Retirement System ("CERS"), a cost sharing, multiple-employer, public employers retirement system. Funding for the Plan is provided through payroll withholdings of 5% for employees hired before September 15, 2008, and 6% for employees hired after September 15, 2008, and a Board contribution of 18.96% of the employee's total compensation subject to contribution.

The Board's total payroll for the year was \$15,882,143. The payroll for employees covered under KTRS was \$12,576,712 and for CERS was \$3,305,431.

For the year ended June 30, 2012, the Commonwealth contributed \$1,524,013 to KTRS for the benefit of our participating employees. The School District's contributions to KTRS for the year ending June 30, 2012 were \$143,768, which represent those employees covered by federal programs.

The contribution requirements for CERS for the year ended June 30, 2012, was \$796,820, which consisted of \$626,591 from the Board and \$170,229 from the employees.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

Benefits under both plans will vary based on final compensation, years of service, and other factors as fully described in the Plan documents.

The “pension benefit obligation” is a standardized disclosure measure of the present value of pension benefits, adjusted for the effects of projected salary increased 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.

KTRS and CERS do not make separate measurements of assets and pension benefit obligation for individual employers. The following tables present certain information regarding the plans’ status as a whole, derived from actuarial valuations performed as of the dates indicated:

	<b>KTRS</b> <b>June 30, 2011</b>	<b>CERS</b> <b>June 30, 2011</b>
Assets available for benefits, at fair value	14,908,138,000	5,629,611,183
Pension benefit obligation	<u>(25,968,692,000)</u>	<u>(8,918,085,025)</u>
(Underfunded)/overfunded pension benefit obligation	<u>(11,060,554,000)</u>	<u>(3,288,473,842)</u>

Ten-year historical trend information showing KTRS’s and CERS’s progress in accumulating sufficient assets to pay benefits when due is presented in their June 30, 2011, comprehensive annual financial reports.

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 or the vested benefits of the District’s portion of the Plan assets.

The District also offers employees the option to participate in a defined contribution plan under Section 403(B), 401(K), and 457 of the Internal Revenue Code. All regular full-time and part-time employees are eligible to participate and may contribute to the maximum amount allowable by law. The District does not contribute to these plans.

**NOTE I – 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 based upon the grantor’s review, the funds are considered not to have 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.

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

**NOTE J – INSURANCE AND RELATED ACTIVITIES**

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 is covered through the purchase of commercial insurance. The District has purchased certain policies, which are retrospectively related which include Workers' Compensation insurance.

**NOTE K – RISK MANAGEMENT**

The District is exposed to various risks of loss related to injuries to employees. To obtain insurance of workers' compensation, errors and omissions, and general liability coverage, the District participates in the Kentucky School Boards Insurance Trust Liability Insurance fund. The public entity risk pools operate as common risk management and insurance programs for all school district and other tax supported educational agencies of Kentucky who are members of the Kentucky School Boards Association. The District pays an annual premium to each fund for coverage. Contributions to the Workers' Compensation fund are based on premium rates established by such fund in conjunction with the excess insurance carrier, subject to claims experience modifications and a group discount amount. Dividends may be declared but are not payable until twenty-four (24) months after the expiration of the self-insurance term. The Liability Insurance fund pays insurance premiums of the participating members established by the insurance carrier. The Trust can terminate coverage if it is unable to obtain acceptable excess general liability coverage and for any reason by giving ninety (90) days' notice. In the event the Trust terminated coverage, any amount remaining in the Fund (after payment of operational and administrative costs for which coverage was provided) would be returned to the members on a pro rata basis.

The District purchases 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.

**NOTE L – DEFICIT OPERATING BALANCES**

There are no funds of the District that currently have a deficit fund balance. However, the following funds have operations that resulted in a current year deficit of expenditures over revenues resulting in a corresponding reduction of fund balance:

Food Service	20,488
Debt Service	4,794,554

**NOTE M – COBRA**

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).

NOTES TO FINANCIAL STATEMENTS (CONTINUED)

**NOTE N – TRANSFER OF FUNDS**

The following transfers were made during the year:

<b>Type</b>	<b>From Fund</b>	<b>To Fund</b>	<b>Purpose</b>	<b>Amount</b>
Matching	General	Special Revenue	Technology Match	56,066
Operating	General	Special Revenue	Reimbursement	18,804
Operating	General	Debt Service	Debt Service	150,695
Operating	Building Fund	Debt Service	Debt Service	2,766,429
Operating	Capital Outlay	Building	Operations	<u>176,440</u>
				<u>3,168,434</u>

**NOTE O – INTERFUND RECEIVABLES AND PAYABLES**

There were no interfund balances at June 30, 2012.

**NOTE P – SUBSEQUENT EVENTS**

Management has reviewed subsequent events through October 29, 2012. There are no material subsequent events to disclose.

**NOTE Q – ON-BEHALF PAYMENT**

For the year ended June 30, 2012, \$4,678,810 in on-behalf payments were made by the Commonwealth of Kentucky for the benefit of the District. Payments for life insurance, health insurance, Kentucky teacher retirement matching pension contributions, administrative fees, technology and debt service were paid by the State for the District. These payments were recognized as on-behalf payments and recorded in the appropriate revenue and expense accounts. These payments were recorded as follows:

General Fund	4,343,785
Food Service Fund	112,657
Debt Service Fund	<u>222,368</u>
Total	<u>4,678,810</u>

MERCER COUNTY SCHOOL DISTRICT  
 COMBINING BALANCE SHEET  
 NON-MAJOR GOVERNMENTAL FUNDS  
 JUNE 30, 2012

	CAPITAL OUTLAY FUND	BUILDING FUND	CONSTRUCTION FUND	TOTAL NON-MAJOR GOVERNMENT FUNDS
<b>ASSETS:</b>				
Cash & Cash Equivalents	124,864	7,863		132,727
Accounts Receivable:				
Taxes				
Accounts				
<b>TOTAL ASSETS</b>	<b>124,864</b>	<b>7,863</b>	<b>0</b>	<b>132,727</b>
<b>LIABILITIES AND FUND BALANCES:</b>				
Liabilities:				
Accounts Payable				
Accrued Sick Leave				
Deferred Revenues				
<b>Total Liabilities</b>	<b>0</b>	<b>0</b>	<b>0</b>	<b>0</b>
Fund Balances:				
Restricted for:				
Capital Projects	124,864	7,863		132,727
Debt Service				
Committed for:				
Accrued Sick Leave				
Site Based Carryforward				
Unassigned				
<b>Total Fund Balances</b>	<b>124,864</b>	<b>7,863</b>	<b>0</b>	<b>132,727</b>
<b>TOTAL LIABILITIES AND NET ASSETS</b>	<b>124,864</b>	<b>7,863</b>	<b>0</b>	<b>132,727</b>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
 COMBINING STATEMENT OF REVENUES AND EXPENDITURES AND CHANGES IN FUND BALANCES  
 NON-MAJOR GOVERNMENTAL FUNDS  
 FOR THE YEAR ENDED JUNE 30, 2012

	CAPITAL OUTLAY FUND	BUILDING FUND	CONSTRUCTION FUND	TOTAL NON-MAJOR GOVERNMENT FUNDS
<b>REVENUES:</b>				
Taxes		1,876,039		1,876,039
Earnings from Investments				
Intergovernmental - State	280,335	721,814		1,002,149
Intergovernmental - Federal				
Other Sources				
<b>TOTAL REVENUES</b>	<u>280,335</u>	<u>2,597,853</u>	<u>0</u>	<u>2,878,188</u>
<b>EXPENDITURES:</b>				
Instructional				
Student Support Services				
Staff Support Services				
District Administration				
School Administration				
Business Support Services				
Plant Operations & Maintenance				
Student Transportation				
Central Office				
Community Service Operations				
Facilities Acquisition & Construction				
Debt Service:				
Principal				
Interest				
<b>TOTAL EXPENDITURES</b>	<u>0</u>	<u>0</u>	<u>0</u>	<u>0</u>
<b>EXCESS(DEFICIT) REVENUES OVER EXPENDITURES</b>	280,335	2,597,853	0	2,878,188
<b>OTHER FINANCING SOURCES(USES):</b>				
Proceeds from Sale of Bonds				
Proceeds from Sale of Assets				
Operating Transfers In		176,440		176,440
Operating Transfers Out	(176,440)	(2,766,429)		(2,942,869)
<b>TOTAL OTHER FINANCING SOURCES(USES)</b>	<u>(176,440)</u>	<u>(2,589,989)</u>	<u>0</u>	<u>(2,766,429)</u>
<b>NET CHANGE IN FUND BALANCES</b>	<u>103,895</u>	<u>7,864</u>	<u>0</u>	<u>111,759</u>
<b>FUND BALANCES - BEGINNING</b>	<u>20,968</u>	<u>0</u>	<u>0</u>	<u>20,968</u>
<b>FUND BALANCES - ENDING</b>	<u><u>124,863</u></u>	<u><u>7,864</u></u>	<u><u>0</u></u>	<u><u>132,727</u></u>

See independent auditor's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
 COMBINING STATEMENT OF REVENUES, EXPENDITURES AND FUND BALANCES  
 AGENCY FUNDS  
 FOR THE YEAR ENDED JUNE 30, 2012

	FUND BALANCE <u>JULY 1, 2011</u>	REVENUES	EXPENDITURES	FUND BALANCE <u>JUNE 30, 2012</u>
Mercer County High School	158,656	417,260	389,737	186,179
Mercer County 9th Grade Academy	18,651	25,110	24,640	19,121
Kenneth King Middle School	61,824	90,736	97,904	54,656
Mercer County Intermediate School	15,735	29,541	32,297	12,979
Mercer County Elementary School	55,540	40,771	52,178	44,133
Harlow Elementary School	<u>14,975</u>	<u>20,897</u>	<u>25,496</u>	<u>10,376</u>
Total Activity Funds (Due to Student Groups)	<u><u>325,381</u></u>	<u><u>624,315</u></u>	<u><u>622,252</u></u>	<u><u>327,444</u></u>

See independent accountant's report and accompanying notes to financial statements.

MERCER COUNTY SCHOOL DISTRICT  
STATEMENT OF RECEIPTS, DISBURSEMENTS AND FUND BALANCE  
HIGH SCHOOL ACTIVITY FUND  
FOR THE YEAR ENDED JUNE 30, 2012

	CASH BALANCE JULY 1, 2011	RECEIPTS	DISBURSEMENTS	CASH BALANCE JUNE 30, 2012	ACCOUNTS RECEIVABLE JUNE 30, 2012	ACCOUNTS PAYABLE JUNE 30, 2012	FUND BALANCE JUNE 30, 2012
General Fund	3,670	3,410	1,467	5,613			5,613
Advertising	0	4,811	1,375	3,436			3,436
Athletic Fees	0	21,436	19,104	2,332			2,332
Fines and Fees	710	415	533	592			592
Titan School Store	808	7,487	5,712	2,583			2,583
Academic Breakfast	250	0	0	250			250
Vending Machines	2,267	1,022	1,276	2,013			2,013
Community Based Ins.	288	442	303	427			427
Pep Club	80	0	0	80			80
Book Rental	27,783	16,455	20,054	24,184			24,184
Toborg Incentive	1,424	0	0	1,424			1,424
Student Fees	4,807	39,019	22,723	21,103			21,103
AP Exams	2,938	18,124	16,151	4,911			4,911
Grad Exp-Homeless	0	336	0	336			336
Concessions	835	1,227	238	1,824			1,824
Lounge	389	3,583	1,538	2,434			2,434
Athletic General	6,272	1,891	3,471	4,692			4,692
Athletics Administration	0	11,895	11,895	0			0
Athletic Receipts	891	56,962	55,992	1,861			1,861
Titan Girls Basketball Tournament	0	11,812	8,117	3,695			3,695
Football	0	13,362	13,160	202			202
Football Coaches	0	4,699	4,557	142			142
Boys Basketball	0	4,587	4,537	50			50
Boys Basketball Coaches	581	24,667	22,834	2,414			2,414
Girls Basketball	0	4,765	4,652	113			113
Girls Basketball Coaches	146	10,885	9,404	1,627			1,627
Varsity Cheerleader	0	96	96	0			0
Heart of the Bluegrass	3,482	4,881	6,317	2,046			2,046
Boys Cross Country	0	289	289	0			0
Girls Cross Country	0	300	300	0			0
Girls Track	0	477	477	0			0
Boys Track	0	462	462	0			0
Girls Tennis	0	1,045	1,045	0			0
Boys Tennis	0	574	574	0			0
Boys Golf	0	399	399	0			0
Baseball	0	3,749	3,749	0			0
Cheerleading Coaches Fund	0	3,148	2,695	453			453
Boys Soccer	0	3,054	2,795	259			259
Girls Soccer	0	2,895	2,666	229			229
Senior Trip	450	4,850	4,825	475			475
Pepsi/Boosters	0	8,059	8,059	0			0
Softball	0	3,102	3,102	0			0
Dance Team	0	500	450	50			50
Volleyball	0	2,195	2,195	0			0

Beta Club	182	450	382	250			250
MCSH Book Club	612	536	582	566			566
DECA Club	424	16	0	440			440
FCA	1,424	235	0	1,659			1,659
FFA	4,445	32,994	20,645	16,794			16,794
Agriculture	1,576	0	0	1,576			1,576
FCCLA	0	14,475	13,369	1,106			1,106
Farm Management	2,149	0	925	1,224			1,224
National Honor Society	708	0	437	271			271
Student Council	640	482	429	693			693
STLP	347	100	100	347			347
Pass Program	205	0	168	37			37
Key Club	237	424	529	132			132
Art	965	2,589	1,568	1,986			1,986
Band	9,530	20,658	26,718	3,470			3,470
Senior Banquet	264	1,000	482	782			782
Chorus	1,685	6,544	4,895	3,334			3,334
Simply Her Beauty	0	127	85	42			42
Drama Dept.	7,850	5,090	3,948	8,992			8,992
Foreign Language	579	0	0	579			579
Advanced Foods	301	815	1,034	82			82
Culinary	72	1,708	1,487	293			293
SHS Spanish	0	489	251	238			238
Child Development	11	0	0	11			11
Horticulture	15,209	27,359	24,809	17,759			17,759
Aquaculture	2,597	0	0	2,597			2,597
Poetry Club	147	0	0	147			147
Library	1,761	2,197	1,876	2,082			2,082
Social Studies	106	0	0	106			106
Science Dept.	51	0	0	51			51
TATU	108	70	0	178			178
Prom Fund	10,162	9,075	9,313	9,924			9,924
Driver's Education	900	10,065	10,965	0			0
Yearbook	10,580	9,862	14,309	6,133			6,133
Colonel Chinn Scholarship	2,766	47	0	2,813			2,813
Darrin Maddox Memorial	1,420	0	200	1,220			1,220
Ray Peavler Scholarship	493	0	0	493			493
Poetry Out Loud	0	1,140	1,110	30			30
Junior Guard	833	0	280	553			553
Disaster Relief	0	151	151	0			0
Summer School	11,880	7,634	18,014	1,500			1,500
Arts & Humanities	866	4,159	4,364	661			661
TAGO	1,039	0	0	1,039			1,039
Project Graduation	5,461	12,156	15,478	2,139			2,139
Total All Funds	158,656	476,014	448,491	186,179	0	0	186,179
Interfund Transfers	0	(58,754)	(58,754)	0	0	0	0
Total	158,656	417,260	389,737	186,179	0	0	186,179

MERCER COUNTY SCHOOL DISTRICT  
SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2012

<u>FEDERAL GRANTOR/PASS-THROUGH GRANTOR/PROGRAM TITLE</u>	<u>CFDA NUMBER</u>	<u>MUNIS PROJECT NUMBER</u>	<u>EXPENDITURES</u>
<u>U.S. Department of Education</u>			
Passed-Through Department of Education			
Title I - School Improvement Grant	84.010	3201	33,424
Title I - School Improvement Grant	84.010	3202	80
Title I - Grants to Local Educational Agencies	84.010	3101	140,616
Title I - Parent Involvement	84.010	3101M	1,863
Title I - Grants to Local Educational Agencies	84.010	3101D	11,964
Title I - Grants to Local Educational Agencies	84.010	3102	525,374
Title I - Grants to Local Educational Agencies	84.010	3102D	63,970
Title I - Parent Involvement	84.010	3102M	362
Title I - Neglected and Delinquent Children	84.010	3130	3,278
Title I - Neglected and Delinquent Children	84.010	3132	4,415
Title I - Neglected and Delinquent Children	84.010	3132T	635
Title I - Homeless Children and Youth - ARRA	84.389	3219	2,878
Title I - School Improvement Grant - ARRA	84.389	3919	3,698
Title I Grants to Local Educational Agencies Total			792,557
Title II, Part A -Teacher Quality Enhancement Grants	84.367	4011	49,731
Title II, Part A -Teacher Quality Enhancement Grants	84.367	4012	96,466
Title II - Part A Total			146,197
Perkins Voc.	84.048	3481	3,050
Perkins Voc.	84.048	3481A	1,260
Perkins Voc.	84.048	3480B	1,017
Perkins Voc.	84.048	3482	21,817
Perkins Voc. - Total			27,144
Federal Ed Tech - Basic	84.318	4251	725
Ed Tech Competitive - ARRA	84.386	4860	13,095
Ed Tech Total			13,820
IDEA - Special Education - Grants to State	84.027	3371	244,985
IDEA - Special Education - Grants to State	84.027	3372	371,945
IDEA - Special Education - Grants to State - ARRA	84.391	4249	49,394
IDEA - Special Education - Preschool Grants	84.173	3131	5,507
IDEA - Special Education - Preschool Grants	84.173	3432	45,983
Special Education Cluster			717,814 *
Education Jobs Funding- ARRA	84.410	4411	141,127 *
Community Based Work Transition	84.341	3711	8,557
Carol White Physical Education	84.215F	5321F	7,560
Total U.S. Department of Education			1,854,776
<u>U.S. Department of Energy</u>			
Passed-Through State Department of Energy Development & Independence			
"SEMP" - School Energy Managers Project - ARRA	81.041	5691	29,583
<u>U.S. Department of Agriculture</u>			
Passed-Through State Department of Education			
National School Lunchroom	10.555	7750002-11	131,665
National School Lunchroom	10.555	7750002-12	494,970
School Breakfast Program	10.553	7760005-11	29,012
School Breakfast Program	10.553	7760005-12	128,417
Child Nutrition Cluster			784,064
Pass-Through State Department of Agriculture			
Food Distribution	10.565	057502-10	93,562
Total U.S. Department of Agriculture			877,626
Total Federal Financial Assistance			2,761,985

\* Tested as major program

MERCER COUNTY SCHOOL DISTRICT  
NOTES TO SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS  
FOR THE YEAR ENDED JUNE 30, 2012

**NOTE A – BASIS OF PRESENTATION**

The accompanying schedule of expenditures of federal awards includes the federal grant activity of the Mercer County 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.

**NOTE B – FOOD DISTRIBUTION**

Nonmonetary assistance is reported in the schedule at the fair value of the commodities disbursed.

MERCER COUNTY SCHOOL DISTRICT  
 SCHEDULE OF FINDINGS AND QUESTIONED COSTS  
 FOR THE YEAR ENDED JUNE 30, 2012

**Section I – Summary of Auditor’s Results**

**Financial Statements**

Type of audit issued: Unqualified

Internal control over financial reporting:

- Material weakness(es) identified? \_\_\_\_\_ Yes      X   No
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? \_\_\_\_\_ Yes      X   None Reported

Noncompliance material to financial statements noted? \_\_\_\_\_ Yes      X   No

**Federal Awards**

Internal control over major programs?

- Material weakness(es) identified? \_\_\_\_\_ Yes      X   No
- Significant deficiency(ies) identified that are not considered to be material weakness(es)? \_\_\_\_\_ Yes      X   None Reported

Type of auditor’s report issued on compliance for major programs (unqualified):

Any audit findings disclosed that are required to be reported in accordance with Section 510(a) of Circular A-133? \_\_\_\_\_ Yes      X   No

Identification of major programs:

<u>CFDA Number</u>	<u>Name of Federal Program or Cluster</u>
84.410 84.027/84.391/84.173	Education Jobs Funding IDEA Cluster

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

Auditee qualified as low-risk auditee?   X   Yes    \_\_\_\_\_ No

**Section II – Financial Statement of Findings**

No matters were reported.

**Section III – Federal Award Findings and Questioned Costs**

No matters were reported.

MERCER COUNTY SCHOOL DISTRICT  
SCHEDULE OF PRIOR YEAR AUDIT FINDINGS  
JUNE 30, 2012

There were no prior year audit findings.

**WHITE AND COMPANY, P.S.C.**  
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Charles M. White, CPA

Email [cmwcpa@windstream.net](mailto:cmwcpa@windstream.net)

October 29, 2012

**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**

Members of the Board of Education  
Mercer County School District  
Harrodsburg, Kentucky

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Mercer County School District, as of and for the year ended June 30, 2012, which collectively comprise the Mercer County School District's basic financial statements and have issued our report thereon dated October 29, 2012. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States, and *Audits of States, Local Governments, and Non-Profit Organizations, Appendix I to the Independent Auditor's Contract – General Auditing Requirements, Appendix II of 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.*

Internal Control over Financial Reporting

Management of Mercer County School District is responsible for establishing and maintaining effective internal control over financial reporting. In planning and performing our audit, we considered Mercer County School District's internal control over financial reporting as a basis for designing our auditing procedures for the purpose of expressing our opinions on the financial statements, but not for the purpose of expressing an opinion on the effectiveness of the Mercer County School District's internal control over financial reporting. Accordingly, we do not express an opinion on the effectiveness of the Mercer County School District's internal control over financial reporting.

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 combination of deficiencies, in internal control such that there is a reasonable possibility that a material misstatement of the entity's financial statements will not be prevented, or detected and corrected on a timely basis.

Our consideration of internal control over financial reporting 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 financial reporting that might be deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over financial reporting that we consider to be material weaknesses, as defined above.

#### Compliance and Other Matters

As part of obtaining reasonable assurance about whether Mercer County School District's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grant agreements, 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 material instances of noncompliance of specific state statutes or regulation identified in *Appendix II of the Independent Auditor's Contract – State Audit Requirements*.

We noted certain matters that we reported to management of Mercer County School District in a separate letter dated October 29, 2012.

This report is intended solely for the information and use of members of the Kentucky State Committee for School District Audits, members of the Board of Education of Mercer County School District, the Kentucky Department of Education, management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

*White and Company, P.S.C.*

Certified Public Accountants

**WHITE AND COMPANY, P.S.C.**  
**Certified Public Accountants**  
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October 29, 2012

**INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE WITH REQUIREMENTS  
THAT COULD HAVE A DIRECT AND MATERIAL EFFECT ON EACH MAJOR  
PROGRAM AN ON INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE  
WITH OMB CIRCULAR A-133**

Members of the Board of Education  
Mercer County School District  
Harrodsburg, Kentucky

Compliance

We have audited the Mercer County School District 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 Mercer County School District's major federal programs for the year ended June 30, 2012. Mercer County School District's major federal programs are identified in the summary of auditor's results section of the accompanying schedule of findings and questioned costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to each of its major federal programs is the responsibility of Mercer County School District's management. Our responsibility is to express an opinion on Mercer County School District's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations, Appendix I to the Independent Auditor's Contract – General Audit Requirements, Appendix II to the 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 Mercer County School District's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination of Mercer County School District's compliance with those requirements.

In our opinion, Mercer County School District complied, in all material respects, with the 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, 2012.

## Internal Control over Compliance

Management of Mercer County School District is responsible for establishing and maintaining effective internal control over compliance with the requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered Mercer County School District's internal control over compliance with the requirements that could have a direct and material effect on a major federal program in order to determine the auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133, 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 Mercer County School 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 a material noncompliance with a type of compliance requirement of a federal program will not be prevented, or detected and corrected, on a timely basis.

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 deficiencies, significant deficiencies, or material weaknesses. We did not identify any deficiencies in internal control over compliance that we consider to be material weaknesses, as defined above.

This report is intended solely for the information and use of members of the Kentucky State Committee for School District Audits, members of the Board of Education of Mercer County School District, the Kentucky Department of Education, management, and federal awarding agencies and pass-through entities, and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

*White and Company, P.S.C.*

Certified Public Accountants

**WHITE AND COMPANY, P.S.C.**  
**Certified Public Accountants**  
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Charles M. White, CPA

Email [cmwcpa@windstream.net](mailto:cmwcpa@windstream.net)

October 29, 2012

**MANAGEMENT LETTER**

Members of the Board of Education  
Mercer County School District  
Harrodsburg, Kentucky

In planning and performing our audit of the financial statements of Mercer County School District for the year ended June 30, 2012, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements. Our professional standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. We feel that the District's financial statements are free of material misstatement. However, we offer the following suggestions that we feel will strengthen your organization's internal control structure.

Prior Year Recommendation:

During the course of the audit, it was noted that an invoice was keyed into the accounts payable system twice and paid twice. The amount of the invoice in question was \$293.10. We recommend that prior to processing a batch of invoices for payment that a detailed report of the pending invoices be printed and compared with the actual invoices in order to catch clerical errors prior to printing of checks.

Current Year Finding:

No such instances were found.

Prior Year Recommendation:

During the course of the audit, it was noted that a vendor allows a 1% discount for prompt payment. The discount was properly computed on the invoice; however, when the invoice was paid, the District failed to take the discount. We recommend that all invoices on which a discount is available be entered into the accounts payable system net of the allowed discount and paid prior to the expiration of the discount period.

Current Year Finding:

Discounts were properly taken.

We would like to offer our assistance throughout the year if and when new or unusual situations arise. Our awareness of new developments when they occur would help to ensure that the District is complying with requirements such as those mentioned above.

Sincerely,

*White and Company, P.S.C.*

Certified Public Accountants

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Charles M. White, CPA

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October 29, 2012

Members of the Board of Education  
Mercer County School District  
Harrodsburg, Kentucky

We have audited the financial statements of the governmental activities, the business-type activities, the aggregate discretely presented component units, each major fund, and the aggregate remaining fund information of Mercer County School District for the year ended June 30, 2012. Professional standards require that we provide you with information about our responsibilities under generally accepted auditing standards (and, if applicable, Government Auditing Standards and OMB Circular A-133), as well as certain information related to the planned scope and timing of our audit. We have communicated such information in our letter to you dated April 3, 2012. Professional standards also require that we communicate to you the following information related to our audit.

Significant Auditing Findings:

*Qualitative Aspects of Accounting Practices*

Management is responsible for the selection and use of appropriate accounting policies. The significant accounting polices used by Mercer County School District are described in Note A to the financial statements. No new accounting policies were adopted and the application of existing policies was not changed during 2012. We noted no transactions entered into by the governmental unit during the year for which there is a lack of authoritative guidance or consensus. All significant transactions have been recognized in the financial statements in the proper period.

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

Management's estimate of the sick leave liability is based on current pay rates and those currently eligible for retirement. We evaluated the key factors and assumptions used to develop the sick leave liability in determining that it is reasonable in relation to the financial statements taken as a whole.

*Difficulties Encountered in Performing the Audit*

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

### *Corrected and Uncorrected Misstatements*

Professional standards require us to accumulate all known and likely misstatements identified during the audit, other than those that are clearly trivial, and communicate them to the appropriate level of management. Management corrected all such misstatements. In addition, none of the misstatements detected as a result of audit procedures and corrected by management were material, either individually or in the aggregate, to each opinion unit's financial statements taken as a whole.

### *Disagreements with Management*

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

### *Management Representations*

We have requested certain representations from management that are included in the management representation letter dated October 29, 2012.

### *Management Consultations with Other Independent Accountants*

In some cases, management may decide to consult with other accountants about auditing and accounting matters, similar to obtaining a "second opinion" on certain situations. If a consultation involves application of an accounting principle to the governmental unit's financial statements or a determination of the type of auditor's opinion that may be expressed on those statements, our professional standards require the consulting accountant to check with us to determine that the consultant has all the relevant facts. To our knowledge, there were not such consultations with other accountants.

### *Other Audit Findings or Issues*

We generally discuss a variety of matters, including the application of accounting principles and auditing standards, with management each year prior to retention as the governmental unit's auditors. However, these discussions occurred in the normal course of our professional relationship and our responses were not a condition to our retention.

### *Other Matters*

With respect to the supplementary information accompanying the financial statements, we made certain inquiries of management and evaluated the form, content, and methods of preparing the information to determine that the information complies with accounting principles generally accepted in the United States of America, the method of preparing it has not changed from the prior period, and the information is appropriate and complete in relation to our audit of the financial statements. We compared and reconciled the supplementary information to the underlying accounting records used to prepare the financial statements or to the financial statements themselves.

This information is intended solely for the use of Mercer County School District and management of Mercer County School District and is not intended to be and should not be used by anyone other than these specified parties.

Sincerely,

*White and Company, P.S.C.*

Certified Public Accountants